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Indian Banking Industry: Competition And Opportunities

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ABSTRACT
The banking industry in India has a huge canvas of history, which covers the traditional banking practices from the time of Britishers to the reforms period, nationalization to privatization of banks and now increasing numbers of foreign banks in India. Therefore, Banking in India has been through a long journey. Banking industry in India has also achieved a new height with the changing times. The use of technology has brought a revolution in the working style of the banks. Nevertheless, the fundamental aspects of banking i.e. trust and the confidence of the people on the institution remain the same. The majority of the banks are still successful in keeping with the confidence of the shareholders as well as other stakeholders. However, with the changing dynamics of banking business brings new kind of risk exposure. In this paper an attempt has been made to identify the general sentiments, challenges and opportunities for the Indian Banking Industry. This article is divided in three parts. First part includes the introduction and general scenario of Indian banking industry. The second part discusses the various challenges and opportunities faced by Indian banking industry. Third part concludes that urgent emphasis is required on the Indian banking product and marketing strategies in order to get sustainable competitive edge over the intense competition from national and global banks. This article is a small seed to existing branch of knowledge in banking industry and is useful for bankers, strategist, policy makers and researchers.

INTRODUCTION
In recent time, we has witnessed that the World Economy is passing through some intricate circumstances as bank’s financial & banking institutions, debt crisis in major economies of the world and euro zone crisis. The scenario has become very uncertain causing recession in major economies like US and Europe. This poses some serious questions about the survival, growth and maintaining the sustainable development. However, amidst all this turmoil India’s Banking Industry has been amongst the few to maintain resilience. The tempo of development for the Indian banking industry has been remarkable over the past decade. It is evident from the higher pace of credit expansion, expanding profitability and productivity similar to banks in developed markets, lower incidence of non-performing assets and focus on financial inclusion have contributed to making Indian banking vibrant and strong. Indian banks have begun to revise their growth approach and re-evaluate the prospects on how to keep the economy moving. In this paper an attempt has been made to review various challenges which are likely to be faced by Indian banking industry

2. HISTORICAL BACKGROUND
Bank of Hindustan was set up in 1870; it was the oldest Indian Bank. Later, three presidency banks under Presidency Bank’s act 1876 i.e. Bank of Calcutta, Bank of Bombay and Bank of Madras were set up, which laid foundation for modern banking in India. In 1912, all presidency banks were amalgamated to form the Imperial Bank of India. Imperial bank carried out limited number of central banking functions prior to establishment of RBI. It engaged in all types of commercial banking business except dealing in foreign exchange. Reserve Bank of India Act was passed in 1934 & Reserve Bank of India (RBI) was constituted as an apex body without major government ownership. Banking Regulations Act was passed in 1949. This regulation brought RBI under government control. Under the act, RBI got wide ranging powers for supervision & control of banks. The Act also provided that no new bank or branch of an existing bank could be opened without a license from the RBI, and no two banks could have common directors. Dr. K.A. Goyal & Vijay Joshi International Journal of Business Research and Management (IJBRM) Volume (3) : Issue (1) : 2012 20 By the 1960s, the Indian banking industry had become an important tool to facilitate the speed of development of the Indian economy. The Government of India issued an ordinance and nationalised the 14 largest commercial banks with effect from the midnight of July 1, 1969. A second dose of nationalization of 6 more commercial banks followed in 1980. The stated reason for the nationalization was to give the government more control of credit delivery. With the second dose of nationalization, the Government of India controlled around 91% of the banking business of India. Later on, in the year 1993, the government merged New Bank of India with Punjab National Bank. It was a compulsory merger between nationalized banks and resulted in the reduction of the number of nationalised banks from 20 to 19. After this, until the 1990s, the nationalised banks grew at a pace of around 4%, closer to the average growth rate of the Indian economy. In the early 1990s, the then Narasimha Rao government embarked on a policy of liberalization, licensing a small number of private banks. The next stage for the Indian banking has been set up with the proposed relaxation in the norms for Foreign Direct Investment, where all Foreign Investors in banks may be given of knowledge in banking industry and is useful for bankers, strategist, policy makers and researchers.

KEYWORDS : Rural Market, Risk Management, Global Banking, Employee and Customer Retention.


voting rights which could exceed the present cap of 10%, at present it has gone up to 74% with some restrictions. The new policy shook the Banking sector in India completely. Bankers, till this time, were used to the 4-6-4 method (Borrow at 4%; Lend at 6% Given at 4%) of functioning. The new wave ushered in a modern outlook and tech-savvy methods of working for traditional banks. All this led to the retail boom in India. People not just demanded more from their banks but also received more.

4. competition FACED BY INDIAN BANKING INDUSTRY

Developing countries like India, still has a huge number of people who do not have access to banking services due to scattered and fragmented locations. But if we talk about those people who are availing banking services, their expectations are raising as the level of services are increasing due to the emergence of Information Technology and competition. Since, foreign banks are playing in Indian market, the number of services offered has increased and banks have laid emphasis on meeting the customer expectations. Now, the existing situation has created various challenges and opportunity for Indian Commercial Banks. In order to encounter the general scenario of banking industry we need to understand the challenges and opportunities lying with banking industry of India.

4.1 Rural Market

Banking in India is generally fairly mature in terms of supply, product range and reach, even though reach in rural India still remains a challenge for the private sector and foreign banks. In terms of quality of assets and capital adequacy, Indian banks are considered to have clean, strong and transparent balance sheets relative to other banks in comparable economies in its region. Consequently, we have seen some examples of organic growth strategy adopted by some nationalised and private sector banks to face upcoming challenges in banking industry of India. For example recently, ICICI Bank Ltd. merged the Bank of Rajasthan Ltd. in order to increase its reach in rural market and market share significantly. State Bank of India (SBI), the largest public sector bank in India has also adopted the same strategy to retain its position. It is in the process of acquiring its associates. Recently, SBI has merged State Bank of Indore in 2010.

4.2 Management of Risks

The growing competition increases the competitiveness among banks. But, existing global banking scenario is seriously posing threats for Indian banking industry. We have already witnessed the bankruptcy of some foreign banks. According to Shrieves (1992), there is a positive association between changes in risk and capital ratio. Research studied the large sample of banks and results reveal that regulation was partially effective during the period covered. Moreover, it was concluded that changes in bank capital over the period studied was risk-based [1]. Wolfast, (2001) studied the Merger and acquisition activity among financial institutions in the USA and found that mergers and acquisitions added to the balance sheets a plethora of information on the maturity profiles of assets and liabilities, lending to sensitive sectors, movements in NPAs, capital provisions, shareholdings of the government, value of investment in India and abroad, operating and profitability indicators of the banks. They concluded that the total investments made in the equity share, units of mutual funds, bonds, debentures, aggregate advances against shares and so on.

4.3 Growth of Banking

The author focused bank supervisory agencies to select a stage of mergers, risk management, financial system stability and market liquidity. The study concluded that large institutions are able to maintain a superior level of risk management [2]. Al-Tamimi and Al-Mazrooei (2007) examined the risk management practices and techniques in dealing with different types of risk. Moreover, they compared risk management practices between the two sets of banks. The study found that the most important types of risk are commercial banks for their exchange risks followed by credit risk, and operating risk [3]. Singh and Jayadev (2009) used selected accounting ratios as risk management variables and attempted to gauge the overall risk management capability of banks. They used multivariate statistical techniques to summarize these accounting ratios. Moreover, the paper also analyzed the impact of these risk management variables on stock returns through cross-sectional analysis. Researchers found that Indian banks' risk management capabilities have been improving over time. Returns on the banks' stocks appeared to be sensitive to risk management capability of banks. The study suggest that banks want to enhance shareholder wealth will have to focus on successfully managing various risks.

4.4 Market Discipline and Transparency

Envelopment Analysis (DEA)-based Malmquist Total Factor Productivity (TFP) index. The empirical study indicated that, after an initial adjustment phase, the Indian banking industry experienced sustained productivity growth, which was driven mainly by technological progress. Banks’ ownership structure does not seem to matter as much as increased competition in TFP growth. Foreign banks appear to have acted as technological innovators when competition increased, which added to the competitive pressure in the banking market. Finally our results also indicate an increase in risk-taking behaviour, along with the whole deregulation process [5]. It was found in the study of Goyal and Joshi (2011a) that small and local banks face difficulty in bearing the impact of global economy therefore, they need support and it is one of the reasons for merger. Some private banks used mergers as a strategic tool for expanding their horizons. There is huge potential in rural markets of India, which is not yet explored by the major banks. Therefore ICICI Bank Ltd. has used mergers as their expansion strategy in rural market. They are successful in making their presence in rural India and strengthens their network across geographical boundary, improves customer base and market share [6].

4.5 Global Banking

It is practically and fundamentally impossible for any nation to exclude itself from world economy. Therefore, for sustainable development, one has to adopt integration process in the form of liberalization and globalization as India's export of red carpet for foreign firms in 1991. The impact of globalization becomes more and more felt in the banking sector and represents a major challenge for banks to compete with global players. If we look at the Indian Banking Industry, then we find that there are 36 foreign banks operating in India, which becomes a major challenge for Nationalized and private sector banks. The number of foreign banks is increasing and they are technologically advanced and having presence in global market, which gives more and better options and services to Indian traders.

4.6 Financial Inclusion

Financial inclusion has become a necessity in today's business environment. Whatever is produced by business houses, that has to be under the check from various perspectives like environmental concerns, corporate governance, social and ethical issues. Apart from it to bridge the gap between rich and poor, the poor people of the country should be given proper attention to improve their economic condition. Dev (2006) stated that financial inclusion is significant from the point of view of living conditions of poor people, farmers, rural non-farm enterprises and other vulnerable groups. Financial inclusion, in terms of access to credit from formal institutions to various social groups. Apart from formal banking institutions, which should look at inclusion both as a business opportunity and social responsibility, the author concludes that role of the self-help group movement and microfinance institutions is important to improve financial inclusion. The study suggests that through regression analysis and Envelopment Analysis (DEA)-based Malmquist Total Factor Productivity (TFP) index. The empirical study indicated that, after an initial adjustment phase, the Indian banking industry experienced sustained productivity growth, which was driven mainly by technological progress. Banks’ ownership structure does not seem to matter as much as increased competition in TFP growth. Foreign banks appear to have acted as technological innovators when competition increased, which added to the competitive pressure in the banking market. Finally our results also indicate an increase in risk-taking behaviour, along with the whole deregulation process [5]. It was found in the study of Goyal and Joshi (2011a) that small and local banks face difficulty in bearing the impact of global economy therefore, they need support and it is one of the reasons for merger. Some private banks used mergers as a strategic tool for expanding their horizons. There is huge potential in rural markets of India, which is not yet explored by the major banks. Therefore ICICI Bank Ltd. has used mergers as their expansion strategy in rural market. They are successful in making their presence in rural India and strengthens their network across geographical boundary, improves customer base and market share [6].

4.7 Employees’ Retention

The banking industry has transformed rapidly in the last ten years, shifting from transactional and customer service-orientated to an increasingly aggressive environment, where competition for revenue is on top priority. Long-time banking industry and are often resistant to perform up to new expectations. The
intergroup conflicts, which all fall under the category of ‘cul
culation problems, human resources problems, ego clashes, and
retention, employees point to issues such as identity, communi-
Each organization has its own unique culture and most often,
biggest challenge for organizations is that when new employees
ny prestige, training, financial compensation and benefits and
nine basic parameters like career and personal growth, compa-
ments spend large amounts of time, effort, and money trying
to invest their money only in endeavours that promote the
community, providing opportunities to the disadvantaged, and sup-
As “banks with a conscience”. They focus on investing in com-
and ethically oriented organization by disbursement of loans
Diminishing employee morale results in decreased revenue. Due
to the intrinsically close ties between staff and clients, losing
to customer service representatives because competition is
always moving in to hire them away. The competition to retain
key employees is intense. Top-level executives and HR depart-
ments spend large amounts of time, effort, and money trying
to figure out how to keep their people from leaving. Sekaran,
U. (1989) studied a sample of 246 bank employees, this study
traced the paths to the job satisfaction of employees at the
workplace through the quality of life factors of job involvement
and sense of competence. Results indicated that personal, job,
and organizational climate factors influenced the ego invest-
ment or job involvement of people in their jobs, which in turn
influenced the intra-psychic reward of sense of competence that
they experienced, which then directly influenced employees’ job
serted in their study that people often leave for reasons unrele-
ted to their jobs. In many cases, unexpected events or shocks
are the cause. Employees also often stay because of attachments
and their sense of fit, both on the job and in their community
[12]. Saxena and Monika (2010) studied a case of 5 companies
out of 1000 organizations and 8752 respondents surveyed
across 800 cities in India by Business Today. The survey was on
nine basic parameters like career and personal growth, compa-
nym prestige, training, financial compensation and benefits and
most often, when brought together, these cultures clash. When there is no
retention, employees point to issues such as identity, communi-
cation problems, human resources problems, ego clashes, and
intergroup conflicts, which all fall under the category of ‘cul-
tural differences’ [13].

4.8 Social and Ethical Aspects

There are some banks, which proactively undertake the respon-
ibility to bear the social and ethical aspects of banking. This is
a challenge for commercial banks to consider the these aspects
in their working. Apart from profit maximization, commercial
banks are supposed to support those organizations which have
some social concerns. Benedikter (2011) defines Social Banks as
“banks with a conscience”. They focus on investing in com-
unity, providing opportunities to the disadvantaged, and sup-
porting social, environmental and ethical agendas. Social banks
try to invest their money only in endeavours that promote the
greater good of society, instead of those, which generate private
profit just for a few. He has also explained the main difference
between mainstream banks and social banks that mainstream
banks are in most cases focused solely on the principle of profit
maximization whereas, social banking implements the triple
principle of profit-people-planet [18]. Goyal and Joshi (2011b)
have concluded in their study on social and ethical aspects of
Banking Industry that Banks can project themselves as a social-
ly and ethically oriented organization by disbursement of loans
merely to those organizations, which has social, ethical and en-
vironmental concerns [19].

5. CONCLUSION

Over the years, it has been observed that clouds of trepidation and
drops of growth are two important phenomena of market,
which frequently changes in different sets of conditions. The pre
and post liberalization era has witnessed various environmen-
tal changes which directly affects the aforesaid phenomena. It
is evident that post liberalization era has spread new colors of
growth in India, but simultaneously it has also posed some chal-
enges. This article discusses the various challenges and oppor-
tunities like rural market, transparency, customer expectations,
management of risks, growth in banking sector, human factor,
global banking, environmental concern, social, ethical issues,
estate and customer retentions. Banks are striving to com-
bat the competition. The competition from global banks and
technological innovation has compelled the banks to rethink
their policies and strategies.

6. SUGGESTIONS

As per the above discussion, we can say that the biggest chal-
lenge for banking industry to serve the mass market of India.
Companies have shifted their focus from product to customer.
The better we understand our customers, the more successful
we will be in meeting their needs. In order to mitigate above
mentioned challenges Indian banks must cut their cost of their
services. Another aspect to encounter the challenges is product
differentiation. Apart from traditional banking services, Indian
banks must adopt some product innovation so that they can
compete in gamut of competition. Technology upgradation is an
inherent advantage to face challenges. The level of consumer
awareness is significantly higher as compared to previous
years. Now-a-days they need internet banking, mobile banking
and ATM services. Expansion of branch size in order to increase
market share is another tool to combat competitors. Therefore,
Indian nationalized and private sector banks must spread their
wings towards global markets as some of them have already
done it. Indian banks are trustworthy brands in Indian market;
therefore, these banks must utilize their brand equity as it is an
valuable asset for them.

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