# INDIAN BANKING INDUSTRY

India's economic development and financial sector liberalization have led to a transformation of the Indian banking sector over the past two decades.

The Indian banking sector has emerged as one of the strongest drivers of India's economic growth. The Indian banking industry (US$ 1.22 trillion) has made outstanding advancement in last few years, even during the times when the rest of the world was struggling with financial meltdown. India's economic development and financial sector liberalization have led to a transformation of the Indian banking sector over the past two decades.

Today Indian Banking is at the crossroads of an invisible revolution. The sector has undergone significant developments and investments in the recent past. Most of banks provide various services such as Mobile banking, SMS Banking, Net banking and ATMs to their clients.

Indian banks, the dominant financial intermediaries in India, have made high-quality progress over the last five years, as is evident from several factors, including annual credit growth, profitability, and trend in gross non-performing assets (NPAs). While annual rate of credit growth clocked 23% during the last five years, profitability (average Return on Net Worth) was maintained at around 15% during the same period, while gross NPAs fell from 3.3% as on March 31, 2006 to 2.3% as on March 31, 2011.

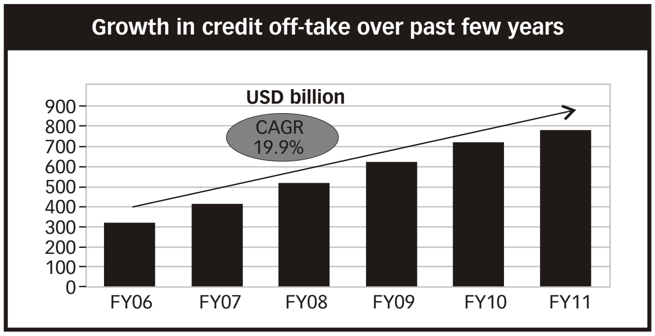
The Indian banking sector is a mixture of public, private and foreign ownerships. The below table highlights top 10 banks which contributed 58% share of the total credit as on March 31, 2011. The State bank of India has recorded highest market share. The Net Interest Margin of HDFC Banks is 4.2% which is highest among others.

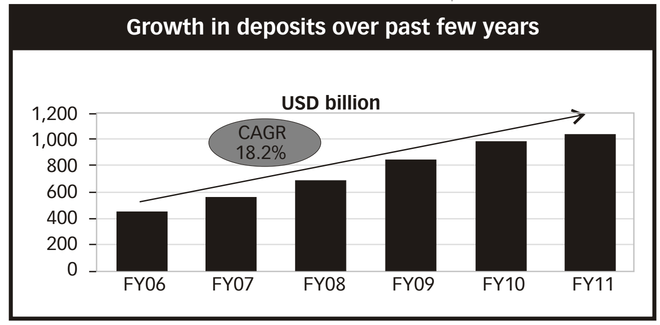
| Name of Bank | Credit Portfolio (Rs.Bn) Mar 2011 | Market Share (%) | NIM (%) Mar-11 | Tier I Capital (%) - Mar 2011 | RONW (%) Mar - 11 | Gross NPA(%) - Mar 11 |
|---|---|---|---|---|---|---|
| State Bank of India | 7567 | 18 | 2.9 | 7.8 | 13 | 3.3 |
| Punjab National Bank | 2421 | 6 | 3.5 | 8.4 | 24 | 1.8 |
| Bank of Baroda | 2287 | 5 | 2.8 | 10.0 | 24 | 1.4 |
| ICICI Bank | 2164 | 5 | 2.3 | 13.2 | 10 | 4.5 |
| Bank of India | 2131 | 5 | 2.5 | 8.3 | 17 | 2.2 |
| Canara Bank | 2125 | 5 | 2.6 | 10.9 | 26 | 1.5 |
| HDFC Bank | 1600 | 4 | 4.2 | 12.2 | 17 | 1.1 |
| IDBI Bank | 1571 | 4 | 1.8 | 8.1 | 16 | 1.8 |
| Axis Bank | 1424 | 3 | 3.1 | 9.4 | 19 | 1.1 |
| Central bank of India | 1297 | 3 | 2.7 | 6.4 | 18 | 2.2 |

Source : Annual Report, ICRA

The Credit off-take has increased at a CAGR of 19.9 % over FY 06-11. The Deposits have grown at a CAGR of 18.2% over FY 06-11 on account of strong growth in saving account. The net NPA has increased from 1% in FY 2008 to 1.12% in FY 10. The High interest rates and lower economic growth has impacted the repayment capacities of borrowers and hence pushing up the NPAs of banks. The net NPA decelerated from 1.12% in FY 10 to 0.97% in FY 11.

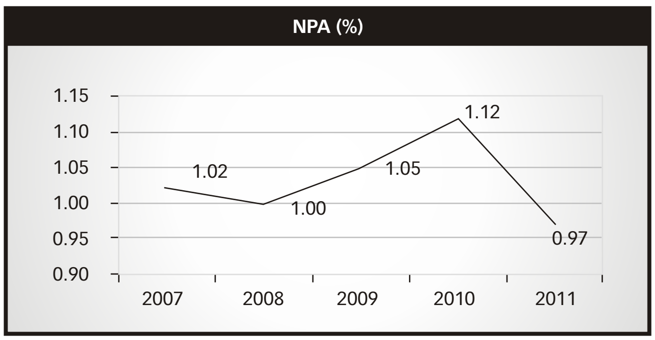
Indian banks enjoyed higher levels of money supply, credit and deposits as a

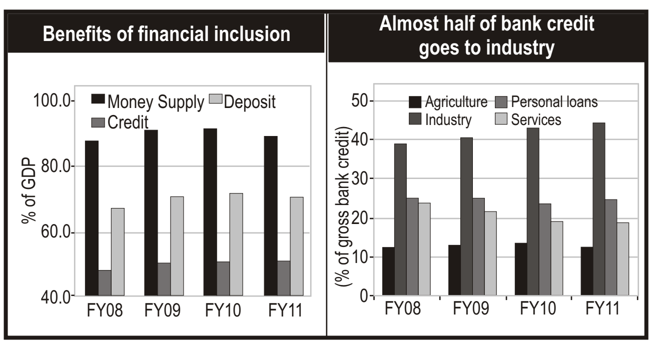



Source: RBI, Aranca Research

percentage of GDP in FY11 as compared to that in FY10 showing improved maturity in the financial sector. Credit growth remained high in the first half of FY11 on account of increased demand from industry and the service sector. Personal loans grew significantly by 17% during 2010-11 as compared with 4.1% during the previous year.




Source:RBI

**HISTORY**

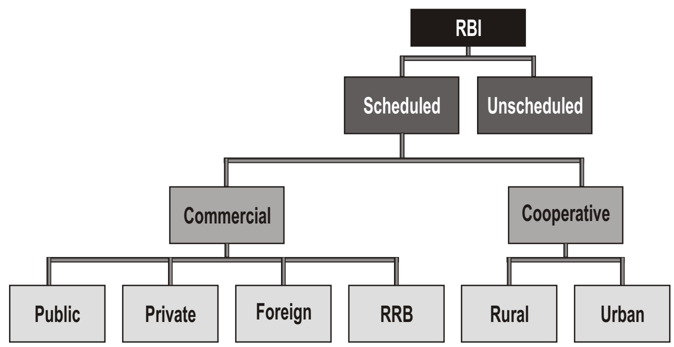
Although some form of banking, mainly of the money-lending type, has been in existence in India since ancient times, it was only over a century ago that proper banking began. The first bank in India, though conservative, was established in 1786. From 1786 till today, the journey of Indian Banking System can be segregated into three distinct phases. They are as mentioned below:

- Early phase from 1786 to 1969 of Indian Banks
- Nationalization of Indian Banks and up to 1991 prior to Indian banking sector Reforms
- New phase of Indian Banking System with the advent of Indian Financial & Banking Sector Reforms after 1991

The banking industry has moved gradually from a regulated environment to a deregulated market economy. The market developments kindled by liberalization and globalization have resulted in changes in the intermediation role of banks. The pace of transformation has been more significant in recent times with technology acting as a catalyst. While the banking system has done fairly well in adjusting to the new market dynamics, greater challenges lie ahead.

**STRUCTURE**

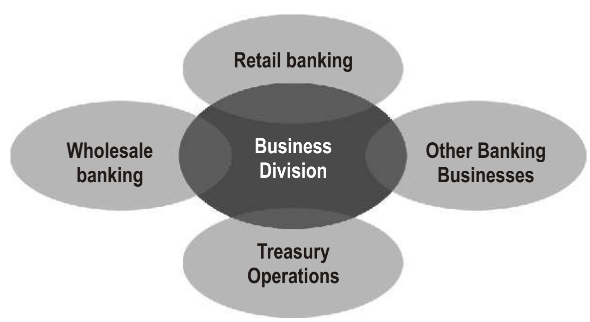
The Reserve Bank of India, the nation's central bank, began operations on April 01, 1935. It was established with the objective of ensuring monetary stability and operating the currency and credit system of the country to its advantage.




In India, the banks are being segregated in different groups. Each group has their own benefits, own dedicated target markets, limitations in operating in India. The commercial banking structure in India consists of Scheduled Commercial Banks and Unscheduled Banks.

Scheduled commercial Banks constitute those banks which have been included in the Second Schedule of Reserve Bank of India (RBI) Act, 1934. For the purpose of assessment of performance of banks, the Reserve Bank of India categorise them as public sector banks, old private sector banks, new private sector banks and foreign banks.

**BUSINESS DIVISION**



**Retail banking -** Loans to Individuals (Auto loan, Housing Loan, Education Loan and other personal loan) or small businesses.

**Wholesale banking** - Loans to Mid and Large corporate (Working Capital loans, Project finance, Term loans, Lease Finance)

**Treasury Operations** - Investment in Equity, Derivates, Commodities, Mutual Funds, Bonds, Trading and Forex operations

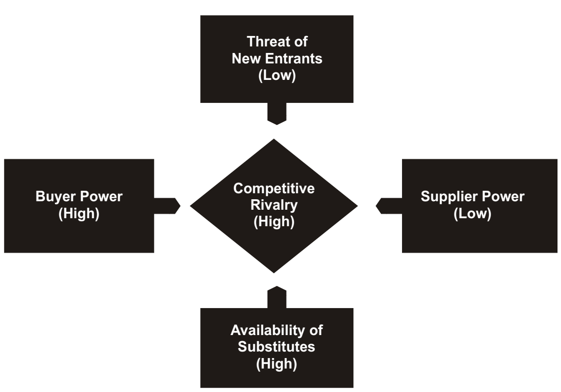
**Other Banking Businesses** - Merchant Banking, Leasing business, Hire purchase, Syndication services etc.

**SWOT ANALYSIS**

| STRENGTHS | WEAKNESSES |
|---|---|
| • Valuable contributor to GDP<br>• Regulatory environment<br>• Government Support | • Increasing NPA<br>• Low penetration<br>• Lack of product differentiation |
| **OPPORTUNITIES** | **THREATS** |
| • Modern Technology<br>• Untapped Rural Market<br>• Globalization | •Unorganized money lending market<br>•Customer dissatisfaction<br>•Rise of monopolistic structures |

**PORTER'S FIVE FORCES MODEL**

Banking is mainly a client oriented business. A high-quality of services to the client is crucial for the growth and stability of any bank. A wider distribution and access of financial services helps both consumers and producers to raise their welfare and productivity. Such access is especially powerful for the poor as it provides them opportunities to build savings, make investments, avail credit, and more important, insure themselves against income shocks and emergencies. To survive in an increasingly competitive environment, bank need to come up with various facilities like Internet banking, mobile banking etc. With the onset of mobile banking, the industry finds itself at the threshold of the next major technological leap.




**Buyer Power** - High bargaining power of customer's on account of banks renders uniform services to the clients. Now a day's almost all banks would like to provide requisite information very easily by way to Internet, Mobile banking to the clients

**Supplier Power**- Low bargaining power of supplier's on account of RBI regulatory benchmarks. Banks have to meet numerous regulatory standards created by RBI

**Competitive Rivalry**- High competition of account of number of prominent public, private, foreign along with cooperative banks

**Availability of Substitutes** - High menace from substitutes like NBFC's, Mutual funds, Government securities and T-bills

**Threat of new entrants** - Low threat of new entrants on account of banking regulations. Before setting up of a new bank, it is essential to take the consent of RBI.

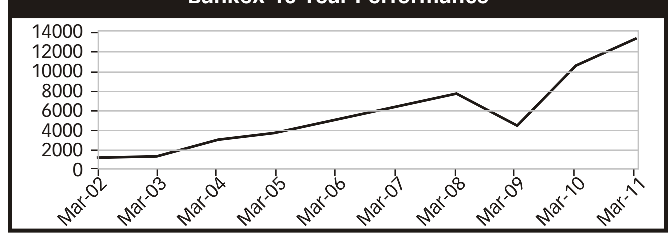
**PERFORMANCE**

The empirical studies have found a strong relationship between economic growth and financial development. Finance plays an important role in the economic growth. The charts depict the performance of Bankex in last 10 year and Relative performance of BSE Bankex & BSE Sensex in 2010-11. The performance of Bankex accelerated during the period March 2002 to March 2008. The performance of bankex decelerated during March 2008 March 2009 but thereafter it has shown increasing trend till March 2011.

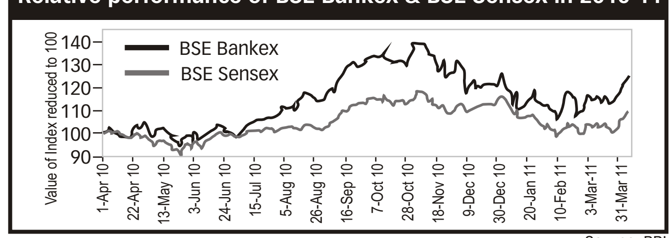
The four-month period (November 2010-February 2011) was marked by a consistent decline in all the indices caused by a number of global and domestic developments. The Sensex declined by 12.4%, while the Bankex Index declined by 18.3%.

Some of the global factors, such as increase in crude oil prices and high commodity prices contributed to inflation in the domestic economy. High inflation coupled with low growth rate in the Index of Industrial Production (IIP) and tightening interest rates has caused some concerns over the short-term economic growth, hitting the stocks in all the sectors, particularly those in the financial services sector.

**Bankex-10 Year Performance**




**Relative performance of BSE Bankex & BSE Sensex in 2010-11**




Source: RBI

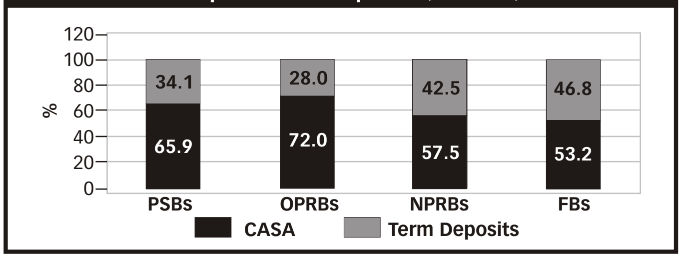
In recent years, Deposit, which constitutes 78 per cent of total liabilities of the banking sector has registered higher growth.

The higher growth in deposits emanated mainly from term deposits. The accelerated growth in term deposit could be as a result of higher interest rate environment. The Deposit and Borrowings chart depicts that the dependence of foreign banks and new private sector banks on borrowings was relatively high as compared with other bank groups.

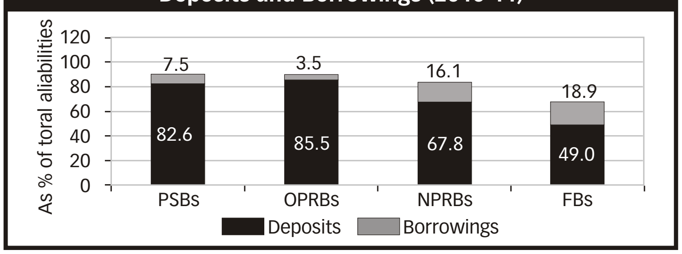
| Consolidated Balance Sheet of SCB at the end of Mar 2011 (Rs. Crore) | | | |
|---|---|---|---|
| **Particulars** | **Public Sector** | **Private Sector** | **Foreign** |
| Deposits | 43,72,985 | 10,02,759 | 2,40,689 |
| Cash and Bal. with RBI | 3,52,379 | 86,111 | 20,293 |
| Investments | 13,28,534 | 4,22,020 | 1,65,499 |
| Loans and Advances | 33,05,632 | 7,97,534 | 1,95,539 |

Source: B/S of Respective Banks (Include 26 Public Sector, 21 Private Sector & 36 Foreign Banks)

**Composition of Deposits (2010-11)**



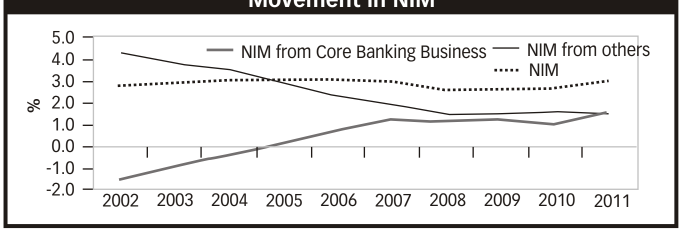

**Deposits and Borrowings (2010-11)**



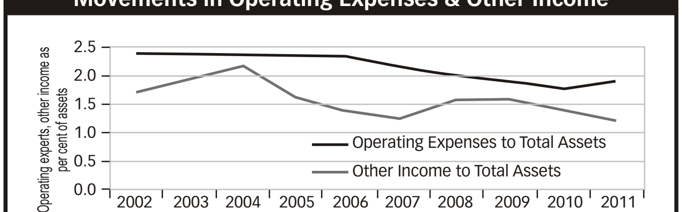

Source: RBI [Public Sector Banks (PSBs), Old Private Sector Banks (OPRBs), New Private Sector Banks (NPRBs), Foreign Banks (FBs)]

The other vital factors which determine the profitability of banking sectors are net interest margin (NIM), operating expenses and other income. Net Interest Margin (NIM) is used to assess efficiency of the banking sector. In India, during the last one decade, NIM was in the range 2.5 per cent to 3.1 per cent. The NIM of the Indian banking sector continues to be higher than some of the emerging market economies of the world.

**Movement in NIM**



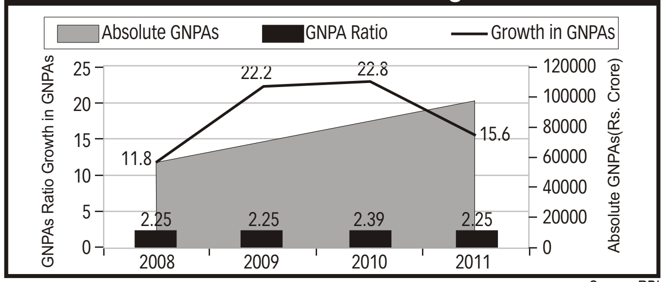

**Movements in Operating Expenses & Other Income**




Source: RBI

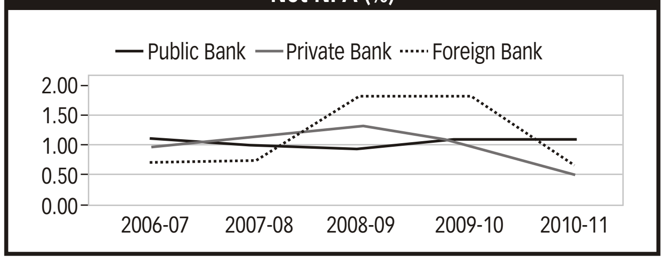
The asset quality of Indian banks has improved dramatically over the past 15 years. The gross NPA has reduced from 15.7% in March 1997 to 2.25 % in March 2011. The improvement in asset quality was visible in private sector banks and foreign banks. The asset quality of Public sector banks witnessed deterioration in 2010-11 owing to deterioration in asset quality of the SBI group. Agricultural sector contributed 44 per cent of the total incremental NPAs of domestic banks in 2010-11.

**Trends in Gross Non-Performing Assets**

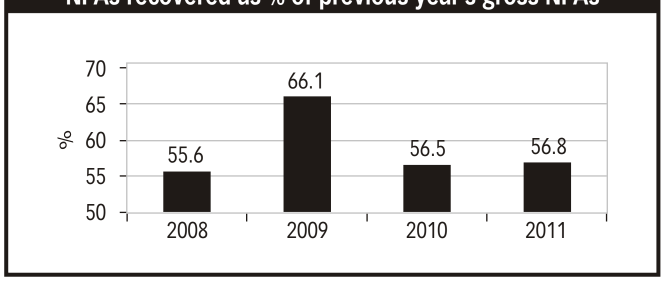



Source: RBI

**Net NPA (%)**



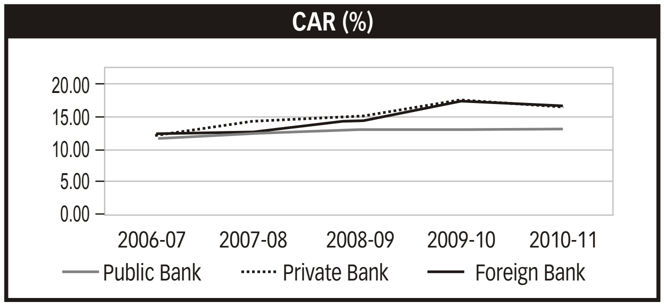

**NPAs recovered as % of previous year's gross NPAs**



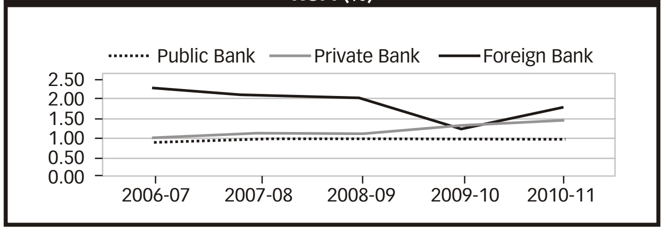

Source: RBI

| Capital to Risk Weighted Assets Ratio (CRAR) | | | | |
|---|---|---|---|---|
| **Bank group** | **Basel I** | | **Basel II** | |
| | **2010** | **2011** | **2010** | **2011** |
| **Public sector banks** | **12.1** | **11.8** | **13.3** | **13.1** |
| Nationalist banks | 12.1 | 12.2 | 13.2 | 13.5 |
| SBI group | 12.1 | 11.0 | 13.5 | 12.3 |
| **Private sector banks** | **16.7** | **15.1** | **17.4** | **16.5** |
| Old private sector banks | 13.8 | 13.3 | 14.9 | 14.6 |
| New private sector banks | 17.3 | 15.3 | 18.0 | 16.9 |
| **Foreign banks** | **18.1** | **17.7** | **17.3** | **17.0** |

**CAR (%)**



ROA (%)




The Capital to Risk Weighted Assets Ratio (CRAR) of all bank groups under Basel I remained well above the stipulated regulatory norm of 9 per cent in 2010-11. Among the bank groups, foreign banks registered the highest CRAR in 2010-11. To improve the capital adequacy of the public sector banks, government infuse corpus so that PSU banks can be in a position to compete with the other key players. The Return on Assets (ROA) of foreign bank is high compared to private and public banks during the period 2006-07 to 2010-2011.

**GLOBAL BANKING TRENDS**

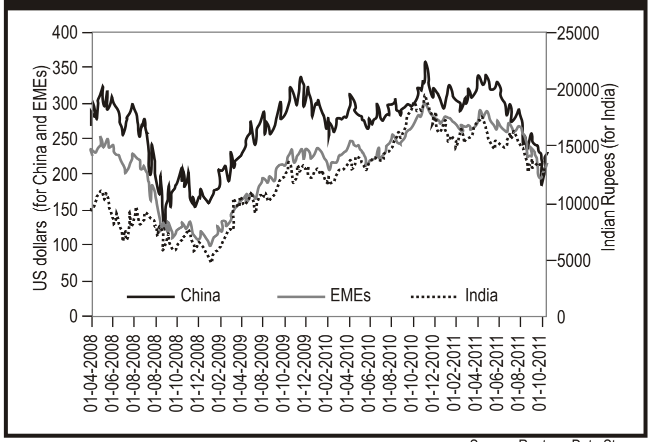
The Global financial crisis makes significant changes in the operating framework of banks. The performance of banks improves owing to strong lending growth and low credit losses. The present global macro-economic situation is differentiated by an unbalanced economic recovery across advanced and emerging economies, high levels of unemployment, inflationary pressures, and elevated levels of government debt. The Return on Assets (RoA), an indicator of banking system's profitability and soundness showed a moderate increase in the US and France in 2010. The RoA of US banks turned positive by 2010 after staying in the negative zone in 2008 and 2009; it showed a further increase in 2011. The RoA of Indian banks showed a modest rise between 2008 and 2010.

**Return on Assets (ROA) of Banks**

| Country | 2007 | 2008 | 2009 | 2010 | 2011* |
|---|---|---|---|---|---|
| Advanced economies | | | | | |
| France | 0.4 | 0.0 | 0.4 | 0.6 | ... |
| Germany | 0.3 | -0.1 | 0.2 | ... | ... |
| Greece | 1.0 | 0.2 | -0.1 | -0.6 | -0.3 |
| Italy | 0.7 | 0.3 | 0.2 | 0.4 | ... |
| Japan | 0.3 | -0.3 | 0.2 | 0.4 | ... |
| Portugal | 1.2 | 0.4 | 0.4 | 0.5 | 0.5 |
| Spain | 1.1 | 0.8 | 0.6 | 0.5 | ... |
| United Kingdom | 0.4 | -0.4 | 0.1 | 0.2 | ... |
| United States | 1.2 | -0.1 | -0.1 | 0.9 | 1.2 |
| Emerging and developing economies | | | | | |
| Russia | 3.0 | 1.8 | 0.7 | 1.9 | 2.3 |
| China | 0.9 | 1.0 | 0.9 | 1.0 | ... |
| India | 0.9 | 1.0 | 1.1 | 1.1 | ... |
| Malaysia | 1.5 | 1.5 | 1.2 | 1.5 | 1.8 |
| Brazil | 3.4 | 1.5 | 2.4 | 3.2 | 3.3 |
| Mexico | 2.3 | 1.4 | 1.5 | 1.8 | 1.6 |

SourceIMF,*Upto the period ending Mar 11, … Not Available

Bank Stock Indices in Select Economies




Source: Reuters, Data Stream

## Key Players

**PUBLIC SECTOR**

## State Bank of India

State Bank of India is the largest banking and financial services company in India. In addition to the banking services, the Bank through their subsidiaries, provides a range of financial services, which include life insurance, merchant banking, mutual funds, credit card, factoring, security trading, pension fund management and primary dealership in the money market. The State Bank Group, with over 16,000 branches, has the largest banking branch network in India. The bank has 131 overseas offices spread over 32 countries. The bank offers convenience of over 21000 ATMs in India.

The bank has recorded tremendous growth in Net Interest Income. The Net Interest Income has registered a growth of 37.41% from Rs.23,671.44 crores in 2009-10 to Rs. 32,526.41 crores in 2010-11on account of growth in interest income on advances and investments. The total assets of the bank increased by 16.17% from Rs.10,53,413.73 crores at the end of March 2010 to Rs. 12,23,736.20 crores as at end March 2011.

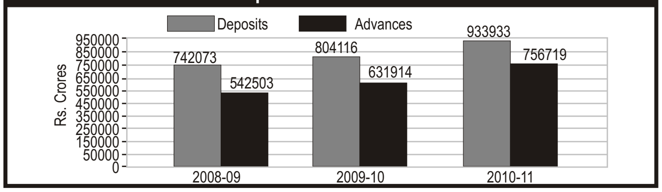
**Financial Highlights (Rs. Crore)**

| Particulars | Mar-11 | Mar-10 | Mar-09 | Mar-08 | Mar-07 |
|---|---|---|---|---|---|
| Deposits | 933932.81 | 804116.23 | 742073.13 | 537403.94 | 435521.09 |
| Investments | 295600.57 | 295785.20 | 275953.96 | 189501.27 | 149148.88 |
| Advances | 756719.45 | 631914.15 | 542503.20 | 416768.20 | 337336.49 |
| Interest Income | 81394.36 | 70993.92 | 63788.43 | 48950.31 | 37242.33 |
| Interest Expenses | 48867.96 | 47322.48 | 42915.29 | 31929.08 | 22184.13 |
| Net Profit | 8264.52 | 9166.05 | 9121.23 | 6729.12 | 4541.31 |

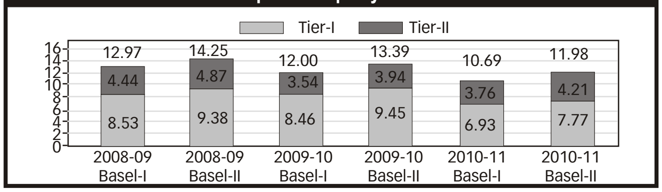
| Key Ratio (%) | | | | | |
|---|---|---|---|---|---|
| **Particulars** | **Mar-11** | **Mar-10** | **Mar-09** | **Mar-08** | **Mar-07** |
| Credit-Deposit | 79.9 | 75.96 | 74.97 | 77.51 | 73.46 |
| Investment / Deposit | 34.03 | 36.98 | 36.38 | 34.81 | 38.22 |
| Interest Expended / Interest Earned | 60.04 | 66.66 | 67.28 | 65.23 | 59.57 |
| Interest Income / Total Funds | 7.14 | 7.03 | 7.56 | 7.6 | 7.02 |
| Interest Expended / Total Funds | 4.29 | 4.69 | 5.09 | 4.95 | 4.18 |
| Net Interest Income / Total Funds | 2.85 | 2.34 | 2.47 | 2.64 | 2.84 |
| Operating Expenses / Total Funds | 2.02 | 2.01 | 1.86 | 2.07 | 2.35 |
| Net Profit / Total funds | 0.73 | 0.91 | 1.08 | 1.04 | 0.86 |
| RONW | 12.62 | 14.8 | 17.05 | 16.75 | 15.41 |

Source: Cline

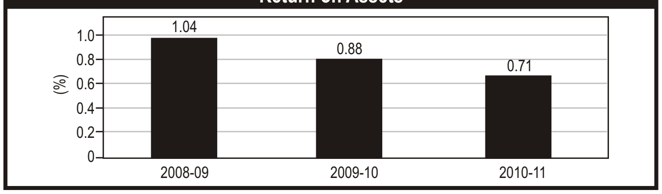
Deposits and Advances



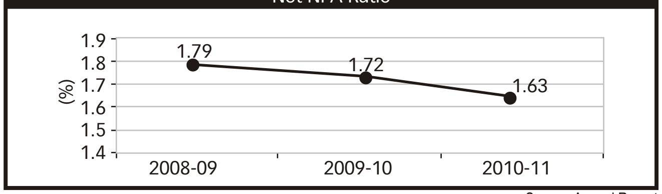

Capital Adequacy Ratio




Return on Assets




Net NPA Ratio




Source: Annual Report

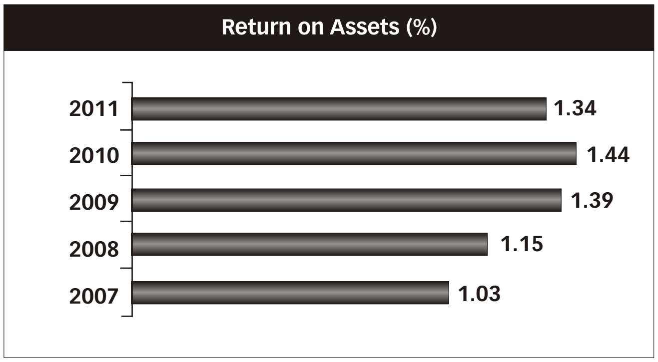
| Peer Comparison (March 2011) | | | | |
|---|---|---|---|---|
| **Particulars** | **State Bank of India** | **Punjab National Bank** | **Canara Bank** | **Bank of Baroda** |
| Net Profit | **8,264.52** | 4,433.50 | 4,025.89 | 4,241.68 |
| NII | **81,394.36** | 26,986.48 | 23,064.02 | 21,885.92 |
| Total Assets | **1,223,736.20** | 378,325.25 | 336,078.76 | 358,397.18 |
| EPS | **126.27** | 136.37 | 89.07 | 105.30 |
| CEPS | **141.87** | 144.45 | 92.49 | 111.49 |
| PE | **21.92** | 8.95 | 7.03 | 9.15 |
| BV | **1,023.40** | 632.49 | 405.00 | 534.43 |
| RONW (%) | **12.62** | 24.45 | 26.42 | 23.50 |

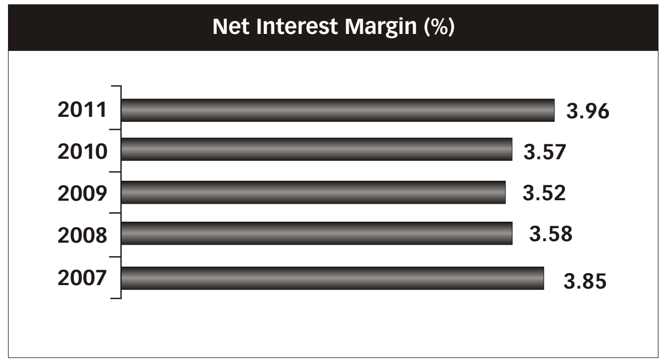
# Punjab National Bank (PNB)

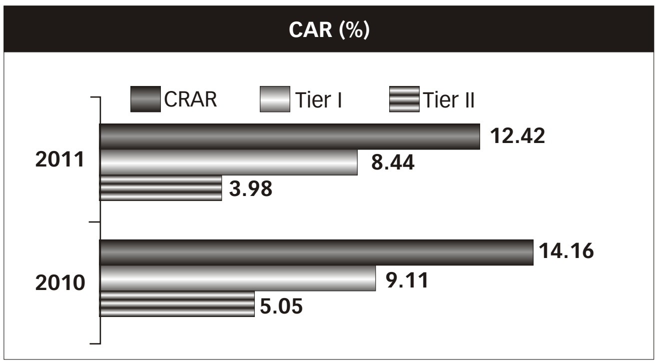
Punjab National Bank is one of the big four banks of India. PNB is ranked as the 2nd largest bank in the country after SBI in terms of branch network, business and many other parameters. They are recognized as the bank offering highest levels of customer satisfaction in Delhi and Chennai. The bank has a wide network of 5189 branches which comprise of 2047 Rural, 1154 Semi Urban, 1111 Urban and 877 Metropolitan branches at the end of March 2011.

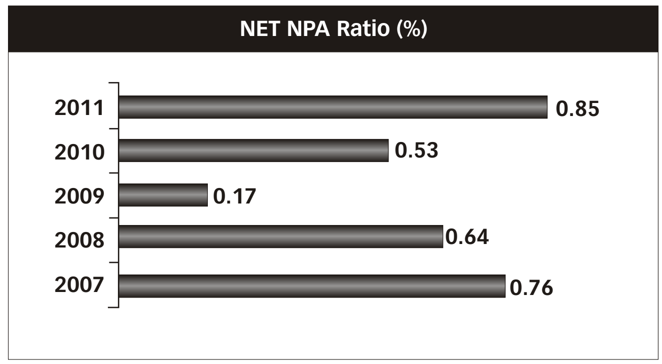
During FY 2010-11, with 39.16% share of CASA to domestic deposits, the Bank achieved a net profit of Rs 4433 crore. Bank has a strong capital base with capital adequacy ratio of 12.42% as on Mar'11 as per Basel II with Tier I and Tier II capital ratio at 8.44% and 3.98% respectively. As on March'11, the Bank has the Gross and Net NPA ratio of 1.79% and 0.85% respectively.

The Bank's total deposits amounted to Rs 3, 12,899 crore at the end of March' 2011, showing an absolute accretion of Rs. 63,569 crore and a growth of 25.5% over previous year. Ratio of Gross NPAs to Gross Advances stood at 1.79% at the end of March' 2011, while the ratio of Net NPAs to Net Advances was 0.85%.



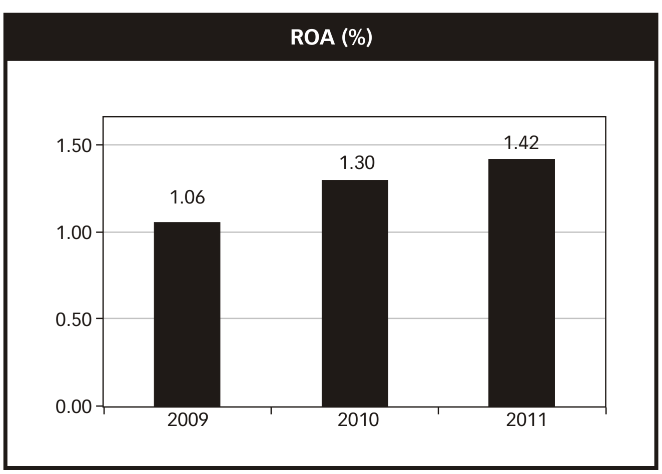



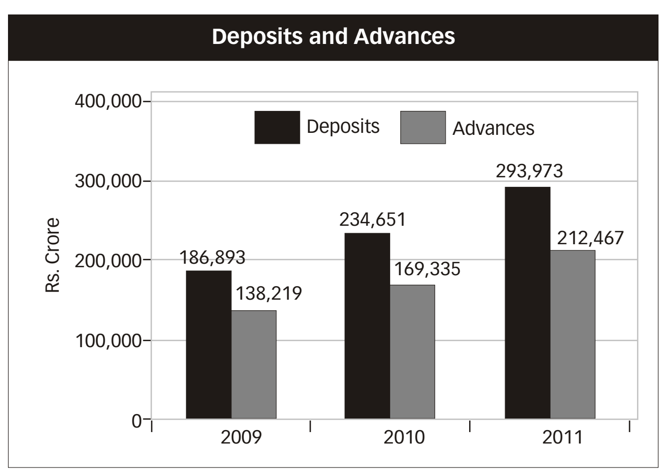

Source: Annual Report

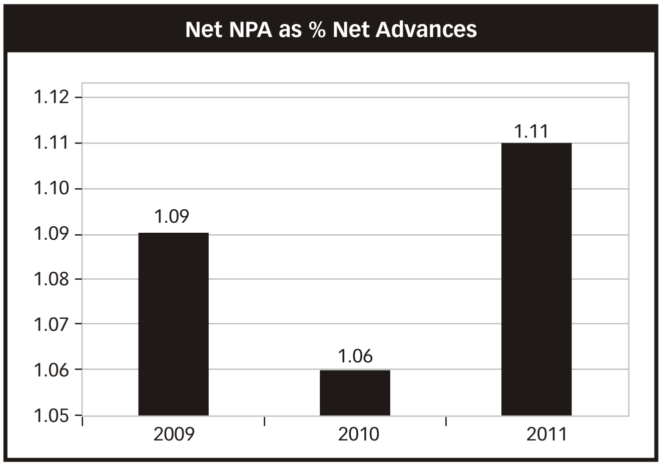
## Canara Bank

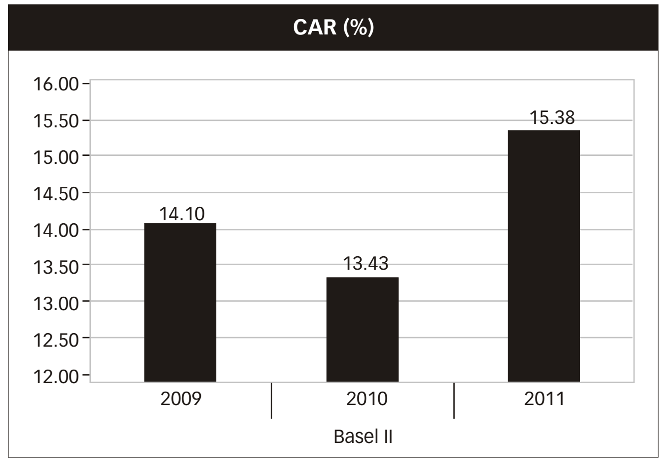
Canara Bank with headquarter in Bangalore operates in four segments, namely treasury operations, retail banking operations, wholesale banking operations and other banking operations. The bank has a branch network of 3257 including 4 overseas branches as on March 31, 2011.

The Net profit recorded a 33.25% growth of Rs. 4026 crore in FY 11 compared with Rs.3021 crore in FY 10. The Total Deposits registered a growth of 25.3% to reach Rs.293973 crore as at March 2011 compared to Rs.234651 crore a year ago. The Cost of Deposits has decreased from 6.12 in FY 10 to 5.80 in FY 11. The CASA deposits grew by 21.8% to reach Rs. 83117 crore as at March 2011. The net interest margin has improved by 32 bps from 2.80 in FY 10 to 3.12 in FY 11.






Source: Annual Report

PRIVATE SECTOR

# ICICI Bank

ICICI Bank Ltd is the second largest private sector bank in India by market capitalization. They are a publicly held banking company engaged in providing a wide range of banking and financial services including commercial banking and treasury operations. The Bank has a network of 2,752 branches and 8,003 ATMs in India, and has a presence in 19 countries, including India.

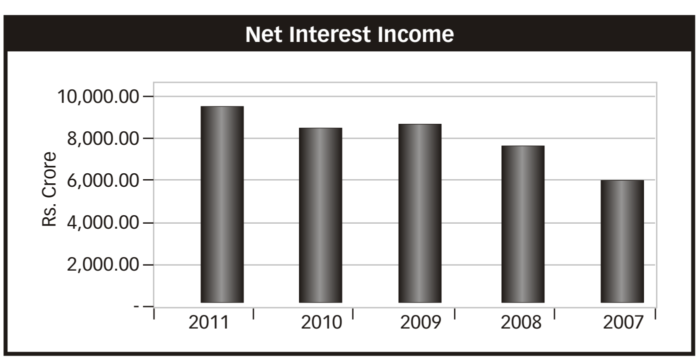
The net profit for fiscal 2011 was Rs. 5151.38 crore, representing a 28% increase over the previous year because of decrease in provisions and contingencies. The net interest income has increased by 11% from Rs. 8114 crore in fiscal 2010 to Rs. 9017 crore in fiscal 2011. The total advances grew by 19.4% in fiscal 2011 on account of strong growth in domestic corporate advances. The return on assets improved substantially to 1.34% in fiscal 2011 from 1.13% in the previous year.

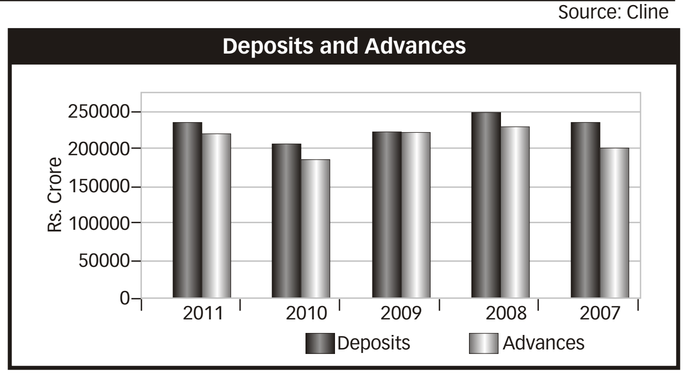
The total deposits have increased by 11.7% from Rs. 202016.60 crore at March 31, 2010 to Rs. 225602.11 crore at March 31, 2011. The proportion of current and savings account deposits in total deposits had increased from 28.7% at March 31, 2009 to 45.1% at March 31, 2011. The net non-performing asset ratio has reduced from 1.87% at March 31, 2010 to 0.94% at March 31, 2011. The capital adequacy position continued to be very strong, with total capital adequacy of 19.5% and Tier-1 capital adequacy of 13.2%.

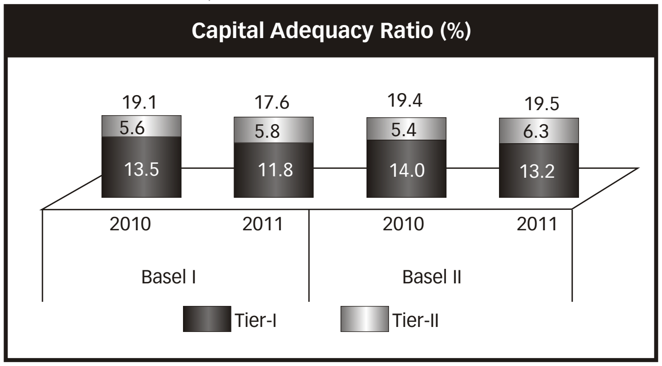
**Peer Comparison (March 2011)**

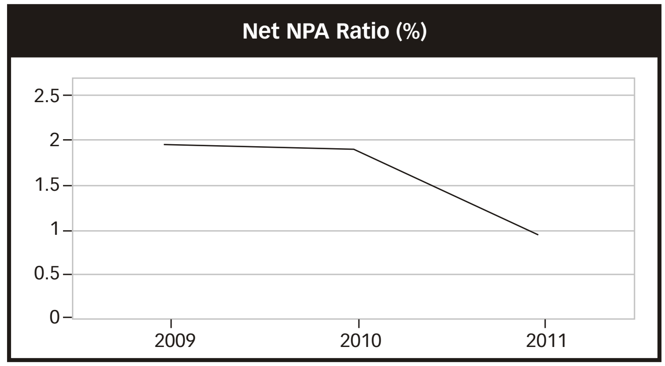
| Particulars | ICICI Bank | HDFC Bank | Axis Bank | Kotak Mah. Bank |
|---|---|---|---|---|
| Net Profit | **5151.38** | 3,926.39 | 3,388.49 | 818.18 |
| NII | **25,974.05** | 19,928.21 | 15,154.81 | 4,303.56 |
| Total Assets | **406,233.67** | 277,352.61 | 242,713.37 | 50,850.66 |
| EPS | **42.97** | 81.72 | 80.21 | 11.04 |
| CEPS | **47.85** | 92.41 | 87.26 | 12.38 |
| PE | **25.9** | 28.67 | 17.5 | 41.38 |
| BV | **478.29** | 545.46 | 462.77 | 92.23 |
| RONW (%) | **9.65** | 16.74 | 19.34 | 14.39 |

Source: Cline



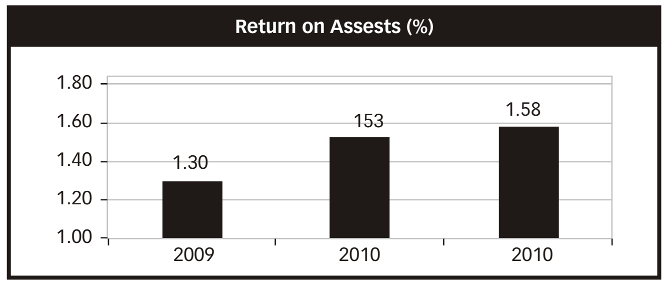


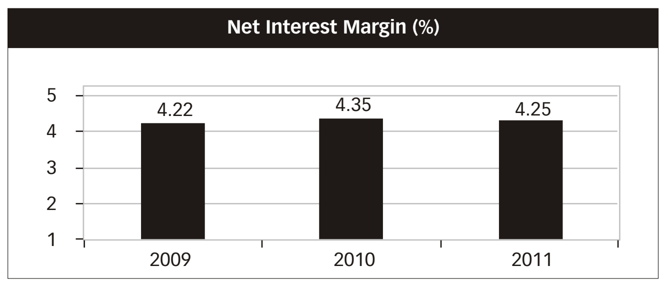



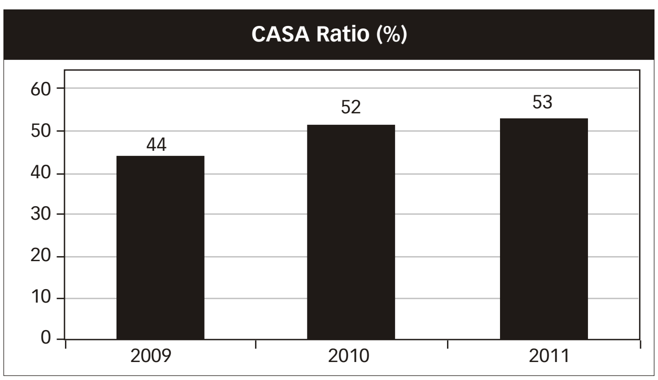

## HDFC Bank

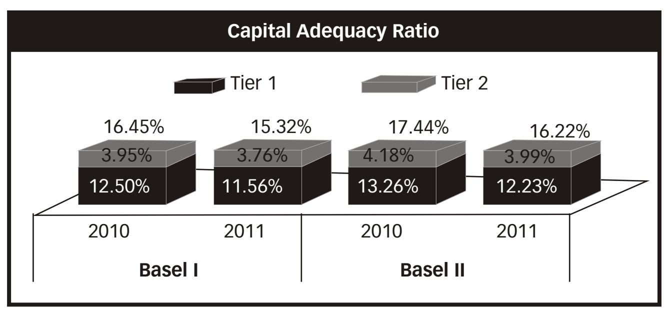
HDFC Bank Ltd is a major Indian financial services company based in Mumbai. The Bank has an enviable network of 1986 branches in 996 Indian cities and 5471 ATMs during the year 2010-11. The company has recorded an increase of 33% in net profit for FY 2011 of Rs. 3926 crore over the previous year. The Capital Adequacy Ratio (CAR) stood at 16.2% as against the regulatory minimum of 9.0%. Of this, Tier I CAR was 12.2% as on March 31, 2011.

The total deposits have increased by 24.6% at Rs. 208586 crore and the total advances were increased by 27% to Rs. 159983 crore over March 31, 2010. The Net interest income grew by 25.7% mainly on account of acceleration in loan growth. The proportion of core current and savings deposits (CASA) to total deposits continued to be healthy at 51% as on March 31, 2011.



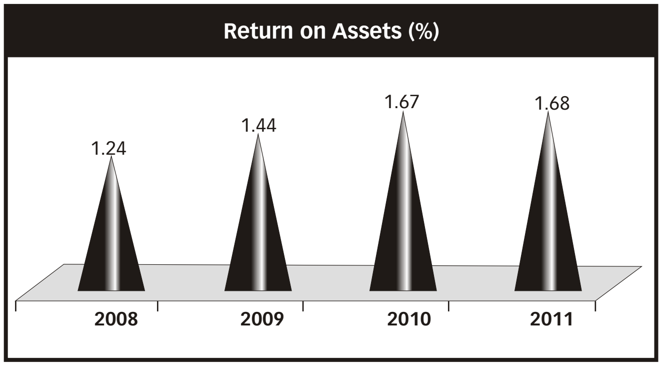

Source: Annual Report

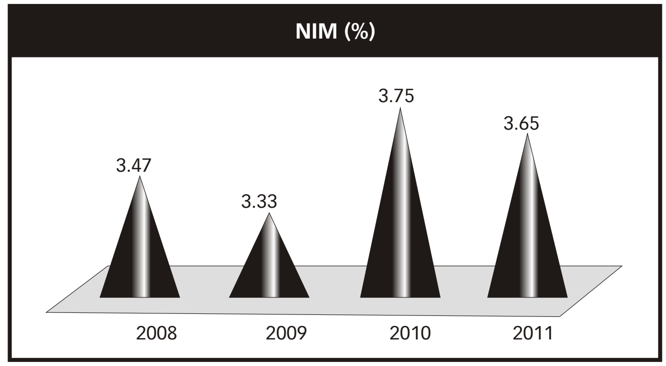
## AXIS Bank

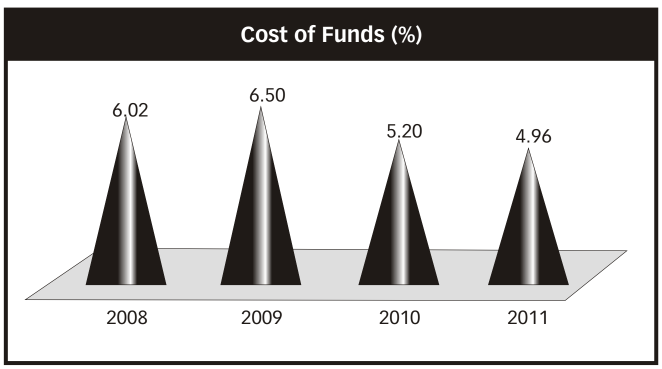
AXIS Bank is one of the fastest growing banks in private sector. The bank operates in four segments, namely treasury, retail banking, corporate/ wholesale banking and other banking business. The bank has a very wide network of around 1390 branches and 6,270 ATMs.

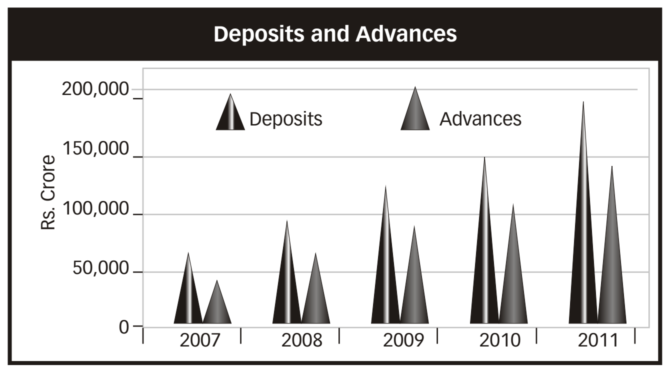
The net profits have grown at a CAGR of 47.52% during last 5 years. The bank reported a net profit of Rs. 3,388.49 crores for the year ended March 31, 2011 over the net profit of Rs. 2,514.53 crores in the previous year. The Net Interest Income increased by 31.14% to Rs. 6,562.99 crores in FY 11 from Rs. 5,004.49 crores in FY 10.

The bank maintain a healthy asset-quality with a ratio of Gross NPAs to gross customer assets of 1.01% compared to 1.13% in previous year and a Net NPA ratio of 0.26% compared to 0.36% in FY 10. The deposit and advances has increased by 33.93% and 36.48% respectively. The Capital Adequacy Ratio under Basel II stood at 12.65% in FY 11 against 15.80% in FY 10.




Source: Annual Report

**CONCERN**

Indian economy is one of the fastest growing economies of the world. The economy with its varied geography and demography has specific requirements in order to traverse to the next orbit and attain its full potential. Banks enable to cope with finance requirement for few industries such as Infrastructure, Housing, Real Estate etc. India's infrastructural financing needs are not only huge but also vital. Traditionally banks have been the major source of infrastructure financing and their exposure to infrastructure is already high at 17 per cent. There are several major concerns which are noted below.

- **Intensifying competition**

Indian banking industry has undergone qualitative changes due to banking sector reforms. Indian banking sector, which is dominated by state-controlled banks, has been facing formidable challenges. Due to this new emerging competition, Indian banks, especially PSBs, are trying their best to improve their performance and preparing to compete in the emerging global market. New private sector banks and foreign banks have more customer-centric policies, high quality services, new attractive schemes and computerized branches. All these services attracted more and more customers to their banks.

In this context, there is a need to examine the efficiency of public sector banks operating in India. Mainly, competition can intensify and banks will become more efficient. The transaction cost of customers could come down and a bank which is efficient, nimble and customer focused would always be able to do better than others. As a result of globalization, many new banks have entered the Indian banking industry, further intensifying the competition.

**Increasing NPA**

The asset quality of banks is one of the most important indicators of their financial health. It also reflects the efficacy of banks' credit risk management and the recovery environment. The Indian banks have shown very good performance as far as the financial operations are concerned. But Non-performing Assets (NPA) has caused some concerns. Despite write-offs, gross NPAs have continued to rise significantly. The new accretion to NPAs has been much faster than the reduction in existing NPAs due to lower levels of upgradation and recoveries.

To improve the banks' ability to manage their non-performing assets (NPAs) and restructured accounts in an effective manner and considering that almost all branches of banks have been fully computerized, the Reserve bank of India in its Monetary Policy Statement 2012-13 proposed the following measures:

To mandate banks to put in place a robust mechanism for early detection of signs of distress, and measures, including prompt restructuring in the case of all viable accounts wherever required, with a view to preserving the economic value of such accounts; and

To mandate banks to have proper system generated segmentwise data on their NPA accounts, write-offs, compromise settlements, recovery and restructured accounts.

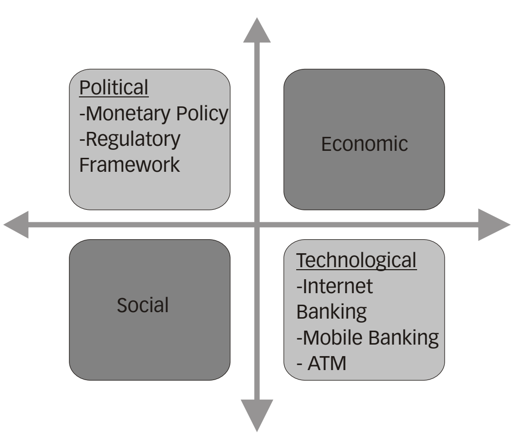
Despite these concerns, it is projected that the Indian banking industry will grow through leaps and bounds looking at the huge growth potential of Indian economy. High population base of India, rising disposable income, etc. will drive the growth of Indian banking industry in the long-term.

## BUDGET 2012-13

The financial market performance is often considered as a barometer of the economy. The Banking system is the dominant life-line of the financial market. The budget 2012-13 was largely positive for the banking sector. Though no major announcements were made, the Finance Minister target to reduce fiscal deficit will indirectly benefit the sector as it will lead to reduced inflation which in turn will lead to a reduction in policy rates.

Budget 2012-13 has proposed that individual tax payers be allowed tax deductions of up to Rs 10,000 on interests that they earn from their saving deposits. This proposal may give some boost to current and savings accounts (CASA) deposits. Any increase in these deposits will positively impact the net interest margins of banks. The other major announcement is to set aside Rs 15,888 crore for recapitalization of public sector bank and the target for agricultural credit raised by Rs. 1,00,000 crore to Rs. 5,75,000 crore.

## PEST ANALYSIS

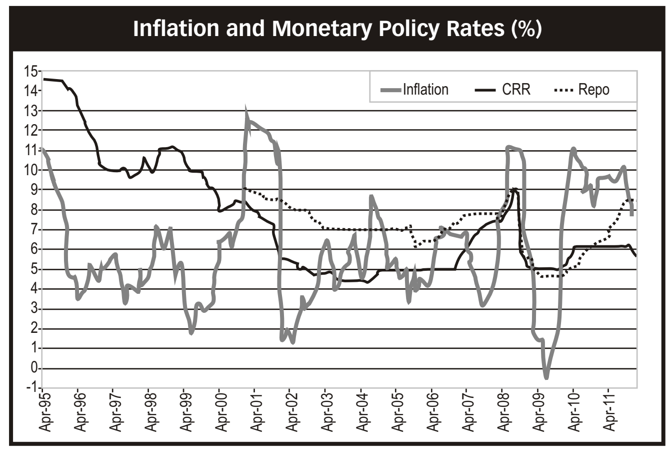



## POLITICAL ANALYSIS

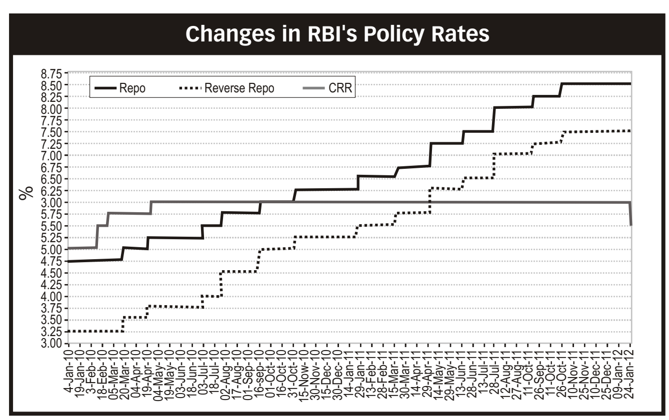
### MONETARY POLICY

Monetary policy becomes more restrictive over the past years. Inflation has remained a policy headache for the government and the central bank for the past two years. Inflation was a primary concern among the policy makers during 2010-11. Inflation, which remained at elevated levels for a large part of FY11, was largely driven by food and fuel items and later on transmitted to manufacturing products to become a general phenomenon. The average inflation rate in India was 7.99% between 1969 and 2010.

The Reserve Bank of India (RBI) in its annual monetary policy for 2012-13 on March 17, 2012 slashed the policy rates by 50 basis points. The repo rate at which banks borrow money from the RBI now stands at 8% from 8.50% earlier. Similarly, the reverse repo rate at which RBI borrows money from banks is now at 7% from 7.50% earlier. The cash reserve ratio (CRR) was left unchanged at 4.75%.




The Reserve Bank of India reduced the Cash Reserve Ratio (CRR) by 75 basis points from 5.5% to 4.75 % with effect from March 10, 2012. This reduction will inject around Rs.48,000 crore of primary liquidity into the banking system to ensure smooth flow of credit to productive sectors of the economy. Earlier, RBI in its third quarter review in January 2012 reduced the CRR by 50 basis points from 6% to 5.5% injecting a liquidity of Rs.31,500 crore into the banking system to mitigate the tight liquidity conditions, which was the first move in the CRR since it was increased to 6% in April 2010.

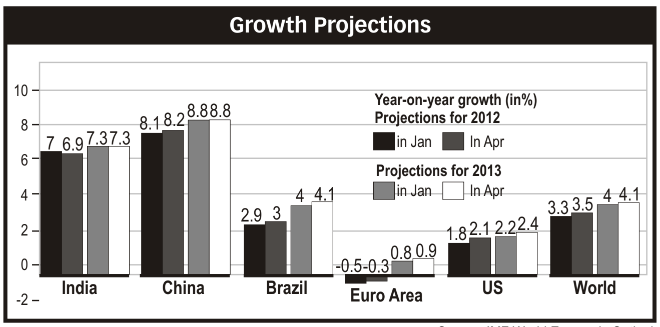


**REGULATION**

The expected integration of various intermediaries in the financial system would require a strong regulatory framework. It would also require a number of legislative changes to enable the banking system to remain contemporary and competitive.

**ECONOMIC ANALYSIS**

The Indian economy has recorded remarkable growth over the past decade. India's economic growth is expected to robust in 2012 and 2013. The International Monetary Fund (IMF) has pared India's economic growth projection to 6.9% in 2012 from its January estimate of 7%, the only emerging economy for which it has done so. Banks provide capital formation to various sectors which directly help in the growth of Indian economy.



Source: IMF World Economic Outlook

**SOCIAL ANALYSIS**

Indian banking system has been progressing rapidly. There are ample opportunities for the banks to cover untapped rural market. Yet, banking facilities are not available in many rural areas. Many farmers are taking loan from moneylender at a very high rate of interest. Small-scale industries would remain important for banks. Changes could be expected in near future for unorganised sectors.

**TECHNOLOGICAL ANALYSIS**

In recent time, Indian banking industry has been consistently working towards the development of technological changes and its usage in the banking operations for the improvement of their efficiency. With the application of new and improved technologies banks expected to reduce costs, time and give customer satisfaction. Core banking has changed the face of banking by offering value added services. Core banking applications helps to provide complete front and backend automation of banks. Technological developments would render flow of information and data faster leading to faster appraisal and decision-making. This would enable banks to make credit management more effective, besides leading to an appreciable reduction in transaction cost.

**Internet banking** or banking via the Internet can be considered a remarkable development in the banking sector. The ability to carry out banking transactions through the Internet has empowered customers to execute their financial transactions within the comfort of their homes and offices. In todays busy world, when people do not have much time even for personal work, Internet banking appears as a boon.

Internet Banking helped give the customer's anytime access to their banks. But for Internet banking there is a requirement of a PC / Laptop with an Internet connection. Mobile usage has seen an explosive growth in economies like India. India has reached 893.84 million mobile subscriber mark (Source: TRAI, Dec 2011) for a population of 1.21 billion. With **Mobile Banking**, customer can check their account balance, transfer funds 24 x 7, bills payments, booking of bus / flight tickets, recharge prepaid mobile and do a lot more effortlessly and securely. Banking through cell phone benefits the banks too. It cuts down on the cost of tele-banking and is more economical.

**ATM** (Automated Teller Machine) is electronic machine, which is operated by a customer himself to deposit or to withdraw cash from bank. ATMs reduce the work pressure on bank's staff and avoid queues in bank premises. ATMs are of great help to travellers. They need not carry large amount of cash with them. They can withdraw cash from any city or state, across the country and even from outside the country with the help of ATM.

**CONCLUSION**

The financial sector reforms have brought about significant improvements in the financial strength and the competitiveness of the Indian banking system. The prudential norms, accounting and disclosure standards, risk management practices, etc are keeping pace with global standards, making the banking system resilient to global shocks.

In the recent past, the Indian banking sector has undergone significant developments and investments. In this sector, there are huge opportunities and numerous challenges. Money laundering is a growing menace and it not only poses serious threat to the stability and integrity of the financial system but also to the sovereignty and safety of nations worldwide. In the coming days, challenges before banks would primarily lie in saving themselves from the growing threat of money laundering.