7. MEASURES TO FACE THESE CHALLENGES

The Indian financial system has come a long way since the days of nationalization of banks and the dependence on development financial institutions. After the introduction of economic reforms in 1991, the growth rate of India’s GDP increased from a little over 1% in 1991-92 to 6.9% in 2004-05. As the world GDP growth is around 3.1%, India can be considered as one of the fastest growing economies in the world. The Indian economy is expected to maintain its high growth course in 2005-06 with a likely growth of 7.2%. A healthy banking system is crucial for the steady growth of an economy. With a network of over 66,000 branches, India has one of the largest banking networks in the world. Since 1991, the Reserve Bank of India took steps to reform the Indian banking system at a measured pace so that growth could be achieved without exposure to any macro-environment and systematic risks. Some of these were deregulation of interest rates, dilution of the government stake in public sector banks, guidelines being issued for risk management, asset classification and provisioning.

The Indian public sector banks face challenges for their existence both in domestic and international markets. During the past few years the RBI has softened its attitude towards private banks in the country. The banks that meet the RBIs capital adequacy requirements can open branches without seeking any prior approval. The private banks are market driven instead of government driven. However, the present Indian public sector banks operate like governments. Better customer services are the key to success in the slogan given by private banks. But public sector banks are burdened with the high non-performing assets and a large work force. Few of Indian public sector banks have small number of branches in foreign countries. These branches generally do no fare well. One of the reasons of deterioration in operations of Indian banks abroad is that their capital base is very weak and do not conform to the international standards. Earnings from operations are not retained in the bank for augmenting the capital base. Thus reserves are dwindling and do not provide adequate funds in the period of depression. This poses a big structural problem.
The Indian Banking Industry is currently in a phase of transition. Government disbursements have begun to pick up, and in the wake of improved corporate performance, the share market has been upbeat. While PSU Banks are shedding flab by implementing VRS schemes and deploying technology aggressively, private players are looking at consolidating their strengths through mergers and acquisitions. Besides consumer satisfaction, product and service differentiation has been the focus area in the banking sector. With these trends, most players are working on aggressive strategies to push in their retail assets by venturing into various categories of consumer loans.

A healthy banking system is essential for any economy striving to achieve good growth and yet remain stable in an increasingly global environment. The Indian banking system, with one of the largest banking networks in the world, has witnessed a series of reforms over the past few years like the deregulation of interest rates, dilution of the government stake in public sector banks and the increased participation of private sector banks. Indian banks have not only been keen to tap the domestic market but also to compete in the global market place. New foreign banks have been equally keen to gain a foothold in the Indian market. The momentum in credit growth has been maintained during 2005-06 as the corporate sector has stepped up its demand for credit to fund its expansion plans and there has also been a growth in retail banking.

Apart from what is mentioned above, banks would need a whole new set of skilled manpower as enablers for implementing Basel II, especially the advanced approaches. Unfortunately, having regard to the manpower profile, especially in the PSBs, these skill sets are not readily available. Hence, banks will have to arrange extensive training both internal and external for their existing workforce and also scout for talented manpower from outside.

The banks will have to be prepared at various degrees to face these challenges. The situation calls for re-looking at strategies on an ongoing basis both in regard to asset allocation and diversification. Without multiplicity of income streams, Indian banks will find it difficult to survive in the emerging scenario. To multiply the income
streams, it is imperative that banks have to go for a total re-look at their technological preparedness, skills and ultimately the quality and the strength of the balance sheet.

The banking sector in India faces the most challenging task of reforming itself in an environment where the operating environment is getting redefined almost every day. The Indian banks, thus, must identify the right strategy for growth, sustaining profitability and keeping their capital adequacy in tune with the mandatory requirements. The investment climate should improve and the primary capital market has to revive to promote capital investment in the real sectors and in consequence the credit demand has to improve.

Banks should upgrade their skills, especially in risk evaluation. A thorough revamping of the legal system must happen so that we make a transition from the current scenario of being defaulter-friendly to the one that is lender-friendly. This will help banks to get enthused about their lending activities.

Another challenge that the banks face today is that of surplus liquidity, which must be tackled at both the macro as well as micro level. With regards to the former, the critical issue is infrastructure related developments and resurgence of primary capital markets. For the latter, banks must focus on sectors which have huge potential for asset creation. All banks have to imbibe the changes the market situation demands, become technologically savvy and assume critical mass of business and sustain profitability.

Financial services providers are most probably the industry category that is facing rapid modernization and inflated competition in today’s world. The fight has begun for getting a larger share of the customer pie with the lowest possible cost to serve the customers. Since profits are drying up in the face of increased competition and customers are moving very fast from one firm to another on service and complete solution provision dimension, it becomes important to have an integrated customer relationship management strategy across the whole organization for generating higher customer life time value. Without this awareness and constant attention to varying customer needs, a financial service provider cannot be competitive in today’s world.
Integration of process, people, technology and information will offer a greater value to the customers.

Banking is essentially an industry which carries on its operations mainly based on the confidence and faith of its customers. It has to undoubtedly grow on the quality of the service rendered by it, since service is the end product of a bank but the efficiency of a bank depends more on how best can it deliver goods to its customers rather than simply the volume of business carried on by it.

The world over the banking environment has become highly competitive. As a result, the conventional banking has undergone a total transformation. The banks have started increasingly employing marketing approach to sell banking services to their customers. Various new and innovative schemes have been introduced with a view to provide greater satisfaction to the customers and win their franchise. In addition, banks have also started using various marketing tools and techniques such as market segmentation, produce differentiation, product positioning and effective promotion to carve niches for themselves in the banking industry.

Public sector banks in India today are not only facing competition from foreign banks and other financial institutions like LIC, UTI but are also operating under highly regulatory environment. RBI, the apex body has also introduced from time to time plethora of laws and regulations, thus restricting the freedom available to the public sector banks in undertaking various banking operations.

In view of the importance of the banking system for financial stability, sound corporate governance is not only relevant at the level of the individual bank, but is also a critical ingredient at the system level. Effective risk management systems determine the health of the financial system and its ability to survive economic shocks. To a large extent, many risk management failures reflect a breakdown in corporate governance which arise due to poor management of conflicts of interest, inadequate understanding of key banking risks, and poor Board oversight of the mechanisms for risk management and internal audit. Corporate governance is, therefore, the foundation for effective risk managements in banks and thus the foundation for a sound financial system. A good “governance culture” is crucial for
financial stability but since it is an ‘intangible’, rules may not be able to capture its essence effectively. Therefore, banks may have to cultivate a good governance culture building in appropriate checks and balances in their operations.

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. Banks are taking the right initiatives by recognising the benefits of modernising their technology infrastructure.

There is a wide degree of variance in the performance of banks. Non-performing assets is one of the biggest challenges for banks to address. Recently, UPA government has increased the service tax from 10% to 12%. This will affect the profit of service industry including the financial service sector which may discourage the financial service sector. So, it is a challenge for the banks to promote their active participation in the process of development to improve the efficiency of banking system.

Due to inadequate infrastructure facilities, private banks can only target the big cities. A large population lives in villages where the private banks do not have a reach. Efforts should be made to tap the financial resources available in rural areas. To face the challenge, it is imperative for the banks to adopt an aggressive marketing strategy for banking operations.

Banks should try to curtail the time required to deposit cash, withdraw money, issue chequebook, bank draft, encashment and renewal of term deposits etc. Thus, the banks should provide prompt services. Banks should become very strict in adhering to the standard time norms and strict actions should be taken against defaulters.

With the changing international scenario, the expectations of bank customers are also changing. Personal Banking is another step toward customer orientation. More emphasis is being placed on relationship banking as compared to transactional
banking. Adoption of modern technology is not just for the purpose of sophistication, or even as a showpiece, but for achieving a clear goal of bringing about significant improvement in customer service and internal accounting. It is very natural that customers expect from a bank efficient, quick and prompt handling of their transactions. Since the foreign banks and private banks have been offering to the customers quick and prompt services, a change in the perception of the customer satisfaction cannot be ruled out. This makes it essential that the banks assign due weightage to the efficiency dimension and the bank managers perform intelligently so that customers get the desired results. In the present environment, bankers operate in a buyer’s market. So, they have to adopt planner marketing approach to find proper outlets for banking services. The banks need to study carefully various segments of the population and formulate appropriate schemes to suit those specific requirements.

Regarding the tools of sales promotion, the bank executives and policy makers are required to concentrate on innovative measures found unique to the customers. Special incentives to customers would pave the avenues for special attractions and personal touch in service. The duration and frequency of innovation would depend upon the stages of bank’s scheme in the banking system.