Banking Structure in India and Its Challenges

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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 faced by Indian banking industry.

Keywords: *Banking, Industry, India*

1.Introduction

In recent time, we has witnessed that the World Economy is passing through some intricate circumstances as bankruptcy of banking & financial 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, 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 hand to keep the economy rolling.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 of Banking Industry in India

The Indian banking industry has its foundations in the 18th century, and has had a varied evolutionary experience since then. The initial banks in India were primarily traders’ banks engaged only in financing activities. Banking industry in the pre-independence era developed with the Presidency Banks, which were transformed into the Imperial Bank of India and subsequently into the State Bank of India. The initial days of the industry saw a majority private ownership and a highly volatile work environment. Major strides towards public ownership and accountability were made with Nationalisation in 1969 and 1980 which transformed the face of banking in India. The industry in recent times has recognised the importance of private and foreign players in a competitive scenario and has moved towards greater liberalisation.

3. Banking Scenario in India

As per the Reserve Bank of India (RBI), India's banking sector is sufficiently capitalised and well-regulated. The financial and economic conditions in the country are far superior to any other country in the world. Credit, market and liquidity risk studies suggest that Indian banks are generally resilient and have with stood the global downturn well.

Indian banking industry has recently witnessed the roll out of innovative banking models like payments and small finance banks. RBI's new measures may go a long way in helping the restructuring of the domestic banking industry.

The digital payments system in India has evolved the most among 25 countries with India's Immediate Payment Service (IMPS) being the only system at level 5 in the Faster Payments Innovation Index (FPII).

4. Market Size

The Indian banking system consists of 27 public sector banks, 22 private sector banks, 44 foreign banks, 56 regional rural banks, 1,589 urban cooperative banks and 93,550 rural cooperative banks, in addition to cooperative credit institutions.

5. Banking Structure in India

Indian Banks are classified into commercial banks and Co-operative banks. Commercial banks comprise: (1) Schedule Commercial Banks (SCBs) and non-scheduled commercial banks. SCBs are further classified into private, public, foreign banks and Regional Rural Banks (RRBs); and (2) Co-operative banks which include urban and rural Co-operative banks.

6. Organisational Structure

Reserve Bank of India: Reserve Bank of India is the Central Bank of our country. It was established on 1st April 1935 accordance with the provisions of the Reserve Bank of India Act, 1934. It holds the apex position in the banking structure. RBI performs various developmental and promotional functions.

6.1 Commercial Banks

Commercial bank is an institution that accepts deposit, makes business loans and offer related services to various like accepting deposits and lending loans and advances to general customers and business man.These institutions run to make profit. They cater to the financial requirements of industries and various sectors like agriculture, rural development, etc. it is a profit making institution owned by government or private of both.Commercial bank includes public sector, private sector, foreign banks and regional rural banks.

6.2 Public Sector Banks

Currently there are 21 Nationalised banks in India. The public sector accounts for 75 percent of total banking business in India and State Bank of India is the largest commercial bank in terms of volume of all commercial banks.Now from April 1, 2017 all the 5 associate banks of SBI and Bhartiya Mahila Bank are merged with State Bank of India. After this merger now SBI is counted among the top 50 largest banks of the world.

6.3 Private Sector Banks

The private-sector banks in India represent part of the Indian banking sector that is made up of both private and public sector banks. The "private-sector banks" are banks where greater parts of stake or equity are held by the private shareholders and not by government.

6.4 Foreign Banks

A foreign bank with the obligation of following the regulations of both its home and its host countries. Loan limits for these banks are based on the capital of the parent bank, thus allowing foreign banks to provide more loans than other subsidiary banks. Foreign banks are those banks, which have their head offices abroad. CITI bank, HSBC, Standard Chartered etc. are the examples of foreign bank in India. Currently India has 36 foreign banks.

6.5 Regional Rural Bank (RRB)

The government of India set up Regional Rural Banks (RRBs) on October 2, 1975. The banks provide credit to the weaker sections of the rural areas, particularly the small and marginal farmers, agricultural labourers, and small entrepreneurs. There are 82 RRBs in the country. NABARD holds the apex position in the agricultural and rural development. List of some RRBs is given below:

6.6 Co-operative Bank

Co-operative bank was set up by passing a co-operative act in 1904. They are organised and managed on the principle of Co-operation and mutual help. The main objective of co-operative bank is to provide rural credit.

7. Issues and Challenges Faced By Indian Banking Industry

Amidst the signs of progress, the Indian banking sector has been facing multiple challenges in recent times. Few of them are -

7.1 Bad Loan

At nearly Rs10 lakh crore, India's pile of bad loans is bigger than the gross domestic products of at least 137 countries. But so far, the RBI's attempts to reduce Non-Performing Assets (NPAs) in the banking sector have yielded little result.

The share of gross NPAs in India could inch up to 10.2% by March 2018, from 9.6% in March 2017, according to the FSR. In September 2016, gross NPAs were at 9.2%.Currently, the worst-hit are the state-owned banks, which dominate the Indian banking system. In March 2017, the average bad loans of PSBs stood at 75% of their net worth. These bad loans are squeezing banks' profitability and capital positions, threatening the health of some of India's biggest banks. In the report, the RBI cautioned that the situation could get worse with any unforseen stress in the economy.

7.2 Cyber Threats

An estimated 95% of transactions in India are paid for in cash but with the growing penetration of computers and smartphones, and increasing access to the internet, Indians are taking to digital channels for their banking needs. Cybercrime is becoming a greater threat as a result.The FSR labeled cyber-attacks as a high-risk zone for India's banking sector. The RBI classifies bank fraud as transactions involving any cheating, negligence, misappropriation of funds, or forged documents.

7.3 Capital Adequacy

One way a bank tries to ensure it is protected from bad loans is by setting aside money as a 'provision'. This money cannot be used for any other purposes including lending. As a result, banks have lower capital available to use for its various operations. The Capital Adequacy Ratio measures how much capital a bank has. When this falls, the bank has to borrow money or use depositors' money to lend. This money, however, is riskier and costlier than the bank's own capital.

7.4 Unhedge Forex Exposure

"The wild gyrations in the forex market have the potential to inflict significant stress in the books of Indian companies who have heavily borrowed abroad," Mundra said in his speech. This stress can affect their ability to pay back debt to Indian banks. As a result, the RBI wants banks to ensure companies they lend to do not expose themselves to unnecessary debt in dollars.

7.5 Non Performing Assets

NPAs have become a grave concern for the banking sector in couple of years and impacted credit delivery of banks to a great extent.As per a survey, net NPAs amount to 12 percent of the total loans in the banking system. However, if restructured assets are taken into account, stressed assets account will be 10.9 percent of the total loans in the system. As per the International Monetary Fund (IMF), around 37 percent of the total debt in India is at risk.India's largest lender State Bank of India (SBI) reported a massive 67 per cent fall in consolidated net profit at 1259.49 crore rupees in the third quarter of the 2015-16 financial year and classified loans worth 20692 crore rupees as having turned bad.

7.6 Reduced Profits

The banking sector recorded slowdown in balance sheet growth for the fourth year in a row in 2015-16. Profitability remained depressed with the return on assets (RoA) continuing to linger below 1 percent. Further, though PSBs account for 72 percent of the total banking sector assets, in terms of profits it has only 42 percent share in overall profits.

7.7 Issue of Monetary Transmission

Like reduced profits, this is also an off-shoot of burgeoning NPAs in the system. With the easing of inflation and moderation in inflationary expectations, the RBI reduced the repo rate by 100 basis points between January and September 2015.However, change in the key policy rate was not reflected in lending rates as banks are not willing to transmit the benefits of low interest policy regime due to low-availability of liquidity against the backdrop of high NPAs.

7.8 Corruption

Scams in the erstwhile Global Trust Bank (GBT) and the Bank of Baroda show how few officials misuse the freedom they granted under the guise of liberalisation for their personal benefit. These scams have badly damaged the image of these banks and consequently there profitability.

8. Conclusion

Banks are at the core of any economic system whether developed or developing. Essentially, a technologically advanced, transparent and efficient banking system is the need of the hour for the growing economy like India.In our country, need for qualitative banking surpasses the conservative economic or financial logic as the financial inclusion is still a distant dream. In addition to the provision of traditional services, many social functions are attached to the banking system financial inclusion and inclusive growth.In order to achieve the goal of faster and inclusive growth, it is high time the government and banking industry undertake a comprehensive relook into the existing policies and structures.