



Indian banking sector-current issues and challenges

Shruthi G¹, S Indumati²

¹ Research Scholar, Department of Studies in Economics and Co-operation, University of Mysore, Manasagangothri, Mysuru, Karnataka, India

² Professor, Department of Studies in Economics and Co-operation, Former Vice Chancellor, Davangere University (University of Mysore), Manasagangothri, Mysuru, Karnataka, India

Abstract

The banking sector is the salvation of any modern economy. The success or failure of any economy is depends on its banking sector which is an imperative financial pillars of the financial system. Amidst the sign of progress, the Indian banking sector has been facing multiple and concurrent challenges such as higher NPAs, Cyber crime, Bank fraud, poor assets quality management and lower capital adequacy ratio. The banking industry is changing at a phenomenal speed. Banks are capable to reach large masses with modern technology to facilitate greater ease of communication and transactions are carried out through the internet and mobile devices. Banking sector has made quick strides in streaming and aligning itself to the new aggressive business environment. In concerned with this, the present study needs to spell out some of the major issues and challenges faced by Indian Banking sector.

Keywords: NPAs, capital adequacy ratio, bank fraud and cyber crime

Introduction

Banks in India considered being lifeline of the economy. They play a catalytic role in activating and sustaining economic growth. As per industrial report, India's banking sector is expanding rapidly and has the potential to become the third largest banking industry in the world by 2025. However, increasing emphasis on globalization of the Indian economy has opened up new avenues and challenges for Indian banks. Liberalization of prudential regulations has thrown in a lot of opportunities for Indian banks to grow and diversify the areas of business operations. Moreover, globalization has ushered in restructuring of the banking and financial sector through a series of mergers and amalgamations and eventually brought in convergence of different activities and business in the banking sector. The Indian banking system has been a complete transformation during the last two decades.

Table 1: Indian Banking Sector- At a Glance (Amount in ₹ crore)

Indicators	2015-16	2016-17	2017-18	2018-19	2019-20
Total Liabilities/assets	131299300	14158600	1,52,55,033	1,66,01,045	1,80,14,875
Deposits	10092700	11113900	1,17,94,005	1,28,86,643	1,39,75,095
Borrowings	1448800	1280700	16,82,309	17,09,670	16,96,046
Loans and Advances	7896500	8118200	87,45,997	96,76,183	1,03,01,914
Investments	3327800	3652200	41,26,237	43,22,464	46,89,842
Off-balance sheet exposure (as percentage of on-balance sheet liabilities)	111	107	113.5	122.8	125.3
Total consolidated international claims	511300	716800	6,38,094	6,29,621	5,78,412
Net Profit	34100	43900	-32,438	-23,397	10,911
Return on Assets (Per cent)	0.4	0.4	-0.15	-0.09	0.15
Return on Equity (Per cent)	3.6	4.2	-2.81	-1.9	0.8
Net Interest Margin (Per cent)	2.6	2.5	2.5	2.7	2.8
Capital Adequacy	13.3	13.6	13.8	14.3	14.7
Gross NPAs	611900	791800	10,39,679	9,36,474	8,99,803
Net NPAs	349800	433100	5,20,838	3,55,068	2,89,531
Bank Credit to Priority sector	882900	992400	11,93,400	12,17,594	12,39,575
Total number of credit cards (in lakh)	250	300	375	471	577
Total number of debit cards (in Lakh)	6620	7720	8,611	9,058	8,286
Number of ATMs	19895200	20835400	2,07,052	2,02,196	2,10,760
Total number of complaints received during the year	10289400	13098700	1,63,590	1,84,730	3,06,702

Total number of complaints addressed	10115300	12534500	1,74,805	1,82,602	3,05,592
Credit-deposits ratio (Per cent)	78.2	73	74.2	75.1	73.7
Number of new bank branches opened	698600	483000	3,938	4,516	4,116

Sources: Report on Trend and Progress of Banking in India, RBI, Various issues.

The table-1 shows Indian banking sector at a glance from 2015-16 to 2019-20. It has included new parameter which has depicted the performance of scheduled commercial banks through profitability, technological development and customer oriented services. An increase in the number of credit cards, debit cards and ATMs indicates pioneer development has taken in the field of technology. Number of new branches opened has indicating financial inclusion has been embedded as an objective of economic policy in India. An increase in the number of addressing the customer complaints proves that today banks are more service oriented rather than profit oriented.

Review of Literature

Goyal Krishna and Joshi Vijay (2014) attempt has been made to identify the general challenges and opportunities for the Indian Banking Industry. The study divided into three parts. First part includes the introduction and general scenario of Indian banking industry. The second part discusses the various challenges and opportunities faced by Indian banking industry. Third part concludes that urgent emphasis is required on the Indian banking product and marketing strategies in order to get sustainable competitive edge over the intense competition from national and global banks.

Sindhu Savita (2018) an attempt has been made to identify the emerging issues in banking sector. The study stated that with changing dynamic forces in banking, it brings many risks to its stakeholders.

Iqbal Javed and Ahmad Firdous Qazi (2017) discussed the various challenges and opportunities like High transaction costs, IT revolution, timely technological up-gradation, intense competition, privacy & safety, global banking, financial inclusion. Banks are striving to combat the competition. The competition from global banks and technological innovation has compelled the banks to rethink their policies and strategies. Different products provided by foreign banks to Indian customers have forced the Indian banks to diversity and upgrade themselves so as to compete and survive in the market.

Manikyam Ratna (2017) the changing banking scenario, the impact of economic reforms and analyses the challenges and opportunities of national and commercial banks.

By reviewing the literature, the present study needs to examine the emerging issues of banking sector other than technological development in the internet banking. Increasing emphasis on globalization of the Indian economy has opened up new avenues and challenges for Indian banks. Financial sector reforms and liberalization of prudential regulations have thrown in a lot of opportunities for Indian bank to grow and diversify their areas of business operations. Since, last two decades, the Indian Banking system has seen a complete transformation from traditional banking system to modern banking system. The pace of transformation has been more significant in recent times with technology acting as a catalyst.

Non-Performing Assets (NPA)

Non Performing Asset means an asset of account of borrower, which has been categorized by a bank or financial institution as sub-standard, doubtful or loss asset, in accordance with the directions relating to asset classification issued by RBI. NPA defined as a credit facility in respect of which the interest or installment or principal has remained past due for a specified period of time.

A Non-performing asset (NPA) shall be a loan or an advance, where:

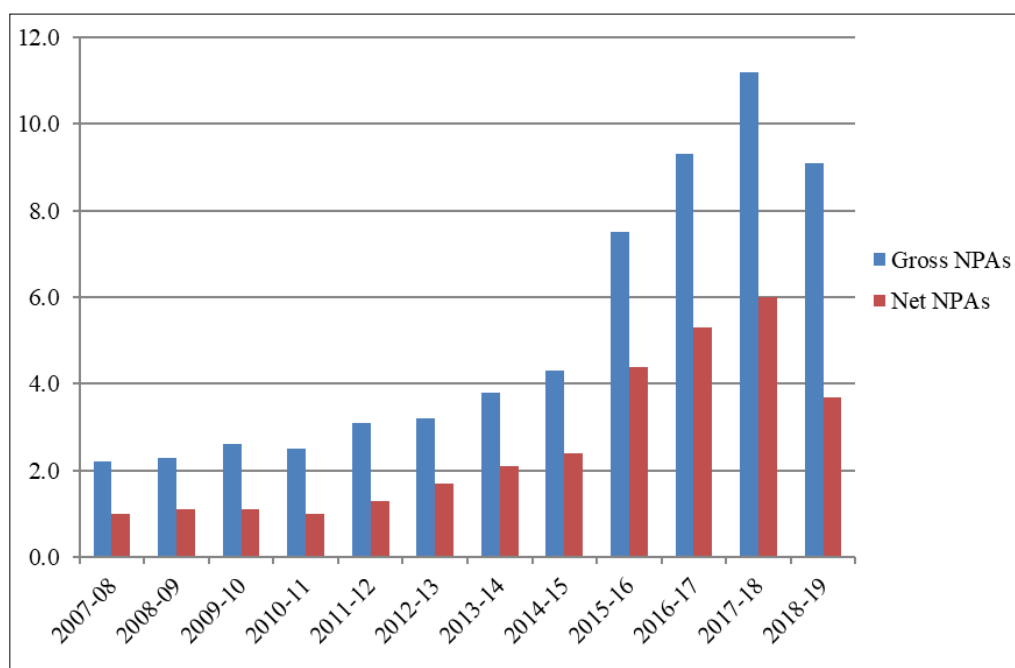
- Interest and /or instalment of principal remain overdue for a period of more than 90 Days in respect of a Term Loan,
- The account remains 'out of order' for a period of more than 90 days, in respect of an overdraft/ cash credit (OD/CC),
- The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted,
- Interest and/ or instalment of principal remains overdue for two harvest seasons but for a period not exceeding two half years in the case of an advance granted for agricultural purpose, and
- Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

The problem of enlargement non-performing asset (NPA) is catching attention and it has assumed great importance in terms of risk management. Banks thus have realized to have effective NPA management on their priority list. The problem of NPAs is one of the fore most formidable factors that had impact on the entire banking system. Higher NPA ratio tremble the confidence of investors, depositors, lenders etc. it also cause poor recycling of funds, which is in turn will have deleterious effect on the deployment of the credit. In March 2017, the average bad loans of public sector banks stood at 75 percent of their net worth. These bad loans are squeezing banks profitability and capital positions, threatening the health of India's biggest banks. Banks are now required to significantly improve, their risk assessment capability and their ability to price risks.

Table 2: Gross NPAs and Net NPAs of Scheduled Commercial Banks

Year	Gross NPAs	Net NPAs
2007-08	2.2	1.0
2008-09	2.3	1.1
2009-10	2.6	1.1
2010-11	2.5	1.0
2011-12	3.1	1.3
2012-13	3.2	1.7
2013-14	3.8	2.1
2014-15	4.3	2.4
2015-16	7.5	4.4
2016-17	9.3	5.3
2017-18	11.2	6.0
2018-19	9.1	3.7

Sources: Statistical Table Relating to Banks, 2018-19



Source: Table-2

Graph 1: Gross NPAs and Net NPAs of Scheduled Commercial Banks

As in the table clearly depicted that both Gross NPAs and Net NPAs has tremendously increasing trend. There has been a rising trend of non-performing assets (NPAs), especially for the PSBs, thereby severely impacting their profitability. During 2007-08, gross NPAs is 2.2 per cent, it has drastically increased to 11.2 per cent in 2017-18 which reflects the severe problem of Non-performing assets.

The transaction cost of carrying NPA's is also a major concern for the Indian banking sector. The operational efficiency of banks has also decreased and it further causes the addition of non- performing assets in their loan portfolios.

Bank Fraud

The Institute of Internal Auditors' "International Professional Practices Framework (IPPF)" (2009) defines fraud as: "Any illegal act characterized by deceit, concealment, or violation of trust. These acts are not dependent upon the threat of violence or physical force. Frauds are perpetrated by parties and organizations to obtain money, property, or services; to avoid payment or loss of services; or to secure personal or business advantage."

RBI has defined bank fraud has as 'A deliberate act of omission or commission by any person, carried out in the course of a banking transactions or in the books of accounts maintained manually or under computer system in banks, resulting into wrongful gain to any person for temporary period or otherwise with or without any monetary loss to the banks'. Banking regulations are also concerned with the increased number of fraudulent transactions in banks.

While the banking industry in India has witnessed a steady growth in its total business and profits, the amount involved in bank frauds has also been on the rise. This unhealthy development in the banking sector produces not only losses to the banks but also affects their credibility adversely. According to Freddie Mac (2015), "Fraud

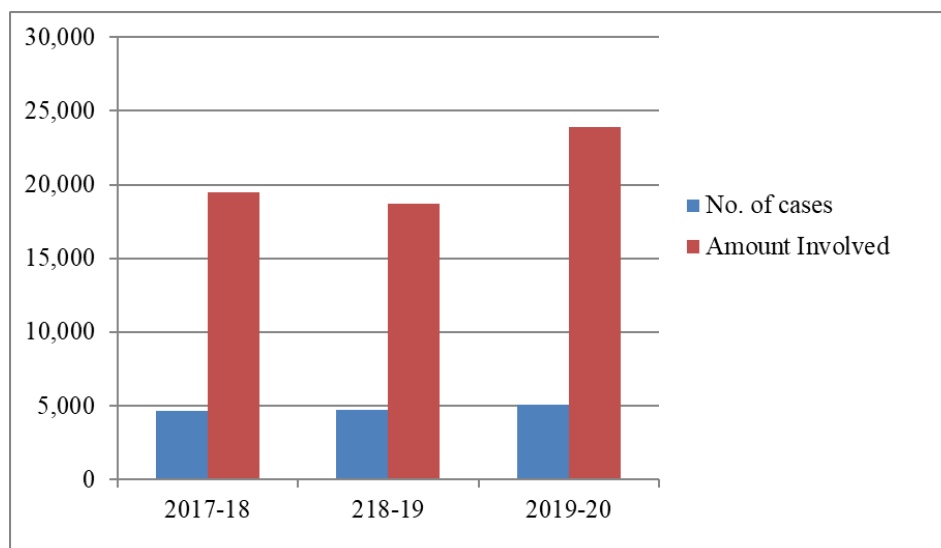
Mitigation Best Practices” include: (a) Fraud Risk Management Policies and Procedures, (b) Regulatory Compliance, (c) Ethical Conduct, (d) New Employee Awareness, and (e) Training.

One of the most challenging aspects in the Indian banking sector is to make banking transactions free from electronic crime. Fraud detection in banking is a critical activity that can span a series of fraud schemes and fraudulent activity from bank employees and customers alike.

Table 3: Frauds in Various Banking Operations Based on Date of Reporting (Amount in crore)

Area of Operation	2017-18		2018-19		2019-20	
	No.	Amount	No.	Amount	No.	Amount
Advances	2,256	17,123	2,120	17,367	2,320	20,556
Card/Internet	845	52	1,191	40	1,372	42
Deposits	875	437	759	809	693	903
Off-balance sheet	10	699	4	132	5	63
Foreign exchange transactions	16	899	17	51	16	2,201
Cash	153	43	160	22	239	37
Cheques/demand drafts, etc.	254	26	234	25	235	40
Inter-branch accounts	4	0	4	10	1	0
Clearing, etc accounts	29	7	17	87	27	6
Non-resident accounts	23	8	8	9	10	3
Others	179	162	176	146	153	77
Grand Total	4,644	19,456	4,690	18,698	5,071	23,928

Sources: Report on Trends and Progress of Banks in India, 2019-20



Source: Table-3

Graph 2: Frauds in Various Banking Operations Based on Date of Reporting

The Table-1.3 clearly shows that, the number bank fraud cases are increasing in trend. The number of cases has increased from 2,256 in 2017 to 2,320 in 2020; as a result amount involved in fraud has also increased to Rs. 20,556 crores in 2020 from Rs. 17,123 crores in 2017. Table clearly witnessed that these days Indian banking sector facing serious challenge to overcome the problem of bank fraud.

Effective customer education, communications programs and to helping customers to prevent fraud, but also helping them understand their own responsibilities should go hand-in-hand with sophisticated cyber security measures. Only by working in partnership with their customers can banking institutions develop truly effective fraud prevention efforts.

Cyber Crime Threat

The development of computers has made a great impact in the banking sector however along with it grew the different ways people would fall prey to different attacks. The spectacular growth in cybercrimes is the main problem for financial institutions in the 21st century. Criminals occasionally committed crimes via telephone lines at the start of the 1970s.

Cyber crime being considered as serious threat to all the aspects of a nation's economics as well as the financial institutions. Cyber crime incidents include but are not limited to credit card fraud, spamming, spoofing, economy laundering, ATM fraud, phishing, identity theft and denial services. Cyber crime can be simply stated as a crime that involves the use of computer and a network as a medium source instruments, target or place of a crime.

According to Global Economic Crime Survey 2014, conducted by PwC, cybercrime was one of the top economic crimes which were reported by various organizations across the world, including India.

With the headways in innovation, the Indian Managing an account Division has been at standard with the developing patterns and critical changes required in its tasks. The calls for development has given this unit monstrous chances and therefore, banks are currently among the greatest recipients of the IT Insurgency. The multiplication in online exchanges mounting on advancements like NEFT (National Electronic Store Exchange), RTGS (Constant Gross Settlement), ECS (Electronic Clearing Administration) and portable exchanges is a look at the profound established innovation in saving money and budgetary issues. In terms of number of cyber crime incidents, India has been ranked among the top 5 countries. The cases related to cybercrimes have grown ruthlessly due to the upsurge in mobile devices with internet connectivity. Smartphone's are nowadays used for numerous online activities like internet banking, online shopping, paying utility bills and are constantly in the eyes of the criminals to obtain access to confidential information.

Cyber Crimes can be broadly classified into categories such as cyber terrorism, Cyber-bullying, Computer Vandalism, Software Piracy, Identity Theft, Online Thefts and Frauds, Email Spam and Phishing and many more. Among the different inspirations for perpetrating a cybercrime, monetary profit remains the consistent victor for the past numerous years surpassing different thought processes including requital, coercion and political causes. Highest number of cyber crime cases were registered in Karnataka (12,020) followed by Uttar Pradesh (11,416), Maharashtra (4,967), Telangana (2,691) and Assam (2,231). Among the Union Territories, Delhi alone accounted for 78 percent of cyber crimes. Indian banks are required to be updated and ahead with the latest development in the information and technology act as well as the various methodologies adopted by advanced countries in order to keep balance on cyber threat.

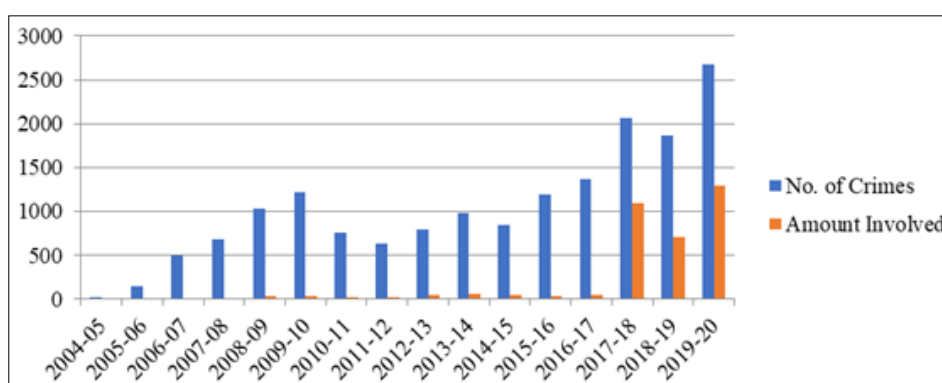
Table 4: Cyber Crime in India based on Date of Reporting (Cases in number and amount in ₹crore)

Year	No. of Crimes	Amount Involved
2004-05	26	3
2005-06	144	6
2006-07	491	11
2007-08	679	15
2008-09	1,036	37
2009-10	1,215	35
2010-11	763	21
2011-12	629	23
2012-13	793	49
2013-14	978	54
2014-15	845	52
2015-16	1,191	40
2016-17	1,372	42
2017-18	2059	1096
2018-19	1866	710
2019-20	2,677	1290

Source: Report on Trend and Progress of Banking in India, 2019-20

Notes:

1. Refers to frauds of ₹1 lakh and above.
2. The figures reported by banks & FIs are subject to change based on revisions filed by them.
3. Frauds reported in a year could have occurred several years prior to year of reporting.
4. Amounts involved reported do not reflect the amount of loss incurred. Depending on recoveries, the loss incurred gets reduced. Further, the entire amount involved is not necessarily diverted.



Graph 3: Cyber Crime in India based on Date of Reporting (Cases in number and amount in ₹crore)

The table and graphs shows clear picture of increasing trend in cyber crime reports in the Indian banking sector, which is a result of advancement in information technology. Most banks in India have migrated to core banking platforms and have moved transactions to payment cards and to electronic channels like ATMs, Internet Banking and Mobile Banking. Fraudsters have also followed customers into this space. As shown in the table number of cyber crimes has increased from 26 to 2677 and amount involved from ₹3 crores to ₹1290 crores in 2004-05 and 2019-20 respectively.

Asset Quality

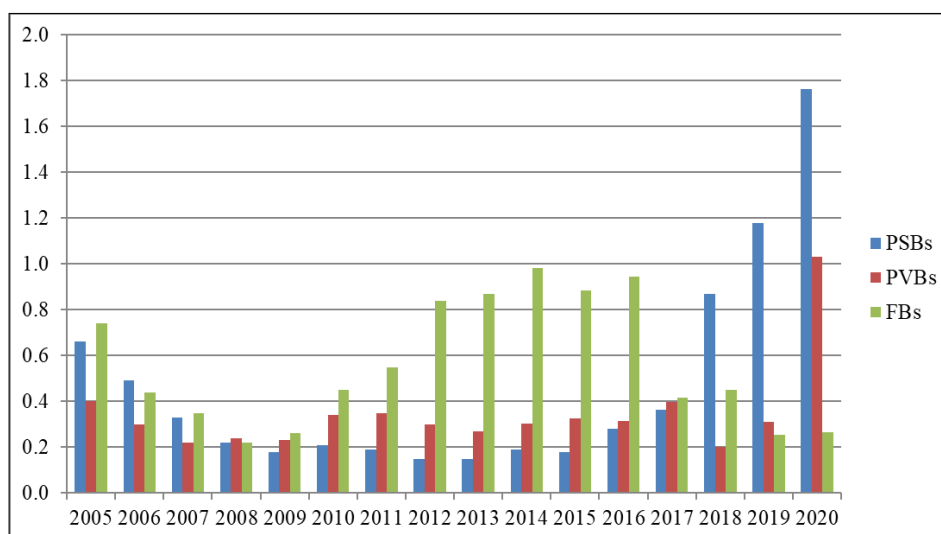
Asset quality is one of the most critical areas in determining the overall financial status of a bank. The primary factor affecting overall asset quality is the quality of the loan portfolio and the credit administration program. Loans typically comprise a majority of a bank's assets and carry the greatest amount of risk to their capital. Securities may also comprise a large portion of the assets and also contain significant risks. Other items which can impact asset quality are other real estate, other assets, off-balance sheet and, to a lesser extent, cash and due from accounts, and premises and fixed assets.

Assets of scheduled commercial banks are classified into four; they are standard assets, sub-standard assets, doubtful assets and loss assets. Among these assets, the status of loss assets indicates the asset quality of the banks. Lower the loss assets better the performance and assets quality of banks. Following table will depict the bank group wise loss assets of scheduled commercial banks.

Table 5: Bank Group Wise Loss Assets of Scheduled Commercial Banks (Percentage of total Assets)

Year	PSBs	PVBs	FBs
2005	0.7	0.4	0.7
2006	0.5	0.3	0.4
2007	0.3	0.2	0.4
2008	0.2	0.2	0.2
2009	0.2	0.2	0.3
2010	0.2	0.3	0.5
2011	0.2	0.4	0.6
2012	0.2	0.3	0.8
2013	0.2	0.3	0.9
2014	0.2	0.3	1.0
2015	0.2	0.3	0.9
2016	0.3	0.3	0.9
2017	0.4	0.4	0.4
2018	0.9	0.2	0.5
2019	1.2	0.3	0.3
2020	1.8	1.0	0.3

Sources: Statistical Table Relating to Banks, 2019-20



Graph 4: Bank Group Wise Loss Assets of Scheduled Commercial Banks (Percentage of total Assets)

The Table-1.4 as well as graph clearly shows that bank group wise loss assets of scheduled commercial banks. Among the scheduled commercial banks, foreign banks witnessed highest percentages of loss of assets from 2005 to 2017. Thereafter public sector banks are facing highest loss of assets till 2020. Thus, indicates poor assets quality management was largely exist in the public sector banks.

Capital Adequacy

The Capital Adequacy Ratio (CAR) is a measurement of a bank's available capital expressed as a percentage of a bank's risk weighted credit exposures. The capital adequacy ratio, also known as Capital to Risk Weighted Assets Ratio (CRAR), is used to protect depositors and promote the stability and efficiency of a nation's financial system by lowering the risk of banks becoming insolvent. Generally, a bank with a high capital adequacy ratio is considered safe and likely to meet its financial obligations.

Table 6: Bank Group Wise Capital Adequacy Ratio (Percent)

Year	PSBs	PVBs	FBs
2000	10.7	12.9	11.9
2001	11.2	11.7	1.6
2002	11.8	12.4	12.9
2003	1.26	12.05	15.2
2004	13.2	11.95	15
2005	12.9	12.3	14
2006	12.2	12.15	13
2007	12.4	12	12.4
2008	12.5	14.25	13.1
2009	13.5	15.2	14.3
2010	13.3	17.4	17.3
2011	13.08	16.46	16.97
2012	13.23	16.21	16.75
2013	12.38	16.84	17.87
2014	12.5	16.64	17.9
2015	11.5	16.23	17.5
2016	11.8	16.7	17.1
2017	12.1	15.5	18.7
2018	11.7	16.4	19.1
2019	12.2	16.1	19.4
2020	12.9	16.5	17.7

Sources: Statistical Table Relating to Banks, 2019-20

The Table-1.5 clearly represents bank group wise capital adequacy ratio of scheduled commercial banks. Higher the ratio, better the performance and stability of the banks. Hence, PSBs witnessed lower capital adequacy ratio followed by private and foreign banks. This indicates the lack of stability in the banking operations of PSBs. Thus PSBs needs to take care of this serious issue.

Conclusion

In the digital age, banks need to be careful while handing the contemporary issues. The bad loans are squeezing banks profitability and capital positions, threatening the health of India's biggest banks. Banks are now required to significantly improve, their risk assessment capability and their ability to price risks. Indian banks are required to be updated and ahead with the latest development in the information technology in order to keep balance on cyber threat and bank fraud. Indian banking sector also has to take care of asset quality and poor capital adequacy ratio, which is emerging issues in the recent days. Banks should go for transparent and non-discriminatory pricing of assets. The risk-return trade-off involved in various operations must be analyzed.

Banks are the lifeline of any economy and it is the collective responsibility of all of us to ensure that we have a strong, resilient and inclusive banking system geared up to face all domestic and global challenges. In this complex and fast changing environment, the only sustainable competitive advantage is to give the customer an optimum blend of technology and traditional service.

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