CHAPTER I

Introduction
CHAPTER 1

INTRODUCTION

1.1 FINANCIAL INSTITUTIONS AND BANKING

Man always keeps himself engaged in some activity to satisfy his material and social needs. These activities are performed with an objective to satisfy a human want, physical or emotional. The sum total of human activity may be classified into two categories: (i) economic and (ii) non-economic. Non-economic activities are performed by human beings to satisfy their sentiments such as charity, religion, love, sympathy, patriotism, recreation etc. and also social obligations such as good neighbourliness, helping the poor and disabled.

Economic activities are undertaken to earn one's living and for production of wealth. (Dr Pawan Chugh, 2005)

Economics and Finance being intrinsically linked result in the necessity of having a Financial System which consists of a variety of institutions, markets and instruments related in the manner as shown below:

![Figure I-1: THE FINANCIAL SYSTEM](source: Prassana Chandra)
Introduction

Banking is probably the most important segment of the financial sector. It plays a pivotal role in the economic development of a country and forms the core of the money market.

As per the Banking Regulations Act 1949

- Banking means accepting for the purpose of lending or investment of deposits of money from public repayable on demand or otherwise and withdrawable by cheque, drafts order or otherwise (5 (i) (b)).
- Banking company means any company which transacts the business of banking (5(i)(c))

With the ongoing rapid transformation of the Indian Economic scenario the importance of having a healthy banking sector has increased several folds.

Mr V Leeladhar (2005), Deputy Governor of the Reserve Bank of India in his speech has highlighted that, "In recent years, there has been a considerable widening and deepening of the Indian financial system, of which banking is a significant component. With greater liberalisation, the financial system has come to play a much larger role in the allocation of resources than in the past and its role in future can be expected to be much larger than at present. The growing role of the financial sector in the allocation of resources has significant potential advantages for the efficiency with which our economy functions. Consequently, the adverse consequences of malfunction of the financial system are likely to be more severe than they used to be in the past. Hence, all our efforts today are focused at ensuring greater financial stability. Given the significance of the Indian banking system, one cannot afford to underplay the importance of a strong and resilient banking system."

In recent years, the banking industry has been undergoing rapid changes, reflecting a number of underlying developments. The most significant has been advances in communication and information technology, which have accelerated and broadened the (dissemination of financial information while lowering the costs of many financial activities. A second key impetus for change has been the increasing competition among a broad range of
domestic and foreign institutions in providing banking and related financial services. Third, financial activity has become larger relative to overall economic activity in most economies. This has meant that any disruption of the financial markets or financial infrastructure has broader economic ramifications than might have been the case previously.

These developments have manifold consequences for the institutional and systemic structure of the financial sector in general and banking in particular. Directly issued securities are replacing bank deposits as a vehicle for savings. Markets for risk have emerged in which exposures to specific market or credit risks can be bought and sold separately from the underlying financial assets. The business profile of financial institutions is also undergoing change. The service traditionally associated with 'banking' is being offered by institutions not normally characterized as banks, while banks have gradually made forays to non-banking activities. Mergers and takeovers of smaller institutions have led to the emergence of transnational conglomerates, offering services ranging from traditional commercial banking to investment banking and insurance.

With increasing globalisation and blurring distinction between different segments of financial intermediaries, there is a growing recognition that safeguarding the health of the financial system is of paramount importance for maintaining financial stability. Not surprisingly, the financial sector especially the banking sector in most emerging economies is passing through a process of change and India is no exception. With the banking sector being the mainstay of financial intermediation in emerging economies, developing a sound and healthy banking system through promotion of prudent financial practices is viewed as a *sine qua non* for safeguarding financial stability. (RBI 2001)

1.2 FAILURE/SICKNESS

A Bank, like any other business, is also susceptible to Failure. Though, unlike other businesses, in the case of a Bank failure the ramifications can be very wide and severe.
Internationally some dramatic major bankruptcies have occurred in recent years. Most notable was the huge Penn Central Company, which involved total assets at the end of 1969 of almost $7 billion and total debts outstanding of over $4 billion. The W. T. Grant bankruptcy was also of substantial magnitude, involving $1.2 billion of assets. A number of bankruptcies have raised questions of impropriety. Illustrative is the Equity Funding Company bankruptcy, which involved writing up fictitious life insurance.

The instabilities of the early 1970s involved large commercial banks as well as nonfinancial enterprises. The Franklin National Bank, which failed in 1974, had reached an asset size of $5 billion and was the twentieth largest of the nation's more than 14,000 FDIC-insured banks. In the same year, the Beverly Hills Bancorp went into bankruptcy. Earlier, the U.S. National Bank of San Diego had to be taken over by the FDIC, and questions of fraud were raised in connection with its prior management. Even large foreign banks ran into difficulties in 1974. The failure of Bankhaus I. D. Herstatt, one of Germany's largest private banks, sent shock waves through the international money markets.

**Failure** can be defined in several ways, and some failures do not necessarily result in the collapse and dissolution of a firm.

**Failure in an economic sense** usually signifies that a firm's revenues do not cover its costs. It can also mean that the rate of earnings on its historical cost of investment is less than the firm's cost of capital. It can even mean that the firm's actual returns have fallen below its expected returns. There is no consensus on the definition of failure in an economic sense.

Although **financial failure** is a less ambiguous term than **economic failure**, it has two generally recognized aspects. A firm can be considered a failure if it cannot meet its current obligations as they fall due, even though its total assets may exceed its total liabilities. This is defined as **technical insolvency**. A firm is a failure, or **bankrupt**, if its total liabilities exceed a fair valuation of its total assets (that is, if the "real" net worth of the firm is negative). *(Fred Weston, 1982)*
When the word *failure* is used, it usually connotes both technical insolvency and bankruptcy.

As Prof Surya Mookherjee (1988) says, in the contemporary business parlance a major highlight of the present decade seems to be the increasing incidence of industrial sickness in India across regions, sectors and industries. To some of us, the trend appears alarming, others have described the situation as grim or bleak and yet there are some who suffer from despondency and grope for antidotes to recuperate and revive the deteriorating and ailing state of industrial health. There happens to be unanimity of opinion that the ailment continues to plague the industrial sector. The crisis tends to perturb the policy makers, administrators, employers, industrialists, business associations, chambers of commerce, trade unions and employees and workers.

The implications of sickness are several: loss of production resulting in slowing the pace of growth of economy; loss of revenue, to the exchequer; increasing burden on the government in taking over sick units; blocking of scarce resources of banks and financial institutions; uncertainty suffered by them in the loan recovery; unemployment and its attendant impact on the morale of workers.

The concept of sickness as envisaged in Sick Industrial Companies (Special Provision) Act 1985 is a situation where an industrial company (being a company registered for not less than seven years) suffers, at the end of any financial year accumulated losses equal to or exceeding its entire net worth and also suffers cash loss in such financial year and the financial year immediately preceding.

"The causes of decline are identified along two lines: a) external to the organization, and b) internal to the organisation. Environment has limited resources. Consequently, only the fittest survive. Organizations that fail to align with the environment decline. The lack of initiative arises primarily from inertial pressure which could be the result of sunken investment, specialised assets, bureaucratic control, internal political and cultural constraints, external
restrictions, and managers' commitment to status quo due to their longer tenure in the organization and the industry", according to Sunil Maheshwari (2003).

Frequently the lack of surplus resources causes excessive control and managerial paralysis leading to failure. Similarly, excessive surplus resources lead to complacency. Careful management under these conditions can prevent possible decline of organizations.

One of the most common reasons for organizational decline has been 'one-man rule.' Organizations which are prone to this policy have a high 'risk of being blind to many perspectives as no one is in a position to play the role of a 'devil's advocate' while strategies are formed. Consequently, they are caught unawares owing to inadequate preparation for contingencies.

Organizations that are owned by large corporate offices before a decision is taken on turnaround or closure. Corporate offices that closely monitor the performance of the organisational unit will force the management of the declining organisation to take quick action to ameliorate the declining conditions thus reducing the period of inaction. However, in organizations that have diffused power structure, the crucial time for early corrective actions gets lost.

There are three broad alternatives for the future of declined organizations: they could be closed, sold, or revived without a change of ownership. The highly integrated firms prefer to turn around their units rather than closing or selling them. This is because the big corporate houses can provide technical, financial, and managerial help to such organizations for their revival which is important for the overall functioning of the group. However, in the loosely integrated organizational units of a corporate house, there is likely to be a longer managerial inaction."
1.3 RESERVE BANK OF INDIA FRAMEWORK TO IDENTIFY AND ARREST FAILURE IN BANKS

Reserve Bank of India (2002) has put together a scheme called ‘Scheme of Prompt Corrective Action’ under which RBI initiates certain Structured Actions in respect of banks which hit the Trigger Points in terms of CRAR, Net NPA and ROA. These are given below:

1. **Trigger Points:**

   **CRAR**
   
   (i) CRAR less than 9%, but equal or more than 6%
   
   (ii) CRAR less than 6% but equal to more than 3%
   
   (iii) CRAR less than 3%

   **NPAs**
   
   (i) Net NPAs over 10% but less than 15%
   
   (ii) Net NPAs 15% and above

   **ROA** below 0.25%

2. **Structured and Discretionary Actions**

   **CRAR** less than 9%, but equal or more than 6%

   **Structured Actions**
   
   - Submission and implementation of Capital Restoration plan by the bank
   - Bank will restrict expansion of its risk-weighted assets
   - Bank will not enter into new lines of business
   - Bank will not access/renew costly deposits and CDs
   - Bank will reduce/skip dividend payments
   - Bank will reduce its exposure to sensitive sectors like Capital Markets, Real Estate or investment in non-SLR securities
Introduction

- RBI will impose restrictions on the Bank on borrowing from inter-bank market
- Bank will revise its credit/investment strategy and controls

CRAR less than 6% but equal to more than 3%

Structured Actions
- All structured actions as in the earlier zone
- Discussion by RBI with the Bank’s board on Corrective Action Plan
- RBI will order recapitalization
- Bank will not increase its stake in subsidiaries
- Bank will revise its credit/investment strategy and controls

Discretionary Actions
- Bank/Govt. to take steps to bring in new Management/Board
- Bank will appoint consultants for business/organisational restructuring
- Bank/Govt. will take steps to change promoters/to change ownership
- RBI/Govt. will take steps to merge the bank if it fails to submit/implement recapitalization plan or fails to recapitalize pursuant to an order within such period as RBI may stipulate

CRAR less than 3%

Structured Actions
- All structured actions as in the earlier zone
- RBI will observe the functioning of the Bank more closely
- RBI/Govt. will take steps to merge/amalgamate/liquidate the bank or impose moratorium on the bank if its CRAR does not improve beyond 3% within one year or within such extended period as agreed to.
Introduction

Net NPAs over 10% but less than 15%

Structured Actions
- Bank to undertake special drive to reduce the stock of NPAs and contain generation of fresh NPAs
- Bank will review its loan policy
- Bank will take steps to upgrade credit appraisal skills and systems
- Bank will strengthen follow-up of advances including loan review mechanisms for large loans
- Bank will follow up suit filed/decreed debts effectively
- Bank will put in place proper credit risk management policies/process/procedures/prudential limits
- Bank will reduce loan concentration-individual group, sector, industry etc.

Discretionary Actions
- Bank will not increase its stake in subsidiaries
- Bank will not enter into new lines of business
- Bank will reduce/skip dividend payments

Net NPAs 15% and above

Structured Actions
- All structured actions as in the earlier zone
- Discussion by RBI with the Bank’s board on Corrective Action Plan
- Bank will not increase its stake in subsidiaries
- Bank will not enter into new lines of business
- Bank will reduce/skip dividend payments

ROA less than 0.25%

Structured Actions
- Bank will not access/renew costly deposits and CDs
- Bank will take steps to increase fee based income
Introduction

• Bank will take steps to contain administrative expenses
• Bank will launch special drive to reduce the stock of NPAs and contain generation of fresh NPAs
• Bank will not enter into new lines of business
• Bank will reduce/skip dividend payments
• RBI will impose restrictions on the Bank on borrowing from inter-bank market

Discretionary Actions

• Bank will not incur any capital expenditure other than technological upgradation and for such emergent replacements within Board approved limits
• Bank will not expand its staff/fill up vacancies

Any other action

Notwithstanding anything contained in the PCA framework, the Reserve Bank reserves the right to direct the bank to take any other action or implement any other direction, in the interest of the concerned bank or in the interest of its depositors.

1.4 TURNAROUND

However, once failure is impending or imminent it becomes imperative to initiate remedial action to reverse the failure trend or in other words a Turnaround.

Turnaround seems to be buzzword of the business parlance today. With increased globalization while the presence of behemoth multi-national corporations is increasing there is a concomitant and ever increasing reporting of loss making (sick) units. As a result we are witnessing heightened M&A (Mergers and Acquisitions) activity.

However, the situation is different today as compared to the situation more than a decade back. At that time the focus, in the case of a sick unit, was its
reference to the Board for Institutional and Financial Reconstruction, the aim being to get financial waivers or doles from the Government with the primary focus being humanitarian protection of the workers. Today, the focus is on TURNAROUND. The fine distinction being that between delaying death/symptomatic treatment and restoration of fighting fitness.

The change in the strategy in the process today and one-and-a-half to two decades back, thus is:

**Earlier Process:**

\[ \text{Running unit} \rightarrow \text{Sickness} \rightarrow \text{BIFR} \rightarrow \text{delayed death/marginal turnaround} \]

**Current Process:**

\[ \text{Running unit} \rightarrow \text{Sickness} \rightarrow \text{Takeover/Management change} \rightarrow \text{COMPLETE TURNAROUND} \]

*Figure I-2: Sickness Flow Chart*

The most recent and high-profile example of this being the Indian steel czar L.N. Mittal, who almost right from the beginning of his career has been acquiring sick steel plants and turning them around.

However, as David Garvin (2005) puts it, "Faced with the need for massive change, most managers respond predictably. They revamp the organisation's strategy, then round up the usual set of suspects - people, pay and processes - shifting around staff, realigning incentives and rooting out inefficiencies. They then wait patiently for performance to improve, only to be bitterly disappointed. For some reason, the right things still don't happen."
The question that arises is that what exactly is Turnaround? Transformation changes are usually in anticipation of or as a reaction to a deep crisis. Broadly there are two reasons for organisational decline. First, the environment in which the organization exists may itself be unfriendly and start to decline. Secondly, the environment may be friendly but the organization may start to decline due to incompetent management. (V. Nilakant, 1998)

Environment decline is referred to as K-decline and Organisation decline is called r-decline. The management of r-decline is called Turnaround Management.

Nilakant also says that, “There is no agreement on what constitutes organisational decline in the literature on organisational change. The most common definition of decline is decrease in profit or budget.”

Therefore, by extension, an increase in profit or budget of a declining organization can be defined as organisational turnaround.

According to Advent's Turnaround Services, “A turnaround is a collection of management interventions designed to take an ailing company and turn its fortunes around and get it back into a profitable mode. There are basically three approaches to turnaround: the “slash and burn” approach which strips the business down to its most valuable assets (from a salability perspective) without great attention to its long-term potential as a going concern with the intent of selling the assets for the benefit of the stakeholders; the “bankruptcy court” approach which places the company temporarily under the protection of the Court while it attempts to make a settlement with creditors and sheds unprofitable practices. The Court must approve most of its initiatives, including any settlement; and the “strategic workout” approach, which works with management and creditors to identify the business’s strengths, stop destructive practices and rebuild in a negotiated environment.”
So, let us try to understand the factors that govern the execution of a successful turnaround?

Is Turnaround merely another application of Business Process Reengineering?

University of California at Berkeley on its website clarifies:

Business Process Reengineering is a term we all have heard a lot of over the past few years especially in relation to large well-capitalized companies that have successfully implemented Business Process Reengineering (BPR). The question put forth here is. Does BPR have a place in turnarounds where time is of the essence? This creates an interesting question; is the company at a critical stage, merely praying for a miracle to survive, or is it under-performing with a viable market niche, or something in-between?

Can Business Process Reengineering be used in a turnaround? Part of the process includes empowering line management and creating an entrepreneurial atmosphere throughout the organization. This process takes time and most companies do not have the time to embark on the process especially in critical situations. The easy part of the turnaround is the first step. Decreasing the expenses, identifying and selling excess inventory, and collecting and installing good credit policies are only part of the solution. BPR provides a company with the possibility for long term success. The company needs to look beyond doing fewer tasks with fewer employees, putting employees on unpaid vacation, or lowering quality and service standards. Yes, many companies in need of restoration require increased productivity, improved inventory turns, cost reductions, but not lower quality and service. Lower quality and service can spell disaster in today’s globally networked market place.

To look closer at the use of BPR in a turnaround you need to determine up front if the company is terminal, critical or in need of long term restoration. The
termically ill company is definitely not a candidate for BPR. The terminally ill company needs to focus on quick reductions in costs and maximizing asset value and cash flow to protect the secured lenders and shareholders. The critically ill company requires a more thorough analysis of the business problems and usually requires quick action followed by a plan for long term restoration.

BPR is not applicable to every situation. It is however a critical tool in any successful turnaround leading to long term survival.

Turnaround Experts, **BIE Interim Executive**, say that, “Whilst change management usually concerns addressing the need for change before a situation becomes critical, an organisation finding itself on the brink of failure may have a more immediate need for change.

Turnaround management can help where a company is:

- making losses
- encountering a serious cash-flow crisis or has exhausted its bank facility
- carrying excessive overheads
- in need of radical action for survival
- in risk of insolvency
- in risk of breaking banking covenants
- on the brink of receivership"

As per **David Garvin (2005)** “Our research into organizational transformation has involved settings as diverse as multinational corporations, government agencies, non-profits, and high performing teams like mountaineering expeditions and fire fighting crews. We’ve found that for change to stick, leaders must design and run an effective persuasion campaign- one that begins weeks or months before the actual turnaround plan is set in concrete.”

“Turnaround leaders must also gain trust by demonstrating through word and
deed that they are the right leaders for the job and convince employees that theirs is the correct plan for moving forward. Accomplishing all this calls for a four part communication strategy:

1. Prior to announcing a policy or issuing a set of instructions, leaders need to set the stage for acceptance
2. At the time of delivery, they must create the frame through which information and messages are interpreted
3. As the time passes, they must manage the mood so that employees' emotional states support implementation and follow-through
4. At critical intervals, they must provide reinforcement to ensure that the desired changes take hold without backsliding

Thomas Stewart (2005) on studying the transformation of the German MNC Siemens says, “How did you know where to begin? You have to do a lot of things at once. You cannot transform a Company along only one dimension. You have to work on all of them at the same time and in a coherent manner. So, we developed our top+ program, which concentrates on three things: Cost reduction, Innovation and Growth.”

“We did a good job of deciding when we should or should not listen to advice from the financial markets. I talk regularly to the analysts, but in the end, you have to make your own decisions. If we had listened to the financial analysts during the 1990s we would have sold most of the company by now.”

(Ashok Hirway, 1988) Strategy for survival after study of three composite textile mills has been suggested as under:

- Honest and efficient management culture will have to be introduced
- Reduction of costs and wastage by optimizing the work force, machine utilization and machine productivity
- Gearing up of Technology, Product mix, product diversification, organisational structure, training etc
- There is required to be a quantum jump in Technology specifically
Introduction

oriented to the products.
• New kind of marketing strategy
• Streamlining of monitoring systems
• Better leadership

(Gary Young, 2000) Although all transformations are somewhat unique, the VHA experience provides a number of useful lessons for managing large scale organisational change. Based on the study the following seven lessons emerge:

1. Appoint leaders whose backgrounds and experiences are appropriate for the transformation
2. Follow a focused and coherent transformation plan
3. Persevere the presence of imperfection
4. Match changes in the external environment with changes in the Internal environment
5. Develop and Manage communication channels from the highest to the lowest levels of organization
6. Do not overlook training and education
7. Balance system wide unity with operating unit flexibility

(Surya Mookherjee, 1993) The KTL(Kamani Tubes Ltd) experience lends credence to the argument that in the event of increasing sickness and closure of enterprise, a viable alternative of restructuring would be to allow workers to form cooperatives and provide necessary financial and infrastructural support to enable them to turnaround the enterprise.

(Surya Mookherjee, 1988) Reserve Bank of India mentions that the primary cause of sickness of 65% of the units was found to mismanagement, weak management and dishonest management

He says that while analyzing the turnaround of Jaipur Metals and Electricals Ltd and Gujarat Tractor Corporation Ltd stresses that one the primary factors in the revival of these units was change in the top management (IAS Officers in both these cases)
Mookherjee says that, “In the final analysis, it is our contention that revival of sick units depends on a joint effort by both the union and management. Added to this, however, is the positive role of the Government.”

Pinto Roy (2005), tells of the ingredients of the turnaround of Jalpac India Ltd as:

- Infusion of fresh capital by angle investor
- Debt restructuring
- Expanding marketing operations
- Value added products
- Cutting down on wastages

Naresh Pandit (1996) in his An Overview of a Grounded Theory of Corporate Turnaround says that, “The content of appropriate recovery strategies were found to be contingent upon six sets of contextual factors: the causes of decline; the severity of the crisis; the attitude of stakeholders; industry characteristics; changes in the macroeconomic environment; and, the firm's historical strategy. The content of recovery strategies was usefully decomposed into operational level actions (management change, improved controls, reduction in production costs, investment in plant and machinery, decentralisation, improved marketing, and restructuring finances) and strategic level actions (asset reduction/divestiture and product/market reorientation). An implementation or process dimension was also discovered. Successful actions to effect recovery fall into four distinct (but overlapping) stages (the management change stage, the retrenchment stage, the stabilisation stage, and the growth stage). A diagrammatical depiction of this framework is given in figure 1”
**Figure I-3: A Theoretical Framework of Corporate Turnaround**

<table>
<thead>
<tr>
<th>CONTEXTUAL FACTORS</th>
</tr>
</thead>
<tbody>
<tr>
<td>The causes of decline</td>
</tr>
<tr>
<td>The severity of the crisis</td>
</tr>
<tr>
<td>The attitude of the stakeholders</td>
</tr>
<tr>
<td>Industry characteristics</td>
</tr>
<tr>
<td>Changes in the macroeconomic environment</td>
</tr>
<tr>
<td>The firm's historical strategy</td>
</tr>
</tbody>
</table>

**IMPLEMENTATION / PROCESS OF RECOVERY ACTIONS**

<table>
<thead>
<tr>
<th>RECOVERY STRATEGY CONTENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operational level:</td>
</tr>
<tr>
<td>Management change</td>
</tr>
<tr>
<td>Improved controls</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Stage</th>
<th>Recovery Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management change stage</td>
<td>Reduction in production costs</td>
</tr>
<tr>
<td>Retrenchment stage</td>
<td>Investment in plant and machinery</td>
</tr>
<tr>
<td>Stabilisation stage</td>
<td>Decentralization</td>
</tr>
<tr>
<td>Growth stage</td>
<td>Improved marketing</td>
</tr>
<tr>
<td></td>
<td>Restructuring finances</td>
</tr>
<tr>
<td></td>
<td><strong>Strategic level:</strong></td>
</tr>
<tr>
<td></td>
<td>Asset reduction/divestiture</td>
</tr>
<tr>
<td></td>
<td>Product/market reorientation</td>
</tr>
</tbody>
</table>
The Japanese methodology for Turnaround, as per Japan Management Consulting Partners, is illustrated below:

Turnaround Methodology Flowchart

1) Diagnostic
This phase is fact driven and goes beyond due diligence. The objective is to gather data needed to create the turnaround plan and the business vision.

2) Define the turnaround strategy
Strategy definition is based on tools of management consulting best practice such as competitive advantage by market segmentation (using Porter model) and SWOT analysis.

3) Build the turnaround team
While making the turnaround diagnostic and defining the turnaround strategy, it is imperative to progressively build a turnaround team based on existing human resources and also external resources such as industry experts and consultants.
4) **Build a business vision**
The purpose of the business vision is to bring the strategy in an appealing manner to all company employees. This phase is often neglected and is a major source of failure for turnaround which fail to mobilize employees.

5) **Create the revival plan a business vision**
The revival plan is the translation of the strategy and business vision in a commitment of the entire company to the turnaround.

6) **Execution**
The execution is based on the revival plan using techniques such as Cross Functional Teams.
Upgrading reporting systems and creating a balance score card system to follow progress are often necessary.

In the case of Banking, sickness is largely reflected in terms of increase in NPAs i.e. Non-Performing Advance. These are also referred to as Non-Performing Assets.
Non Performing Advance is defined as an advance where payment of interest or repayment of instalment of principal (in case of Term Loans) or both remains unpaid for a period of two quarters or more. An amount under any of the credit facilities is to be treated as 'past due' when it remains unpaid for 30 days beyond due date. *(RBI, 1999)*
The major challenge before any bank is to contain its NPAs while embarking on growth.

Outlining the Challenges faced by the Indian Banking sector, renowned consultants **ECS Limited**, explain that:
“The banking industry in India is undergoing a major transformation due to changes in economic conditions and continuous deregulation. These multiple changes happening one after another has a ripple effect on a bank trying to graduate from completely regulated sellers market to completed deregulated customers market.
• **Deregulation**: This continuous deregulation has made the Banking market extremely competitive with greater autonomy, operational flexibility, and decontrolled interest rate and liberalized norms for foreign exchange. The deregulation of the industry coupled with decontrol in interest rates has led to entry of a number of players in the banking industry. At the same time reduced corporate credit off take thanks to sluggish economy has resulted in large number of competitors battling for the same pie.

• **New rules**: As a result, the market place has been redefined with new rules of the game. Banks are transforming to universal banking, adding new channels with lucrative pricing and freebees to offer. Natural fall out of this has led to a series of innovative product offerings catering to various customer segments, specifically retail credit.

• **Efficiency**: This in turn has made it necessary to look for efficiencies in
the business. Banks need to access low cost funds and simultaneously improve the efficiency. The banks are facing pricing pressure, squeeze on spread and have to give thrust on retail assets

- **Diffused Customer loyalty**: This will definitely impact Customer preferences, as they are bound to react to the value added offerings. Customers have become demanding and the loyalties are diffused. There are multiple choices, the wallet share is reduced per bank with demand on flexibility and customization. Given the relatively low switching costs; customer retention calls for customized service and hassle free, flawless service delivery.

- **Misaligned mindset**: These changes are creating challenges, as employees are made to adapt to changing conditions. There is resistance to change from employees and the Seller market mindset is yet to be changed coupled with Fear of uncertainty and Control orientation. Acceptance of technology is slowly creeping in but the utilization is not maximised.

- **Competency Gap**: Placing the right skill at the right place will determine success. The competency gap needs to be addressed simultaneously otherwise there will be missed opportunities. The focus of people will be on doing work but not providing solutions, on escalating problems rather than solving them and on disposing customers instead of using the opportunity to cross sell.

**Strategic options with banks to cope with the challenges**
Leading players in the industry have embarked on a series of strategic and tactical initiatives to sustain leadership. The major initiatives include:

- Investing in state of the art technology as the back bone of to ensure reliable service delivery
• Leveraging the branch network and sales structure to mobilize low cost current and savings deposits

• Making aggressive forays in the retail advances segment of home and personal loans

• Implementing organization wide initiatives involving people, process and technology to reduce the fixed costs and the cost per transaction

• Focusing on fee based income to compensate for squeezed spread, (e.g. CMS, trade services)

• Innovating Products to capture customer ‘mind share’ to begin with and later the wallet share

• Improving the asset quality as per Basel II norms

Fig 1-6 Strategic options with banks to cope with the challenges

They suggest the Banks, in their transformation agenda have to address the following key challenges, which we find are similar to the Change Levers discussed later and which form the structure of this research:
Introduction

Strategy
Sales & Marketing strategy for both retail & wholesale banking
Expanding geographies

Brand
Understanding the values of the brand
Repositioning the brand to communicate the values

Organization restructuring
Re organization of the bank in line with the strategic thrust

Re engineering of the key business processes
Redesign of Sales processes to increase conversion ratio
Six Sigma process improvements for branch channel, Call Center & back office processes
Centralization of branch operations and deferred processes to free up resources

Cost efficiency
Reduction in Total cost of acquisition
Reduction in Transaction costs
Reduction in fixed and overheads cost

Right sizing and matching of skills
Manpower modeling for branch & back office at various volume scenarios
Productivity improvement for sales & service functions
Competency Assessment & profiling

Creating a high performing organization
Define new roles & responsibilities, KRA
Assessing competencies of people across levels and match the
position with the skill set
Designing and implementing a new PMS for restructured organization

**Change management & creating a new mind set**

Developing critical mass of champions and drive ‘Change’ across the organization to move from conventional banking to new age banking

To arrest deep-set sickness, reverse the disintegration process and then to set sail on a hitherto sinking ship is a Herculean task. However, sterling performances in Turnaround Management, in the corporate sector, their careful analysis and its ongoing in-depth research and documentation has given a management framework, which can be followed to effect a successful turnaround.

Each new turnaround, especially in a new sector, continuously adds to this body of knowledge.

Sickness and turnaround thereof is a major problem, however, as Kotler (2000) says, “Behind every problem is a brilliantly disguised opportunity.

**1.5 CHAPTER SCHEME FOR THE STUDY**

This study has been structured into seven chapters.

**CHAPTER I: INTRODUCTION.** This chapter introduces the topic and establishes the gap and the need for the study. It explores the management thought on organisational failure, sickness and turnaround.

**CHAPTER II: REVIEW OF LITERATURE.** This chapter delves deeper into the sea of literature with special emphasis on causes of organisational failure, implementation of change and turnaround. It also takes a focused look at these factors in the banking industry.

**CHAPTER III: OVERVIEW OF THE BANKING INDUSTRY.** This chapter gives a brief overview of the global and Indian economy and then looks at the Indian banking industry in some detail, including what the future portends. The
Introduction

chapter also gives a flavour of the turnaround at The Bank of Rajasthan Ltd.

CHAPTER IV: RESEARCH METHODOLOGY. This chapter gives the methodology adopted for the purpose of this research work. It also details out the Need for the study, its Objectives and the Hypothesis that have been framed.

CHAPTER V: CAUSES OF DECLINE OF THE BANK UNDER STUDY. This chapter studies the decline of the bank, its financials and the perceived reasons for its decline.

CHAPTER VI: TURNAROUND OF THE BANK UNDER STUDY. Moving from the decline of the previous chapter this chapter covers the process, perception and the perceived methodology of accomplishing the turnaround.

CHAPTER VII: CONCLUSIONS AND RECOMMENDATIONS. This chapter details out the salient findings of the research as well as the results of the Hypothesis. It also makes recommendations, based on the results of the research, to the management of The Bank of Rajasthan Ltd.