

Understanding the Role of Private Sector Banks in India

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Abstract

Banks play an important role in the economic development of a country. Banks are a fundamental component of the financial system. In India private banks are available in plenty and known for offering expeditious service to their customers. In Today's competitive business environment, the banking industry like many other financial service industries is facing a hastily changing market, new technologies, economic fears, ferocious competition, and especially more demanding customers; and the changing climate has presented an unparalleled set of challenges. The Private Banks are accountable for a share of 18.2 percent of the Indian banking industry. Major changes took place in the functioning of Banks in India only after liberalization, globalization and privatization. This study is a small step in understanding of private sector banks role in India

Key Words: Credit-Deposit (C-D) ratio, Foreign Direct Investment (FDI), Public & Private Banks, Return on Assets (RoA), Public Sector Banks (PSB).

I. Introduction:

The "private-sector banks" are banks where greater parts of stake or equity are held by the private shareholders and not by government. The private sector banks are split into two groups, old and new. The old private sector banks existed prior to the nationalization in 1969 and kept their independence. The new private sector banks are those that have gained their banking license since the liberalization in the 1990s.

In India private banks are available in plenty and known for offering expeditious service to their customers. Indian Banking has been dominated by public sector banks since the 1969 when all major banks were nationalized by the Indian government. However, since liberalization in government banking policy in the 1990s, old and new private sector banks have re-emerged. They have grown faster & bigger over the two decades since liberalization using the latest technology, providing contemporary innovations and monetary tools and techniques.

In 1994, the Reserve Bank of India opened the door for private banks and handed out the policy to control the private banks. The policy also included the liberation for Private Banks in terms of their free and independent operation. The first private bank is Trust Bank later known as Oriental Bank of Commerce, then other private Banks like HDFC Bank, International Bank, ING Vysya Bank, Kotak Mahindra Bank, SBI Commercial Bank, Karnataka Bank, Kashmir Bank, ICICI Bank and more came. Private banks in India achieved a milestone for serving people and showed its great commitment. Private banks in India have earned great response for its service and also known for bringing revolution for serving millions of customers. It offers best option for saving and also offers various schemes with maximum return. It offers its service 24 hours and made the job of fund transfer easier by offering new banking service. Besides, there are lots of ATM machines have been set up by such private banks and made the task of withdrawing liquid money easier. The private banks are accountable for a share of 18.2 percent of the Indian banking industry.

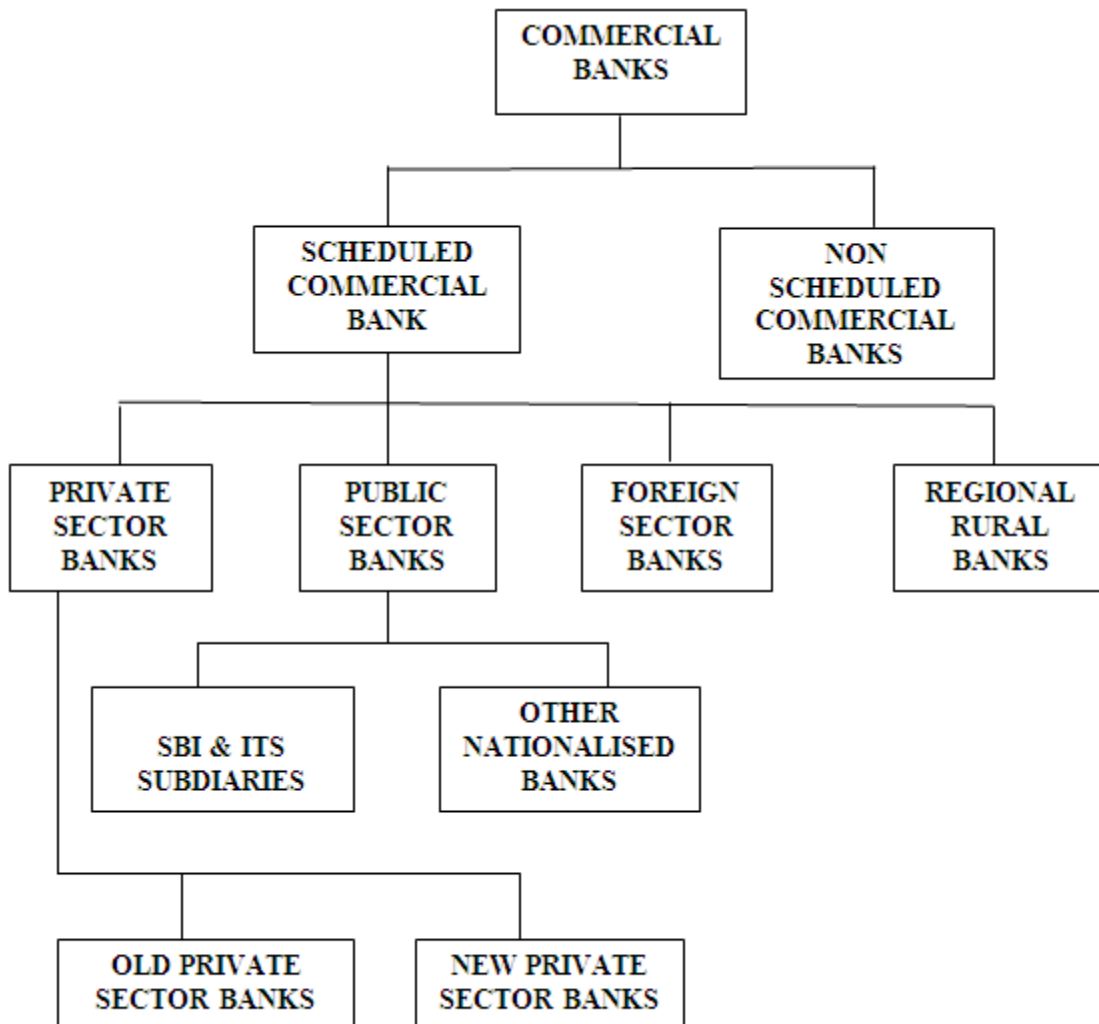


Fig.1 Indian Banking Scenario

II. Comparison between Private and Public Sector Banks:

The private sector banks introduced the concept of online banking in India. This was mostly because the private banks were technologically well equipped. Online banking is extremely common today since you can sit anywhere and go ahead with your banking transactions. You do not have to personally visit your bank. The Private sector banks use state of the art technology and fully computerized systems since the time they entered the Indian market whereas the Public Sector Banks (PSB) are not. However despite the technological

challenges the public sector banks in India are still the preferred destinations for many as they are considered as safer options for money deposit.

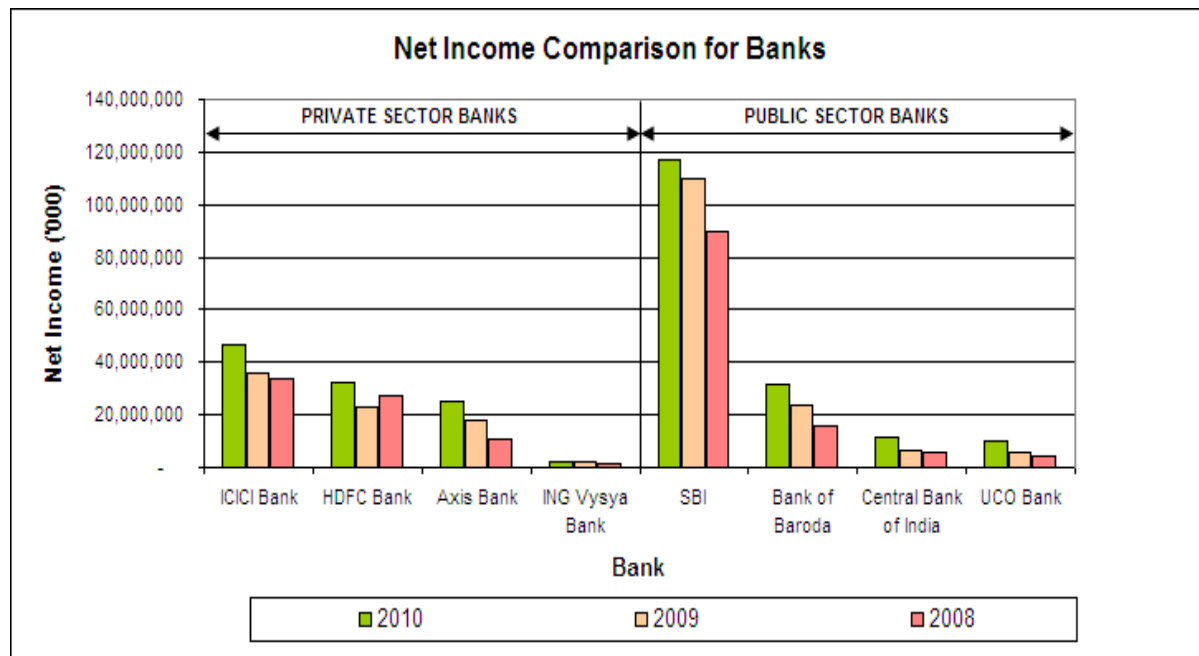


Fig.2 Comparison between Private sector & Public sector banks

III. Private Bank Statistics:

Private Banks recorded growth of 20% in FY12 vs. 21.5% in FY11. The share of private banks in aggregate deposits stood at 18%. Private Banks recorded decelerated growth in deposits of 17.1% in FY12 vs. 21.9% in FY11.

In terms of assets, aggregate loans and advances, private banks accounted for 19%. credit to industry and services sector which accounts for more than two-thirds of total bank credit, experienced subdued growth.

Since deposits are the most important source of funds for banks, subdued growth of deposits translated into decelerated bank credit growth. As a result, growth in advances for all

bank groups registered slower growth in FY12 compared to previous year. Private banks recorded decelerated growth of 21.2% in FY12 vs. 26.1% in FY11.

As on Jan 2013, aggregate bank credit stood at Rs 50,427.9 bn. Total advances of private banks stood at Rs 9,928.6 bn. The credit-deposit (C-D) ratio was higher at 78.6% in FY12 against 76.5% in FY11. Private banks C-D ratio (82.27%) in FY12. Private banks recorded an increase in Return on Assets (RoA) from 1.43% in FY11 to 1.53% in FY12.

Banks at a Glance (FY12) - Operational Performance

	PSBs	Private sector banks	Foreign banks	All SCBs
Key Balance Sheet Indicators (Rs bn)				
Total Liabilities/Assets	60,380	16,778	5,836	82,994
Deposits	50,020	11,746	2,771	64,537
Loans and Advances	38,783	9,664	2,298	50,746
Growth (y-o-y) (%)				
Total Liabilities/Assets	14.1	20.0	18.8	15.5
Deposits	14.4	17.1	15.1	14.9
Loans and Advances	17.4	21.2	17.6	18.1
Key ratios (%)				
CRAR Basel II	13.23	16.21	16.74	14.24
Gross NPA Ratio	3.3	2.1	2.6	3.1
Net NPA Ratio	1.7	0.5	0.6	1.4
Credit-Deposit	77.53%	82.27%	82.93%	78.6%

Source: RBI, D&B Research

Fig.3 Banks at a Glance

Banks at a Glance (FY12)

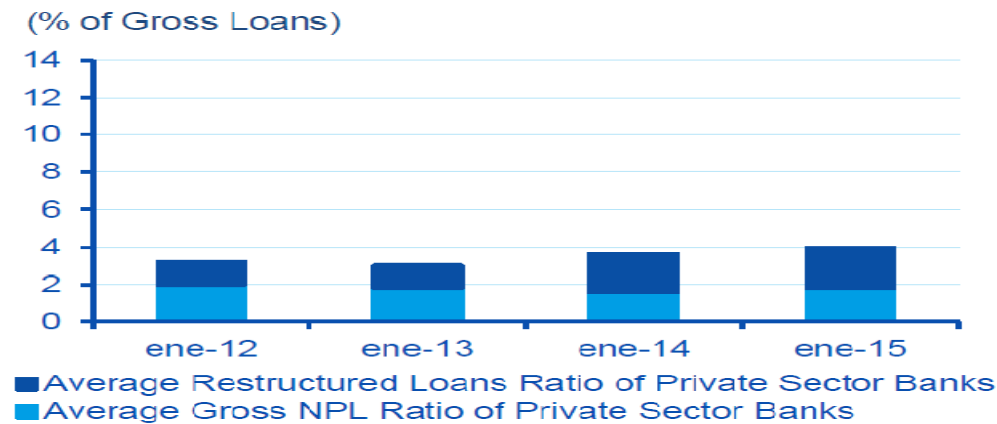
	PSBs	Private sector banks	Foreign banks	All SCBs
Key ratios (%)				
Return on assets (RoA)	0.88	1.53	1.76	1.08
Return on equity (RoE)	15.33	15.25	10.79	14.6
Cost of deposits	6.36	6.43	4.34	6.28
Return on advances	10.3	10.99	9.61	10.4
Return on Investments	7.54	7.26	8.1	7.53
Return on funds	9.52	9.69	8.91	9.52
Cost of funds	6.06	5.84	3.83	5.9
Spread	3.46	3.85	5.08	3.62

Source: RBI, D&B Research

Fig.4 Banks at a Glance

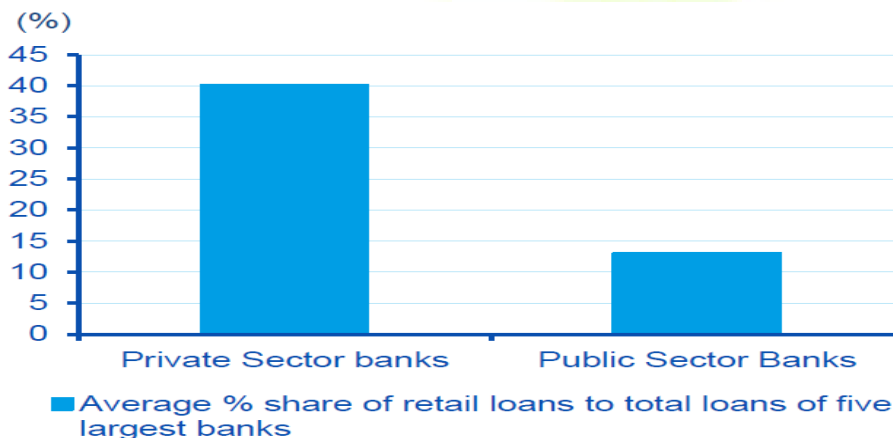
IV. Private Banks Role:

The importance of private sector in Indian economy over the last 15 years has been tremendous. The opening up of Indian economy has led to free inflow of Foreign Direct Investment (FDI) along with modern cutting edge technology, which increased the importance of private sector in Indian economy considerably. Banks play a major role in this. Private sector Indian banks have exhibited profitability improvements, better asset quality trends, lower credit costs and healthy capital levels over the years.



Source: BBVA Research, RBI, Haver Analytics

Fig.5 Private Sector Indian banks have asset quality concerns under control



Source: BBVA Research, RBI, Haver Analytics

Fig.6 Private Sector Banks have benefitted from a higher port folio of retail loans

V. Private Sector Banks in the Recent Few Years:

Private sector banks have managed to record better growth than their public sector counterparts in the past few years, as the latter remain burdened with asset quality woes. Year 2015 has seen private sector banks wrest more market share from public lenders. “Presently, the PSBs with a predominantly high share in infrastructure financing are observed to be facing the highest amount of stress in their asset quality and profitability,” noted the Financial Stability Report released by the Reserve Bank of India. In 2015, PSBs seemed to lag private banks on asset quality, profitability, and credit growth, among others. For instance, the PSBs recorded the highest level of stressed assets at 14.1 per cent, followed by private banks at 4.6 per cent, and foreign banks at 3.4 per cent. Because of the pressure on asset quality, the PSBs have also been lending more cautiously, resulting in muted credit growth for them.

Going ahead, the picture doesn't seem too rosy for public sector banks as well. A research report by Brickwork Ratings has estimated PSBs would have lost market share by two per cent in FY15, which has been gained by the private sector banks. “If the current growth trend continues for another three years, by FY18, our estimate is that PSBs' share would have come down to 71 per cent (from 75 per cent in FY15) and the entire gain will be of private banks.”

VI. Conclusion:

Private Banks play a pivotal role for a country's economic development. They are the major players in today's market. Private banking has invited foreign economies to invest in our developing country. The Statistics helps us to understand the private bank sector in India. Private sector, Indian Banks have exhibited profitability improvements, better asset quality trends, lower credit costs and healthy capital levels over the years. Private banks in India has a got a great response in terms of service and quality banking. Globalization has encouraged multinationals and foreign banks to set up their business unit in a developing country like India.

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