



## Recent trends in Banking Sector: Challenges and opportunities

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### Abstract:

*The Banking Industry in India has a huge canvas of history, which covers the traditional banking practices from the time of Britishers to reforms period. The banking sector plays a dominant role in building the economy of an individual as well as a nation. The growth of banking sector depends upon the services provided by them to the customers in various aspects. Today, banking is known as an innovative banking. The use of technology has brought revolutionary changes in the working style of private and public sector banks along with new challenges related to security and privacy of transactions. There has been a considerable innovation and diversification in the business of major banks in the areas of consumer credit, debit and credit cards, merchant banking, retail banking, internet and phone banking, In this paper, an attempt has been made to explain the recent trends of banking sector. The study also identifies the challenges and opportunities for the Indian banking sector along with some feasible measures.*

**Keywords:** Banking Sector, Economic reforms, E-banking, Private Sector bank and Public Sector Bank

### Introduction:

A bank is generally understood as an institution which provides fundamental banking services such as accepting deposits and providing loans. The face of Indian Banking has changed over the years. The banking system in India is significantly different from other Asian nations because of the country's unique geographical, social and economic characteristics. The country's economic policy frameworks are reflected in the structure, size and diversity of the Indian banking and financial sector. Banking

Sector in India plays an important role in equitable income distribution, balancing regional economic growth, elimination of monopoly in trade and industries as well as poverty.

For the past three decades, India's banking system has several outstanding achievements to its credit. The banks are the main participants for the financial system in our country. It offers several amenities and opportunities to their customers. In the competitive banking world, customers' services are the most powerful weapon



for their better growth. Most of the private sector and public sector banks as well as foreign banks have focused on offering new technology- based services to its customers like internet banking, online banking, mobile and phone banking, RTGS, ATM, Tele banking, EFT etc.

Today, the banking industry is stronger and capable to face the competition of global banking. Indian banking industry is gradually moving towards adopting the best practices in accounting, corporate governance and risk management. Technology has opened up new markets, new products, new services and efficient delivery channels for the banking industry. The digital India campaign started by Narendra Modi has transformed the banking sector. Digitization led to financial inclusion, controlling of black money and cashless transactions. In fact, digitization is not an option for banking industry rather it is inevitable.

In recent turmoil period, Indian banking industry has been amongst few to maintain resilience. The tempo of development for the Indian banking industry has been remarkable over the past decades which are evident from the higher pace of credit expansion, increasing profitability and productivity, lowering NPA as well as focussing on financial inclusion. **These factors show that Indian banking system is vibrant and strong.** Massive branch expansion in the rural and underdeveloped areas, mobilisation of saving and diversification of credit facility has resulted in widening the Indian banking sector. It has transformed the fundamental character of class banking into mass banking.

#### Objective of the Study:

- To study the Indian banking sector.
- To examine the recent trends and technological development in banking sector.
- To identify the challenges of the Indian banking sector.
- To study the opportunity for the Indian banking sector.
- To suggest measures for improvement in banking sector.

#### Research Methodology:

The study is based on secondary data. The secondary data has been collected from various sources like annual reports of RBI and banks, Reference books, journals, magazines and from various websites.

#### Review of Literature:

**Garg (1994)** studied that Indian scheduled commercial banks have achieved remarkable progress in last two decades under study, particularly in branch expansion in rural areas, deposits mobilization and credit deployment to priority sector and small borrowers. Banking sector reforms is an integral part of the economic reform package.

**Avasthi & Sharma (2000-01)** have analyzed in their study that advances in technology are set to change the face of banking business. Technology has transformed the delivery channels by banks in retail banking. It has also impacted the markets of banks. The study also explored the challenges that banking industry and its regulator face.

**B. Janki (2002)** analysed that how technology is affecting the employee's



productivity. There is no doubt in India; particularly public sector banks will need to use technology to improve operating efficiency and customer services.

**MD Patra (2002)** suggested that several fundamentals must come together in order to make the Indian banking system stronger, efficient and low cost like strengthening of prudential norms and market discipline; adoption of international benchmarks as appropriate to the Indian situation; management of organizational change and consolidation within the financial system; and human resource development as the catalyst of the transformation.

**Jegade et al.(2004)**. Financial reforms were designed to enable the banking industry developed.

**S. Chatterjee (2004)** stressed on the retail banking. He stated that with the jump in the Indian economy from a manufacturing sector to the nascent service sector, a large portion of consumer is getting translated into a larger demand for financial products and customisation of services as becoming the norm of competitive advantage. In his article he studied the reasons behind the euphemism regarding the retail focus of the Indian banks.

**Kumar (2006)** another path-breaking innovation in the banking sector in recent times is the emergence of internet banking. Customer can access his account anywhere even from the comfort of his computer in the house with the added benefit of funds transfer facility. Internet banking is estimated to be even more cost effective for banks as compares to ATMs. Internet banking also provides the customers with value added services like

payment of insurance premium, payments of utility bills, booking railway tickets etc.

**Zhao et, al. (2008)** looks at the deregulation- prudential re-regulation framework which has been adopted in Indian banking sector and its impact on competition and performance. Authors argued that deregulation induced competition should lead to efficiency and better performance in banking industry.

**Biresh et al. (2011)** examined the performance of banks in India in post transition period and concluded that the positive trend of the reform process is visible through the increase in technical efficiency over the years of the post transition period.

To sum up the literature review indicates that worldwide the importance of e-banking is emphasized and use of the technology lead to increase the productivity. The emergence of internet banking has made easy access to the customers at large.

#### **Historical Background:**

When we study the historical background of Indian Banking sector, we find that Bank of Hindustan was set up in 1870. Later on, three management banks under the presidency banks Act, 1876 were set up as Bank of Bengal, Bank of Bombay and Bank of Madras in the year 1809, 1840 and 1843 respectively. In 1921 all presidency banks were amalgamated to form the imperial Bank of India. Imperial Bank carried out limited functions of central banking prior to the establishment of RBI. In 1865, the first bank established exclusively by Indians is Allahabad Bank. RBI was constituted as an apex bank in 1935.



Banking regulation Act was passed in 1949. Under the Act, RBI has wide ranging power for supervision and control of banks as well as licensing power. The Banking industry in India functions under the eagle's eye of RBI. The History of Indian banking can be divided into three main phases:

**Phase 1 (1786-1969)** - Initial phase of banking in India when many small banks were set up.

**Phase II (1969-1991)** - Nationalization, regularization and growth

**Phase III (1991 onwards)** - Liberalization and its consequences

The Indian banking sector is generally classified into scheduled bank and non scheduled bank. Scheduled banks are those banks which are included in the II schedule of RBI Act, 1934. The Scheduled banks are further classified into nationalized bank, State Bank of India and its associates, Regional Rural banks, foreign banks and other private sector banks. Thus, we see that the journey of Indian banking industry is very longer.

Before 1991, India had nationalized a large share of its banking sector. In 1969, the government of India nationalized more than 80% of bank branches. In 1980, the government brought additional number of banks by nationalizing banks with deposit more than 200 crores. Between 1969 and 1991, density of coverage and number of bank branches grew significantly. In addition to large deposits and credit growth, priority sector lending grew from 14 to 41%. However, by 1991, the banks efficiency and productivity had declined. In 1991, the government undertook a number of banking reforms. Under the

regime of banking sector reforms, IT Act, 1999 gave new dimensions to the Indian Banking sector. It affected the productivity, profitability and efficiency of the bank to a large extent.

In 1998, the Committee on banking sector Reforms recommended a further set of measures to strengthen the banking sector. In 2000, a number of Committees relating to banking reforms were constituted and further reforms have been instituted gradually. The Committee recommended on microeconomic and regulatory frameworks for India, financial inclusion and financial development. In 2014, the Committee to review the governance of Board of Banks in India was constituted. The Committee recommended for enhancing the governance and management of public sector banks.

#### **Current Scenario:**

The present banking scenario provides a lot of opportunities as well as challenges. Today, the service sector in India is contributing half of the Indian GDP and the banking is the most popular service sector in India. The significant role of banking industry is to speed up the socioeconomic development. Many leading banks operating in the market have used the changed rules and regulations such as CRR, interest rate and special offers to customers. In addition to this, now a days banks are entered in non-banking products such as insurance in which area there are tremendous opportunities

Indian Banking system is characterised by high share of public sector banks, having over 70% of total assets. These banks have large stock of non-performing



assets (NPAs) with share of 88% of the stock on March, 2016. The NPA of public sector banks increased from Rs. 2.78 lakh crore in March, 2015 to 7.33 lakh crore in June, 2017. The share of NPA in public sector banks is more than 3 times of private sector banks. The assets and profitability have also been deteriorating over time. The decline in banks' profit is largely due to higher growth in risk provision, loan write-offs and decline in net interest income. The stress on banking sector has translated into a slowdown in industrial credit. High NPAs are likely to obstruct banks' ability to meet higher capital requirement. The Government has infused funds to address the challenges. The measures for the recapitalization under the Indradhanush Plan in 2015-16 acknowledged the government recognition of NPAs ratio and their adverse effect on the economy. To overcome the problems, the Ministry of Finance announced Rs. 2.1 lakh crore Plan to recapitalize banks. The Indradhanush Plan also includes wider banking reform to strengthen institutional governance and provide incentives in the banking system. The insolvency and bankruptcy code also provided a channel for addressing NPA.

#### **Recent Trends in Banking Sector:**

**1. Electronic Payment Services (E Cheques):** Coming across E-governance, Email, E-Commerce e-tail etc. a new technology is being developed in US for the introduction of E-Cheque. It will eventually replace the conventional paper cheque. India, as forerunner to the introduction of E-Cheque, the negotiable instrument Act has already been amended to include truncated cheque and E-Cheque Instrument.

**2. Real Time Gross Settlement (RTGS):** RTGS system introduced in India since March, 2004 is a system by which electronic instruments can be given by banks to transfer funds from their accounts to the accounts of another bank. The RTGS system is maintained and operated by RBI and provides a means of efficient and faster fund transfer among banks. The fund transfer between banks take place on a real time basis. Therefore, money can reach to the beneficiary instantaneously and the beneficiary banks have the responsibility to credit his account within two hours. RTGS system is used only for large value transactions.

**3. Electronic Fund Transfer (EFT):** Electronic Fund Transfer is a system where anyone who wants to make payment to another person/ company etc. can approach his bank and make cash payment or give cheque/ authorisation to transfer funds directly from his own accounts to the bank account of the beneficiary. Complete details should be furnished to the bank at the time of requesting for such transfer so that the amount reaches to the beneficiary account correctly and faster. RBI is the service provider of EFT.

**4. Electronic Clearing Service (ECS):** Electronic Clearance Service (ECS) is a retail payment system that can be used to make bulk payments/receipts of a similar nature especially where each individual payment is of a repetitive nature and of relatively smaller amount. This facility is meant for companies and government departments to make/receive large volumes of payments rather than for fund transfer by individual. ECS is introduced by RBI which is parallel to automated clearing house system. It is used by utility service providers for



collection of electricity bill, telephone bill etc.

5. **Point of Sale Terminal:** Point of Sale Terminal is a computer terminal that is linked online to the computerized customer information files in a bank and magnetically encoded plastic transaction card that identifies the customer to the computer. During a transaction, the customer's account is debited and the retailer's account is credited by the computer for the amount of purchase.

6. **Automatic Teller Machine (ATM):** Automatic teller machine is the most popular device in India. It enables the customers to withdraw their money at any time without interacting with a human teller. In addition to cash withdrawal ATM can be used for payment of utility bills, fund transfer between accounts, deposits of cheque and cash into accounts and even for balance inquiry etc. This system was introduced to the Indian banking industry by HSBC bank, Mumbai during 1987.

With the advent of ATMs, banks are able to serve the customers outside the banking hall. Now the ATMs are equipped with modern technology and facilitate various features for its customers. ATM has reduced 50% workload of bank's cashier.

7. **Tele Banking:** Tele Banking is another innovation, which facilitates 24 hours banking to the customer. Tele Banking facilitates the customer to do entire non cash related banking on telephone. Under this device automatic voice recorder is used for simpler query and transaction. For completed queries and transactions manned phone terminals are used. This software identifies the voice of the caller and provides him suitable reply. Now Tele banking is becoming popular rather than ATM.

8. **Phone Banking:** Customer can now dial of the banks designed telephone number and by dialling his ID number will be able to get connectivity to bank's designated computer. By phone banking the customer can do the entire noncash relating banking on telephone anywhere and at anytime.

9. **Mobile Banking:** Mobile banking facility is an extension of internet banking. The bank in association with the cellular service providers offers this service. This facility is available even to those customer with only credit card account with the bank. For this service, mobile phone should either be SMS or WAP enabled.

10. **Internet Banking:** Internet banking enables a customer to do banking transaction through the bank website on the internet. It is a system of accessing accounts and general information through a computer either sitting in his office or home. This is also called virtual banking. Internet banking has changed the way of banking transaction.

11. **Electronic data interchange (EDI):** Electronic data interchange is the electronic exchange of business documents such as purchase order, invoices, shipping notice etc. in a standard computer processed, universally accepted format between trading partners. It can be also used to transmit financial information & payments in electronic forms.

12. **Smart Card:** These cards are microchip installed plastic cards. These devices facilitate value stored. One smart card can contain the different types of cards issued by different banks.



### Challenges:

**1. Customer satisfaction:** Today, in banking sector customers are more value oriented in their services. Hence, each and every bank has to take care about fulfilment of customer satisfaction. Good customer services are the paramount brand ambassador for any bank growing business. Greater customer satisfaction is the only way to retain customer loyalty and stay ahead of competition. Thus, only those banks that focus on the needs of their clients will succeed. Public sector banks should provide customer satisfaction more or at par with private sector banks to go ahead.

**2. Global Competition:** Due to liberalisation, privatization and globalisation banks are facing a severe competition. The nationalised and commercial banks have competitions from foreign and new private sector banks. In addition to internal competition among public and private banks, Indian banks lag behind global banks in term of financial depth or the size of global banks. Credit deposit ratio of banks in India was 77% as compared to 119% in Brazil and 312% in China in 2015. The foreign banks operating in India are major challenges for nationalized and private sector banks. The competition in banking sector brings various challenges before the banks such as product positioning, innovative ideas, new market trends, cross selling etc. Banks are restructuring their administrative folios by converting man power into machine power.

**3. Management of Non-performing assets (NPAs):** Non-performing assets (NPAs) are another challenge to the banking sector, particularly to public sector banks

in India. PSBs in our country are the biggest contributors to the large and rising stock of NPAs with a share of 88% as on March, 2016. Rising NPAs in PSBs has declined its return on assets and return on equity. The main reasons of increasing NPAs are vehicles loans and unsecured loans. Thus, every bank has to take care for regular recovery of loans to reduce NPAs. There is need to have long term solutions for overcoming this challenge. The internal control system, risk management system and debt recovery tribunals have to be strengthened by banks to detect and minimize NPAs.

**4. Technology:** In the deregulated environment, managing a wide range of products on shrinking margins in an extremely competitive environment and offering top class customer services will create new challenges. In this context technology will be the key factor to reduce transaction cost by offering customised products, managing risk and various innovations of technology in banking sector such as ECS, RTGS, EFT, NEFT, ATM, Retail Banking, Online Banking, Mobile Banking and Smart Card etc.

**6. Government Ownership:** At present, the government is the owner of about three fourth of the total assets in the Indian banking system. On the ownership issue, Government should reduce its ownership stake in the public sector banks. The predominance of government owned banks in India requires more capital which increases the burden of the government. Thus, an optimal ownership mix should be permitted to balance between efficiency, equity and financial stability.



**8. Gaps in the Flow of Credit:** A high proportion of socially and economically underprivileged section of the society in India is concentrated in the informal economic activities since more than 69% population in India lives in rural areas. Available data indicates that cooperative banks, commercial banks, public sector banks as well as private sector banks have not provided adequate sources of credit as per requirements in the rural & backward areas.

**9. Corporate Governance:** RBI has asked the banks to set up specialized committee such as risk management committee, compensation committee and audit committee etc. The public sector banks, new private banks, and foreign banks should ensure corporate governance in all the activities to safeguard the interest of the shareholders.

**10. Recapitalization:** Adequate capital is essential to strengthen the health of public sector banks.

#### **Opportunities:**

**1. Retail Lending:** Recently banks have adopted customer segmentation which has helped in customizing their product folios well. Thus, retail lending has become a focus area particularly in respect of financing of consumer durables, housing, automobiles etc. Retail lending has also helped in risk dispersal in enhancing the earnings of banks with better recovery rates.

**2. Rural Area Customer:** 69% of the total population in rural India is largely untapped market for the banking sector. Hence, the banking sector must expand their wings for availing untapped market.

**3. Good Customers services:** Good Customer services are the best brand ambassador for any bank for growing its business. While increasing competition, customer services have become the backbone for judging the performance of banks. Every engagement with customers is an opportunity to build faith in themselves.

**4. Internet banking:** It is clear that online finance will pick up and there will be increasing convergence in terms of products offerings such as banking services, sharing trading, insurance, loans. Anytime anywhere banking will become common and will have to upscale. Such upscaling could include banks launching separate internet banking service apart from traditional banking services

**5. Product Differentiations:** Apart from traditional banking services Indian bank must adopt some products innovation so that they can provide services to their customers and meet the global competition as well.

**6. Expansion:** Expansion of branch size in order to increase market share is another opportunity of banking sector to combat competitors. Thus, Indian nationalized banks and commercial banks must spread their wings towards global market.

**7. Indian Customers:** Today, the biggest opportunity for Indian banking sector is Indian customers. Young Indian customers have changed their life style at young age since they are more interested in assets creation and transactions by availing loans from banks. Banking sectors also have an opportunity since Consumers goods companies supply goods



to young Indians by availing financial assistance from banks.

**8. Other Opportunities:** There are so many opportunities of Indian banking sector in coming future by entering in a new business and new markets by providing high level customers services.

**Suggestive measures for improvement in banking sector**

For improvement in banking sector following measures may be taken:-

- Recapitalisation in banking sector by corporate debt market and debt recovery mechanism.  
Prioritizing following areas:-
  - i) Improving governance and strengthening institutions particularly in public sector banks.
  - ii) Development of corporate bond market.
  - iii) Encouragement of entry of private and foreign banks
- Reducing operating expenses of public sector banks.
- Framing strict policies and risk management policies.
- Rendering better services to customers
- Issuing separate licenses for wealth management and investment banking.
- Introducing Reforms in corporate debt market, government debt market & money market.
- Focusing on asset-liability management of banks,
- Increased usage of technology in banking sector.
- Focusing on financial inclusion.
- Transparency in clearing and settlement practices.

- Collaborative banking instead of merger and acquisition.
- Adopting CAMELS rating for updating the risk profile of bank.
- Adopting sound risk assessment process and rating system for prevention of emergence of NPAs in banking sector.
- Adopting latest customer friendly technology to explore the global opportunities.
- Adoption of internet and retail banking
- Banks to provide solutions to customer anywhere & anytime regarding financial information.
- Identifying marketing areas

**Conclusions:**

In this paper banking sector of India has been critically analyzed with its recent trends, challenges and opportunities. The paper concludes that transformation is taking place almost in all categories of banks in India. The transformation will be helpful to cope up new economic and financial policies of the banks. IT is playing a crucial role to create the drastic changes in the banking industry, particularly in private bank and foreign banks. It has helped the banking sector in terms of cost cutting, speedy and making fast transfer of money. The immense opportunities are also available for the public sector banks, if they change/modify and adopt new policies to combat the challenges. Adoption of stringent prudential norms, well-capitalized banking system, corporate governance reforms, improved financial supervision, efficient debt recovery mechanism, managing nonperforming assets, facilitating financial inclusion, better risk management systems, adoption of internationally accepted



accounting practices, disclosures and transparency will ensure the Indian Banking industry to pace with global banking system.

Adoption of technology has been changing the work culture in the banks. The banking today is redefined and re-engineered with the use of Information Technology and

offer more sophisticated services to customers. The e-banking, mobile banking, Net banking and ATMs facility have gained success among the customers. Payment settlement systems like RTGS, NEFT, EFT, ECS and CTS have also been successful in facilitating the customers. Mobility and customer convenience are viewed today as the primary factors of growth in banking sector. The banking sector in India is progressive due to innovative facilities offered by banks. The economic growth of the country is an indicator for the growth of the banking sector. By the government support and a careful re-evaluation of existing business strategies can set Indian banks bigger and stronger.

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