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DIVERSIFICATION AND BRAND INDIA: DOES BANKS HAVE ANY ROLE?

KEY WORDS: Brand India, Diversification, ROA, ROE, SHROA & SHROE

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ABSTRACT

Banks in India, to a large extent, has become functionally dynamic and operationally efficient. One of the important developments one can witness in the sector is the growing scale of diversification of revenue earning sources. In this paper an attempt has been made to identify the diversifying role of the banks i.e. commercial banks in creating Brand India and to measure the degree and impact of Income Diversification on banks performance and on Brand India. Results indicate that banks are playing a very vital role in creating a better image of the country i.e. Brand India. by way of developing a better relations with investors, acting as a middleman for the country for creating a brand value etc. and at the same time income diversification is also found to be positively correlated with returns and also have significant positive impact on returns.

Introduction:

Being one of the fastest growing economies in the world, the Indian economy is at the centre stage of the changing economic order in the world. A nation of over 1.2 billion people with a median age of 24 years, Brand India today is very relevant for the growth of global economy. In marketing the term 'Brand' is defined as the term, symbol, word or picture given to the product to distinguish it from the other producers and to help the customers to identify it. Brand is essentially a seller's promise to consistently deliver a specific set of features, benefits, and servicers to the buyers. In case of "Brand India" the entire country i.e. India is defined as or considered as a brand which has been given a name, term, symbol or picture such as "Make in India" a name or term and the symbol of lion as a picture and investors (both domestic and foreign) is considered as a customer. In order to developed any country we need money, cash or finance and these are mainly come from the financial intuitions i.e. banks. Bank is something which is considered as a backbone any financial system, specially a country like India where bank has developed a huge network by spreading itself in all around the country through its branches. If the banking system of the country collapse the image i.e. Brand Image of the will also collapse, the trust of the customers, investors and stakeholders will also collapse. In the year 2009 when recession hit India, it has been found that most of the countries of the word have suffered in a worst from the recession but India has not suffered much as compare to other countries of the world. The one of the main reason was the strong structure of the Indian banking system; it is the banking system which enables the country like India to recover from the shock of recession and gave the opportunity to the other sectors of the economy to recover from the recession loss also such as tourism, trade, textile, IT etc. in short we can say that n order to a country as brand we need the support of our banking system. The Indian banking sector has undergone rapid transformations following the waves of reforms mainly in post 1990s. The overall orientation of the banks has changed enormously due to technological up gradation, competition and liberalization. As a consequent factor, like many countries of the world, there has been an increased trend towards Income and Geographical diversification. That is, the banks are steadily shifting away from its traditional loan making activities that generate interest income to certain diversified activities that generate non-interest income in the form of fees, commission etc. This increased reliance on non-traditional or non-interest making activities are expected to yield the potential diversification benefits in the sense that it can stabilize the earnings of a bank by reducing the cyclical variations of bank's earnings and create resilience to counter adverse shocks affecting revenue and profits. Geographical diversification is simply defined as expanding the customer reaching capacity of the banks by setting up branches in all parts of the economy. Geographical diversification is laid on the fundamental argument that banks should concentrate only on those areas/regions in which it has its inceptions by creating awareness among the customers of that particular regions about their products and services. The Reserve bank of India has made some guidelines regarding the opening of a new bank branch in Rural, Urban, Semi-urban and Metropolitan region of the country which will be extremely helpful in the process of creating a Brand India

CONCEPTUAL FRAMEWORK:

Brand India

Brand India can simply may be defined as process to attract business. Just like in marketing certain strategies have been developed to attract customers to purchase and use the product similarly in case of Brand India also certain strategies and concepts has been developed to attract the customers, here the customers are the domestic and global investors to make investment in the field of service sector, manufacturing, information technology, infrastructure, information technology enabled services, etc. the main strategy behind this concept is to present India a huge market of product and services and a heaven like destination for investment in different sectors. Few intuitions/organizations such as India Brand Equity Foundation (IBEF), a Public-private partnership between the Ministry of Commerce and Industry, Government of India, and the Confederation of Indian Industry and soon have also involved themselves in the process of developing the country India as a Brand India. Our honorable Prime Minister Shri Narendra Modi ji have also gave some outline in creating the country India as a Brand India. He said to build "Brand India" should focus on 5-Ts - Talent, Tradition, Tourism, Trade And Technology and he also said that his Govt. will apply the "good governance" model which worked on a seven-point "rainbow" principle - focus on India's culture, agriculture, women, natural resources (water, land and forests and environment), youth power, democracy and knowledge

Diversification:

Conceptually, diversification is a business strategy which allows an entity to enter into new field of business with diversified products and services with the underlying objective of reducing risk and improving returns. If implemented successfully, such a strategy is expected to act as a cushion to protect the organization from any uncertainty affecting the main line of business. The entire strategy of diversification is based on the conventional wisdom of not to put all eggs in the same basket. Diversification is also recognized as a competitive strategy for banking businesses across the world. There are a good number of ways in which a particular bank can diversify its operation. The most popular among them is Income and Geographical Diversification. Income diversification is defined as diversifying its streams of income mainly by increasing the proportion of Non-Interest Income to the Total Operating Income thereby increasing the contribution of non-interest earning sources of income. Interest received or earned by way of providing different services such as merchant banking services, consultancy services, insurance services can be defined as non-interest income whereas income earned by way of lending loans both short term and long term can be defined as interest income. Another way of diversification is expanding its customers reaching capacity to all parts of the economy by way of branch expansion. This is referred to as Geographical Diversification; it can simply be defined as an expansion of customer reaching capacity of the banks by spreading or setting up its branches in different parts of the country. Historically, regulations have restricted the banking activities leaving a very little scope for diversification. In the era of deregulation, disintermediation coupled with technological change and recurrent bank consolidation, diversification was felt to be the need of the hour. Consequently, banks all over the world are now venturing into new areas and horizons distinct from its traditional banking activities to include all those activities which allow banks to earn non-interest income.

REVIEW OF LITERATURE:

Brand India today is today become very relevant for the growth of global economy. India has emerged as one of the decisive nations shaping the contours of the world economy. Today, the triumph of Brand India is visible in almost all fields and sectors both in the domestic and overseas markets. Following are the list of some literature related to brand India and diversification of banking activities:

Ramalingam(2006) said that India has a great potential in creating a better brand value for the country. Brand India is visible in almost all fields and sectors both in the domestic and overseas markets. Saxena(2012) found that Brand is the biggest asset of any company. A global brand should provide relevant meaning and experience to people across multiple societies. The perception of quality that is associated with the global brands is difficult to unlock but it's easier to create a blue ocean of opportunities for Indian brands. Kesari & Srivastava (2012) made an attempt to investigate the luxury consumer behavior, with reference to shopping. They found increasing globalization is reducing the homogeneity of consumer behaviors within countries. Stiroh (2002) found U.S. banking industry is steadily increasing its reliance on non-traditional business activities that generate fee income, trading revenue and other types of noninterest income. Greater reliance on noninterest income, particularly trading revenue is associated with higher risk. Similar study has been conducted by D'Souza and Lai (2004) where they made an attempt to measure the effects of diversification on risk and returns and on bank efficiency in Canada during the period of 1997-2003. They found, so far as returns are concerned, returns are not as high as compared to the risk taken by the banks. Efficiency of the banks have not improved as compared to the amount of risk taken by the banks but it has been found that a merger between banks with different business lines having some similarities in the composition of their portfolio can result in improving efficiency of the banks. Lepetit et al (2005) conducted a study in 14 European countries and they found, the banks which have expanded into non-interest income activities has taken a higher level of risks as compared to the banks which are dealing in traditional activities. A closer investigation revealed that risk is positively correlated with the share of fee based activities but not with trading activities. Another study by Templeto & Severien (1992) in USA contradicts the above findings. Their study revealed that banks which expanded its financial services such as underwriting and insurance were in better position to reduce its overall risk. Odesanmi and Wolfe (2007) investigated the impact of revenue diversification on insolvency risk, using a panel dataset of 322 listed banks across 22 countries including India. They found that diversification across the country both interest and non-interest income helps in generating revenue and decreases insolvency risk, this is because a large number of banks in emerging economies are in a better position to exploit the diversification opportunity. A cross country comparison was undertaken by Choi and Kotrozo (2006) to examine the effects of diversification on risk and performance by examining the effects of both activity and geographical diversification. They found benefits arising from activity diversification are highly associated with the risk taking capacity of banks. A different study in terms of country wise comparison has been conducted out by Berger, Hasan, and Zhou (2010) in China investigating the effects of product and geographical diversification strategies on performance of banks, using a sample of 88 Chinese banks during 1996-2006.They found that all four dimensions of diversification (loans, deposits, assets, and geography) are associated with reduced profits and higher costs. Furthermore, they observed that banks with foreign ownership (both majority and minority ownership) and banks with conglomerated affiliation are associated with lesser benefits of diversification, suggesting that foreign ownership and conglomerate affiliation play an important role in the area of diversification. Acharya, Hasan, and Saunders (2004) in Italy studied the effect of focus (specialization) Vs. diversification on the return and the risk of banks. They found both industrial and sectoral loan diversification reduce bank return while endogenously producing riskier loans. In addition to that Turkmen and Yigit (2012) also examined the effect of sectoral diversification on the performance of Turkish banks. They found sectoral diversification has made no impact on improving bank performance because of which a negative relationship between sectoral diversification and bank performance was noticed. As credit has been spread in different sectors of the economy such as Food, Beverage and Tobacco, Construction, Metal and Crude mine, Financial Institutions, and Textile products the expenses of the banks have increased, at the same time Return on Equity have decreased.

Though there are good number of studies on diversification concerning different countries, but there exist scanty of literature pertaining to Indian banking sector over this issue. There is a need to study how diversification of revenue deliver benefits for banks and make them resilient to adverse effects on income and bank earnings shocks in India. However, Ramasastri, Samuel and Gangadaran (2004) made an attempt in India to examine whether Non-interest Income of the bank has helped in stabilizing the total income i.e. operating revenue of the schedule commercial banks during the period of 1997-2003. At the aggregate level they found that Interest Income of the banks is more stable than Non-interest Income. Further it was identified that in case of State Bank of India, Foreign banks and old private sector banks non-interest income helped stabilize operating income. However in case of nationalized banks and new private sector banks the results were opposite.

METHODOLOGY:

On the basis of the literature reviewed, it is found that very few studies have been conducted in Brand India and diversifying role of banks in creating brand India. The present paper has been divided into three sections, first section deals with identifying the role of the banks in creating Brand India and second section deals with measuring the degree of Income Diversification of banks in India and comparing the same between public and private sector banks operating in India and the third section is devoted to measuring the impact of Income Diversification on banks' risk and returns.

Research objective:

The major objectives of this paper are:

1. To identify the diversifying role of the banks i.e. commercial banks in creating Brand India.
2. To measure the degree of Income Diversification on banks performance and on Brand India
3. To measure the impact of Income Diversification on banks performance and on Brand India

Further in order to measure the impact of diversification on banks Risk and Returns following hypotheses have been formulated

H1: Income Diversification has no significant impact on Return on assets (ROA) of the Banks.

H2: Income Diversification has no significant impact on Return on Equity (ROE) of the Banks.

H3: Income Diversification has no significant impact on Risk Adjusted Return on assets (SHROA) of the Banks.

H4: Income Diversification has no significant impact on Risk Adjusted Return on Equity (SHROE) of the Banks.

Data

All bank level data in the study has been obtained mainly from the Reserve Bank of India publications, i.e., Report on Trends and Progress of Banks in India, Statistical Tables Relating to Banks in India etc. The study period cover the period of 20 years starting from 1/4/1995 to 31/03/2014 covering 40 commercial banks

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including 25 public sector banks and 15 Indian private sector banks are taken into consideration.

Income Diversification Index:
Diversification(Income): Sum of squared Income (Interest income and Non-interest income) share will be subtracted from one(1).

$$\mathrm{DIV-ICMj} = 1 - \left\{ \sum_{i=1}^{2} \mathrm{Pi}^2 \right\}$$

Where, DIV-ICM = Diversification of Income, "j" stands for bank, i.e. (j= 1,2,3,…..,40) and "i" indicates the category of income i.e.(I= 1&2).

$$\mathrm{P1} = \left(\frac{NET}{NOR}\right) \quad \& \quad \mathrm{P2} = \left(\frac{NON}{NOR}\right)$$

NET = Net- Interest income,
NON = Non-Interest income and
NOR = It is the sum of Net-interest income and Non-interest income (NOR= NET+NON).

Diversification variables measure the degree of bank diversif ication. A higher value indicates a more diversified mix. The value 0 means a complete concentration (the bank is specialized in one area), while 1 means a complete diversification.

Financial Performance Measures:

Return on Assets (ROA): $= \dfrac{\text{NET PROFIT AFTER TAX}}{\text{TOTAL ASSETS}}$

Return on Equity (ROE): $= \dfrac{\text{NET PROFIT AFTER TAX}}{\text{TOTAL EQUITY}}$

SHROAi,t = $\dfrac{ROA\ j,t}{\sigma \mathrm{ROA\ j,t}}$

Where, SHROAj,t indicates risk adjusted returns of the bank. ROA j,t= Return on Assets for "j" bank in the year "t".σROA j,t represents the Standard Deviation of Return on Assets for the "j" bank in the year "t".

SHROEi,t = $\dfrac{ROE\ j,t}{\sigma \mathrm{ROE\ j,t}}$

Where, SHROEj,t indicates risk adjusted returns of the bank. ROE j,t= Return on Equity for "j" bank in the year "t".σROE j,t = Standard Deviation of Return on Equity for the "j" bank in the year "t".

Impact of Income Diversification on the Risk & Returns:
To examine the impact of diversification on bank's risk and returns a panel data regression model has been used:

To examine the impact of diversification on bank's risk and returns a panel data regression model has been used:

$$\mathrm{ROA}_{i,t} = \alpha_{i.t} + \beta_1(\mathrm{DI}_{,t}) + \beta_2(\mathrm{SIZE}_{i,t}) + \beta_3(\mathrm{LEV}_{i,t}) + \sum_{k=1}^{2}(\beta_k\ \lambda_{i,t}) + \sum_{s=1}^{20}(\beta_s\ ™_{i,t}) + \epsilon_{i,t}$$

$$\mathrm{ROE}_{i,t} = \alpha_{i.t} + \beta_1(\mathrm{DI}_{,t}) + \beta_2(\mathrm{SIZE}_{i,t}) + \beta_3(\mathrm{LEV}_{i,t}) + \sum_{k=1}^{2}(\beta_k\ \lambda_{i,t}) + \sum_{s=1}^{20}(\beta_s\ ™_{i,t}) + \epsilon_{i,t}$$

$$\mathrm{SHROA}_{it} = \alpha_{i.t} + \beta_1(\mathrm{DI}_{,t}) + \beta_2(\mathrm{SIZE}_{i,t}) + \beta_3(\mathrm{LEV}_{i,t}) + \sum_{k=1}^{2}(\beta_k\ \lambda_{i,t}) + \sum_{s=1}^{20}(\beta_s\ ™_{i,t}) + \epsilon_{i,t}$$

$$\mathrm{SHROE}_{i,t|} = \alpha_{i.t} + \beta_1(\mathrm{DI}_{,t}) + \beta_2(\mathrm{SIZE}_{i,t}) + \beta_3(\mathrm{LEV}_{i,t}) + \sum_{k=1}^{2}(\beta_k\ \lambda_{i,t}) + \sum_{s=1}^{20}(\beta_s\ ™_{i,t}) + \epsilon_{i,t}$$

Where, ROA indicates the Return on Assets, ROE is the Return on Equity, SHROA is the Risk Adjusted Return on Assets, SHROE is the risk Adjusted Return on Equity and i identifies the two categories of bank (i= 1 & 2), t expresses the time variable (t = 1994-95,…, 2013-14);); β_s are the parameters to be estimated, ™ & λ is a matrix of control variables i.e. time and bank. α represents the constant term and represents the error term of the model.

ROLE OF BANKS IN CREATING BRAND INDIA:
Banks is considered as a backbone in any financial system of the country. If the banking system of the country collapses the entire structure will collapse and it will make a very bad impact in the image of the country. In this segment of the paper an attempt has been made to identify the factors which directly or indirectly made impact in creating a band Image of the country i.e. Brand India.

1. Direct Relation with Image of the Country: Every bank has direct relation in creating the image of the country. Bank act as major pillar of the entire financial structure of the country, if the banking system of the entire collapse the entire image of the country will also collapse which will directly made impact in the creating the brand value for the country.

2. Connection With All The Sectors Of The Economy: Bank has direct connection with all the sectors of the economy such as tourism, education, information and technology and soon. Banks provide funds to all these sectors in the form of Loan and advances, investment in a particular project, CSR investment etc. which help these institutions to run in a proper manner and which ultimately help these institutions to work in a proper manner and create a better image for themselves and for the country.

3. Correlation with Investors: if banks of the country developed a better correlation with the domestic and foreign investors, it makes easy for investors to make investment n a particular project or area, which ultimately create a better image of the country among investors.

4. Provide Funds for Research and Development: A country has always been identified for its uniqueness or specialization in a particular area or field. China has developed a good image of a big electronic manufacturing hub and all these are possible through research and development. And to carry out these research and development every individual, organization or institution needs funds and funds are provided by the banks, which eventually helps the country in creating a brand value for the country.

5. Act as a Middleman in Creating A Brand: when a new product is lunched, the middleman face a lot of difficulties to convince the seller about the product. Similarly, in case of a country also if the banks have able to develop a good image outside of the country it will ultimately helps the country (India) to convince the other country about their brand value.

6. Utility services: Banks provides large number utility services to its customers i.e. investors such as merchant banking and investment banking services, underwriting services, factoring and forfeiting etc. which enables the investors to carry out its transactions in a proper manner with its trading partner. This creates a good brand value not only for the bank but also for the country.

7. Helps in Decision making: Decision to make investment in a particular area/project is largely depends the condition of fund availability to the organization. If banks provide attractive services in the form of making loans and advances to its customers i.e. investors it eventually leads to the formation of a good image of bank as well as the country.

EMPIRICAL RESULTS:

Figure: 1
Trend in Income Diversification Index of Public, Private and All Commercial Banks from 1995-2014

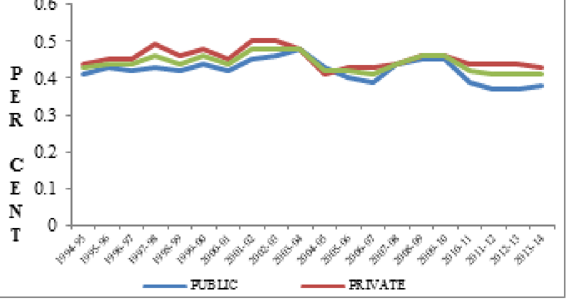

Figure 1 depicts the trend in Income Diversification Index of Public, Private & All Commercial Banks taken together from 1994-2014. Before the year 2003-2004 both Public and Private Sector banks and so as all the commercial banks taken together reflected a mixed trend. Thereafter a fall is registered for both the bank type. But the fall continued for a longer period for Public Sector Banks. From the mid of 2006-07 all the banks registered increase in Diversification Index. Again a declining trend is observed from mid of 2010 onwards. The decline is sharper for Public Sector Banks than Private Sector Banks. In almost all the years the DI is higher for Private Banks than the Public Sector Banks. An important observation that follows from the figure is that both the categories of bank behave in a similar fashion with regards to income diversification. The recessionary period is characterized by an increasing trend in DIV-ICM, this reveals the efforts on the part of Indian banks to neutralize the anticipated loss from normal earning sources by resorting to non-interest earning sources.

In order to identify the manner in which Diversification impacts bank performance it is first necessary to identify the relationship between the dependent and explanatory variables. The dependent variable so selected is ROA, ROE, Risk Adjusted ROA(SHROA), Risk Adjusted ROE(SHROE). The explanatory variables are Income Diversification Index (DIV-ICM), Size of the banks i.e. log of total Assets (SIZE), Leverage Ratio (LEV) taken as a proxy for leverage i.e. the fragility or sensitivity of a bank. Table 1 represents the results of Correlation Analysis between these variables. The results indicate a positive correlation between Income Diversification and return of the banks. And there also exists a negative correlation between Size and Income Diversification of the banks, it means with the increase in the size of the bank the income diversification does not increases.

Table: 1 Correlation Matrix between Dependent and Explanatory Variables

N=40	ROA	ROE	SHROA	SHROE	DIV-ICM	SIZE	LEV
ROA	1	.676**	.945**	.687**	.530**	-0.061	0.089
ROE	.676**	1	.612**	.972**	.508**	-0.059	-0.265
SHROA	.945**	.612**	1	.644**	.457**	-0.024	0.121
SHROE	.687**	.972**	.644**	1	.541**	0.003	-0.181
DIV-ICM	.530**	.508**	.457**	.541**	1	-.547**	-.403*
SIZE	-0.061	-0.059	-0.024	0.003	-.547**	1	.831**
LEV	0.089	-0.265	0.121	-0.181	-.403*	.831**	1

**- significant at 0.01 per cent level of significant & *. Correlation is significant at the 0.05 level.
Note: ROA= Return on Assets, ROE= Return on Equity, SHROA= Risk Adjusted Return on Assets, SHROE= Risk Adjusted Return on Equity, DIV-ICM= Income diversification Index, SIZE= Log of total Assets & LEV= Equity/TA i.e. Leverage.

Source: Computed using SPSS 16, www.rbi.org.in

Table: 2 reports the results of regression, it can be seen that diversification index (both Income) has a positive coefficient in all the cases. Thus, it indicates that diversification has a positive impact on all types of returns of the banks. This is also found to be statistically significant in all the cases. Similarly SIZE also bears the positive relationship with all types of returns as indicated by the positive coefficients and it was also found statistically significant for SHRAO and SHROE but not for ROA and ROE. Thus, it can be sated that large sized banks have a greater positive impact on all the types of returns. The coefficient of LEV indicates a negative impact on ROA, ROE, SHROA & SHROE. This relation is found to be statistically significant only in case of ROE & SHROE. This indicates that with the increase in the proportion of Equity to Total Assets of the banks, the returns declines. Public sector banks have lesser ROA, ROE, SHROA & SHROE. The variable YEAR also represents negative impact in all types of returns of the banks but it was found statistically insignificant. On the basis of the results so obtained it can be said that income diversification has a significant positive impact on the Return on assets (ROA), Return on equity (ROE), Risk adjusted ROA (SHROA) & Risk Adjusted ROE (SHROE). *Hence, the null hypotheses i.e. the diversification (income) has no significant impact on ROA, ROE, SHROA, SHROE have been rejected*.

Table: 2 Regression Results

Regressors	Return on Assets(ROA)		Return on Equity(ROE)		Risk Adjusted ROA(SHROA)		Risk Adjusted ROE(SHROE)	
	Coef. (Std. Err.)	Sig.	Coef. (Std. Err.)	Sig.	Coef. (Std. Err.)	Sig	Coef. (Std. Err.)	Sig
DIV-ICM (Income Diversification Index)	4.919 (1.106)	0.000	0.911 (1.8583)	0.000	1.139 (.3001)	0.001	1.333 (.2376)	0.000
SIZE (log value of Total Assets)	0.155 (.0557)	0.009	2.824 (1.0199)	0.009	0.327 (.1647)	0.050	0.399 (.1304)	.0.005
LEV (Leverage Equity/TA)	-3.181 (2.0714)	0.135	1.764 (.37872)	0.000	5.178 (6.1160)	0.404	-0.200 (.4843)	0.000
BANK (Category of Bank i.e. Public & Private)	-0.385 (.0932)	0.000	-0.526 (1.7055)	0.760	-0.848 (.2754)	0.004	-0.091 (.2181)	0.678
YEAR (Time period 1995-2014)	-0.154 (.0837)	0.075	-3.168 (1.5304)	0.047	-0.353 (.2471)	0.162	-0.302 (.1957)	0.133
_Cons (Constant term)	-0.714 (1.5842)	0.655	0.769 (.2896)	0.012	-0.363 (.4677)	0.443	0.685 (.3704)	0.074
R^2	0.7616	0.6328	0.6399	0.6458				
Observations (Adj R^2)	0.7120	0.5617	0.5702	0.5772				
Prob > F	.0000	.0000	.0000	.0000				

Source: Statistical Table Related to Banks in India(www.rbi.org.in), Computed using STATA 11

CONCLUSION:

The study is primarily concerned with identifying the role diversification(income) in creating brand India and measuring the impact of diversification on bank's risk and returns. Bank is an important pillar of the financial system of the country so its play a very important role in creating the overall brand image of the country. The study reflects Income diversification has a positive impact on all types of returns of the banks and Size i.e. Total Assets of both categories of the banks also bears the positive relationship with all types of returns of the banks i.e. ROA, ROE, SHROA, & SHROE and diversification has some significant impact in all types of returns of the banks, hence our null hypotheses have been rejected. In the rapidly changing business environment within which a bank is to function requires it to orient itself to the changing needs. Diversification has become the need of the hour so in order to build good brand image a bank needs to utilize the option of diversification in banking to make our country a better place for business.

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