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Financial Performance of Indian Banking Sector: Challenges and Opportunities in the Scenario of Startup India

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Abstract

Financial sector is playing a major role in the economic development of India. It is generally considered that a strong and healthy banking system is a requirement for sustainable economic growth. Indian banks are facing major challenges in this dynamic environment. The current study is mainly concerned with the analysis of comparative profiles of Public Banks, Private Banks and Foreign Banks in India during the period 2012-2016 that reflects the impact of new competitive environment on the bank's performance in terms of various selected parameters. The study also highlights that due to digitalization and startup India there are various opportunities and challenges in this high tech scenario. For financial performance data was collected through secondary sources from Trend and Progress Report of RBI and the tool used -for data analysis of the profile of bank group wise is Compound Annual Growth Rate (CAGR) which is expressed in percentages. The results have found strong evidence that the Private Sector Banks surpasses the other bank groups and topped the position in all the parameters and technological innovations are creating a lot of opportunities for Indian banking sector.

Keywords: *Financial Performance, Startup, Indian Banking Sector.*

Introduction

With the potential to become the fifth largest banking industry in the world by 2020 and third largest by 2025 according to KPMG-CII report, India's banking and financial sector is expanding rapidly. The Indian Banking industry is currently worth Rs. 81 trillion (US $ 1.31 trillion) and banks are now utilizing the latest technologies like internet and mobile devices to carry out transactions and communicate with the masses. The Indian banking sector consists of 26 public sector banks, 20 private sector banks and 43 foreign banks along with 61 regional rural banks (RRBs) and more than 90,000 credit cooperatives

The future of banking in India looks not only exciting but also transformative. Despite the somewhat difficult current operating environment, banks remain the largest financial sector intermediary in India. The current weakness in economic activity has muted credit demand from banks. Part of this slowdown is due to excess capacities in many sectors, together with the increase in leverage on corporate balance sheets, impeding their ability to absorb credit. In addition, alternative sources of financing, both domestic and offshore, have also emerged.

As the domestic economy remained sluggish, the growth in the Indian banking sector too remained under pressure in FY15. Credit off take slowed down to 9.4% in FY15 from 14.3% recorded in FY14. Poor earnings growth by companies, slow pace of investments, risk aversion of banks due to rising bad loans, and availability of alternative funding sources for corporates pulled down credit growth during the year.

Similarly, the growth in deposits of scheduled commercial banks (SCBs) at 10.7% in FY15 was much lower than the growth at 14.1% in the previous financial year. The base rate of major banks remained unchanged at 10.0% -10.25% in FY15. As a part of the monetary transmission, base rate of major banks fell to 9.75%-10% in April and declined further to 9.3%-9.7% by the end of 2015. Even deposit rates have fallen from 8%-9.25% in FY15 to 7%-7.9% towards the end of 2015.

There remains a wide disparity in the credit performance of public and private sector banks.

While the credit growth of public sector banks has more than halved to 7.1% that of private sector banks has improved from below 17% to 18.7% in FY15. The net interest margin and spread witnessed marginal decline in FY15. The aggregate profit after tax (PAT) of banks has risen by 10.1% in FY15 as compared to a decline of 14% in the preceding year. Although the growth in the net interest income has tapered down a bit, rationalization of operating expenses backed by moderation in the growth of the wage bill and a sharp decline in the growth of provisions and contingencies pulled up the profit growth during the year

In terms of profitability, the return on assets (RoA) remained static at 0.8% whereas the return on equity (RoE) dipped slightly from 10.7% to 10.4% in FY15. Among banks, public sector banks reported a marginal decline in RoA from 0.5% to 0.46%. Private sector banks saw their RoA improve from 1.65% to 1.68% during the year.

The gross NPAs of banks (PSBs + private) increased over the last one year from 3.9% to 4.6% as on March 2015. The stressed advances that include restructured advances rose from around 10% to 11.1% of total advances during the year. The PSBs recorded the highest level of stressed assets at 13.5% of the total advances as compared to 4.6% in case of private banks.

Objectives of Study

a) To explain the national and commercial banking scenario in India.
b) To analyze the financial trends of Indian Banking Sector
c) To compare the financial performance of public, private and foreign banks in India.
d) To study the challenges and opportunities for banks in changing scenario.

Research Methodology

The study is carried out to make quantitative and comprehensive evaluation of Indian Banking Industry. For the purpose descriptive research design (observational method & case- study method) has been adopted which is based on the secondary data and the secondary sources of data were the various websites, published annual reports and literatures of the banking companies, RBI annual report, IMF annual & periodical reports and academic journals.

Challenges Faced By the Indian Banks

1) **Basel III implementation**- In India, as per the RBI, implementation of Basel III started form 1 April 2013 and will be completed in a phased manner by 31 March 2018. The key elements of Basel III norms are definition of capital, enhancing risk coverage of capital, leverage ratio and liquidity framework.

Capital mobilization-Capital mobilized by commercial banks is the monetary value that the mobilization of commercial banks in the market through the operation of deposit, loan and number of other sources. Following the financial liberalization, some shifts have taken place in the ownership pattern of bank deposits.

Risk management system-To overcome the risk and to make banking function well, there is a need to manage all kinds of risks associated with the banking. Risk management becomes one of the main functions of any banking services.

Governance- Effective corporate governance is critical to the proper functioning of the banking sector and the economy as a whole. The executives are very much concerned about the integrity of accounting statements and quality of transparency and disclosures and feel that selective leak of sensitive information and dubious accounting practices have been the biggest concerns from the corporate governance perspective.

Asset quality- An asset can turn into a NPA when the borrower defaults on his repayment of interest or principal on agreed terms. It is often said that general economic slowdown impinges on the performance of banks and financial institutions, since slump in major economic activities results in poor recoveries and consequent deterioration in asset quality.

Financial inclusion- Providing affordable banking services to the lowest strata of the population is one of the primary goals. RBI has mandated that commercial banks achieve financial inclusion by offering no-frills saving-bank accounts and easy access to credit facilities through genera-purpose credit cards.

Opportunities for banking sector:

Technology and the banking Services in the Indian Market: Understood simply, fintech refers to the scope of financial services that can be available on digital platforms. This new disruption in the banking and financial services sector has had a wide-ranging impact. Key service offerings to emerge on digital platforms include:

Peer-to-Peer (P2P) Lending Services: Companies use alternative credit models and data sources to provide consumers and businesses with faster and easier access to capital. P2P lending allows online services to directly match lenders with borrowers who may be individuals or businesses. Examples are Lendbox, Faircent, i2iFunding, Shiksha Financial, Gyan Dhan, and Market Finance.

Payment Services: Companies allow both private individuals and businesses to accept payments over the web and on mobile without needing merchant accounts. Transfers are made directly to the bank account linked to the payee in order to secure against fraud. Examples are Mobikwik, Paytm, and Oxigen Wallet.

Remittance Services: A few startup ventures, albeit registered abroad, are trying to address the gaps in remittance transactions (both inbound and outbound) as the current process is cumbersome and expensive. These startups aim to disrupt the current monopoly held by firms like Western Union and MoneyGram. Examples are Instarem, FX, and Remitly.

Personal Finance or Retail Investment Services: Fintech companies are also growing around the need to provide customized financial information and services to individuals, that is, how to save, manage, and invest one's personal finances based on one's specific needs. Examples are FundsIndia.com, Scripbox, PolicyBazaar, and BankBazaar.

Miscellaneous Software Services: Companies are offering a range of cloud computing and technology solutions, which improve access to financial products and in turn increase efficiency in day to day business operations. The scope of fintech is rapidly diversifying at both macro and micro levels, from providing online accounting software to creating specialized digital platforms connecting buyers and sellers in specific industries. Examples include Catalyst Labs in the agriculture sector, AirtimeUp which provides village retailers the ability to perform mobile top ups, ftcash that enables SMEs to offer payments and promotions to customers through a mobile based platform, Profitbooks (online accounting software designed for non-accountants), StoreKey, and HummingBill.

Equity Funding Services: This includes crowd funding platforms that enable the funding of a project or business venture by raising funds from a large number of people. Such internet-mediated platforms are gaining popularity across the world as access to venture capital is often difficult to secure. These services are particularly targeted at the early stage of a businesses' operation. Examples include: Ketto, Wishberry, and Start51.

Cryptocurrency: India being a more conservative market where cash transactions still dominate, usage of digital financial currency such as 'bitcoin' has not seen much traction when compared to international markets. There are, however, a few bitcoin exchange startups present in India – Unocoin, Coinsecure, and Zebpay.

Analysis of Financial Performance

The capital adequacy ratio (CAR) of banks slipped from over 13% to 12.9% as on 31 March 2015. PSBs continued to report the lowest CAR that stood below 12% whereas private banks recorded a CAR of around 16% as at 31st March 2015.

Balance Sheet Ratios:

Balance Sheet Ratios					
	Mar '18	Mar '17	Mar '16	Mar '15	Mar '14
Capital Adequacy Ratio	13.2	12.86	13.1	13.08	13.47
Advances / Loans Funds(%)	72.98	74.23	78.32	78.1	77.34

Investment Valuation Ratios:

Investment Valuation Ratios					
	Mar '18	Mar '17	Mar '16	Mar '15	Mar '14
Face Value	10	10	10	10	10
Dividend Per Share	1.5	4.2	4.7	6.6	7.5
Operating Profit Per Share (Rs)	29.18	37.24	35.14	43.38	53.99
Net Operating Profit Per Share (Rs)	338.21	330.07	328.05	323.26	284.6

Debt Coverage Ratios:

Debt Coverage Ratios					
	Mar '18	Mar '17	Mar '16	Mar '15	Mar '14
Credit Deposit Ratio	73.35	74.83	74.89	74.57	73.07
Investment Deposit Ratio	28.48	28	29.16	30.36	32.11
Cash Deposit Ratio	5.03	4.84	4.87	5.09	5.82
Total Debt to Owners Fund	13.49	13.69	14.5	13.88	13.61

Financial Charges Coverage Ratio	1.27	1.28	1.28	1.34	1.45
Financial Charges Coverage Ratio Post Tax	1.07	1.1	1.12	1.18	1.24

Profit and Loss Account Ratios:

Profit And Loss Account Ratios					
	Mar '18	Mar '17	Mar '16	Mar '15	Mar '14
Interest Expended / Interest Earned	72.63	71.86	71.41	67.43	63.88
Other Income / Total Income	9.88	7.92	8.25	8.48	9.15
Operating Expense / Total Income	16.89	15.52	16.41	17.52	15.58

Leverage Ratios:

Leverage Ratios					
	Mar '18	Mar '17	Mar '16	Mar '15	Mar '14
Current Ratio	0.03	0.03	0.03	0.03	0.02
Quick Ratio	25.51	22.7	21.67	19.43	20.1

Profitability Ratios:

Profitability Ratios					
	Mar '18	Mar '17	Mar '16	Mar '15	Mar '14
Interest Spread	6.1	5.97	5.96	6.69	7.33
Adjusted Cash Margin(%)	4.78	6.64	7.6	11.01	13.63

Net Profit Margin	4.37	6.34	7.6	11.38	14.28
Return on Long Term Fund(%)	94.61	102.4	107.18	103.28	104.6
Return on Net Worth(%)	5.27	8	9.81	14.79	18.47
Adjusted Return on Net Worth(%)	5.27	8	9.81	14.79	18.47
Return on Assets Excluding Revaluations	280.63	261.46	248.16	242.89	214.94
Return on Assets Including Revaluations	338.54	308.84	298.4	269.27	242.02

Management Efficiency Ratios:

Management Efficiency Ratios					
	Mar '18	Mar '17	Mar '16	Mar '15	Mar '14
Interest Income / Total Funds	8.3	8.44	8.8	9.2	9.38
Net Interest Income / Total Funds	2.27	2.38	2.52	3	3.39
Non Interest Income / Total Funds	0.91	0.73	0.79	0.85	0.95
Interest Expended / Total Funds	6.03	6.07	6.28	6.21	5.99
Operating Expense / Total Funds	1.56	1.42	1.57	1.76	1.61
Profit Before Provisions / Total Funds	1.55	1.61	1.67	2.03	2.66
Net Profit / Total Funds	0.36	0.54	0.67	1.05	1.34
Loans Turnover	0.13	0.13	0.13	0.14	0.15
Total Income / Capital Employed(%)	9.21	9.17	9.59	10.06	10.33
Interest Expended / Capital Employed(%)	6.03	6.07	6.28	6.21	5.99
Total Assets Turnover Ratios	0.08	0.08	0.09	0.09	0.09
Asset Turnover Ratio	0.08	0.09	0.09	0.09	0.1

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Total Advances:

Total Advances(Amount in Rs. Billion)				
YEAR	**Public sector**	**private sector**	**Foreign banks**	
2008	8856	2259	770	
2009	11340	3176	989	
2010	14651	4201	1279	
2011	18191	5259	1631	
2012	22828	5850	1697	
2013	27335	6442	1674	
2014	33465	8118	1994	
2015	39428	9814	2347	
2016	45601	11592	2689	
2017	52159	13613	2996	
2018	56167	16087	3366	

The above table highlights the total advances of public banks, private banks and foreign banks. This is clear from the analysis that advances of public sector banks are increasing rapidly and alarming a very critical position in the way of their growth.

Conclusion

Indian banks have to operate in an increasingly globalised environment due to regulatory factors, technological factors; cross-border financial flows over which they may not have any control. The banks should be efficiently mobilizing required amount of capital from the market for meeting their current and future business growth and prudential requirements. The banks should be able to enlarge their outreach in terms of customer base and product choices by leveraging technology enabled payment systems in affordable, accessible, acceptable and assured manner. There is enormous scope for increasing for increasing the size and capacity of the banking structure. As advances of public sector banks are increasing continuously in comparison of private and foreign banks. There should be strong mechanism to control over increasing NPA. There is a need for reorienting the banking structure to make it more dynamic and flexible while ensuring safety and systemic stability. The competition from global banks and technological innovation has compelled the banks to rethink their policies and strategies. Different products provided by foreign banks to Indian customers have forced the Indian banks to diversify and upgrade themselves to compete and survive.

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