Changing Dynamics of Indian Banks

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Abstract

Banking is the life blood of an economy and it is the pillar and strength of modern business. It is a main and an essential part of the human life and it is in its growing phase. Banking industry and sound financial system plays a key and significant role in the economic development in developed and developing countries .The banking system in India is dominated and large area is controlled by nationalized banks. In India 27 public sector banks, 21 private sector banks and 45 foreign sector banks exist and working properly. Paper is prepare to focuses on how the technology is playing an important role for transformation of banking system in India. This paper includes the history of the banking industry, financial innovations, performance and the future growth of the Indian banking system. Financial innovations are like, RTGS, EFT, ATM, ECS Retail banking, NEFT, e-commerce, e-marketing, e-banking. Now Indian banking model is Internet-based model and it carries its business to create a sustained competitive advantage by using this model. Now banks are totally depends on information technology and the technology risks increase, both for individual banks and the financial industry at large but Continuous technology advancement and innovations are playing great role in the satisfaction of customers, suppliers and counterparts.

Keywords

Banking System, Financial Innovations, Information Technological, Technological Changes, Financial Sectors.

1. Background of Banking in India

India had a centuries old tradition of indigenous Banking. The theory of Banking was not new to India. There are several books that shows banking has a powerful existence. Initially, the money related issues, i.e. lending money etc. were controlled by Seths, Sahukars, Mahajans. They followed a simple and easy process to take loan for distribution hassle free loan and charged a high rate of interests and no record was maintained so that they can exploit urban and rural people.

The origin of Modern Banking in India starts when the British came into India and starting rule over here. They established the first bank that is Bank of Hindustan which was in Calcutta in 1770 .It works as per rules and regulation of European and British management. It was lost its existence in 1830-32 by liquidation. The development and progress of banking in India can be understood by dividing into three different phases as follows:

Phase I: Phase I was Nationalization of Banks in 1969. At that time the rural population of the country was dependent on unorganized sector, such as small money lenders, sahukars and zamindars. At the time of Independence financial requirements fulfill by the unorganized sector. At that time the Indian Banking sector was working under private ownership. For development of the economy and setup of organized financial system the Government of India decided to nationalized the Reserve Bank of India in 1949. **In 1955** the another bank Imperial Bank of India was nationalized and named the State Bank of India. Further The Banking Regulation Act, 1949 was enacted in 1949.

Phase II: This period is known as the Nationalization Period (1969 to 1991). In 1969, banks were nationalized by the Government of India. The number of such nationalized banks was 14 and their deposits was more than 50 crores. The result of nationalizations was that the Indian Banking system enormously started developing and for the development and advancement of the rural, illiterate and weaker public of the nation. The Narasimham Committee in 1974 recommended the establishment of Regional Rural Banks (RRB) as rural, illiterate and weaker as they were not considered under this system. For removal of this problem Regional Rural Banks (RRB) was introduced. On 2nd October 1975, RRBs were established .The objective of RRBs is to disburse the credit to villagers and rural public. After it six more banks were proposed to nationalize. Finally, in 1980 six banks were nationalized. With the great effect of Phase II of nationalization, the target of priority sector lending was also raised to 40%.

Phase III: Liberalization Phase (1990 to till): for the financial stability, systematic development and increasing profitability of Public Sector Banks, Government of India decided to arrange a meeting and according to suggestion of this meeting a committee was set up under the chairmanship of Shri. M. Narasimham. As per the recommendation of the committee several steps were taken to reform the banking system in the country. These are

- To make banks financially strong, competitive, and conducive for the development of the financial system.
- Government and RBI advice to implement the same policies for both the banks, Public sector banks and Private sector banks .They should be treated equally. More suggestions are related to no more nationalization of banks.
- It was emphasized that banks should avoid the traditional system of banking and encouraged to adopt a new and progressive function such as merchant banking and underwriting, retail banking, etc. for the financial stability.
- Foreign banks would be invited and facilitate them so that they can open offices in India either as branches and legalized to set up joint ventures with Indian banks and Promote to start other newer forms of financial services.
- In phase III RBI took a decision to issue license to private sector banks such as Centurion Bank, Global Trust Bank, Times Bank and Development Credit Bank, ICICI Bank, Axis Bank, Bank of Punjab, IndusInd Bank, HDFC Bank, IDBI Bank to entry in the Banking sector. All these banks are Private Banks.

2. Organization of Banking in India

The organisation of Indian banking sector can be understood by categories into two sets. The first one is scheduled banks and another is non-scheduled banks. According to the guideline of the Reserve Bank of India Act, 1934 all banks, which are included in the Second Schedule Banks are schedule Bank. Scheduled Co-operative can be further classified as Scheduled State Co-operative Banks and Scheduled Urban Cooperative Banks. On the basis of their ownership and/or nature of operation and functions Scheduled Commercial Banks in India are classified into five different categories.

- State Bank of India and its Associates
- Nationalised Banks
- Private Sector Banks
- Regional Rural Banks
- Foreign Banks

Reserve Bank of India

Indian Banking structure is totally controlled by RBI. It came into existence on 1st April 1935 under the RBI Act 1934. Reserve Bank of India is recognised as The Banker's bank, Head Bank, Apex Bank and Central Bank of India. Reserve Bank of India kept reserves of all Public and commercial banks and it has a power to control of currency and the issue of currency in India.

Commercial Banks: Commercial Banks can be divided into Scheduled and Non-scheduled banks:

- **Scheduled Banks:** For a Scheduled Bank the following two conditions which has to be fulfilled. The first one is that Scheduled banks should include in the 2nd schedule of RBI Act, 1934 and another one is the minimum limit should not be less than Rs.5 lakh for paid up capital and collected funds by the of bank.
- **Non-scheduled banks:** These banks are not included in the list of scheduled banks that's why they called non-scheduled banks. These banks are not entitled for granting loans from RBI for meeting their general activities only avoiding in emergency unlike scheduled banks.

Commercial bank includes public sector banks, private sector banks and foreign banks.

1. Public sector banks: There are 26 public sector banks with the inclusion of SBI, its five associate banks, IDBI bank Ltd. and nineteen nationalized banks. In terms of the volume State Bank of India is the major commercial bank and 90 percent of total banking business in India is covered by public sector Banks.
2. Private sector banks: Private sector banks are those which have equity, by private shareholders not by the Government. For example: ICICI Bank, HDFC Bank, AXIS Bank etc. the Private sector bank playing a major role by increasing the efficiency and customer satisfaction in the development of the Indian banking industry. They are giving competition to public sector banks.

3. Foreign Banks: Foreign banks operate their branch in India and have their head offices out of India. They run their banking operation and services in India, but controlled and handled from Head Office. CITI bank, HSBC bank, Standard Chartered bank etc. are the examples of foreign banks which are giving their services in India.

Regional Rural Bank (RRB)

To Assist Rural and Poor People RRB's were established on 2nd October 1975 under the provisions of RRB Act 1976. To develop the rural economy, it was necessary to set up a bank which could help the rural public staying there. They are working in all states apart from Sikkim and Goa. These regional rural Banks are sponsored by its state itself .These are the state oriented banks. Their borrowers include small and marginal farmers, rural people, labour involved in agricultural activities, artisans etc. The control of RRB is done by NABARD. NABARD assisted RRB by Providing short term and medium term loans and fulfil their requirements accordingly.

Co-operative Bank

Co-operative bank was set up by passing a co-operative act in 1904.Various amendments were done timely. Now they are organised properly. They worked on the principal of co-operation and mutual help. The main objective of a co-operative bank is to provide rural credit, short term agriculture loan for agricultural, rural development, non-agricultural loans, employment oriented schemes and short term loans.

3. Changing Dynamics in Banking

There is regular changes, technological evolution, up gradation, and advancement in the banking industry. For that it is necessary to controlled by the various committees so that this industry can perform its services properly. These committees were set up and controlled by RBI and the government of India. The advancements in technology have changed the market scenario. Now, due to technology and internet connection, it is easy to access the services in the mobile and internet banking services it is getting popularity among the urban as well as rural public. The banking sector is trying to improve its operations and services. It is starting to give emphasis on customer services and for better customer services banks are regularly upgrading their technology and system to make it sound. For it banking industry is implementing various changes time to time.

4. The Changing Dynamics are as follows

Computerization: The computerisation of Indian Banks is started from 1980. Computerization means each and every Indian banks and its branches had to start the installation and setup of computers to systematise the functioning of the branches. It focuses on particularly at that branch where the load of transactions are higher. Computerization helps in growing and developing in the economy as a whole. All the information of customers is stored in computers and can be checked when required. This system is known as KYC.

Set up of Satellite Banking: With the help of satellite banking it is very easy to establish a good connectivity among various banks and its branches. It will help banks to give their services to underserved areas, villagers and reach at hilly areas of India, and in such a way they are providing better facilities, such as electronic funds transfers etc. Although Satellite Banking is expensive services for the banks but it facilitates banks to serve their customers in time and with satisfaction and expanding market share.

Development of Distribution Channels: With the advancement of technology the banking distribution channel has changed. Now the bank branches is not only the channel of distribution for a bank but upcoming and latest channels of distribution are ATMs, internet banking, mobile and telephone banking and card based delivery systems.

Automatic Teller Machines: First Time foreign banks introduced ATMs in the Indian banking industry in 1990s. Innovations in ATM technology have changed the environment completely. With the foreign banks, Public sector banks, private sector banks, cooperative banks have also started and introduced their ATM networks to expand their market. Now the ATMs has different phases of development.

Multilingual ATMs: Now ATMs are available in multilingual. Due to the Illiteracy and the problem with English language this new technology was not getting success. With the Installation of multilingual ATMs the banking functions become easy and many people are availing this type of services.

Multifunctional ATMs: Now the ATMs are also in advanced versions. It can perform multi-function at a time. Now the facility of Multifunctional ATMs are provided by public, private and foreign banks in India, Multifunctional ATMs are designed in such a way that it can execute a wide range of different services such as distributing cash and providing account information, prepaid and post-paid mobile recharges, Ticket booking (Air, Bus, Railway etc.), and PIN management, Bill payment (electricity & water bill), Cash payment, Cash recycling to minimized operating costs of ATM, Top-Up addition, Ticketing of different events, Money transfer and Examination fees etc. Some new areas are being explored via multifunctional ATMs, such as and advertising. Through Multifunctional ATMs banks are generate good revenue for the banks by effectively performing various services at a place and at a time.

ATM Network Switches: By using this technology, only one ATM card from a bank can be used with the ATMs of other banks means with the use of one ATM Card can operate ATMs of different banks. This facility is providing better customer convenience. Under this service, banks generate revenue by charging a fee for permitting the customers holder of ATM of other bank to access its ATM.

The various ATM network switches are Cash Tree, BANCS, Cash net Mitr and National Financial Switch. These are linked to Visa or Mastercard gateways. IDRBT, controller of the National Financial Switch, decided to reduce the cost of operations by waived the switching fee as the demand of the ATM are increasing regularly.

Internet Banking: Internet banking in India started from 2000. Internet banking services are offered in three levels.

1) The first level include a bank's informational website. On this website only customer queries are handled related to bank transactions.
2) The second level includes Simple Transactional Websites. This website will assists customers to give them instructions regarding the transactions.
3) The third level includes offering Fully Transactional Websites. This website will allow for easy and safely fund transfers and various value added services for bank customer.

Phone Banking and Mobile Banking: Phone and mobile banking are an updated and current scenario for the Indian banking industry. It is the updated and latest trend in Indian Banking Sector which works through a system that is known as an Interactive Voice Response System (IVRS) or telebanking executives of the banks. All the functions and transactions can be accomplished via phone banking and mobile banking. These Transactions may be information about Bank balance, last 5 transaction enquiries, stop payment SMS services and other instructions on cheques and funds transfers of small amounts etc. You have to follow strict rules for the security issues before using a phone and mobile banking.

Card Based Delivery Systems: In the card based delivery system mechanisms, various banking services such as credit cards, debit cards, smart cards etc. are introduced and they have been enormously fruitful in India since their launching.

Payment and Settlement Systems: Innovations, advanced technology and strong communication infrastructure have a great impact on banks. Through this development Bank's payment and settlement systems become secure as this is the central and the major portion of the businesses by of banks.

Paper Based Clearing Systems: Among the all-important amendments, the introduction of MICR technology was the main amendment done with this improvement in paper based clearing.

Cheque Truncation System (CTS): Under the process of Truncation no cheque is moved from one bank to another bank means the movement of the cheque is stopped under this process. The electronic image of the cheque sent to the drawee branch along with the relevant information like the MICR fields, date of presentation, presenting banks etc. Thus, with the implementation of this process reduces the risk of frauds, carrying cost, reconciliation problems, logistics and distribution problems and the cost of collection of cheque.

Electronic Clearing Service: The Electronic Clearing Service (ECS) presented by the RBI. It was introduced in 1995. ECS working is in two types 1) ECS debit clearing and 2) ECS credit clearing service. Electronic credit clearing works with that mechanism that is used to for update the transaction in single debit multiple credits. It deals with the transactions related to releasing of salary, Payment of dividend, pension transfer, payment of interest, etc. ECS debit clearing service operation is working with the mechanism of single credit multiple debits. It includes the transaction related to utility service like collection of electricity bills, telephone bills and other charges. This system supports banks for collections of principal amount and interest repayments also.

Electronic Funds Transfer Systems: An electronic funds transfer (EFT) is a mechanisms that proceeds over a computerized network with Internet Services, among accounts with the same bank or different accounts in different bank and financial institutions. It is the Electronically Funds Transfer (EFT) from one bank account to another bank account by using the online Mechanism System. The EFT System was working in India since 1995. It covers 15 centres. Clearing houses are managed and controlled by the Reserve bank of India.

Real Time Gross Settlement (RTGS): RTGS services were started from 2004. It works on the system of Systemically Important Payment Systems (SIPS). It is a facility for transfer of amount with the minimum value of 2 lakh. It deals with the amount which monetary value is higher.

Technology Vendors: Most of the banks are now preferring to engage with IT vendors for minimising the complexities involved in it by introducing specialized software which help in risk management systems, retail and corporate banking, credit card management. Management systems, complete back office support, including data management systems.

FDI in Commercial Banks: Foreign capital has been invited for rapid growth and development of the banking sector. For this foreign capital is invited as foreign direct investment and foreign institutional investments. FDIs and FIIs are permitted to invest in India by the Government in almost all the sectors of the economy along with the banking sector.

Developments in India's Banking Industry Include

- The Indian banking system is very wide as it consists of 27 public sector banks, 26 private sector banks, 49 foreign banks, 56 regional rural banks, 1,562 urban cooperative banks and 94,384 rural cooperative banks.
- In September 2018, Government of India took initiative for achieving the objective of financial inclusion by launching India Post Payments Bank (IPPB) and it achieved by opening bank branches across 650 districts of India.
- When we talk about the advancing and deposits of banking. The figures tells that In FY17-18, total advancing increased at a CAGR of 10.94 per cent and total deposits increased at a CAGR of 11.66 per cent. India stand, fourth rank in retail credit market among all countries. The value of retail credit is reached to US$ 281 billion till year 2017. India's digital lending is going to increase regularly. It

stood at US$ 75 billion in FY18 and now it is estimated to increase by five-times by FY2023 in the digital disbursements.

- In August 2017, it was announced by the Global rating agency Moody's that the Indian banking system was not fluctuate rapidly, as it is stable, that is a good indication of future growth. Four Indian banks upgraded from Baa3 to Baa2 by Global rating agency Moody's In November 2017.
- Various mergers and acquisition have taken took in 2017. The major merger deal in the micro finance segment of FY17 was with the IndusInd Bank Limited and Bharat Financial Inclusion Limited. Through mergers and acquisitions national, global and multinational banks are extending their business operations exchange their technology and human resource and eliminate the competition.
- The Indian banking sector is also working for microfinance. According to the Data availability In May 2018, in microfinance sector the total equity funding's was growing up at the rate of 39.88 to Rs 96.31 billion and the total equity funding's in 2017-18 it was Rs 68.85 billion
- RBI also amends laws related to investment policies that these investments will not exceed 10 percent of the unit capital of investment instruments in real estate investments trusts (REITs) and infrastructure investment trusts (InvITs).
- The Government of India supposed to implement a two percentage point discount made via digital payments on business-to-consumer (B2C) transactions in the Goods and Services Tax (GST)
- For the development of MSME sector SIDBI (Small Industries Development Bank of India) decided to launch an online portal Finally 'Udyami Mitra' a new online portal was launched by SIDBI to support, improving credit availability and financial assistance to Micro, Small and Medium Enterprises' (MSMEs) in the country.
- To support the public sector banks through banking reforms and capital infusion Government of India has released a two-year plan with the amount of Rs. 2.11 lakh crore (US$ 32.5 billion). With the implementation of a two year plan public sector banks are playing a great role for in the development of the financial system and give it a boost up to the MSME sector. In this regard the Lok Sabha has taken the decision to issue various bonds worth Rs 80,000 crore.

- To support the banking sector and overcome the problem of bankruptcy a new amendment was passed by President Ram Nath Kovind. The Insolvency and Bankruptcy Code (Amendment) Ordinance, 2017 to pave the loopholes in the current system and to make the process effective so that banking sector perform their work properly.
- National Bank for Agriculture & Rural Development (NABARD) sanctioned around 204,000 Point of Sale terminals to improve banking infrastructure, particularly in the villages Financial Inclusion Fund was used for implementation for Point of Sale terminals. This step increases the user of debit cards and no. of transactions of debit cards. Due to the demand of Point of Sale (PoS), the terminals were increased by 1.25 million by 2017. The total number of saving and deposit bank accounts opened in different banks under Pradhan Mantri Jan Dhan Yojana (PMJDY) reached 333.8 million till November 2018. PMJDY scheme is nationwide, open ended scheme with lots of benefits and incentives.

5. Challenges and Opportunities of Indian Banking:

After Liberalization, Privatization and Globalization in India, Indian banks are facing many problems and challenges. These are as follows:

a. Low profitability and productivity
b. Lack of integrity
c. Increase of administrative and office expenses
d. Survival of loss making branches
e. Scandals
f. Lack of professional behavior
g. Lack of professional and friendly approaches with customer
h. Non-performing assets
i. Customer oriented market
j. Difficulty in customer satisfaction
k. Recession period face by the Industry
l. Handling work force
m. Controlling of technological innovation

Opportunities

In present scenario Banks have some prospects in India. By facing challenges banks can grab the opportunities, the bank can have better advantages from the following opportunities:-

1. Offering of innovative products
2. Customized service approach
3. Customer relationship management
4. Professional approaches
5. Managerial excellence
6. Technological and Marketing advancement
7. Customized services
8. Branch expansion
9. Deposit Mobilization
10. NPA management
11. Asset reconstruction
12. Motivational HRM policies
13. Changes to make easy lending process
14. Merger and acquisition
15. Total quality management
16. Cyber services

6. Conclusion

Today, Indian Banking industry is one of the most growing and flourishing industries. To increase in the banking services it is better to understand the customers, and by using new techniques bank will be successful in meeting their customer needs. For this with traditional banking services, Indian banks should adopt various product innovations, new services and various application with the use of Information Technology. It is the demand of today to use the information technology. The benefit of Information Technology will help to compete the current challenge and to saturate sufficiently to the public living in rural areas. Some new and innovative programs, agenda and software in regional languages could be developed to fascinate urban, rural and poor people of India. Banking systems of any country need to be effective and efficient. Effective implementation of Banking innovations and Services can lead economic development of any country and can provide ample business opportunities.

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