CHAPTER 1

INTRODUCTION TO THE STUDY

1.1 BACKGROUND TO THE STUDY

Banks are financial institutions which plays a vital role in structuring and stabilizing the economies of the developing and as well as developed countries. Banks are the one which ensures the free flow of money in the society among the people belongs to various economic classes through the deposits and credits. The individuals in the society who have surplus money they want to save the money for the future commitment or accumulating wealth for the future generations, at the same time the individuals who are in need of the money may want to borrow the money for present commitment and willing to repay it in Equated Monthly Installments (i.e. EMI) with reasonable interest. The peculiar characteristics of the banks are they have the customers from different economic classes. The terms ‘business’ and ‘risk’ are most of the time closely associated, because there is no business without risk. In general, ‘high risk may yield high returns’, ‘low risk may yield low returns’. Obviously, banks are no exception to this. Like other business organization, banks are also facing the various kinds of risks such as credit risk, market risk, liquidity risk, operational risk, etc. In banking industry scenario, credit risk plays a critical role, whether it may be private, public or even cooperative banks.

The term ‘credit risk’ refers to risk associated with the disbursement of loans and receiving the appropriate payment with the interest
as per repayment schedule. In other words, the risk of loss of principal or loss of a financial reward stemming from a borrower's failure to repay a loan or otherwise meet a contractual obligation. However, interest rate risk is directly linked to credit risk implying that high or increment in interest rate increases the chances of loan default. Credit risk and interest rate risk are intrinsically related to each other and not separable (Drehman et al. 2008).

Increasing amount of non-performing loans in the credit portfolio is inimical to banks in achieving their objectives. Due to the increasing spate of non-performing loans, the Basel II & III Accord emphasized on credit risk management practices. Compliance with the Accord means a sound approach to tackling credit risk has been taken and this ultimately improves bank performance. Through the effective management of credit risk exposure, banks not only support the viability and profitability of their own business, they also contribute to systemic stability and to an efficient allocation of capital in the economy (Psillaki et al. 2010).

Credit operation and risk management is the important portfolio of the banking institutions because which may affect the liquidity, operation and reputation of the banks in the society. Risk management was introduced by RBI in 1998 and that is actually the beginning of systematic modern Credit Risk Management in Indian Banks. Hence the researcher has made an attempted to explore the various credit operations and risk management strategies following by IDBI bank and its impact on organizational performance.

1.2 INTRODUCTION TO INDUSTRY PROFILE

The banking industry in India has the potential to become the fifth largest banking industry in the world by 2020 and third largest by 2025 according to KPMG-CII report, India’s banking and financial sector is
expanding rapidly. Indian banks have adopted better operational strategies and upgraded their skills. They have withstood the initial challenges and have become more adaptive to the changing environment. In the complex and fast changing environment, the only sustainable competitive advantage for banks is to give the customer an optimum blend of technology and traditional service. As per the Reserve Bank of India (RBI), India’s banking sector is sufficiently capitalized and well-regulated. The financial and economic conditions in the country are far superior to any other country in the world. Credit, market and liquidity risk studies suggest that Indian banks are generally resilient and have withstood the global downturn well. Indian banking industry has recently witnessed the roll out of innovative banking models like payments and small finance banks. The central bank granted in-principle approval to 11 payments banks and 10 small finance banks in FY 2015-16. RBI’s new measures may go a long way in helping the restructuring of the domestic banking industry.

The Indian banking system consists of 26 public sector banks, 25 private sector banks, 43 foreign banks, 56 regional rural banks, 1,589 urban cooperative banks and 93,550 rural cooperative banks, in addition to cooperative credit institutions. Public-sector banks control nearly 80 percent of the market, thereby leaving comparatively much smaller shares for its private peers. Banks are also encouraging their customers to manage their finances using mobile phones. The value of mobile banking transactions in December 2015 increased four times year-on-year and jumped by 46 per cent over the previous month to Rs 49,029 crore (US$ 7.34 billion), as per data from the RBI. Standard & Poor’s estimates that credit growth in India’s banking sector would improve to 11-13 per cent in FY17. The Indian banking sector’s assets reached US$ 1.8 trillion in FY14 from US$ 1.3 trillion in FY10, with 70 per cent of it being accounted by the public sector.
Total lending and deposits increased at a Compound Annual Growth Rate (CAGR) of 20.7 per cent and 19.7 per cent, respectively, during FY07-14 and are further poised for growth, backed by demand for housing and personal finance. Total asset size of banking sector assets is expected to increase to US$ 28.5 trillion by FY25. Deposits have grown at a CAGR of 13.6 per cent during FY05–15 to an estimated US$ 1.48 trillion in FY15. Deposit growth has been mainly driven by strong growth in savings amid rising disposable income levels.

Indian banks are increasingly focusing on adopting integrated approach to risk management. Banks have already embraced the international banking supervision accord of Basel II. According to RBI, majority of the banks already meet capital requirements of Basel III, which has a deadline of March 31, 2019. Most of the banks have put in place the framework for asset-liability match, credit and derivatives risk management. Rising incomes are expected to enhance the need for banking services in rural areas and therefore drive the growth of the sector; programmes like MNREGA have helped in increasing rural income aided by the recent Jan Dhan Yojana. The Reserve Bank of India (RBI) has relaxed its branch licensing policy, thereby allowing banks (which meet certain financial parameters) to set-up new branches in tier-2 to tier-6 centers, without prior approval from RBI. It has emphasised the need to focus on spreading the reach of banking services to the un-banked population of India.

**Concepts & Definitions**

According to Section 5(b) of Banking Regulation Act, 1949, the term ‘Banking’ can be defined as “the accepting for the purpose of lending or investment of deposits of money from the public, repayable on demand or otherwise and withdrawal by cheque, draft, and order or otherwise”.
Section 49A of the Act prohibits any institution other than a banking company to accept deposit money from public withdrawal by cheque. Students may note that the essence of banking business is the function of accepting deposits from public with the facility of withdrawal of money by cheque. In other words, the combination of the functions of acceptance of public deposits and withdrawal of the money by cheques by any institution cannot be performed without the approval of Reserve Bank. A bank is an institution which deals in money and credit. Thus, bank is an intermediary which handles other people's money both for their advantage and to its own profit. But bank is not merely a trader in money but also an important manufacturer of money. In other words, a bank is a factory of credit.

Although the above definitions have described the meaning of bank, none of them precisely defined, 'Banking' incorporating its entire functions. However, an attempt has been made in Section 5(1) (b&c) of the Banking Regulation Act, 1949 to define 'Banking' and 'Banking Company'. According to Section 5 (1) (b), "Banking means accepting for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise and withdrawal by cheques, draft, order or otherwise".

**Indian Banking Industry Analysis with Regards to Deposits**

**Deposit growth has been steady increased**

- Total money supply increased at a CAGR of 11.14 per cent during FY06–16*
- Between FY06–16*, narrow money supply (M1) rose at a CAGR of 7.69 per cent to US$ 392.8 billion, broad money supply (M2) increased at a CAGR of 6.49 per cent to US$ 395.3 billion and money supply (M3) grew at a CAGR of 11.14 per cent to US$ 1.8 trillion by the end of October’15
- Time deposits with banks have shown highest average growth of 12.9 per cent during FY06–16*, and stood at US$ 1.44 trillion by

![Graph showing growth in money supply over past few years (US$ Billion)](source: RBI, Tech Sci Research)

Note: CAGR - compound annual growth rate, M1 is define by sum of currency with public and Deposit money of the public, M2 is the sum of narrow money and post office saving deposit. M3 refers ton sum of M2 and time deposit with banks. FY16* as on oct 2015

Figure 1.1 Growth in money supply over past few years (US$ Billion)

Indian Banking Industry Analysis with Regards to Credit Growth Rate

- Credit off-take has been surging ahead over the past decade, aided by strong economic growth, rising disposable incomes, increasing consumerism and easier access to credit
- Total credit extended went up to US$ 1,089 billion by FY15
- Credit to non-food industries increased 9.75 per cent to US$ 1,073.4 billion in FY15, from the previous financial year
- Demand has grown for both corporate.
Overview of Banking Sector in India

With the potential to become the fifth largest banking industry in the world by 2020 and third largest by 2025 according to KPMG-CII report, India’s banking and financial sector is expanding rapidly. The Indian Banking industry is currently worth Rs. 81 trillion (US $ 1.31 trillion) and banks are now utilizing the latest technologies like internet and mobile devices to carry out transactions and communicate with the masses. The Indian banking sector consists of 26 public sector banks, 20 private sector banks and 43 foreign banks along with 61 Regional Rural Banks (RRBs) and more than 90,000 credit cooperatives. Further, while a significant portion of the stress was recognised as Non-Performing (NPAs) in H2, FY2016, ICRA estimates of additional weak assets of around 6-7% (including standard restructured advances of 3.3%) could keep NPA generation at high levels in FY2017 as well.

While all banks’ fresh NPA generation rate was 6% for FY2016, banks’ fresh NPA generation is likely to moderate to around 4-4.5% in FY2017 as a large proportion of the weak advances may have been classified as non-performing.
NPAs in FY2016. On the back of significant deterioration in asset quality, banks are focussing more on recoveries, pursuing highly indebted corporates to divest, bring new investors or sale of assets in order to repay loans. In this regard, some of the stressed borrowers have announced plans or deals to sell / divest assets to pare down debt, successful execution of these efforts in a significant way could help reduce pressure on banks’ asset quality.

Further, some improvement in operating environment for few of the credit intensive sectors and RBI’s recent regulation for Scheme of Sustainable Structuring of Stressed assets (S4A) could ease some pressure on asset quality profile over the short to medium term. RBI’s recent norms of scheme for sustainable structuring of assets (S4A) could also augur well for identification of unviable exposure and up-gradation of viable exposure (though with a lag of one year) and potentially could reduce the pressure on banks’ reported Gross NPA %. Furthermore, implementation of the Bankruptcy Code could help improve bank’s recoveries over the medium to long term.

It is believe that banks’ asset quality matrices are unlikely to improve substantially in near term though Gross NPAs could be nearing peak levels and could increase to 8.0-8.5% by March 2017 (vs. 7.7% as on March 2016). Significant improvement in asset quality will hinge upon economic recovery in credit intensive sectors, as well as successful execution of sale of assets by some stressed corporate groups. While banks’ asset quality indicators may not worsen materially from current levels, their credit cost could remain at elevated levels over next 1-2 years as banks’ build provisioning cover against the elevated Gross NPA % as well as other weak assets. All banks’ credit cost increased to 2.4% in relation to average advances in FY2016 vs. 1.4% in FY2015. Banks’ provision cover was around 41.7% as on March 31, 2016 (vs. 44.4% as on March 31, 2015). As credit cost is likely to remain high in FY2017 as banks will have to increase
provisions with passage of time, profitability of banks could therefore remain low (return of equity in single digits) in FY2017 as well (vs. 3% in FY16 and 11% in FY2015).

On the PSBs profitability metrics, 14 out of 26 PSBs reported losses in FY2016. While their profitability profile is not expected to be as weak in FY2017 as it was in FY2016, a significant improvement is unlikely with most of them likely to report subdued profitability over the next 1-2 years. Despite significant fall in PSBs net profitability profile, their operating profits remain sizeable in relation to their asset quality stress; PSBs operating profits (pre-provisioning) during FY2016 was around Rs 1.2 trillion, equivalent to approximately 37% of their net NPAs as on March 2016. In ICRA’s estimate, overall losses on stressed advances of PSB’s are expected to be Rs 2.6-2.9 trillion (215-245% of pre provisioning operating profits). Furthermore, softer trend in G-sec yields could offer banks with opportunities to book treasury gains which could be used to absorb credit cost in FY2017.

**Growth in Indian Banking Sector**

An IBA-FICCI-BCG report suggests that India’s Gross Domestic Product (GDP) growth will make the Indian banking industry the third largest in the world by 2025, India’s banking and financial sector is expanding rapidly. Indian banks have adopted better operational strategies and upgraded their skills. They have withstood the initial challenges and have become more adaptive to the changing environment. In the complex and fast changing environment, the only sustainable competitive advantage for banks is to give the customer an optimum blend of technology and traditional service.

According to the report, the domestic banking industry is set for an exponential growth in coming years with its assets size poised to touch USD 28,500 billion by the turn of the 2025. With the deposits growing at a CAGR
of 21.2 per cent (in terms of INR) in the period FY 06–13, there has been evident growth in the overall industry. This growth can be attributed to banks shifting focus to client servicing. Public as well as private sector banks are underlining the importance of technology infrastructure, in order to improve customer experience and gain a competitive edge. Utilizing the popularity of internet and mobile banking, banks are increasingly adopting an integrated approach for asset–liability match, credit and derivatives risk management.

**Factors Contributing Growth of Banking Sector in India**

The Banking Laws (Amendment) Bill that was passed by the Parliament in 2012 allowed the Reserve Bank of India (RBI) to make final guidelines on issuing new bank licenses. Moreover, the role of the Indian Government in expanding the banking sector is noteworthy. It is expected that the new guidelines issued by RBI will curb practices of impish borrowers and streamline the loan system in the country. In the coming time, India could see a rise in the number of banks in the country, a shift in the style of operation, which could also evolve by incorporating modern technology in the industry. Another emerging trend witnessed by the banking sector is the use of social media platform like Facebook to attract customers. In September 2013 ICICI bank launched a Facebook bill payment and fund transfer service called ‘Pockets’ for customer convenience.

According to a report by Zinnov, a Globalization and Market Expansion firm, ‘IT adoption in BSFI sector in India’, the Information Technology Industry spend in BFSI vertical is expected to reach USD 3.5 billion by Financial Year 2014. The study also highlighted ‘the growing maturity of Indian BFSI organizations in IT adoption, as technology is seen as a driver of business value. Technology firms have great potential to explore in the BFSI sector, which contributes to eight per cent of India’s Gross Domestic Product.
Life Insurance

The Indian life insurance industry is estimated to grow at a Compounded Annual Growth Rate (CAGR) of 14.1 per cent, and reach US$ 111.9 billion in 2015 from US$ 66.5 billion in 2011, according to a report by BRIC data. This would make India the third-largest market for life insurance in the world by 2015. India’s present position is at number 12, among top global markets for life insurance. Number of policies sold is expected to increase to 95.21 million in 2017 from 53.23 million in 2010. The 2014-15 union budget should exempt life insurance products from taxation to provide investors an incentive to buy a policy. The insurance industry can gain leverage from India's burgeoning population only by providing a special tax window for life insurance policies.

Health Insurance

In the non-life insurance industry, health insurance is the second largest segment in India; with players in both the public and private sectors playing an active role. The industry is concentrated around 4 major public sector companies namely, New India Assurance, United India Insurance, National Insurance and Oriental Insurance. The Indian health insurance industry has seen major growth in the past 6 years. The Indian health insurance industry is expected to grow at a CAGR of 37.2% from FY’2011 - FY’2016; with surging medical costs, rising population and increased awareness among consumers in the country.

Recruitment Trends in BSFI Industry

The Banking and Financial Services Industry is expected to recruit about 8.4 million people as per the growth rate each year. BSFI workforce requirement between 2008 and 2022 is expected to be about 4.2 million and sector may create up to 20 lakh new jobs in the next 5-10 years. Advantaged
by issuance of new licences and efforts being made by the RBI and the Government to expand financial services into rural areas, the hiring trend may further get a boost from the public sector banks. Since most banking workforce is scheduled to retire in the times to come, they would be in dire need of fresh talent. According Randstad India, global HR service provider in India, the banking sector will generate 7-10 lakh jobs in the coming decade and the sector would be the among top job creators in 2016.

According to ‘Human Resource and Skill Requirements in the Banking, Financial Services & Insurance Sector (2022) report, apart from the on-rolls employment there is significant contractual employment across all the above segments through various financial positions such as Direct Selling Agents (DSA’s), Insurance agents, Mutual Fund Advisors, etc.

**Role and Importance of Banks in Economic Development of India**

Financial stability is one of the major factors for accelerating the rapid development of a country, and therefore banks play an important and active role in economic development of a country. If the banking system in a country is effective, efficient and disciplined, it is ensured that economic prosperity as a base stone which would bring a rapid growth in the various sectors of the economy

**Mobilising Saving for Capital Formation**

The commercial banks help in mobilizing savings through network of branch banking. People in developing countries have low incomes but the banks induce them to save by introducing variety of deposit schemes to suit the needs of individual depositors. They also mobilize idle savings of the few rich. By mobilizing savings, the banks channelize them into productive investments. Thus they help in the capital formation of a developing country.
Financing Industry

The commercial banks finance the industrial sector in a number of ways. They provide short-term, medium-term and long-term loans to industry. In India they provide short-term loans. Income of the Latin American countries like Guatemala, they advance medium-term loans for one to three years. But in Korea, the commercial banks also advance long-term loans to industry. In India, the commercial banks undertake short-term and medium-term financing of small scale industries, and also provide hire-purchase finance. Besides, they underwrite the shares and debentures of large scale industries. Thus they not only provide finance for industry but also help in developing the capital market which is undeveloped in such countries.

Financing Trade

The commercial banks help in financing both internal and external trade. The banks provide loans to retailers and wholesalers to stock goods in which they deal. They also help in the movement of goods from one place to another by providing all types of facilities such as discounting and accepting bills of exchange, providing overdraft facilities, issuing drafts, etc. Moreover, they finance both exports and imports of developing countries by providing foreign exchange facilities to importers and exporters of goods.

Financing Agriculture

The commercial banks help the large agricultural sector in developing countries in a number of ways. They provide loans to traders in agricultural commodities. They open a network of branches in rural areas to provide agricultural credit. They provide finance directly to agriculturists for the marketing of their produce, for the modernization and mechanization of their farms, for providing irrigation facilities, for developing land, etc. They
also provide financial assistance for animal husbandry, dairy farming, sheep breeding, poultry farming, pisciculture and horticulture. The small and marginal farmers and landless agricultural workers, artisans and petty shopkeepers in rural areas are provided financial assistance through the regional rural banks in India. These regional rural banks operate under a commercial bank. Thus the commercial banks meet the credit requirements of all types of rural people.

**Financing Consumer Activities**

People in underdeveloped countries being poor and having low incomes do not possess sufficient financial resources to buy durable consumer goods. The commercial banks advance loans to consumers for the purchase of such items as houses, scooters, fans, refrigerators, etc. In this way, they also help in raising the standard of living of the people in developing countries by providing loans for consumptive activities.

**Financing Employment Generating Activities**

The commercial banks finance employment generating activities in developing countries. They provide loans for the education of young person’s studying in engineering, medical and other vocational institutes of higher learning. They advance loans to young entrepreneurs, medical and engineering graduates, and other technically trained persons in establishing their own business. Such loan facilities are being provided by a number of commercial banks in India. Thus the banks not only help in human capital formation but also in increasing entrepreneurial activities in developing countries.
Help in Monetary Policy

The commercial banks help the economic development of a country by faithfully following the monetary policy of the central bank. In fact, the central bank depends upon the commercial banks for the success of its policy of monetary management in keeping with requirements of a developing economy.

Thus the commercial banks contribute much to the growth of a developing economy by granting loans to agriculture, trade and industry, by helping in physical and human capital formation and by following the monetary policy of the country.

Structure of India’s Banking Sector

The Indian financial system comprises a large number of commercial and cooperative banks, specialized developmental banks for industry, agriculture, external trade and housing, social security institutions, collective investment institutions, etc. The banking system is at the heart of the financial system.

The Indian banking system has the RBI at the apex. It is the central bank of the country under which there are the commercial banks including public sector and private sector banks, foreign banks and local area banks. It also includes regional rural banks as well as cooperative banks.
Reserve Bank of India

The central bank plays an important role in the monetary and banking structure of the nation. It supervises, controls, and regulates the activities of the banking sector. It has been assigned to handle and control the currency and credit of a country. In older days, the central banks were empowered to issue the currency notes and bankers to the Union governments. The Reserve Bank of India, the central bank of our country, was established in 1935 under the aegis of Reserve Bank of India Act, 1934. It was a private shareholders institution till January 1949, after which it became a state-owned institution under the Reserve Bank of India Act, 1948. It is the oldest central bank among the developing countries. The country had no central bank prior to the
establishment of the RBI. The RBI is the supreme monetary and banking authority in the country and controls the banking system in India. It is called the Reserve Bank’ as it keeps the reserves of all commercial banks.

**Commercial Banks**

Amongst the banking institutions in the organized sector, commercial banks are the oldest institutions, some of them having their genesis in the nineteenth century. Initially, they were set up in large numbers, mostly as corporate bodies with shareholdings by private individuals. In the sixties of the twentieth century, a large number of weaker and smaller banks were merged with other banks. As a consequence, a stronger banking system emerged in the country. Subsequently, there has been a drift towards state ownership and control. Today 27 banks constitute strong public sector in Indian commercial banking. Commercial banks operating in India fall under different sub-categories on the basis of their ownership and control over management. Commercial banks mobilize savings of general public and make them available to large and small industrial and trading units mainly for working capital requirements.

**Public Sector Banks**

Public sector in Indian banking emerged to its present position in three stages. First, the conversion of the then existing Imperial Bank of India into the State Bank of India in 1955, followed by the taking over of the seven state associated banks as its subsidiary banks, second the nationalization of 14 major commercial banks on July 19, 1969 and last, the nationalization of 6 more commercial banks on April 15, 1980. Thus 27 banks constitute the Public sector in Indian Commercial Banking.
Private Sector Banks

After the nationalization of major banks in the private sector in 1969 and 1980, no new bank could be set up in India for about two decades, though there was no legal bar to that effect. The Narasimham Committee on Financial Sector Reforms recommended the establishment of new banks in India. Reserve Bank of India, thereafter, issued guidelines for the setting up of new private sector banks in India in January 1993. These guidelines aim at ensuring that the new banks are financially viable and technologically up-to-date from the start. They have to function in a professional manner, so as to improve the image of commercial banking system and to win the confidence of the public.

Foreign Bank

Foreign Commercial Banks are the branches in India of the joint stock banks incorporated abroad. Their number has increased to forty as on 31st March, 2002. These banks, besides financing the foreign trade of the country, undertake normal banking business in the country as well. In order to operate in India, the foreign banks have to obtain a license from the Reserve Bank of India. A foreign branch bank is a type of foreign bank that is obligated to follow the regulations of both the home and host countries. Because the foreign branch banks' loan limits are based on the parent bank's capital, foreign banks can provide more loans than subsidiary banks.

Co-operative Banks

Besides the commercial banks, there exist in India another set of banking institutions called co-operative credit institutions. These have been in existence in India since long. They undertake the business of banking both in urban and rural areas on the principle of co-operation. They have served a
useful role in spreading the banking habit throughout the country. Yet, their financial position is not sound and a majority of co-operative banks has yet to achieve financial viability on a sustainable basis.

The cooperative banks have been set up under the various Co-operative Societies Acts enacted by the State Governments. Hence the State Governments regulate these banks. In 1966, need was felt to regulate their activities to ensure their soundness and to protect the interests of depositors. Consequently, certain provisions of the Banking Regulation Act 1949 were made applicable to co-operative banks as well. These banks have thus fallen under dual control viz., that of the State Govt. and that of the Reserve Bank of India which exercises control over them so far as their banking operations are concerned.

Cooperative banks are so-called because they are organized under the provisions of the Cooperative Credit Societies Act of the states. The major beneficiary of the Cooperative Banking is the agricultural sector in particular and the rural sector in general. The cooperative credit institutions operating in the country are mainly of two kinds: agricultural (dominant) and non-agricultural. There are two separate cooperative agencies for the provision of agricultural credit: one for short and medium-term credit, and the other for long-term credit. The former has three tier and federal structure.

**Regional Rural Banks**

Regional Rural Banks are relatively new banking institutions which supplement the efforts of the cooperative and commercial banks in catering to the credit requirements of the rural sector. These banks have been set up in India since October 1975, under the Regional Rural Banks Act, 1976. At present there are 196 RRBs functioning in 484 districts. The distinctive feature of a Regional Rural Bank is that though it is a separate body corporate
with perpetual succession and a common seal. It is very closely linked with the commercial bank which sponsors the proposal to establish it and is called the sponsor bank. The central government establishes a RRB, at the request of the sponsor bank and specifies the local limits within which it shall establish its branches and agencies.

Issues and Challenges Faced by India’s Banking Sector

The major challenge faced by the Indian Banking and Financial sector is that the level of financial exclusion in India is alarming and there is an urgent need to find a plausible solution to the same. The IBA–BCG survey of banks revealed that the level of confidence in finding profitable solutions for financial inclusion is not very high. Financial inclusion has solely been the responsibility of public banks up until now, but by using inclusive growth as one of the criteria for new licences (new banks have to open 25 per cent of their branches in rural areas); the RBI will have made the new private sector banks responsible as well. Currently, public sector banks have more branches than any other bank group in the rural and semi-urban areas. Amidst the signs of progress, the Indian banking sector has been facing multiple challenges in recent times. Few of them are:

Non-Performing Assets

NPAs have become a grave concern for the banking sector in couple of years and impacted credit delivery of banks to a great extent. As per a survey, net NPAs amount to only 2.36 percent of the total loans in the banking system. However, if restructured assets are taken into account, stressed assets account will be 10.9 percent of the total loans in the system. As per the International Monetary Fund (IMF), around 37 percent of the total debt in India is at risk.
India’s largest lender State Bank of India (SBI) reported a massive 67 per cent fall in consolidated net profit at 1259.49 crore rupees in the third quarter of the 2015-16 financial year and classified loans worth 20692 crore rupees as having turned bad. As per an estimate, the cumulative gross NPAs of 24 listed public sector banks, including market leader SBI and its associates, stood at 393035 crore rupees as on 31 December 2015. The Economic Survey 2015-16 also alarmed the policy makers about growing bad debts with the banks and their potential to disrupt the growth prospects in the future.

**Reduced Profits**

The banking sector recorded slowdown in balance sheet growth for the fourth year in a row in 2015-16. Profitability remained depressed with the Return on Assets (RoA) continuing to linger below 1 percent. Further, though PSBs account for 72 percent of the total banking sector assets, in terms of profits it has only 42 percent share in overall profits.

**Issue of Monetary Transmission**

Like reduced profits, this is also an off-shoot of burgeoning NPAs in the system. With the easing of inflation and moderation in inflationary expectations, the RBI reduced the repo rate by 100 basis points between January and September 2015. However, change in the key policy rate was not reflected in lending rates as banks are not willing to transmit the benefits of low interest policy regime due to low-availability of liquidity against the backdrop of high NPAs.
Consumer Expectations and Competition due to Growth of Technology

All PSBs are now on CBS platform and have developed capabilities to offer anywhere banking. Few have also started offering basic banking transactions on mobile for their customers. But this is just scarping the surface as the technology can be leveraged for a far greater effect to match with the expectation of consumer. PSBs must be able to leverage technology for building data warehouses and then be able to do data mining and analytics. The goal should be to use data for effective decision making at various levels, including product customization, developing business models and delivery channels, etc.

PSBs must be able to pitch suitable products for their customers through internet and mobile banking channels. Traditional businesses are slowly moving on-line and e-commerce is the preferred choice of the gen-next customer. The challenge before the PSBs is to upscale their capabilities, train their employees on the new technologies to benefit from the possibilities that adoption of technology can open up. A good thing going for the banks is the current recruitment of youngsters in the work force. These new-generation staffs are tech-savvy and can quickly connect with technology. The enterprising among them must be accorded freedom to experiment and suggest ways in which the bank could reengineer its processes for its own benefit and that of its customers.

Corruption

Scams in the erstwhile Global Trust Bank (GBT) and the Bank of Baroda show how few officials misuse the freedom they granted under the guise of liberalisation for their personal benefit. These scams have badly damaged the image of these banks and consequently there profitability.
Crisis in Management

Public-sector banks are seeing more employees retire these days. So, younger employees are replacing the elder, more-experienced employees. This, however, happens at junior levels. As a result, there would be a virtual vacuum at the middle and senior level. The absence of middle management could lead to adverse impact on banks’ decision making process.

Government Measures to Strengthen the Indian Banking Sector

The government and the regulator have undertaken several measures to strengthen the Indian banking sector.

- The Reserve Bank of India (RBI) has issued guidelines for Priority Sector Lending Certificates (PSLCs), according to which banks can issue four different kinds of PSLCs—those for the shortfall in agriculture lending, lending to small and marginal farmers, lending to micro enterprises and for overall lending targets – to meet their priority sector lending targets.

- The Reserve Bank of India (RBI) has allowed additional reserves to be part of tier-1 or core capital of banks, such as revaluation reserves linked to property holdings, foreign currency translation reserves and deferred tax assets, which is expected to shore up the capital of state-run banks and privately owned banks by up to Rs 35,000 crore (US$ 5.14 billion) and Rs 5,000 crore (US$ 734 million) respectively.

- Scheduled commercial banks can grant non-fund based facilities including Partial Credit Enhancement (PEC), to those customers, who do not avail any fund based facility from any bank in India.
• Ministry of Finance has planned to inject Rs 5,000 crore (US$ 734 million) in eight public sector banks in order to boost their capital,

• To reduce the burden of loan repayment on farmers, a provision of Rs 15,000 crore (US$ 2.2 billion) has been made in the Union Budget 2016-17 towards interest subvention.

• Under Pradhan Mantri Jan Dhan Yojna (PMJDY), 217 million accounts! have been opened and 174.6 million RuPay debit cards have been issued. These new accounts have mustered deposits worth almost Rs 37,000 crore (US$ 5.53 billion).

• The Government of India is looking to set up a special fund, as a part of National Investment and Infrastructure Fund (NIIF), to deal with stressed assets of banks. The special fund will potentially take over assets which are viable but don’t have additional fresh equity from promoters coming in to complete the project.

• The Reserve Bank of India (RBI) plans to soon come out with guidelines, such as common risk-based Know-Your-Customer (KYC) norms, to reinforce protection for consumers, especially since a large number of Indians have now been financially included post the government’s massive drive to open a bank account for each household.

• To provide relief to the state electricity distribution companies, Government of India has proposed to their lenders that 75 per cent of their loans be converted to state government bonds in two phases by March 2017. This will help several banks, especially public sector banks, to offload credit to state
electricity distribution companies from their loan book, thereby improving their asset quality.

- Government of India aims to extend insurance, pension and credit facilities to those excluded from these benefits under the Pradhan Mantri Jan Dhan Yojana (PMJDY).

- To facilitate an easy access to finance by Micro and Small Enterprises (MSEs), the Government/RBI has launched Credit Guarantee Fund Scheme to provide guarantee cover for collateral free credit facilities extended to MSEs upto Rs 1 Crore (US$ 0.15 million). Moreover, Micro Units Development & Refinance Agency (MUDRA) Ltd. was also established to refinance all Micro-Finance Institutions (MFIs), which are in the business of lending to micro / small business entities engaged in manufacturing, trading and services activities upto Rs 10 lakh (US$ 0.015 million).

1.3 SIGNIFICANCE OF THE STUDY

‗Credit Risk Management‘ is the buzzword, in banking institutions, which ensures the long-term success of the organization, because it protects shareholders and depositors money and prevents the organizations from bankruptcy. The herculean problems faced by the banks are assessing the credit worthiness of the individuals or business organizations who applies for various kinds of loans. The term ‘credit worthiness’ refers to the ability of the individuals or business organizations to repay the borrowed money as per the repayment schedule. There are no mystic formulae to exactly identifying the ‘credit worthiness’ of the individuals or business organizations, but still the banks are devising various risk management strategies to enhance the success rate in credit operations. For example, there are few credit rating agencies in
India, such as CRISIL, ICRA, CARE, ONICRA, FITCH (India Ratings & Research) & SMERA, which will rate the individuals and business organizations based on their past financial transactions, but still the ‘credit score’ by the credit rating agencies is not the magic wand to ensure 100% success in credit operations, because the ‘credit worthiness’ may get affected at any time due to loss of job, loss in business, illness, emergency situations in the family or even by wilful default of the creditors. The Reserve Bank of India has devised lot of strategies to prevent wilful default by the creditors and also established the penal measures to be taken against the wilful defaulters.

The banks can’t avoid lending loans and advances, because the interest of loans is the main sources of income to the commercial banks. Hence it plays an important role in gross earnings and net profit of the banks. Bank lending is very crucial for it makes possible the financing of agricultural, industrial, construction, and commercial activities of a country. The strength and soundness of the banking system primarily depends upon health of the advances. Therefore the ability of banks to formulate and adhere to policies and procedures that promote credit quality and curtail non-performing loans is the means to survive in the stiff competition. Inability to create and build up quality loans and credit worthy customers leads to default risk and bankruptcy as well as hampers in economic growth of a country. However, little work is done to search the ways and means that enable to quality loan creation and growth as well as to determine the relationship between the theories, concepts and credit policies both at country level or regional level.

Moreover the most significant demonstrating factor that highlight or induce the study is the total Gross Non-Performing Assets (GNPAs) of Indian banks stood at Rs. 5, 94,929 crores as at end March 2016, marking a
substantial jump of about Rs. 200,000 crore in just one quarter (at the end of December 2015 quarter, the total GNPAs stood at about Rs 4, 00,000 crore) over 90 per cent of this is on the books of Public-Sector Banks (PSBs). High level of NPAs and fresh generations of NPAs, restrictive practices in deployment of staff, low level of skill in credit operation, risk management, foreign exchange, treasury management and in-adequate training facilities to meet the requirement contributes poor efficiency in areas like credit operation and risk management which in turn contributes poor quality of credit management for generation of fresh NPAs. Hence the study is important where the bank wants to reduce its level of Non-Performing Assets (NPA) by tightening its credit policy and maintain an effective credit operation and risk management to increase their profitability. Hence, this study is assumed to be significant in indicating best practice and concepts for prudent lending to enhance the performance of credit operation and risk management to all managers and policy makers of the bank as well as to all financial institutions. Moreover, it may help as a benchmark for researchers who are interested in the area to extend it further.

1.4 SCOPE OF THE STUDY

1. Banks major revenue is receiving interest on loans & advances provided to many customers. Though the banks are able to generate good volume of interest, it is equally essential to assess/ evaluate credit worthiness of every loan applicant.

2. It would help the bankers to ensure high degree of safety or protective cover against possible future NPAs. On the other hand, bankers could not make stringer measures in providing loans. Because, more lending would result in more interest revenue. Adequate measures are to be taken by the banker to have protective cover over various risks associated with lending
3. The level of NPA (Non Performing Assets) in India is considerably increasing even after meticulous efforts taken by each banker under the direction of RBI. Complications are also more like profitability of the bank, reputation, consistency in performance, high regulation from RBI etc.

4. Credit operation requires high degree of analytical skills right from scrutinizing the application to tracking the repayment up to last installment.

The study covered credit policies, procedures, and credit operations of the Bank. It assessed the loan growth and performance. The study is concerned with identifying the major reasons for best practices of credit risk management, loan growth, and causes of loan default. The lending rules and procedures of the bank is the same in all branches, the result obtained, taking Case Study of this specific region is assumed to reflect the situation of all branches of the bank in the country under normal circumstances. The study reveals risk management which involves identifying, measuring, monitoring and controlling risks in the bank. It ensures to eliminate, reduce and control risks techniques for achievement of business strategy and objectives. The researcher has focused on business performance of bank and its attributes such as financial, operational and employees’ performance with respect to the credit risk management. It also recommends various ways to improve the credit operation and risk management of the IDBI banks through which better and strong business performance could be achieved in the fierce competitive banking industry.
1.5 CHAPTER SCHEME

Chapter one highlights on the back ground of the study which comprises of introduction, need for the study, and statement of the problem, research objectives, the scope and limitations of the study with the chapter scheme.

Second chapter deals with review of the literature of the previous studies that are suitable to the current research study. The review of several studies conducted in the field towards credit operations and risk management in banking sector and its relationship with business performance are represented in the chronological order.

The chapter three emphases on the theories supporting this thesis and theory connected to evaluation of credit operations and risk management. Moreover theories associated to business performance and its association with financial, operational and employees’ performance with various theoretical frameworks that are related to for the current study has been chapterized.

Fourth chapter represents the profile, overview, growth, structure, issues and government role in strengthening the Indian banking sector.

Chapter five describes research methodology and research methods underpinning the study. Hence it comprises of research design, data collection, sample design, research instrument, scale measurement and statistical tools for data analysis which focuses on research methodology and strategy with a view to identifying an appropriate approach for this particular research.

Sixth chapter entirely emphases on data collection, procedures, analysis and interpretation on the result of the outcome which are linked to the research questions and hypotheses development.
Chapter seven concludes the study with a detailed summary and findings from data analysis and interpretations of the research study. It also contains suggestions and identifications of theoretical contributions of the research, limitations of the study, and deals the concluding conclusion with further research.