A STUDY OF BANKING SECTOR IN INDIA AFTER REFORMS

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ABSTRACT

The financial sector reforms have brought about significant improvements in the financial strength and the competitiveness of the Indian banking system. The efforts on the part of the Reserve Bank of India to adopt and refine regulatory and supervisory standards on a par with international best practices, competition from new players, gradual disinvestments of government equity in state banks coupled with functional autonomy, adoption of modern technology, etc are expected to serve as the major forces for change. New businesses, new customers, and new products beckon, but bring increased risks and competition. The present study examines the growth structure and the scope of banking sector in India after reforms. Effective banking sector reforms can be done through political willingness and commitment and establishment of rule of law in the country.

***Keywords**: Banking Sector Reforms, Performance of Indian Banking, Rural Banking, Universal Banking.*

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INTRODUCTION

The financial sector reforms have brought about significant improvements in the financial strength and the competitiveness of the Indian banking system. The efforts on the part of the Reserve Bank of India to adopt and refine regulatory and supervisory standards on a par with international best practices, competition from new players, gradual disinvestments of government equity in state banks coupled with functional autonomy, adoption of modern technology, etc are expected to serve as the major forces for change. New businesses, new customers, and new products beckon, but bring increased risks and competition. How might that change banks? To attract and retain customers, the banks need to optimize their networks, speed up decision-making, cut down on bureaucratic layers, and sharpen response times.

The reform has lead to new trends of being ahead and being with, by and for the customer. While the private sector banks are on the threshold of improvement, the Public Sector Banks (PSBs) are slowly contemplating automation to accelerate and cover the lost ground. VRS introduced to bring up the productivity, the concept of universal competition set in just to ensure customer convenience all the time. Also, the strength factor has lead to mergers and Indian banks have explored this opportunity.

REVIEW OF LITERATURE

Mr. Besant kalian (1989):- The paper makes an effort to first gather the major reforms measures and policies regarding the banking industry by the govt. of India and the Central Bank of India (Reserve Bank of India) during the last fifteen years. Secondly, the paper will try to study the major impacts of those reforms upon the banking industry. A positive responds is seen in the field of enhancing the role of market forces, regarding prudential regulations norms, introduction of CAMELS supervisory rating system, reduction of NPAs and regarding the up gradation of technology. But at the same time the reform has failed to bring up a banking system which is at par with the international level and still the Indian banking sector is mainly controlled by the govt. as public sector banks being the leader in all the spheres of the banking network in the country.

Rajesh Chakrabarti:- The banking sector as a whole and particularly the public sector banks still suffer from considerable NPAs, but the situation has improved over time. New legal developments like the SARFAESI Act provide new options to banks in their struggle against NPAs. The adoption of Basel-II norms however imply new challenges for Indian banks as well as regulators. Over time, the Indian banking industry has become more competitive and less concentrated. The new private sector banks have been the most efficient though the recent collapse of Global Trust bank has raised issues about efficiency and regulatory effectiveness.

B.Sathish Kumar (2002) :-This paper analyze that economic reforms totally have changed the banking sector. RBI permitted new banks to be started in the private sector as per the recommendation of Narashiman committee. The Indian banking industry was dominated by public sector banks. But now the situations have changed new generation banks with used of technology and professional management has gained a reasonable position in the banking industry. The main idea of this article is to make an evaluation of the financial performance of Indian private sector banks.

Ben Naceura and Mohammed Omran (1989):-In this paper, we examine the influence of bank regulation, concentration, and financial and institutional development on commercial bank margins and profitability across a broad selection of Middle East and North Africa (MENA) countries. We cover the 1989-2005 period and control for a wide array of macroeconomic, financial, and bank characteristics. The empirical results suggest that bank-specific characteristics, in particular bank capitalization and credit risk, have a positive and significant impact on banks' net interest margin, cost efficiency, and profitability. As for the impact macroeconomic and financial development indicators bear on bank performance, we conclude that these variables have no significant impact on net interest margins, except for inflation. However, inflation shocks seem to be passed mainly through the deposit rates and this type of transmission means that banks bear the entire negative cost of inflation.

The number of branches has been increased. The present table and diagrams below show the growth of number of branches and business during the period from 2005 to 2009. The number of branches in 2005 were 70606 and in 2009-82408.

TABLE: 1

OFFICES OF COMMERCIAL BANKS IN INDIA - 2005 TO 2009

Bank Group	As on March 31				
	2005	2006	2007	2008	2009
	(1)	(2)	(3)	(4)	(5)
State Bank of India and its Associates	14006	14294	14651	15814	16731
Nationalised Banks $	35096	35848	37413	39204	40766
Foreign Banks	242	259	272	279	295
Regional Rural Banks	14763	14776	14812	15029	15384
Other Scheduled Commercial Banks	6462	6828	7415	8294	9186
Non-Scheduled Commercial Banks	37	41	46	46	46
Total	**70606**	**72046**	**74609**	**78666**	**82408**

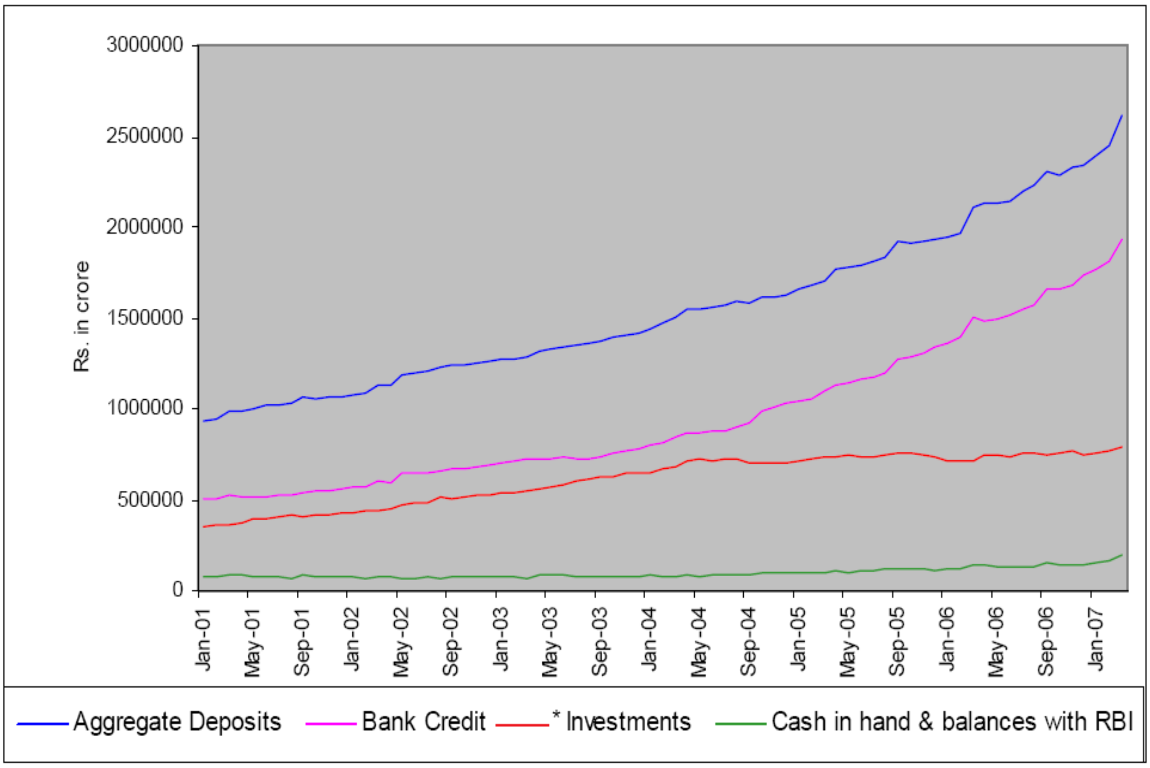
Notes : No. of offices includes administrative offices.
$ Includes IDBI Bank Ltd.
Data for 2005 to 2008 have been revised and data for 2009 are provisional.

Source : Master Office File (latest updated version) on commercial banks, Department of Statistics and Information Management, RBI.

The diagram below highlights the business of banking sector during the period from 2001 to 2009. The total aggregate deposit in 2005 was less than 10 million crore rupees but in 2009 it was above 25 million crore rupees. Similarly, bank credit and investment have increased manifold. This shows a positive impact of reforms on banking sector undertaken by the Government.

SCHEDULED COMMERCIAL BANKS' BUSINESS IN INDIA: 2001 TO 2009

(As on the last reporting Friday of Month)



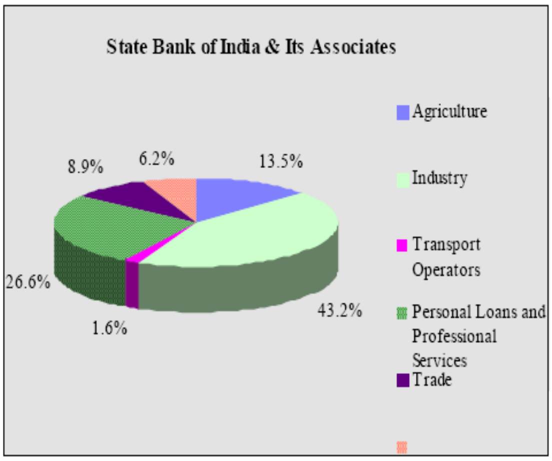
Note : * Include investments in Government and other approved securities only.

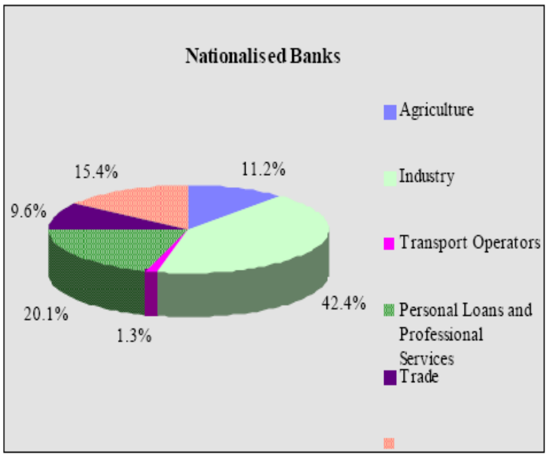
Source:- Department of Statistics and Information Management, RBI.

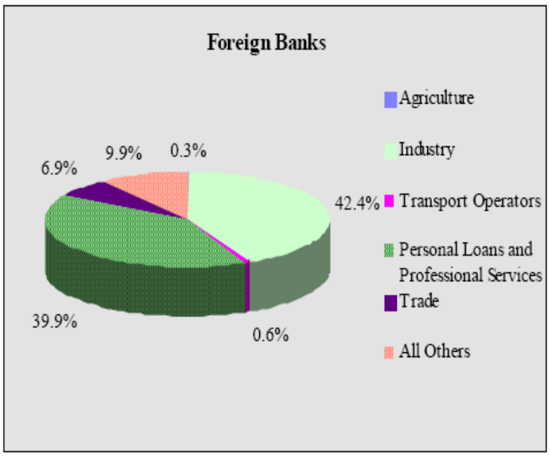
The diagrams below show the occupation-wise distribution of Credit by different banks.

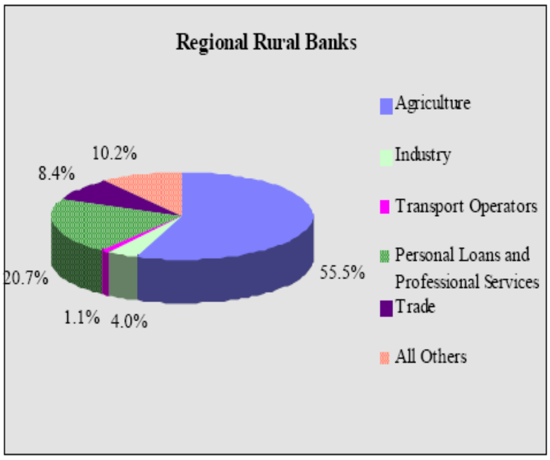
Occupation-Wise Distribution of Credit by Scheduled Commercial Banks - 2008

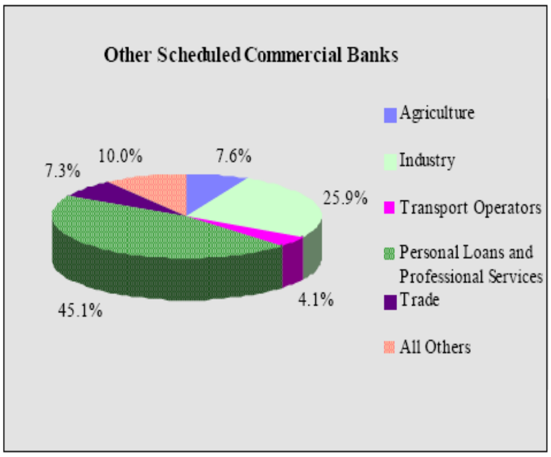
(As on March 31)

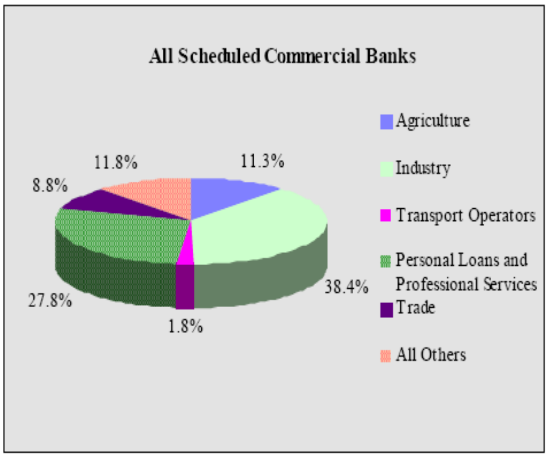












Source:- Department of Statistics and Information Management, RBI.

Universal Banking

RBI states: *"The emerging scenario in the Indian banking system points to the likelihood of the provision of multifarious financial services under one roof. This will present opportunities to banks to explore territories in the field of credit/debit cards, mortgage financing, infrastructure lending, asset securitisation, leasing and factoring. At the same time it will throw challenges in the form of increased competition and place strain on the profit margins of banks"*

The evolving scenario in the Indian banking system points to the emergence of universal banking. The traditional working capital financing is no longer the banks major lending area while FIs are no longer dominant in term lending. The motive of universal banking is to fulfill all the financial needs of the customer under one roof. The leaders in the financial sector will be aiming to become a one-stop financial shop.

Universal Banking includes not only services related to savings and loans but also investments. However in practice the term 'universal banks' refers to those banks that offer a wide range of financial services, beyond commercial banking and investment banking, insurance etc. Universal banking is a combination of commercial banking, investment banking and various other activities including insurance. If specialized banking is the one end universal banking is the other. This is most common in European countries.

The main advantage of universal banking is that it results in greater economic efficiency in the form of lower cost, higher output and better products. The spread of universal banking ideas will bring to the fore issues such as mergers, capital adequacy and risk management of banks. Universal banks may be comparatively better placed to overcome such problems of asset-liability mismatches (for banks). However, larger the banks, the greater the effects of their failure on the system. Also there is the fear that such institutions, by virtue of their sheer size, would gain monopoly power in the market, which can have significant undesirable consequences for economic efficiency. Also combining commercial and investment banking can gives rise to conflict of interests.

Rural Banking

Economically empowering, i.e. access to inexpensive credit and other micro-finance services, including savings and insurance, India's rural population will have a significant impact on India's economic growth. Economic empowerment is defined here as. The modern banking system has failed to deliver inexpensive credit to India's 600,000 villages - despite several expensive attempts to do so. Do we need to rethink the appropriate institutional structure for rural banking in India? The problems of widespread poverty, growing inequality, rapid population growth and rising unemployment all find their origins in the stagnation of economic life in rural areas.

The **development strategy** adopted and the increasing diversification and commercialization of agriculture underline the need for the rapid development of rural infrastructure and a larger flow of credit. Activities allied to agriculture – livestock breeding, dairy farming, sericulture etc are being taken up on commercial lines. Further, hi-tech agriculture with an export orientation has brought about higher productivity in cotton, oilseeds, etc.

Progressive and not-so-small farmers have no difficulty in obtaining credit from the commercial banks. Credit for the poorer households is the real problem.

The Narasimham Committee observed that the manning of rural branches "has posed problems for banks owing to the reluctance of urban-oriented staff to work in the rural branches and the lack of motivation to do so. More local recruitment and improved working conditions in rural areas should help to meet this problem."

The makers of banking policy are now focusing on technology-led banking in the rural sector. This requires a restructuring of cooperatives to enable them to meet the challenges of competition. It also requires a change in mindset. While the government should promote the restructuring and modernization of cooperatives through an incentive/disincentive package and by providing adequate infrastructure in the rural areas, the actual task should be left to the cooperative leadership and the apex bodies of cooperatives.

The major function of a financial system is to strengthen the savings-investment process of the country. For the matter of economic development, the financial system mobilizes and pools together the financial resources from various surplus units and ultimately channelizes all those resources for productive investments. This can be done with the help of effective banking sector reforms which required firm political willingness and commitment and establishment of rule of law in the country.

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