CHAPTER-III

Indian Banking Industry

India is among the most robust economies of the world on date. At the moment it is burgeoning to step up the recently achieved growth and development. This optimism in the economy is being consolidated by the increasing confidence of foreign investors in this country. In every nook and corner of the business world, India is the buzz world. Indian economy is now being treated as the next big thing in the world of business and commerce. This emergence of India as a robust economy has prompted the MNCs to come and invest in this country. Result, almost in every sector of the economy the presence of the multinational is being felt. But this development in way has demoralized the Indian industrialists. These are now coming back with vengeance.

In the last decade or so one sector which is the fastest growing in the country is service sector. Now it has taken over other basic sectors such as agriculture and manufacturing. Even in the service sector, the maximum change has been witnessed by IT, ITES, Tourism and Banking and financial services.

According to the World Development Indicators 2003 released by the World Bank, India's services sector registered an average 7.9% growth per annum between 1990 and 2001 against 6.9% between 1980 and 1990 beating the global rate of 3.1%. India's services sector has emerged among the top five fastest growing in the world during 1990-2001.

A view of India's banking industry

India's banking industry is one of the major beneficiaries of the country's
ascendant economic power. Improving consumer purchasing power, coupled with more liberal attitudes toward personal debt, is fueling India's explosive banking segment. Global banks should be encouraged further by the relatively underpenetrated status of the country's various retail lending segments. The retail market for mortgages, credit cards, automobile loans and other consumer loans has jumped from its 1999 total of US$9.7 billion to approximately US$36.0 billion in 2004. Even with this strong performance, significant opportunities for continued retail lending growth remain as retail lending figures lag India's regional peers.

Unlike most rapidly-expanding, emerging markets, India's banking sector has exhibited financial stability and a trend toward improved governance under the management of its central bank, the Reserve Bank of India (RBI). One challenge the RBI had to contend with was the legacy of policy-directed, corporate lending by the state-owned banks that had produced high levels of non-performing assets (NPAs). Through structural reform, remedial legislative actions, and favorable returns from the fixed income Treasury Markets, Indian banks have cut gross NPA levels from 15.7 percent in 1997 to 8.8 percent in 2003. Fortunately, new entrants to the market are not subjected to the same mandatory lending requirements as domestic banks and can therefore "cherry-pick" the most desirable clients, allowing them to lower their own risk of NPAs through more rigorous risk management strategies.

Global banks in India: Gaining a foothold
The competitive environment in India presents both challenges and
opportunities to global banks seeking market entry. Entrenched domestic competitors and restrictive equity ownership ceilings imposed by the government create obstacles for banks establishing a foothold in India. Primary challenges include tough competition and government ceilings on foreign equity ownership. Opportunities exist because global banks often have technological advantages, well-honed, efficient processes and appealing products and services.

For the most part, global banks must execute on an organic growth strategy to expand their footprint in India. Merger and acquisition activity in the banking sector remains limited by government regulation. This is difficult news for global banks that have relied on acquisitions as a market entry or expansion strategy. Unless the government shifts its posture on foreign equity ownership, global banks will have to rely on organic growth to expand their presence in India.

Let’s find out the status of retail banking in the country -

**Retail Banking in India:**

With a jump in the Indian economy from a manufacturing sector, that never really took off, to a nascent service sector, Banking as a whole is undergoing a change. A larger option for the consumer is getting translated into a larger demand for financial products and customisation of services is fast becoming the norm than a competitive advantage. With the Retail banking sector expected to grow at a rate of 30% [Chanda Kochhar, ED, ICICI Bank] players are focussing more and more on the Retail and are waking up to the potential of this sector of banking. At the same time, the banking sector as a
whole is seeing structural changes in regulatory frameworks and securitisation and stringent NPA norms expected to be in place by 2004 means the faster one adapts to these changing dynamics, the faster is one expected to gain the advantage.

**Potential for Retail in India:**

The Indian players are bullish on the Retail business and this is not totally unfounded. There are two main reasons behind this. Firstly, it is now undeniable that the face of the Indian consumer is changing. This is reflected in a change in the urban household income pattern. The direct fallout of such a change will be the consumption patterns and hence the banking habits of Indians, which will now be skewed towards Retail products. At the same time, India compares pretty poorly with the other economies of the world that are now becoming comparable in terms of spending patterns with the opening up of our economy. For instance, while the total outstanding Retail loans in Taiwan is around 41% of GDP, the figure in India stands at less than 5%. The comparison with the West is even more staggering. Another comparison that is natural when comparing Retail sectors is the use of credit cards. Here also, the potential lies in the fact that of all the consumer expenditure in India in 2001, less than 1% was through plastic, the corresponding US figure standing at 18%.

**Competitiveness of the industry players:**

The fact that the statistics reveal a huge potential also brings with it a threat that is true for any sector of a country that is opening up. Just how
competitive are our banks? Is the threat of getting drubbed by foreign
competition real? To analyze this, one needs to get into the shoes of the
foreign banks. In other words, how do they see us? Are we good takeover
targets?

Going by international standards, a large portion of the Indian population is
simply not “bankable” – taking profitability into consideration. On the other
hand, the financial services market is highly over-leveraged in India.
Competition is fierce, particularly from local private banks such as HDFC
and ICICI, in the business of home, car and consumer loans. There, precisely
lie the pitfalls of such explosive growth. All banks are targeting the fluffiest
segment i.e. the upwardly mobile urban salaried class. Although the players
are spreading their operations into segments like self-employed and the
semi-urban rich, it is an open secret that the big city Indian yuppies form the
most profitable segment. Over-dependence on this segment is bound to bring
in inflexibility in the business.

**IT in Indian banking**
Indian banks have a chequered history. The British legacy left behind a host of large and small privately-held banks. The late 60s saw the nationalisation of banks, leading to the emergence of the public sector banks. The 90s saw the banking industry embracing technology in a massive way, led in particular by the new private banks and MNC banks. Among these series of technology innovations, Internet banking for the retail segment is a recent phenomenon that has generated a lot of interest in the Indian banking industry. Private and foreign banks have been the early adopters while the PSU banks are also beginning to latch on to the bandwagon.

As per IDC estimates, the total number of registered users for Internet banking in India is over two million. But this figure needs to be adjusted for dormant users and multiple accounts (a user having accounts with more than one bank). India has a little less than a million active Internet banking users. And though this is just 0.096 percent of the total population, it represents 15 percent of the India's Internet user population. Thus indicating that the concept of Internet banking is surely catching on.

Impressive as these figures might be, the truth is that India lags behind other countries in Internet banking. In the US, the number of commercial banks with transactional websites is 1,275 or 12 percent of the total number of banks. Of these, seven could be called 'virtual banks.' Ten traditional banks have established Internet branches or divisions that operate under a unique brand name. At present, in the US approximately 78 percent of all commercial banks with assets more than $5 billion, 43 percent of banks with $500 million to $5 billion in assets, and 10 percent of banks under $500 million in assets have transactional websites.

From the Asian market experience, it is clear that Internet banking is here to
stay and will be a major channel to acquire and service customers. Markets like Korea and Singapore have nearly 10 percent of their population banking over the Internet. Though, these markets are way ahead of India both in terms of Internet penetration and online banking penetration, India is a big potential market and is fast catching up with its Asian counterparts.

Financial services have been the major users of IT and communication technologies. IT expenditure by US banks has recorded a compounded annual growth rate of over 8.7 per cent. The management information system (MIS), BANKNET communication network for inter-bank & intra-bank services, distributed computing devices, open systems, high-speed data networks (LAN, MAN, WAN, ISDN, etc.), related database management services (RDBMS) have been important development milestones in IT with major impact on financial services.

The development of optical fibre has greatly improved the communication speed, anticipated to touch 2 trillion bits per second eventually. Packet switching transmission method like asynchronous transfer mode achieving a speed upto 622 million bits per second has been the major breakthrough in communication technology. CD-ROMs with a storage capacity of 1.6 GB of data have been instrumental in fast information retrieval and access. Use of multimedia for storage of text, graphics, video, sound, etc. has immensely benefited the information storage system. All these technologies are used extensively by the banking and financial services sectors. The following are the emerging IT systems related to financial services:

**Automated Teller Machines (ATM)**

ATMs, though operational in the country for quite some time, are expected to make a big headway in India. It has been estimated there are around
400,000 ATMs worldwide out of which 100,000 are located in Japan alone. The latest generation networked ATMs allow the user to perform up to 150 kinds of transactions ranging from simple cash withdrawals and deposits, to fund transfer to trading in stocks to buying mutual funds to something mundane like payment of electricity bills, booking air-tickets and making hotel reservations.

ATMs are synonymous with credit cards; 578 million credit cards issued worldwide were involved in a transaction of over US $ 1092 billion by June 1993. India is poised to become one of the world's largest credit card users by 2000 AD.

'Virtual' Bank

Multimedia technology has been quite effective in bringing the banking services to the doorstep of its customers. The customer activated terminal (CAT) or Kiosk is an interactive multimedia display unit, housed in a small enclosure, typically consisting of a computer workstation, monitor, video-disk player and a card reader. It allows the customers to browse through information and use the available banking services at their own speed. Some banks are thinking of establishing 'virtual' branches where a customer can walk through the door, explore services by touching parts of the screen and at any time call up a member of the bank/office staff by video conferencing. While the banks do not need to invest heavily in real estate for setting up such a branch, the customer gets the benefit of 'one-stop banking' at a convenient location.

Home Banking

Smart phones with screen built-in modems and programmable microprocessors let the customer access a variety of financial services from
Electronic Funds Transfer at Point of Sale (EFTPOS)
While travellers' cheques meant 'pay-now-buy-later' and credit cards had 'buy-now-pay-later' advantages, EFTPOS or debit cards signify 'buy-now-pay-now' but without cash transaction. The user presents his ATM card when he buys goods and the EFTPOS system immediately debits his bank account.

Smart Cards
The 'Processor' type smart cards with in-built integrated circuits (ICs) or microchips offer a wide range of transactional opportunities even from remote areas. The smart cards are extensively being used for employee 'clocking in', withdrawing cash from ATM, using pay-phones, payment of various bills, etc.

Electronic Data Interchange (EDI)
EDI typically denotes paperless financial transactions across the locations. EDI is fast becoming the norm for inter-company transactions and also for procurement of boughtout items from the suppliers. The companies can now operate their bank accounts through corporate banking terminals in their own offices, which are linked to the bank computers. Companies can thus carry out transactions like transferring funds, managing its cash flow, opening letters of credit, etc. without any paper work. Singapore has established trade net to facilitate electronic submission of trade documents by traders to various Government agencies and the response of these agencies to the sender. It has reduced document processing time from one day to 15-30 minutes and the estimated saving are of the order of $ 1 billion annually.
**Image Processing**

As financial services including capital markets and banking are highly document intensive, image processing technology can have a far reaching impact for such applications for its 'Less paper' handling characteristics. In banks, image technology could be used for automatic identification or character recognition to read text and diagram wherein the cheques or documents can be scanned.

**Expert System**

The financial services sector is increasingly using decision support systems (DSS) or expert systems for functions such as credit risk appraisal, forecasting loan delinquencies, investment decisions, etc. One of the most promising developments in this field is the use of 'neural network' approach to build an expert system, which lets the software literally learn from example and experience. Several banks today are using neural network programme to detect credit card fraud. It is also being used by some leading investment banks to track stock price patterns and predict their movements.

**The Indian saga**

In contrast, Indian banks have an insignificant Internet banking record. ICICI Bank kicked off online banking way back in 1996 and a host of other banks soon followed suit. But even for the Internet as a whole, 1996 to 1998 marked the adoption phase, while usage increased only in 1999—due to lower ISP online charges, increased PC penetration and a tech-friendly atmosphere. Reveals Anup Bagchi, head, Internet Banking, ICICI Bank, "We had launched the Internet banking service even before the RBI had formulated its guidelines. Fortunately, as it was a comparatively new
concept, the regulating authorities were extremely co-operative with us.”

After ICICI, Citibank, IndusInd Bank and HDFC Bank and Timesbank (now part of HDFC Bank), were the early ones to bite the technology bullet in 1999. Says C N Ram, head, information technology, HDFC Bank, “Our vision was very clear, we were not enamoured by the concept of Internet banking but looked at it more as an add-on service which our customers should gradually adopt.” In line with this strategy, initially the Net banking facility was provided in order to meet the information requirements of the customers and gradually it ventured into fund transfers and third party transfers.

Though adoption of Internet banking by Indian banks and their customers would not set the Arabian Sea on fire, no one can deny the obvious benefits that this service offers. Costs of banking service through the Internet amount to a fraction of the costs through conventional methods. Industry estimates assume teller cost at Re 1 per transaction, ATM transaction costs at Re 0.45, phone banking at Re 0.35, debit cards at Re 0.20 and Internet banking at Re 0.10 per transaction. Says V K Ramani, president, information technology, UTI Bank, another of the early adopters, “No wonder, the cost-conscious banks in the country are now actively considering using the Internet as a channel for providing services. People were sceptical about even ATM at the beginning, but look how it has picked up today.” However, he warns that banks cannot expect instant returns, unless the Internet population itself does not reach a critical mass. Besides, he also feels that fully computerised banks, with better management of their customer base are in a stronger position to cross-sell their products through this channel.

Nitin Chopra, head, consumer banking, ABN-AMRO Bank, feels that the
prohibitive costs of real estate would always make Internet banking a much more viable option in the long run than physical banks. In today’s environment besides their physical branches, banks need to grow non-branch delivery networks as a part of their growth strategy. ATMs are currently the hot favourite for most banks, but Internet banking definitely has the potential to leave the rest behind. Therefore, on the whole, Internet banking increases operational efficiencies and reduces costs, besides giving a platform for offering value added services to the customer, thereby fulfilling all the essential prerequisites for a flourishing banking industry.

The PSU lethargy

As in all forms of technology innovations, PSU banks have remained laggards in the race for adopting Internet banking practices. There are very few nationalised banks like State Bank of India, Bank of Baroda, Allahabad Bank, Syndicate Bank and Bank of India, that offer Internet banking services. Some others like Union Bank of India, Canara Bank and Punjab National Bank are on the verge of doing so. SBI’s Internet banking initiative, launched in July 2001, is in fact doing quite well and has over 18,000 registered customers across 150 branches. The enthusiastic response has encouraged the SBI management to extend the service to an additional 500 branches. But despite positive news like this, PSU banks still have a lot of catching up to do on the Internet banking services front.

DD Krishnamoorthy, deputy general manager, information technology, Bank of India says that the primary reason preventing PSU banks from introducing online banking services, has been the absence of a legal framework to back up, and regulate Internet banking operations in the country. Though the Information Technology Act 2000 attempted to address
a number of e-commerce regulatory issues, he feels that there still are several grey areas which have neither been spelt out properly, nor have the courts suggested workable modes of implementation. Though Internet banking is only an extension of traditional banking services, there are several instances which contradict the legal framework for this banking in India provided by a set of enactments like the Banking Regulations Act, 1949, the Reserve Bank of India Act, 1934 and the Foreign Exchange Management Act, 1999.

However, not many are willing to buy the argument that it's the lack of regulations that is preventing the PSU banks from taking the Internet plunge. Says an industry analyst, “More than a lack of regulatory framework, it is lack of zeal and a mindset attuned towards resisting any new technology that is holding back the nationalised banks. On top of this, the highly politicised unions are also an impediment as they feel that Internet banking would expose the low productive levels of the workforce.”

The average customer profile of PSU banks is also comfortable with the traditional banking system and is not too keen on adopting an online model. Typically, most PSU banks have the majority of their customer base in the smaller cities or towns and even in remote villages. Even in bigger cities, a large proportion of their customers are either senior citizens or at least 50+ who have a natural aversion towards adopting new technology. This not the case with private or MNC banks, where the clientele is mostly urban-based falling in the 20-40 age group and who have a higher exposure to technology.

Even the IDC survey seems to confirm this premise. Among the elite Internet banking users, that is, those customers who belong to Socio-
Economic Class A1 (SEC A1) in the top five cities, it has been found that people access their account through the Internet once every week. Similarly users visit their ATM centre on an average of two times per week. The workplace happens to be the most favoured place to access Internet for banking purposes. The home comes a close second while cybercafes take the third place. ATM in the close vicinity to the office is the most preferred place among users for banking. The users (24 percent) who access the ATM near their office mostly go during the first half of the day, between 9 AM to 12 PM, but most preferred time by all users (41 percent) is between 6-9 PM.

**Bouquet strategy**

This probably explains why more and more banks are looking at Internet banking as another attractive addition to their bouquet of delivery channels. At least in urban areas, ATMs are already fast becoming the most popular mode of banking, while phone banking and mobile banking are also on the upswing as the user base grows. Internet banking now seems to be the perfect model to complement the whole system. Says Ram, “In fact, currently telephone banking is much more popular than Internet banking. But we at HDFC Bank are working on a strategy to integrate various channels like the telephone, ATM, Internet, mobile, branches, etc. Customers have real-time access in all wherein any action in any of the above mentioned channels would be immediately reflected in the account of the account holder.”

All these initiatives taken by banks are part of their channel diversification strategy, where they intend to put the strategy matrix in place. This will be done through sprucing up the channel strategy in depth and width in which width would mean the various varieties of channel and depth would mean
the value added services in each channel. Adds Ramani, "We can divide the user group into 50 percent that would not prefer transacting through the Internet, 25 percent that are open to the idea, and the other 25 percent that are the ones who can be given credit to popularise the use of Internet for transaction purposes."

What is ultimately emerging is that though there is certainly a high level of importance attached to Internet banking, it is at present not necessarily a priority for all banks. As far as banks are concerned, migrating customers to any self-directed channel is the main goal. However, the future of banking will be one in which customers can address most of their needs through self-directed means and the key differentiator will be how effective a bank is in getting its customers online and deriving measurable value from this presence. One can sum up the whole Internet banking scenario with the adage, "For while winners may not see massive gains, the losers will fade from view as their ability to compete is eroded with every mouse click."

**India's Net banking almanac**

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**Challenges and opportunities in future:**

Today, our financial system is rapidly changing. Some of the features of this change are:

- Increasing sophistication of capital markets
- Emergence of global investments
- Industry consolidation
- Heightened focus on customer relations
- Proliferation of new players entering the market

In this milieu old methods of intermediation will not serve the purpose. However, it has been empirically proved that every problem is an opportunity in disguise.
Indeed, Mieko Nishimizu of the World Bank feels "India has the capacity to become the heart of Asia's economic dynamism." Some figures bear out his observation.

India's financial savings rate compares favourably with those of other emerging market economies: Argentina 81%, Mexico 68%, India 93%. However, private credit to GDP in our country is only 36% whereas it is 130% in China and Korea and 145% in Malaysia.

An efficient financial sector is an engine for economic growth. It converts the fuel of savings into kinetic energy for the economy. The Banking industry which is at the core of the financial sector must take the lead. The reform process started in the 90's has given the industry a great opportunity. Not only must the sector become more efficient it must also indentify sectors having growth opportunities and devise strategies to move savings into these sectors. With very few greenfield industries on the financial horizon there is an urgent need to look at new sectors.

**Need for innovation in Indian banking:**

Innovating for the Services Sector will pose a unique challenge to the Banking industry. Yet, the process of product innovation will not, in essence, be substantially different from the process of innovating any other financial product. Banks aspiring to product innovation leadership must ensure that they have the appropriate customer knowledge, technology, processes and organizational enablers. Implementation requirements will include delivery channels, more powerful processing capabilities and ability to seamlessly link various processes.

Peter Drucker has been quoted as arguing that one of the reasons the financial services industry was in trouble was that there had been no
innovations in the industry since the 1970s. In contrast, he said, the years 1950 to 1970 brought in one innovation after another. Faced with three options to continue to do what the industry did traditionally but faster, allowing outsiders to grab parts of the market and innovating by itself, the third choice was the only option he stated. Innovation he pointed out, did not require creativity at all - all it called for was the capacity to work hard. He cited the example of the rapidly growing affluent and aging middle class in developed and emerging countries. While individual purchases by this segment are relatively modest, the sums they collectively pour into investments "dwarf by several orders of magnitude everything all the world's super rich together have available.."

OPPORTUNITIES FOR INNOVATION

The growth in the Services Sector will bring to the fore another segment of consumers with large disposable incomes, thus presenting the Banking industry with another growth opportunity.

In all likelihood, we will see another phenomenon. Medium sized businesses, points out Drucker dominate all economies - whether developed or emerging. These companies, in terms of products, technology, marketing and customer service they usually have the needed critical mass. But in financial management many, perhaps most, do not have the size to support the competence they need. They operate with woefully low productivity of capital and have either too little or too much cash. Many of these companies outsource their data processing and information systems, their housekeeping and even their personnel management. Their decision to outsource the
management of their finances is waiting only for a service provider. This is another great opportunity for the banking system.

**TOOLS FOR INNOVATION**

The tools for doing this work are fully developed eg. EVA or cash flow forecast and cash management. The task is made easier by the fact that the financial management needs of such companies are easily understood and addressed. Banks could benefit not only from the fees but also through substantial profits from "securitising" the financial needs of such clients.

**INNOVATION AND DELIVERY SYSTEMS**

The Bank of America: A success story

It has now become a truism that the Banking system cannot do away with the branch for the purposes of delivery of products and services. Whatever be the form it takes, the branch is here to stay. Any product however, well it is designed must ultimately stand the test of being delivered to the customer. The eternal challenge for the designer is to anticipate how the dynamics of the market where the product is actually delivered to the customer will change the requirements of the customer calling for addition or deletion of features in the product. By the time feedback is received it is quite often too late: the customer has already voted with his feet. With regard to Banking the situation is even more complicated by the fact that some of the most important features of the product are

(a) The manner in which it is delivered and
The ambience in which it is delivered. Both these features can drastically enhance or depreciate any other feature that the product may have.

In this background the experiments conducted by Bank of America in Atlanta are worth examining. The bank decided to take an unprecedented step: it would create an "innovation market" within the bank's existing branches.

One of the most interesting features of the experiment was the Bank's decision to prepare the physical infrastructure at the branches before experimenting with innovation. Twenty branches of the Bank were reconfigured into three alternative models: five were redesigned as "express centers"; efficient, modernistic buildings where consumers could quickly perform routine transactions such as deposits and withdrawals. Another five were turned into "financial centers" spacious, relaxed outlets where customers would have access to trained staff and advanced technologies required for sophisticated services such as stock trading and portfolio management. The remaining ten branches were configured as "traditional centers" familiar looking branches that provided conventional banking services though often supported by new technologies and redesigned processes.

The innovation process evolved at Bank of America has five stages

1. **Evaluate ideas**

   a) conceive ideas
b) assess ideas
c) prioritize ideas

2. Plan and Design

a) Assign and scope
b) Complete the design
c) Build rollout plan

3. Implement

a) Develop Test Plan
b) Implement idea

4. Test

a) Monitor performance
b) Report Results
c) Improve process

5. Recommend

a) Complete recommendation
b) Review and approve
c) Communicate Recommendation
These processes were rigorously monitored and controlled by formulating a three point formula for implementation at every stage:

a) Desired outcome (b) Success factors (c) Key measures

Through this process the Bank appears to have made a break through by bringing the product innovation process into financial services. Systematic experimentation has been at the heart of all innovation. Advances in services have not kept pace with advances in products because experimentation in a live setting entails particular challenges. This experiment has proved that these challenges can be met and addressed. This paper is ended on this note because it is yet another example of how the banking industry is able to adapt and innovate to every type of challenge

**Technology: A strategic resource:**

Banking in the 21\textsuperscript{st} century has become technology driven to become customer driven. Off late banks have been using technology to reduce cost and enhance efficiency, productivity, and customer convenience. Technology intensive delivery channels like – Net Banking, ATMs, tele-banking, Mobile banking etc have created a win-win situation by extending great convenience and multiple options for customers while providing tremendous cost advantages at banks in India.

The state of technological updation at a bank can act as a strategic resource for Indian banks. To begin with it was a case of haves and have-nots, but now everybody in the industry have computerization at banks. But if a bank embraces latest technological advances it can again create a sizable difference from its competitors.

Technological upgradation at any bank provides following strategic advantages –

1. Cost Competitiveness: Any bank which is using computers at banks can reduce the size of its man power, thereby reducing cost. Again the speed of work also increases with computers, which further leads to speedy processing of transactions.

2. Productivity enhancement: If any bank embraces IT, there are great chances of productivity improvement as the speed per transaction improves. For every man hour a particular bank may get more productivity.
3. Technology as a differentiator: Technology induction also creates a differentiation among the existing banks as a bank which has got latest technology, would provide better experience to the customers of that bank. For instance the banks which have the facility of net banking are clearly differentiated from others.

Public sector banks are not behind

Contrary to conventional wisdom public sector banks are not far behind the private banks, and in a number of cases they fare better than the private banks. Public sector banks are back with a bang, bagging six of the top 10 slots in this year’s Business Standard Banking Annual Survey. While only one foreign bank made it to the top 10, three private banks were also represented.

The Hyderabad-based Andhra Bank has emerged as numero uno in this year’s survey, making it the first instance in the history of the Banking Annual of a public sector bank topping the charts. Andhra Bank ranks second on the profitability front, third on the growth parameter and fifth in productivity.

It has reported the highest return on equity (RoE) – 40.31 per cent – and logged a net profit growth of 99.2 per cent in 2003, riding high on other income which almost doubled to Rs 604 crore from Rs 304 crore. Its net profit margin improved to 14.4 per cent in 2003 from 8.7 per cent in 2002. However, in the safety and efficiency categories it has been ranked lower at the 12th and 32nd slots, respectively.

Another state-owned bank, State Bank of Indore, grabs the overall second
position. This State Bank of India associate tops the profitability charts but is placed 16th on both the productivity and safety parameters and 18th on the growth parameter. State Bank of Indore stands second in RoE and fifth in the return on assets.

Private sector Jammu & Kashmir Bank (best bank of 2001) ranks third in this year’s annual survey. It stands fourth in profitability and sixth in safety. It occupies the 13th position in efficiency, 32nd in growth and 37th in productivity.

The winners list also includes Catholic Syrian Bank (best bank of 2002), Union Bank of India, Indian Overseas Bank, Karur Vysya Bank, Deutsche Bank, State Bank of Hyderabad and State Bank of Mysore.

**Profitability:** State Bank of Indore tops the profitability charts followed by Andhra Bank, Catholic Syrian Bank, Jammu & Kashmir Bank and Indian Overseas Bank.

**Safety:** The safest of the lot is Kotak Mahindra Bank, followed by Bank of America, Corporation Bank, HSBC and Deutsche Bank. Kotak Mahindra Bank stands tall at the top with a 30.47 per cent capital adequacy ratio.

**Growth:** Dena Bank, with the highest net profit growth of 905 per cent in 2002-2003 tops the list, followed by Indian Bank, Andhra Bank, United Bank of India and Allahabad Bank.
Efficiency: On efficiency, Union Bank of India leads the pack. It is followed by Bank of Nova Scotia, IndusInd Bank, Bank of Punjab and HDFC Bank.

Indian banking has put up a good show in 2002-2003. The highlights of the year are a 52.3 per cent growth in net profit – from Rs 11,330 crore in 2002 to Rs 17,254 crore in 2003 – and a substantial reduction in non-performing assets.

Net non-performing assets (NPAs) declined by 7.6 per cent to Rs 32,174 crore in 2003 compared with a rise of 13.2 per cent in fiscal 2002. Gross NPAs too dropped by 2.8 per cent to Rs 67,218 crore. In 2002, the gross NPAs rose by 11.3 per cent. The average net NPA to net advances ratio came down to 6.54 per cent in 2003 from 8.84 per cent in 2002.

One of the contributing factors to the growth in bottomlines was high treasury income. In percentage terms, the treasury income of these banks grew by 34 per cent, down from 42.2 per cent in the previous year. However, in absolute terms, the contribution of the treasury segment was Rs 31,328 crore in 2003, sharply higher than Rs 23,388 crore in 2002.

Despite the continuous slide in interest rates, interest income rose marginally more at 12 per cent to Rs 1,39,341 crore in 2003 compared to a 11.4 per cent rise in 2002 to Rs 1,24,386 crore. In contrast, banks’ interest expenditure (paid on deposits) rose by 8.1 per cent to Rs 92,542 crore in 2003 as against 12.8 per cent in 2002. This clearly shows that the drop in lending rates is sharper than the drop in deposit rates.
The industry saw a 13.4 per cent surge in its deposit portfolio to Rs 13,41,071 crore in 2003 versus a growth of 14.9 per cent to Rs 11,82,462 crore in 2002. Advances went up by 15.1 per cent to Rs 7,33,655 crore. In 2002, these banks showed a 24.05 per cent rise in their advances.

Investments rose 18.7 per cent to Rs 6,87,284 crore against a 20.9 per cent growth in 2002.

The share of public sector banks in total deposits slipped to 80.5 per cent from 81.9 per cent while that of private banks increased from 13.1 to 14.4 per cent. In the case of advances also, the share of PSU banks dropped from 75.3 to 74.9 per cent while that private banks rose from 17.3 to 18 per cent.

*Just too many players.* 27 Public sector banks, 31 Private banks and 29 Foreign banks. The Indian banking sector is headed for consolidation. The presence of many regional players will see few banks emerging as global competitors.

**Will the government remove the CAP on voting rights?** The anticipated removal of CAP of 10% on voting rights will see Foreign banks establish themselves in the Indian market.

**What do the numbers say?** Likely rise in interest rates will see bank margins under pressure. Treasury gains to wilt in the current scenario. Bank profits in the future to be driven by Core income.

**How far is the retail boom sustainable?** Retail market to grow at a CAGR of 8% till 2007. Corporate lending to rise on back of planned fresh capacities, to improve credit off take.
Future belongs to technology. Cheaper delivery points like Internet and telebanking to improve their shares. ATM banking costs 80% while Internet and telebanking costs only 15% compared to normal banking transactions.

Are Indian banks ready for the Basel II challenge? Basel II is to be implemented by 2006. Banks need to put in place a strong internal rating system for credit deployment. Large IT investment needed.

Where Does India stand Vis-à-vis its global peers? India’s comparison table on few parameters with other global peers on a country level.

Any successful Indian enterprise of today will have its business infrastructure tightly coupled with its information infrastructure. In such a scenario where business relies heavily on IT, it's important to know that a problem exists before it impacts critical business applications.

Good infrastructure management ensures that all the components required to deliver quality performance are performing at optima levels. And through proactive and centralized management of the infrastructure, a company can even forsee performance breakdowns and compromises.

Trends in 2004

So what do we expect will Indian enterprises do in the area of enterprise infrastructure and asset management in 2004? S.R. Balasubramanian, Vice President, Information Technology, HDFC Bank says, "Enterprises will put more focus on implementing automation tools. These tools will help IT personnel get alert messages much before a failure occurs. Companies will be able to avoid possible downtime and make sure that customer service is always maintained."

"In the area of infrastructure management, Indian enterprises will concentrate on managed services in 2004. Industries will try to focus on their
core businesses and outsource infrastructure management functions. And depending on the cost, leasing may be a favoured option," says Subhash Palav, General Manager - Information Technology, HPCL.

V.K. Ramani, President, Information Technology, UTI Bank, spoke of banking industry specific trends of 2004. "The adoption of technology for banking services will continue at a healthy pace. The major thrust will be in areas like procurement of ATMs, expansion of LANs and WANs, building data center infrastructure, power supply setups, building security infrastructure, and the need for network monitoring tools. Facilities management practices will be the key to successful operations."

Challenges to infrastructure

Although 2004 will see a number of changes in the way Indian enterprises will manage infrastructure, the operations are not without challenges. "Currently, land lines form the primary means of communication, but their reliability needs to be improved considerably. Regardless of advancement in technology, the last mile connectivity still remains a challenge. There are also other challenges like obsolescence of equipment, and poor service support at remote locations," says Palav.

The banking industry will continue to grow at a quick pace in 2004. A quick growth rate along with rapid amendments in governing rules will pose a number of serious challenges.

Ramani comments on these challenges. "The challenges are a function of growth in a number of branch applications and the increase in products and services. The Governments will depend on the Banks' retail outlets for collection of taxes and other revenue. So it will be a challenge to find ways
to integrate banking systems with the payment mechanisms. This effort will require a large-scale process engineering function."

Assets to keep

Managing IT assets is a responsibility that many Indian CIOs may not take seriously. But IT asset management is all about nurturing the infrastructure, which runs the IT in organization, and is directly related to TCO. Gone are the days when CIOs thought that the network's fine if the software and databases are working fine. They now have to pay more attention to the other peripheral areas like power and air-conditioning.

Says Balasubramanian, "Your applications may be up-and-running but if the AC is not working you have to shut down your server. And this infrastructure which is vital for functioning of IT should be owned by the IT department."

Ramani feels that in the banking industry aspects like replacements, upgrades, obsolescence, and inventory management are very important. At the desktop level the mapping of inventory will become critical, as the users will access several applications. And the computing power of servers needs to be harnessed for better ROI.

A basic way to begin enterprise asset management is to plan activities like server and desktop consolidation, and right-sizing hardware with applications. You can use rack and blade servers to save space, power requirements, and cost. The use of thin clients for workstations that run specific applications is a good idea to save license fees and avoid system administration hassles.
Critical aspects

The monitoring of availability, response times, and fault repairing will be the key components of network management in banking and financial company networks. Sophisticated software tools will increasingly be in demand as the critical business operations will depend on network performance and availability.

The introduction of real-time gross settlement system by RBI will require the banks to remain connected. And failure to respond to transactions will result in financial loss to the banks.

Channel management will depend on a robust connectivity infrastructure. Internet and intranet services will aid the communication systems for customer interaction and transaction settlements. And intranets will enable the banks to optimize the utilization of the information repository that is available for efficient conduct of business.

Multiplicity of database servers and application servers will be the inevitable consequence of increasing computerization. Consistency of response and synchronization of databases need to be addressed as strategic requirements.

Handling critical aspects

In reality many organizations are busy fighting fires, and there's less scope and thought for better infrastructure management. An ideal situation is where the CIO is very aware of all the options available to get better value out of the existing infrastructure. The CIO can do with the efficient use of strategies, management skills, and technology tools.

Here's some of the goals the Indian CIO can have for better infrastructure management in 2004:
Increase productivity by automating manual processes. Reduce complexity through more accurate and efficient data collection, and manage diverse platforms by sharing common tools and services. Reduce costs by building the system with application-focused products that cross all platforms with the ability to deploy infrastructure management solutions only as needed. Maximize the existing infrastructure investment by effectively centralizing existing and new environments. Deliver a common communications infrastructure through a central GUI and by providing a common presentation interface with the ability to view all components of your infrastructure. Keep track of all IT infrastructure assets and make strategies to utilize them optimally to derive best value out of it.