CHAPTER – IV
BANKING SECTOR IN INDIA

Section 4.1 of this chapter introduces Banking sector in India and its evolution, and highlights different stages of growth. Section 4.2 discusses the factors that lead to nationalisation of banks. Section 4.3 discusses the types of banks in the era of liberalisation. Section 4.4 discusses the impact of international regulations on banking sector. Section 4.5 introduces recommendations of various committees. Section 4.6, compares the performance of Indian banks with their counterparts. Section 4.7 sets ground for the Human resource perspectives in the banks.

4.1 Introduction to the Banking Sector in India

Banks in India have enjoyed the role of most powerful agents of social and economic transformation. Through banking reforms, the banks realised that they can no more operate in isolation. Different approaches were made by banks to facilitate the new role which they have taken up. All banks invariably took up expansion, only to realise they had inappropriate organisation structure to facilitate expansion.

Banking in India has its origin as early as the Vedic period. It is believed that the transition from money lending to banking must have occurred even before Manu, the great Hindu Jurist, who has devoted a section of his work to deposits and advances and laid down rules relating to rates of interest. During the Mogul period, the indigenous bankers played a very important role in lending money and financing foreign trade and commerce. During the days of the East India Company, it was the turn of the agency houses to carry on the banking business. The General Bank of

---

India was set up in the year 1786. Next came Bank of Hindustan and Bengal Bank.\textsuperscript{92} The East India Company established Bank of Bengal (1809), Bank of Bombay (1840) and Bank of Madras (1843) as independent units and called them Presidency Banks. These three banks were amalgamated in 1920 and Imperial Bank of India was established which started as private shareholders banks, consisting majority of European shareholders.

In 1865 Allahabad Bank was established and first time exclusively by Indians, Punjab National Bank Ltd. Followed the suit in 1894 with headquarters at Lahore. Between 1906 and 1913, Bank of India, Central Bank of India, Bank of Baroda, Canara Bank, Indian Bank, and Bank of Mysore were set up. Reserve Bank of India came in 1935.

During the first phase the growth was very slow and banks also experienced periodic failures between 1913 and 1948. There were approximately 1100 banks, mostly small. To streamline the functioning and activities of commercial banks, the Government of India came up with The Banking Companies Act, 1949 which was later changed to Banking Regulation Act 1949 as per amending Act of 1965 (Act No. 23 of 1965). Reserve Bank of India was vested with extensive powers for the supervision of banking in India as the Central Banking Authority.

Government of India took major steps in this Indian Banking Sector Reform after independence. Imperial Bank of India was nationalised in 1956 with extensive banking facilities on a large scale especially in rural and semi-urban areas. It formed State Bank of India to act as the principal agent of RBI and to handle banking transactions of the Union and State Governments all over the country.

\textsuperscript{92} Khan, M Y. (2005), Financial Services, 2\textsuperscript{nd} Ed., Tata Mc Graw Hill, New Delhi.
Seven banks forming subsidiary of State Bank of India were nationalised in 1960 on 19th July, 1969, major process of nationalisation was carried out. It was the effort of the then Prime Minister of India, Mrs. Indira Gandhi. 14 major commercial banks in the country were nationalised. Second phase of nationalisation Indian Banking Sector Reform was carried out in 1980 with seven more banks. This step brought 80% of the banking segment in India under Government ownership. From 1955 to 1969 State Bank of India and its Associates were the only public sector banks. Public sector banks dominated the commercial banking sector with 79.7% of the assets in 1999-2000.

Government of India took following measures to Regulate Banking Institutions in the Country:

- 1949: Enactment of Banking Regulation Act.
- 1955: Nationalisation of State Bank of India.
- 1959: Nationalisation of SBI subsidiaries.
- 1961: Insurance cover extended to deposits.
- 1971: Creation of credit guarantee corporation.
- 1975: Creation of regional rural banks.
- 1980: Nationalisation of seven banks with deposits over 200 crore.

4.2 Nationalisation of Banks

Under nationalization Act of 1969, Government decided to nationalize fourteen largest private owned domestic banks. The trend repeated again when government acquired the ownership of six more banks under same act, leading to the

---

ownership of twenty banks. After the nationalisation of banks in 1969, the branches of the public sector bank India rose to approximately 800% in deposits and advances took a huge jump by 11,000%. Banking in the sunshine of Government ownership gave the public implicit faith and immense confidence about the sustainability of these institutions. These banks had to play a supportive role to other sectors - agriculture, small scale industries, retail trade, small business and small transport operators Poverty alleviation and Employment generation programmes.

This phase has introduced many more products and innovative facilities in the banking sector in its reforms measure. In 1991, Reserve Bank of India, under the chairmanship of M Narasimham, has set up a committee to work towards the liberalisation of banking practices. It covered the areas of interest rates deregulation, credit rules, entry deregulation for both domestic and foreign banks, CRR and SLR etc. Licensing a small number of private banks- came to be known as *New Generation tech-savvy banks*, and included Global Trust Bank Axis Bank, ICICI Bank and HDFC Bank. As a part of industry reforms, new private sector banks were permitted to make an entry in to industry leading to increased competition.

This phase has introduced many more products and facilities in the banking sector in its reforms measure. The country was flooded with foreign banks and their ATM stations. Efforts are being put to give a satisfactory service to customers. Phone banking and net banking is introduced. The entire system became more convenient and swift.

### 4.3 Current Scenario of the Banking Industry

The industry is currently in a transition phase. On the one hand, the PSBs, which are the mainstay of the Indian Banking system, are in the process of shedding
their flab in terms of excessive manpower, excessive Non Performing Assets (NPA) and excessive governmental equity, while on the other hand the private sector banks are consolidating themselves through mergers and acquisitions.

PSBs, which currently account for more than 78 percent of total banking industry assets are saddled with NPAs (a mind-boggling Rs 830 billion in 2000), falling revenues from traditional sources, lack of modern technology and a massive workforce while the new private sector banks are forging ahead and rewriting the traditional banking business model by way of their sheer innovation and service. The PSBs are of course currently working out challenging strategies even as 20 percent of their massive employee strength has dwindled in the wake of the successful Voluntary Retirement Schemes (VRS) schemes.

The private players however cannot match the PSB’s great reach, great size and access to low cost deposits. Therefore one of the means for them to combat the PSBs has been through the merger and acquisition (M&A) route. Over the last two years, the industry has witnessed several such instances. For instance, HDFC Bank’s merger with Times Bank, ICICI Bank’s acquisition of ITC Classic, Anagram Finance and Bank of Madura. Centurion Bank, Indusind Bank, Bank of Punjab, Vysya Bank are said to be on the lookout. The UTI bank- Global Trust Bank merger however opened a Pandora’s box and brought about the realization that all was not well in the functioning of many of the private sector banks.

Private sector Banks have pioneered internet banking, phone banking, anywhere banking, mobile banking, debit cards, Automatic Teller Machines (ATMs) and combined various other services and integrated them into the mainstream banking
arena, while the PSBs are still grappling with disgruntled employees in the aftermath of successful VRS schemes. Also, following India’s commitment to the WTO agreement in respect of the services sector, foreign banks, including both new and the existing ones, have been permitted to open up to 12 branches a year with effect from 1998-99 as against the earlier stipulation of 8 branches.

Talks of government diluting their equity from 51 percent to 33 percent in November 2000 have also opened up a new opportunity for the takeover of even the PSBs. The FDI rules being more rationalized in Q1FY02 may also pave the way for foreign banks taking the M&A route to acquire willing Indian partners.

Meanwhile the economic and corporate sector slowdown has led to an increasing number of banks focusing on the retail segment. Many of them are also entering the new vistas of Insurance. Banks with their phenomenal reach and a regular interface with the retail investor are the best placed to enter into the insurance sector. Banks in India have been allowed to provide fee-based insurance services without risk participation invest in an insurance company for providing infrastructure and services support and set up of a separate joint-venture insurance company with risk participation.

Ray and Sanyal (1995) focus their study on economies of scale for Indian banks and found out that such economies will decrease with size. This study was based upon sample of public sector banks.94

---

A study by Chatterjee (1997) is a lot closer to the research presented above. This research emphasizes on interrelationship between size of the bank and economies.95

Banks are affected by various risk factors such as Market movements in interest rates; Credit spreads; liquidity issue- RBI has infused liquidity by continuously cutting the CRR. Banks are still hesitant to keep their credit tap open; Technology dependence and technology related frauds; Credit risk control; Competition from new entrants; corporate governance and volatility.

Most banks use derivative instruments to manage their risks as well as to help clients manage their risks. Some of them believe that their risk management department can anticipate future risks thereby keeping it under control. Banks have also started to develop systems and procedures to increase the effectiveness of compliance procedures, by using technology for compliance, running the business, managing risk and thus providing many more technology driven services.

Due to a significant over supply of products and services in all sectors differentiation through strong brand building is becoming more and more important. Banks have to communicate as to how unique it is in satisfying customer needs and to prevent customers from switching over to other rival banks. Banking business is mainly built on relationship and trust; hence they try to build their brands through various forms of advertisements and promotions by way of celebrity endorsements, etc. Banks have raised their promotional budgets by about 40%. Banks need to make sure they inspire trust while building or re-building brands- so as to shed their old fashioned image in order to appeal to the younger generation.

Dealing with banks is not a pleasant experience for customers. Most disgusted customers either bear it or switch to other banks. But given the diversity of their client base, it isn’t easy for the banks too. Banks usually have to understand the need of different segments of its customers. There are various problems relating to banking such as credit card issues-cards sent which were not asked for, data errors, bad treatment from recovery agents to name a few.

Four powerful trends have altered the banking industry, consolidation, globalization of operations, and universalisation of banking. Banks are focusing on inclusive growth, primarily through customization of products and adoption of technology. They are trying to bring in low-income households into the financial access net. They are providing access to finance to all sections of the society irrespective of their geographic sector, income, education, etc. since among the financially excluded households, about 76% is rural, that’s way too large a market. And so to cater to that as well as the other segments of the market new schemes such as no frills (zero balance) accounts, models like Business Correspondents (BC’s), information communication technologies, etc.

4.4 Types of Banks in India
1) Central Bank

The Reserve Bank of India is the central Bank that is fully owned by the Government. It is governed by a central board (headed by a Governor) appointed by the Central Government. It issues guidelines for the functioning of all banks operating within the country.

---

Function of a central bank

- Issues the nation's currency
- Regulates the supply of credit in the economy
- Manages the external value of its currency in the foreign exchange markets
- Holds deposits representing reserves of other banks and other central banks
- Acts as Fiscal Agent for the central government, when the government sells new issues of securities to finance its operations and Attempts to maintain an orderly market in these securities by actively participating in the government securities market.

2) Public Sector Banks

Public sector banks are those banks run under the control of government and their prime motive is the welfare of the general public. A public sector bank also looks for funding developmental work in the country as the government has a majority share in it. Publicly owned banks, which are controlled by the government, have numerous responsibilities pertaining to the banking sector of the country, such as administering various activities for the commercial banks of that country. They also determine the rates of interest offered by banks doing business in that country, as well as playing a major role in maintaining liquidity in the banking sector.

- Eg:
  - Bank Of Maharashtra
  - Bank Of India
  - SBI
  - Punjab National Bank
  - Bank of Baroda
3) **Private Sector Banks**

- Personalized financial and banking services that are traditionally offered to a bank's rich, high net worth individuals (HNWIs). For wealth management purposes, HNWIs have accrued far more wealth than the average person, and therefore have the means to access a larger variety of conventional and alternative investments. Private banks aim to match such individuals with the most appropriate options.

- Services include: protecting and growing assets in the present, providing specialized financing solutions, planning retirement and passing wealth on to future generations.

- Eg:
  - HDFC
  - Kotak Bank
  - The Bank of Rajasthan
  - Bank of Punjab
  - AXIS Bank

4) **Co-operative Banks**

- A co-operative bank is a financial entity which belongs to its members, who are at the same time the owners and the customers of their bank.

- Co-operative banks are often created by persons belonging to the same local or professional community or sharing a common interest.

- Co-operative banks generally provide their members with a wide range of banking and financial services (loans, deposits, banking accounts…).
• Co-operative banks differ from stockholder banks by their organization, their goals, their values and their governance.

• There are State co-operative Banks, Central co-operative banks and Primary Agriculture Credit Societies.

• Eg:
  – Ahmedabad Mercantile Co-Op Bank Ltd.
  – Solapur Janata Sahakari Bank Ltd.
  – Rupee Co-operative Bank Ltd.

5) Development Banks

• National or regional financial institution designed to provide medium- and long-term capital for productive investment.

• Such investment is usually accompanied by technical assistance.

• Some development banks are government owned and operated, while others are private.

• Eg:
  – ICICI
  – NABARD
  – Export-Import Bank of India
  – IDBI

6) Investment Banks

• Firm that originates, underwrites, and distributes new security issues of corporations and government agencies.
• This includes underwriting, acting as an intermediary between an issuer of securities and the investing public, facilitating mergers and other corporate reorganizations, and also acting as a broker for institutional clients.

• An investment bank is a financial institution that raises capital, trades securities and manages corporate mergers and acquisitions. Investment banks work for, and profit from, companies and governments, by raising money through issuing and selling securities in capital markets (both equity and debt) and insuring bonds (e.g. selling credit default swaps), and providing advice on transactions such as mergers and acquisitions. A majority of investment banks offer strategic advisory services for mergers, acquisitions, divestiture or other financial services for clients, such as the trading of derivatives, fixed income, foreign exchange, commodity, and equity securities.

• Eg:
  – ICICI Securities
  – Barclays India
  – Kotak Investment banking
  – SBI Capital Market

7) Merchant Banks

• Banks which engaged in trade finance.

• Banks which provide capital to firms in the form of shares rather than loans.

• A merchant bank is a financial institution primarily engaged in offering financial services and advice to corporations and to wealthy individuals.
  – A bank that deals mostly in (but is not limited to) international finance, long-term loans for companies and underwriting. Merchant banks do not
provide regular banking services to the general public. Their knowledge in international finances makes merchant banks specialists in dealing with multinational corporations. Examples of such banks include, Tata Finance Merchant Banker Ltd, DSP Merrill Lynch Ltd, ICICI and IDBI.

8) Foreign Banks in India

Banks authorized by Govt. of India to operate in India. These counterparts helped in improving banking system in India. Examples of such banks includes Standard Chartered Bank, HSBC bank and ABN Amro Bank.

4.5 Recommendations of the Committee to Review Financial System 1991 (Narasimham Committee)\textsuperscript{97}

In August 1991, the Government of India appointed a committee to review the financial system under the Chairmanship of Sri M Narasimham, former Governor of the Reserve Bank of India to examine all aspects relating to the structure, organization and functioning of the financial system. The Committee’s report was tabled in Parliament on December 17, 1991.

The main recommendations of the committee were the following:

1. Phased reduction of Statutory Liquidity Ration (SLR) to 25 per cent over a period of five years.
2. Progressive reduction in Cash Reserve Ratio (CRR).
3. Phasing out of directed credit programmes and redefinition of the priority sector.
4. Deregulation of interest rates so as to reflect emerging market conditions.

5. Stipulation of minimum capital adequacy ratio of 4 per cent to risk weighted assets by March 1993, 8 per cent by March 1996, and 8 per cent by those banks having international operations by March 1994.

6. Adoption of uniform accounting practices in regard to income recognition, asset classification and provisioning against bad and doubtful debts.

7. Imparting transparency to bank balance sheets and making full disclosures.

8. Setting up of special tribunals to speed up the process of recovery of loans.

9. Setting up of Asset Reconstruction Fund (ARF) to take over from banks a portion of their bad and doubtful advances at a discount.

10. Restructuring of the Banking System so as to have three or four large banks which could become international in character, 8 to 10 national banks and local banks confined to specific regions and rural banks including RRBs confined to rural areas.

11. Setting up one or more rural banking subsidiaries by public sector banks.

12. Permitting RRBs to engage in all types of banking business.

13. Abolition of branch licensing.

14. Liberalizing the policy with regard to allowing foreign banks to open offices in India.

15. Rationalization of foreign operations of Indian Banks.

16. Giving freedom to individual banks to recruit officers.

17. Inspection by supervisory authorities based essentially on the internal audit and inspection reports.

18. Ending duality of control over banking system by Banking division and RBI.

19. A separate authority for supervision of banks and financial institutions which would be a semi-autonomous body under RBI.
20. A revised procedure for selection of Chief Executives and Directors on Boards of Public Sector Banks.

21. Segregation of direct lending functions of IDBI to a separate institution.

22. Obtaining resources from the market on competitive terms by DFIS.

23. Speedy liberalization of capital market by removing restrictions on premium dispensing with prior government approval, etc.

24. Supervision of merchant banks, mutual funds, leasing companies, etc., by separate agency to be set up by RBI and enactment of separate legislation providing appropriate framework for mutual funds and laying down prudential norms for such institutions.

The committee also recommended proper sequencing of reform of financial system.

**A critical review of the recommendations**

The possible impact of these diverse recommendations can now be studied:

a. The lowering of reserve rates will enable banks to enlarge their credit portfolio thus improving their profits.

b. Relaxation of regulations with respect to licensing will enable banks to open branches in potential centers freely, and as an incentive for better performance.

c. Deregulation of interest rates will enable a competitive environment to grow, and provide for efficiency of the Banking System.

d. Effective supervision of the Banking System through off-site surveillance and on-site supervision through the new wing of the Reserve Bank of India under Department of Supervision.
e. Prudential Norms to enable a better and transparent accounting system for the banks.

f. Setting up of recovery tribunals will help reduce the non-performing assets in the banking system.

g. Capital Adequacy Measures will strengthen the banking system.

In short, the recommendations are aimed at strengthening the banking system so as to enable it to take on its foreign counterparts ably in the wake of increasing globalisation and integration with the world economy.

Several recommendations have been accepted and implemented in a phased manner. Among these are the reductions in SLR/CRR, adoption of prudential norms for asset classification and provisions, introduction of capital adequacy norms and deregulation of most of the interest rates.

**Narasimham Committee- II**

This Committee is also called the “Committee on Banking Sector Reforms” and was appointed by Central Government and was headed by Shri M. Narasimham. This Committee submitted its report on 23.4.1988.

**Recommendations**

1) Three Tier Banking: There should be three types of banks: (i) Two or three large Indian Banks with international character; (ii) Eight or Ten large National Banks to take care of the needs of large/medium corporate sector, and (iii) Large or Local Area/ Regional Banks to serve local trade, small industry and agriculture.
2) Universal Banking: The distinction between Development Finance Institutions and commercial banks should disappear paving the way for universal banking. DFIs should also give working capital finance while commercial banks term loans.

3) Narrow Banking: Week banks whose accumulated losses and net NPAs exceed their capital funds can be rehabilitated by branding them as “Narrow Banks” (banks which restrict their operation to only certain activates).

4) Mergers: Merger among the banks to be encouraged especially among the strong banks to obtain “Force Multiplier Effect”.

5) Govt. Holding in Banks: Govt. holding in banks should be reduced to 33%. The Govt. should not disinvest its capital. The capital should be increased by market subscription to bring down the Govt. holding to 33%.

6) Capital Adequacy Requirement: The Capital Adequacy ratio should be increased from existing 8% to 9% by 2000 AD. And to 10% by 2002. (Since accepted) The start up capital for new private banks be increased.

7) Asset Classification: An account should be classified as NPA if interest or installment is not serviced for a period of 90 days.

8) Provision Requirement: Banks should make general provision of 1% on their standard assets.

9) Directed Credit: The directed credit should also encompass other areas of credit like food processing, fisheries, dairy etc.

10) Autonomy to Banks: Functional autonomy should be given to the banks. The appointment of M.D/Chairman should be left to the Board of the banks.

11) Recruitment Policy: The recruitment procedure and remuneration policies should be changed to attract specialized officers.
12) Other Recommendation:

(a) To revamp existing banking laws, particularly RBI Act, BR Act, SICA, etc;

(b) Setting up of ARC (Asset Reconstruction Fund for bank NPAs);

(c) Segregating regulatory & supervisory function of RBI;

(d) RBI should become a regulator and maintain arm’s length from banks. No RBI nominee in Boards of Banks;

(e) Autonomy Status for Board for Financial Supervision;

(f) Professionalization of Bank Boards;

(g) Thrust on technology upgradation.

4.6 Indian Versus International Banks

International banks are major players in the banking sector. Even though the previous year was affected by economic slowdown international banks still took the 1st place in the banking sector. HSBC is the world’s number one brand according to the banker. SBI stood at the 36th place from 58th place the previous year. There is no doubt that our Indian banking sector is improving but there still exists a gap between the performance of Indian and international banks.

There are various reasons and strategies adopted by them which contribute to the excellent performance of these international banks. They are as follows:

1) Customer centric: International banks treat its customer as king just like any other FMCG company treats its customers. They adopt the strategy of customization and differentiation of their products and services in order to have a competitive edge. They also segment the market and provide products and services that are most suitable to that particular segment.

They also provide high quality service which provides customer satisfaction.
2) **State-of-the-art technology:** Technology is a key driver in the banking industry, which creates new business models and processes, and also revolutionises distribution channels. Banks which have made inadequate investment in technology have consequently faced an erosion of their market shares. The beneficiaries are those banks which have invested in technology. Adoption of technology also enhances the quality of risk management systems in banks. Recognising the benefits of modernising their technology infrastructure banks are taking the right initiatives. It also helps in minimizing the number of intermediaries in the banking sector.

3) **Universal banking:** International banks have started providing all services under one umbrella. Customers are provided with wide variety of products and services under a single bank. The term is also called as universal banking or mega banks. Most foreign banks have become providers of all services under a single roof. This is done by mergers and acquisitions. For instance Bank of America acquired Merryll Lynch, Citigroup merged with Citicorp. This facilitates foreign banks the advantage of being 1 step ahead of Indian banks. ICICI bank is also a universal bank.

4) **Global network:** Foreign banks have their reach all over the world. Duetsche bank has its bank spread all over 76 countries. This also facilitates risk management as the losses arising due to a crisis in one country will be offset by the revenue generated from another country. It also leads to transfer of technology, information and know-how. HSBC has its bank ALMANAH (Islamic bank) in the Middle East specially designed for the people in that region and the bank carries out its operations by considering the culture and beliefs of Islam.
5) **Risk management techniques:** Foreign banks have adopted effective risk management strategies unlike Indian banks to face and overcome uncertainties to be faced in the future.

6) **Diversity strategy:** Deutsche bank has foreseen a problem of the future. They believe that the skilled and experienced staff will soon attain old age and there will be shortage of skilled people in future as a result of old age. Thus, they introduced equal number of young employees in order to facilitate flow of information, skill and knowledge from experienced employees to young employees. This will facilitate the presence of adequate number of skilled staff in future.

7) **High quality service:** Services rendered by international banks have higher quality standards when compared to Indian standards with respect to speed, time taken and so on. The efficiency level is higher than Indian banks and this in turn provides them with a higher edge compared to other banks.

Some steps to be taken by Indian banks to compete with international banks

1) **Application of advanced technology:** Indian banks will have to concentrate on adopting state-of-the-art technology and facilitate efficiency in performance and improve revenue by reducing cost. Technology helps in facilitating superior quality service to customers and this will be a competitive advantage to Indian banks.

2) **Capacity building:** As dictated by the changing environment, banks need to focus on appropriate capacity building measures, to equip their staff to handle advanced risk management systems, and supervisors also need to equally equip themselves with appropriate skills, to have effective supervision of
banks adopting those systems. In the likelihood of a high level of attrition in the system, banks need to focus on motivating their skilled staff and retaining them. Skill requirements would be significantly higher for banks planning to migrate to the advanced approaches under Basel II. Capacity building gains greater relevance in these banks, so as to equip themselves to take advantage of the incentives offered under the advanced approaches.

3) **Enhancing corporate governance:** The issues related to corporate governance have continued to attract considerable national and international attention in light of a number of high-profile breakdowns in corporate governance. This becomes all the more relevant for banks since they not only accept and deploy large amount of uncollateralized public funds in fiduciary capacity, but also leverage such funds through credit creation. Banks are also important participants in the payment and settlement systems. In view of the above, legal prescriptions for ownership and governance of banks in Banking Regulation Act, 1949 have been supplemented by regulatory prescriptions issued by RBI from time to time.

4) **Basel II implementation:** Basel II implementation is widely acknowledged as a significant challenge faced by both banks and the regulators internationally. It is true that Basel II implementation may be seen as a compliance challenge. While it may be so for some banks but on the other hand Basel II implementation has another dimension which offers considerable opportunities to banks viz., refinement of risk management systems; and improvement in capital efficiency.

5) **Comprehensive risk management:** Under Basel I banks were focused on credit and market risks. Basel II has brought into focus a larger number of risks requiring banks, to focus on a larger canvas. Besides the increase in the number of risks, banks are now beginning to focus on their inter-linkages with
a view to achieve a more comprehensive risk management framework. Basel II implementation, therefore, is being increasingly seen as a medium through which banks constantly endeavor to upgrade the risk management systems to address the changing environment. Further, in the initial stages, banks were managing each risk in isolation. It is no longer adequate to manage each risk independently. Enterprises worldwide are, therefore, now putting in place an integrated framework for risk management which is proactive, systematic and spans across the entire organization. Banks in India are also moving from the individual silo system to an enterprise wide risk management system. While the first milestone would be risk integration across the entity, banks are also aware of the desirability of risk aggregation across the group both in the specific risk areas as also across the risks. Banks would, therefore, be required to allocate significant resources towards this endeavor.

6) **Capital efficiency**: Basel II prescriptions have ushered in a transition from the traditional regulatory measure of capital adequacy to an evaluation of whether a bank has found the most efficient use of its capital to support its business i.e., a transition from capital adequacy to capital efficiency. In this transition, how effectively capital is used will determine return on equity and a consequent enhancement of shareholder value. In effect, banks may adopt a more dynamic approach to use of capital, in which capital will flow quickly to its most efficient use. This revised efficiency approach is expected to guide the return-on-equity strategy and influence banks’ business plans. With the extension of capital charge for market risks to the AFS portfolio this year and the coming into force of Basel II norms in March 2007, banks would need to shore up the capital levels not only for complying with these requirements but also for supporting the balance sheet growth. With a view to enhancing the options available to banks for augmenting their capital levels, the Reserve
Bank has recently permitted banks to issue new capital instruments, including perpetual instruments. A notable feature of these instruments is that these are designed to help banks in not only managing their capital effectively but also efficiently.

7) **Universal banking:** Indian banks will have to adopt strategies like joint ventures, mergers and acquisitions in order to provide all services of banking under one roof.

8) **Global network:** A global network of Indian banks will have to be established. Global presence helps in capturing new markets, new customers and increase in revenue and efficiency in performance. Differentiation and customization can be used as strategies to capture the global market. A wider reach of market will minimize risk and increase productivity.

Federation of Indian Chambers of Commerce & Industry (FICCI) annual survey 2010 on the Indian banking system: the current state and road ahead. As the world witnessed the global financial meltdown, the Indian banking sector is one of the few to maintain resilience and continue to provide growth opportunities. FICCI conducted a survey on the Indian banking sector to assess the competitive advantage offered by the banking sector and the policies and structures required to further stimulate the pace of growth. The major strengths identified were the regulatory system, economic growth and the relative insulation from external market. The study also concluded that public sector banks and private sector banks view difficulty in hiring highly qualified youngsters as the major threat to their HR practices ahead of high staff cost overheads, poaching of skilled quality staff and high attrition rates.

---

The banking sector demands a unique set of HR strategies. These strategies are needed to ensure that the people of the organization are managed carefully just as their client’s finances. HRM in the sector needs to embrace cutting edge strategies for restructuring, recruiting and rewarding its human capital. The uniqueness lies in the fact that intangible assets like human resources are needed to effectively deliver outstanding services in this service oriented industry.

Table – 4.1: Turnover (deposits and advances) Per Employee (Rs. In Lakhs)

<table>
<thead>
<tr>
<th>Year</th>
<th>SBI and associate Banks</th>
<th>Nationalised Banks</th>
<th>Private Banks</th>
<th>Foreign Banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990-91</td>
<td>38.49</td>
<td>40.22</td>
<td>27.37</td>
<td>145.32</td>
</tr>
<tr>
<td>1991-92</td>
<td>42.99</td>
<td>44.10</td>
<td>35.42</td>
<td>199.49</td>
</tr>
<tr>
<td>1992-93</td>
<td>47.28</td>
<td>48.23</td>
<td>43.50</td>
<td>233.03</td>
</tr>
<tr>
<td>1993-94</td>
<td>49.61</td>
<td>50.96</td>
<td>55.31</td>
<td>286.39</td>
</tr>
<tr>
<td>1994-95</td>
<td>56.59</td>
<td>60.09</td>
<td>73.73</td>
<td>328.19</td>
</tr>
<tr>
<td>1995-96</td>
<td>65.67</td>
<td>67.63</td>
<td>100.45</td>
<td>379.53</td>
</tr>
<tr>
<td>1996-97</td>
<td>72.51</td>
<td>76.87</td>
<td>131.41</td>
<td>450.79</td>
</tr>
<tr>
<td>1997-98</td>
<td>84.43</td>
<td>91.90</td>
<td>168.37</td>
<td>484.22</td>
</tr>
<tr>
<td>1998-99</td>
<td>102.45</td>
<td>107.44</td>
<td>193.05</td>
<td>502.75</td>
</tr>
<tr>
<td>1999-00</td>
<td>122.11</td>
<td>126.15</td>
<td>255.23</td>
<td>632.15</td>
</tr>
</tbody>
</table>

The above table clearly shows the difference in the performance of Indian banks compared to foreign banks. As all banks perform almost same functions it becomes very difficult to differentiate in core activities. But banks can concentrate on differentiating through use of their Human resources. The banking sector demands a unique set of HR strategies. These strategies are needed to ensure that the people of the organization are managed carefully just as their client’s finances. HRM in the sector needs to embrace cutting edge strategies for restructuring, recruiting and rewarding its human capital. The uniqueness lies in the fact that intangible assets like human resources are needed to effectively deliver outstanding services in this service oriented industry.
With a view to bring in more objectivity some public sector banks have designed a new Performance Appraisal System for Managers. The new system of self-evaluation has been incorporated according to which appraisee and appraiser identifies the key performance areas along with the specific function. Evaluation is done on the basis of employees’ contribution or efforts with respect to these areas and the progress made.

The modified performance appraisal system was intended to lead to all-round development of employees. Attempt to reassess staff requirement, optimum utilization of available manpower, was considered as priority. There has also been a strategic change in staff development, by relating it to workload, with a view to increasing staff productivity, at branches and administration offices.

In order to boost the motivation of employees and urge for individual development the banks undertook several measures and also continued efforts through a series of educative literature and providing appropriate forums for skill identification. Classroom as well as on-the-job training continued to be strongly emphasised in human resource development strategy of almost all the banks in public sector.

Banks were forced to rethink about employee engagement. They soon relaised that HRD is more than training programmes. Training of employees is only one component of HRD. Therefore, other aspects of the HRD system, like, performance appraisal system, job rotation, career path plan and organisation development, etc., have also, come into practice.
A distinguished panel of Managing Directors and CEOs of some well-known banks in the country presented their views on the challenges and opportunities faced by the banking sector. One of the relevant points noted by them is the HR related issues which include career planning, VRS, compensation, empowerment of employees and training. Following are the HR issues and challenges identified in the banking sector.

**Human Resource Risk**

When employees with specialized skills and knowledge resign or retire, they bring certain systems to a halt. This is called as HR risk. To ensure protection against this risk, banks may have to recruit and pay the same salary to individuals with similar knowledge and experience. Thus getting a replacement talent is very difficult.

**Empowerment and motivation**

Employees become committed to their job through involvement, empowerment and delegation of authority. The complex and competitive scenario in banking calls for developing highly committed and motivated employees who aim to achieve their organizational goals. Unfortunately banks have not developed a culture of motivation and empowerment. This makes the process of change difficult.

**Building efficiency**

One of the crucial factors behind success in banking are a continued and sustained buildup of education, attitudes, skills and knowledge among the employees, particularly the frontline staff, working in the bank branches. This can be achieved through professionalization, which is an integral part of HRM. This would enhance their personal growth and also contribute to the organization’s success. Efficiency can be built by the HR department by adopting best selection practices.
Sarkar & Das compared performance of Public Sector Banks, Private Banks, and Foreign Banks for the year-1994-95 on their profitability, productivity & financial management.\textsuperscript{99} They found that Public Sector Banks compare poorly with the other two categories of banks. Ram Mohan’s study covers a recent period, 1996-97 to 1999-2000, he found that over these years the profitability of the Public sector Banks did improve in comparison to the Private and Foreign Banks, but they have lagged behind in their ability to attract deposits.\textsuperscript{100} Inability to upgrade technology platform, inability to improve staffing and employment practices, which may have negative implications on their profitability.

\section*{4.7 Human Resources Perspective}

Public sector banks play a dominating force in the Indian banking system has lacked a proactive HR environment. However, much has changed with the opening of other sectors and increased competition from newer banks in the system. Banks are increasingly beginning to recognize Human resources as a possible area of core competence, and seek to pursue and retain the best talent in the industry. Federation of Indian Chambers of Commerce & Industry (FICCI) conducted its annual survey in 2010 on the Indian banking system which revealed the following.

There is a realization that skill development is extremely important for staff retention as well as the quality of manpower, and all respondents to our survey had in place a system of continuous professional learning. A few respondents were in the process of revamping their training processes and emphasis is being laid on hard as


well as soft skills. Banks are keen to tie up with external training agencies for in-house training. Some have even roped in top universities and business schools to help them in their initiative, while others have their own staff colleges for training employees. Survey results shows that 81.25% feel that the current economic situation is in fact advantageous for them, as it provides them with access to quality manpower. 62.50% of banks participated in the survey also feel that they have sufficient autonomy to offer attractive incentive packages to employees to ensure their commitment levels.

Fig. 4.1 : HR Threats for Public Sector Banks

(source: Federation of Indian Chambers of Commerce & Industry (FICCI) annual survey 2010 on the Indian banking system: the current state and road ahead.)

Thus, on the whole, we see that Public Sector Banks, Private Sector Banks as well as Foreign Banks view difficulty in hiring highly qualified youngsters as their biggest HR threat ahead of high staff cost overheads, poaching of skilled quality staff and high attrition rates.101

Another approach for improving efficiency of banking sector in India is through consolidation of operations. As this consolidation is an important factor to achieve the level of efficiency and profitability. Consolidation is expected to ensure technological progress, excess retention capacity, and deregulation of various functional and product restrictions.

Organisational career management is a comprehensive approach to all activities and techniques facilitated by the organization concerned with the career development of employees. HR is issues in the banking sector includes bank’s tendency to generalize skills and expertise in handling banking operations, lack of objective measures of individual performance, transparency in HR policies, and core competence development.

Most of the public sector banks have employees with 30-35 years of service. As the competition in the banking sector grew, new generation banks started offering host of new products and services. Public sector banks started hiring young people who could market new products.

People play an important role in a service organization. There is a need to consider them as important. More the process relays on human resource more it poses threat in terms of attracting, managing, developing and retaining talented employees. Thus human resource threat is becoming inevitable year after year. This is more so in the middle management levels and branch head levels. Human resource departments in the banks are evolving, from the routine recruitment; training, transfer and firing to it need to transform the same through motivation and empowerment. Human resource departments need to consider the frustrations of middle managers, otherwise they may lose their valuable intangible assets.

Above arguments prove that there is potential human resource threat to Indian banking system. It is understood that for years human resource played the traditional role of hiring, firing, transfers and training. There is need for intervention in human resource issues of bank. It is also seen that banks lack policies to address career and work related issues. Inadequate career advancement policies have forced managers to the verge of crisis. There is a need to address these issues urgently. The above features of human resource issues in banks make this industry an apt case for addressing issues concerning Mid-career crisis.