International Journal of Research in Innovative Multidisciplinary Studies
ISSN: 2583-4916
Jul – Dec, 2022 Vol 1., No. 2

A critical evaluation of the working of Banking Sector in India in the recent Years

ARUN PAUL
Alliance University, Bangalore

Banking sector serves as the support ecosystem for the Indian economy. It has been facing certain challenges relating to structural and operational efficiencies. This study aims to identify and understand these challenges and perform an evaluation of the working of the banking sector in India in the recent years.

Keywords: Banking, Banking Sector, Indian Economy

I. INTRODUCTION

The Indian banking industry is composed of public sector banks, private sector banks, foreign banks, cooperative banks, regional rural banks, payments banks, small finance banks. Their history dates back to the 18th century when the traditional way of Indian banking gave way to the modern forming of banking systems. The first bank established in India was the Bank of Hindustan which was founded in 1770 in Calcutta however it was closed down in 1832. Thereafter, Oudh Commercial Bank was established which is popularly considered to be the first commercial bank of India. Experiencing the growth of banking industry, Allahabad bank was formed in 1865 and Punjab National Bank was formed in 1894. Bank of Bengal, Bank of Bombay, Bank of Madras were established in the 19th century and were later merged to form the Imperial Bank. Post-independence, banking was considered to be an important sector for driving the economy and accordingly several initiatives were taken to develop this sector. In 1949, Banking Regulation Act was introduced to govern the working of the banking industry. In 1955, the Imperial Bank was nationalized and this led to the emergence of State Bank of India (SBI). This was followed by nationalization of SBI subsidiaries in 1959. In 1969, fourteen banks were nationalized i.e., brought under the control of the Government. In 1980, six more banks were nationalized. Pursuant to the second phase of nationalization, the government held the controlling stake of around 90% of the banking industry. Nationalization was proposed so as to promote financial inclusion and to ensure that the banking operations reach to the farther areas. In 1991, Liberalization, Privatisation and Globalization (LPG) reforms were introduced which covered opening of the banking sector as well. Thereafter, ten private banks were given the license to conduct banking activity. The prominent ones include ICICI Bank, HDFC Bank, Axis Bank and IndusInd Bank. In 2001, Kotak Mahindra Bank and in 2004, Yes Bank got the approvals to operate in the banking industry.

The banking regulator in India is called as the Reserve Bank of India (RBI). It is the central bank of India and is required to regulate and supervise the banking system. RBI further undertakes currency issuance, management of foreign exchange reserves, and maintenance of monetary stability. To manage the diversity of the Indian financial sector, other regulators work in conjunction with the RBI. These bodies include the Securities and Exchange Board of India (SEBI) to manage the capital markets, the Insurance Regulatory and Development Authority of India (IRDAI) to manage the insurance sector and the Pension Fund Regulatory and Development Authority of India (PFRDA) to manage the pension and social security component of the economy.

II. OBJECTIVES

The objective of this study is to perform an evaluation of the banking sector in India. The study aims to understand how the banking sector has been performing and what challenges has it been facing in the last few years.

III. METHODOLOGY AND ANALYSIS

The banking industry has been facing certain challenges which have been hampering its growth prospects. One of the challenges is the twin balance sheet problem. This phenomenon came into prominence recently when the banks were unable to grant more loans as their asset sides were filled with non-performing assets (NPAs) while the corporates were unable to access higher credits as they were unable to clear their liabilities. NPAs refers to those loans and advances which are unlikely to be repaid back. The level of Gross NPAs touched as high as 9% of gross advances recently. Such high amount of unrecoverable loans put a stress on the bank’s ability to function and to pass on the loans in an ongoing manner. Another example of twin balance sheet problem may be the case of IDBI Bank and Lanco Infratech. Another major challenge that the banking sector in India is facing is inadequate level of financial inclusion. Financial inclusion signifies the availability and accessibility of financial services. Financial inclusion affects the monetary component of the amount of assets involved under consideration. Another issue that has recently turned up is that of cyber security. With increased integration of digital banking services, the threat of cyber-attacks has also increased. Banks are in need to invest in modern security systems and protocols to prevent the customer's personal data and to prevent financial frauds. The banking sector is under stress from competitive forces from Non-Banking Financial Companies (NBFCs). NBFCs signifies those financial institutions that provide different financial services involving insurance, loans, investments, credit facility etc. but are not considered to be a bank. They are gaining market share gradually due to their availability, accessibility, affordability and flexibility. Banking industry share in the market needs to cater to this aspect as well.

Another important issue facing the banking sector in India is the issue of financial literacy. Many individuals in India lack basic financial knowledge and are not aware of the various financial products and services available to them. This can lead to a lack of trust in the banking system and can also result in individuals falling prey to financial frauds. Banks need to invest in financial literacy programs and educate their customers on how to manage their finances and make informed financial decisions.

In order to perform and outstanding achievement in the banking sector, the companies need to hire skilled talent. However, the banking sector in India has been facing shortage of skilled manpower in the recent years. Banks today require personnel armed with the knowledge of artificial intelligence, data analytics, cybersecurity and forensic accounting which are difficult to find.

The banking industry has been trying to improve the overall customer experience. With increased competition, customer experience is becoming a metric to measure the performance of a bank with its peer. With higher number of alternatives being made available to customers, the banking industry need to focus on providing a convenient and memorable to retain and capture the market share. This involves exploration and investment in digital technologies, innovative solutions and disruptive ideas. Thereafter, the banking industry in India is facing the issue of sustainability. Banks need to undertake viable banking operations and take into considerations different economic, social and environmental factors for analytical decision making.

The banking sector has suggested that they have been facing certain challenges when it comes to compliance with multiple laws, rules and regulations. With banks undertaking foreign transactions, the complexity of regulations has also been increasing. For instance, compliance with the Foreign Contribution Regulation Act (FCRA), the Prevention of Money Laundering Act (PMLA), Foreign Exchange Management Act (FEMA) and the Reserve Bank of India (RBI) regulations require professional competence and availability of skilled mindset. Furthermore, banks require dedicated software systems and compliance management systems to avoid delays and lapses in meeting the compliance part and regulatory requirements.

IV. CONCLUSION

Accordingly, the banking industry has been facing certain emerging challenges amongst which some have been discussed herein such as increasing levels of non-performing assets, inadequate level of financial literacy, lack of financial inclusion, loss of market share to non-banking financial companies (NBFCs), lack of skilled manpower, the requirement to improve customer experience and the requirement to adopt sustainable banking practices. In order to solve the challenges, it is hereby proposed that the banks may consider investing in advanced technology, developing skilled workforce, improving customer service, and prioritizing the sustainability levels. The banking industry further needs to assess the level of financial inclusion. A considerable part of the population still does not possess accessibility to basic banking services and products. This is seen more in rural areas, tier 2 and tier 3 cities where there is a shortage seen in the number of bank branches and ATMs. This research suggests Banks also need to focus on expanding their reach to unbanked and underbanked areas by opening more branches, providing mobile banking services and other digital platforms.

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