## CHAPTER 3

### INDUSTRY PROFILE

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3.1 Introduction to chapter 3

In this chapter the researcher has made an attempt to discuss select information, data & statistics about service industry, banking industry & retail banking industry in particular. Also, some brief & relevant information on the regulatory authority of Indian banking sector i.e. Reserve bank of India is covered in this chapter.

3.2 Overview of Service Sector in India:

Over the past few years especially in last two decades, the service industry in India has shown tremendous growth not only in absolute numbers but also in terms of its overall contribution to India’s Gross Domestic Product.

Service sector is the largest sector of India as far as the overall contribution to the GDP is concerned.

Following figure clearly shows that, the contribution of service sector to India’s GDP is continuously growing from year 1950:
In India, Gross Value Added (GVA) at current prices for Service sector is INR 73.79 lakh crore in FY 2016-17.

Service sector contributes 53.66% (INR 73.79 lakh crore) to India's GVA for FY 2016-17 whereas Industry sector contributes 29.02% (INR 39.90 lakh crore) & Agriculture sector contributes 17.32% (INR 23.82 lakh crore).

Following figure depicts the same.

[Source: www.statisticstimes.com]
India has already moved from an agriculture based economy of the past to a service driven economy of today.

According to a recent report by India Brand Equity Foundation published on its website in June 2017, the share of Service sector in India’s GDP is expected to reach 62% by FY 2020.

3.2.1 Few statistics about service sector:

As per the report of India brand equity foundation published in October, 2017,

a. The services sector of India remains the growth engine for India’s economy and contributed 53.8% of India’s Gross Domestic Product in FY 2016-17.

b. 28.6% of India’s population is employed in the services sector in FY 2016-17.

c. India earned foreign exchange reserves of US$ 67.5 billion in FY 2016-17 through exports of various services.

d. Growth rate of service sector in India was 7.7% in FY 2016-17.

e. India registered the second highest growth rate in services industry exports in the world in 2016 at 3.6% year-on-year.

This clearly shows that, Service sector in India is a key driver of economic growth.

The government’s recent decision to launch & implement ‘Startup India’ campaign aims to create an inclusive environment for entrepreneurs with an impetus for innovation. Services industry is a big part of this system.

Low setup costs make this sector an attractive investment destination and the 60.7% share in India’s Foreign Direct Investment inflows in FY 2016-17 is a clear indication of the same.

India also has reasonably well developed & robust financial markets.

All these factors make Indian services sector an attractive destination for both the investors & entrepreneurs.
3.2.2 Share of Services Sector Grows at the fastest CAGR:

As per the data from India budget & a report by IBEF published in Nov 2017,

India achieved CAGR i.e. Compound Annual Growth Rate of 13.20% between FY 2011-12 & FY 2016-17 in services share to Gross Value Added (GVA).

In terms of overall GDP, India is ranked 5thin year FY 2016-17 & in terms of services GVA India ranked 13thas of FY 2014-15.

Services sector GVA was 53.8% of India’s total GVA in FY 2016-17.

Acceleration in the growth of Public Administration & other services (11.3% in FY 2016-17 from 6.9% in FY 2015-16) supported the increase in FY 2016-17, which was in turn supported by the implementation of the 7thPay commission.

3.2.3 Service Sector PMI

As per the data from India budget, Bloomberg & a report by IBEF published in Nov 2017,

The Nikkei India Services PMI i.e. Purchasing Managers’ Index increased from 45.9 in July 2017 to 50.7 in September 2017.

Previously, the Index was going up for three consecutive months supported by a faster increase in new business inflows giving boost to growth in both activity and employment.

3.2.4 India’s Services Trade

As per the data from Economic survey of FY 2016-17 & a report by IBEF published in Nov 2017, till the global financial crisis of 2008, India’s services exports registered a good growth for almost a decade.
Growth of Services export reduced to 11.9% CAGR during FY 2005-06 to FY 2014-15 from growth of 21.6% CAGR during FY 1994-95 to FY 2004-05.

As a result of high growth in some sectors like transportation & business services, services exports grew by 5.7% in FY 2016-17.

Business services exports and financial services exports account for 20.2% and 3.1% of the total services, registered a growth of 13.6% and 3.1% in FY 2016-17 respectively.

Travel accounts for 14.2% of the total services exports, and it recorded a growth of 9.3% due to a considerable rise in foreign tourist traveling to India.

Transportation services exports increased by 13.2% in FY 2016-17 as compared to -19.9% in FY 2015-16.

Because of higher payments in two service categories- travel & miscellaneous (mainly software and financial services), India’s service imports registered a growth of 13.0% in FY 2016-17.

Even though services exports growth was 5.7%, growth in services imports led to a reduction in net services receipts by 3.2 %.

Following figure shows the data related to India’s service sector exports & imports in FY 2016-17. It can be observed that IT & miscellaneous industries are the ones which contribute maximum towards India’s exports.
3.2.5 High FDI Inflows in Service sector

As per the data from Economic survey of FY 2016-17 & a report by IBEF published in Nov 2017,

The share of services sector is 60.7% of the total FDI equity inflows in India during FY 2016-17.

In FY 2016-17, growth rate of FDI inflows reduced to 8.7% (US$ 43.5 billion) due to negative growth in computer hardware and software, trading, construction & hotels and tourism.

To ensure that India remains an attractive investment destination, the Government has brought a number of reforms like the “abolition of the Foreign Investment Promotion Board (FIPB) and the introduction of composite caps in the FDI policy”. This permits 100% FDI under automatic route for any financial sector activity that is regulated by any financial sector regulator.
3.3 Overview of Banking sector in India:

3.3.1 Definition of Banking:

Section 5 (1) (b) of the Banking Regulation Act, 1949 defines Banking as: “The accepting for the purpose of lending or investment, of deposits from the public, repayable on demand or otherwise & withdrawal by cheque, draft, order or otherwise.”

3.3.2 Importance of banking sector:

Banking industry is one of the largest industries in India in terms of the revenue & the employment provided. A nation’s economy can virtually come to a standstill in absence of a well regulated & robust banking system.
Banking industry is a backbone of a nation’s economy as major chunk of the funds in the country flow through banking system. Proper functioning of the banking system is extremely critical for a smooth operation of the country’s economy.

3.3.3 Brief outline of banking industry:

The Indian banking system is broadly classified in two major segments i.e.

a. Corporate Banking segment
b. Retail Banking segment

The Corporate Banking segment deals with the Medium to Large Corporates & their banking requirements.

The Retail Banking segment deals with the Individual customers (Salaried people, Students, Home makers, Retired people etc.) & their banking requirements. Retail banking segment is also called as **Branch Banking segment** as it comprises of various branches of a particular bank located in different areas of a city covering a large customer base.

There are different types of banks in India as follows:

a) Public Sector banks
b) Private Sector banks
c) Foreign banks
d) Regional Rural Banks
e) Urban Cooperative banks
f) Rural Cooperative Credit Institutions

In India, the regulator of the banking industry is Reserve Bank of India (RBI) which is headed by the Governor of this organization. Currently Mr. Urjit Patel is heading the Reserve Bank of India as RBI Governor.
There are various services provided by Retail Bank. These are divided into following major heads:

a) **Account related services** (Savings & Current account)
b) **Investment related services** (Fixed Deposit, Recurring Deposit, Life Insurance, Health Insurance, Mutual Fund, Private Equity, Portfolio Management Services & Gold etc.)
c) **Loan related services** (Home loan, Personal Loan, Vehicle loan, Agricultural loan, Loan against property, Education loan, Credit card, Cash credit, Overdraft, Letter of credit, Bank guarantee etc.).

Through these services, the bank gets an opportunity to interact with its customers. Through a positive interaction, it can strengthen the relationship with its customer.

As it’s a well-known fact that after the opening up of Indian banking industry to Private sector banks & foreign banks, there is a tremendous increase in the competition amongst various players within the banking industry.

To grow & survive in such a stiff competition, the banks need to build & strengthen the relationship with the customers so that customer retention is high & also to increase the market share.
3.3.4 Evolution of the Indian Banking Sector

Following table highlights the brief evolution of banking sector in India

**Table No. 3.1**

**Evolution of the Indian Banking Sector**

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<th>Period</th>
<th>Evolution in Indian banking sector</th>
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| 1      | 1921-1935| a. Closed market  
b. State-owned Imperial Bank of India was the only bank existing |
| 2      | 1935-1936| a. RBI was established as the central bank of country  
b. Quasi central banking role of Imperial Bank came to an end |
| 3      | 1936-1955| a. Imperial Bank expanded its network to 480 branches  
b. In order to increase penetration in rural areas, Imperial Bank was converted into State Bank of India |
b. Entry of private players such as ICICI intensifying the competition  
c. Gradual technology upgradation in PSU banks |
| 5      | 2000-2015| a. In 2003, Kotak Mahindra Finance Ltd. received a banking license from RBI and became the first NBFC to be converted into a bank.  
b. In 2009, the government removed the Banking Cash Transaction Tax which had been introduced in 2005. |
| 6      | 2016 onwards| a. NABARD sanctioned US$ 2.84 billion loan to National Water Development Agency for 50 irrigation projects in October 2016.  
b. As per RBI, in September 2017, India recorded highest foreign exchange reserves of approximately US$ 402.51 billion. |

[Source: Indian Bank’s Association, Aranca Research, BMI]
3.3.5 Structure of Indian banking sector

Figure No. 3.5
Structure of Indian banking sector

[Source: Reserve Bank of India’s ‘Report on Trend and Progress of Banking in India’, Aranca Research]
3.3.6 Indian Banking Sector driving growth in the Indian economy

As per the data from Reserve Bank of India, Aranca Research & a report by IBEF published in Nov 2017,

During FY 2005-06 to FY 2016-17, growth rate in deposits in India was registered at a CAGR of 16.04% from US$ 325 billion in FY 2005-06 to US$ 1,669 billion in FY2016-17.

Significant growth in savings due to rising disposable income of the people is the major factor impacting deposit growth.

Access to banking system has also improved a lot in recent past owing to persistent efforts from government to promote banking expansion in rural areas.

India’s banking sector has remained stable in spite of global disturbances, due to which the public confidence has remained intact over the years.

Due to Pradhan Mantri Jan Dhan Yojana, deposits have also increased. As of 25th October, 2017, US$ 10,412.62 million were deposited in these accounts, while 305.2 million accounts were opened.

Following figure depicts the growth in deposits in Indian banking sector from FY 2005-06 to FY 2016-17:
3.4 **Introduction to Retail banking industry in India**

Retail banking refers to banking system in which banks carry out transactions directly with consumers & not with large companies, businesses / corporates or other banks.

In retail banking the banks deliver services to individuals and small business concerns and the transactions are in large numbers and low values. The retail banking portfolio encompasses deposits and loans / assets linked products as well as other financial services offered to individuals for personal use.

The products delivered to the customers through the branch network, as well as through other multiple service delivery channels like Phone Banking, ATMs, Mobile Banking & Internet Banking.

Following are the three major characteristics of today’s retail banking sector:

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**Figure No. 3.6**

*Growth in bank deposits over the past few years (US$ billion)*

[Source: report by IBEF published in Nov 2017]
- Multiple product offerings – i.e. Savings account, Current account, NRI account, Fixed deposits, Recurring deposits, credit cards, insurance, Mutual fund investment and securities.

- Multiple distribution channels – bank branch, call center & internet

- Multiple customer groups – consumer small & medium scale businesses

### 3.4.1 Features of retail banking

Retail banking refers to the dealing of commercial banks with individual consumers. It covers both the liability side & asset side of a balance sheet. On the liability side, it includes various deposits i.e. Savings / Current account deposits, Fixed deposits, Recurring deposits whereas, on the asset side, it includes various kinds of loans i.e. Home loan, personal loan, vehicle loan, agricultural loan, educational loan etc.

**Characteristics of Retail Banking Sector:**

- Retail banking objective is to do banking business in large volume of transactions involving low value.

- Retail banking business is an attractive market segment with opportunities for growth and profits.

- The retail banking portfolio includes deposits and assets linked products & also other financial services provided to individual customers for personal consumption.

- Retail banking is based on the principle of “do not keep all the eggs in one basket”.

- Retail banking industry is diverse and extremely competitive. The products offered by retail banks are very similar in nature & customer-friendly.
✓ Banks adopt multiple channels of distribution of retail banking products. The channels include call center, bank branch, mobile phones, internet, ATMs etc.

✓ It provides an opportunity to banks to diversify their portfolio of assets. Since loans are given to a large number of consumers and transactions are of very low value, the risk of NPA is reduced because all the consumers do not make default in making loan repayment on time.

3.4.2 Retail banking products

Retail banking includes a comprehensive range of financial products such as deposit products, loan products and payment services.

The typical products offered in the Indian retail banking industry are as follows:

3.4.2.1 Retail deposit products (Retail liability products)

✓ Savings bank account
✓ Current account
✓ Recurring deposit account
✓ Fixed deposit account
✓ Salary account (mostly it’s a zero balance account)
✓ No frill account for common man (Generally opened in rural areas)
✓ Senior citizen deposit account etc.

3.4.2.2 Retail loan products (Retail asset products)

✓ Home loans to resident Indians for - purchase of land & construction of house or purchase of ready built house or for repairs and renovation of an existing house.
✓ Home loans to NRIs i.e. Non Resident Indians.
✓ Vehicle loans for new/ used two wheelers and four wheelers
✓ Consumer loans for purchase of jewels, for domestic consumption etc.
✓ Education loans for pursuing higher education not only in India but also abroad.
✓ Trade related loans (in the form of advances) to individuals for setting up business, retail trade etc.
✓ Crop loan to farmers

3.4.2.3 Third party products (Fee income products)

These products are not the products of the bank per se but the bank markets these products as a third party i.e. it acts as an intermediary between the customer & the company to which these products belong. In this process, the bank earns a commission / fee from other companies. These products are mentioned below:

✓ Mutual funds
✓ Life insurance
✓ Health insurance
✓ Gold
✓ Venture capital
✓ Private equity

3.4.2.4 Retail banking services

✓ Depository services
✓ Safe deposit lockers
✓ Banc assurance products etc.
✓ Currency exchange services
3.5 Regulatory Authority for banking sector in India

The regulatory Authority for banking sector in India is Reserve Bank of India (RBI).

3.5.1 Establishment

In accordance with the provisions of the Reserve Bank of India Act, 1934, the Reserve Bank of India was established on 1st April, 1935. The Central Office of the Reserve Bank was initially established in Kolkata (then Calcutta) but was moved to Mumbai in the year 1937.

The RBI is headed by its governor who occupies its central office in Mumbai where policies are formulated.

The Reserve Bank of India is fully owned by the Government of India.

3.5.2 Main Functions of RBI

As mentioned on the Reserve Bank of India website, there are six types of functions the RBI performs as mentioned below:

a. Monetary Authority:

✓ Formulation, implementation and monitoring of the monetary policy.
✓ Objective of monetary policy is to maintain price stability without ignoring the GDP growth.

b. Regulation & supervision of the financial system:

✓ RBI Prescribes broad parameters of banking operations within which India’s banking & financial system functions.
✓ Here, the objective is to maintain public confidence in the system, to protect depositors' interest & to provide cost-effective banking services to the citizens.
c. Manager of Foreign Exchange

✓ RBI Manages the Foreign Exchange Management Act, 1999.
✓ Here the objective is to facilitate external trade & payment and promote orderly development and maintenance of foreign exchange market in India.

d. Issuer of currency:

✓ RBI issues and exchanges or destroys currency and coins found unfit for circulation.
✓ Here the objective is to give the citizens adequate supply of good quality currency notes and coins.

e. Developmental role

✓ RBI Performs a wide range of promotional functions to support national objectives.

f. Related Functions

✓ RBI acts as a Banker to the Government i.e. it performs merchant banking function for the central and the state governments & also acts as their banker.
✓ Banker to banks: RBI maintains banking accounts of all scheduled banks.