

INTRODUCTION

In the contemporary perspective, Indian economy is considered as one of the fastest growing and emerging economies in the world. Financial activities of banking sector are crucial drivers to increase the economic empowerment of the country. If the banking system in a country is efficient and disciplined, it brings about a rapid growth in the various sectors of the economy. Banking sector is the backbone of any economy as it provides finance to various segments and helps in sustainable socio-economic development. It plays an important role in the mobilization of deposits from customers and disbursement of credit to various sectors for productive purpose. The attribute of the economy hinges on the strength and efficiency of the financial system, which in turn depends on a sound and solvent banking system. A sound banking system efficiently deploys mobilized savings in productive sectors and a solvent banking system ensures that the bank is capable of meeting its obligation to the depositors. It ultimately reflects the health of the banking industry.

Banking sector in India has undergone significant transformation since the nationalization of 14 major commercial banks in 1969. It brought several diversifications, modifications and innovations in the structure and functioning of banks. However, services rendered by banks witnessed major changes after liberalization, globalization and financial sector reforms, carried out from the early 1990s. With the financial sector reforms, the banking industry has experienced tremendous changes in terms of business process, market orientation and management sophistication. The economic development through liberalization and globalization has resulted in many positive developments in the Indian banking sector. The Reserve Bank of India (RBI) has taken efforts to bring changes in policies and regulations, which include introduction of prudential norms, capital adequacy norms, enhancing the payments system to strengthen the banking sector. The banking system in India has become service oriented, maturing from the days of 'walking in business' to the situation of 24 hour banking solutions. With such widespread and rapid growth in the banking industry, the banks have stepped into various allied businesses such as insurance, mutual funds, venture capital, leasing and other para-banking activities like leasing, hire purchase and factoring. Consequently, banks are not only considered as dealers but also as the leaders of economic development.

The Banking Sector is the most dominant segment of the financial sector in the Indian economy. The banking sector plays a crucial role as it deals with huge amounts of public money and is highly sensitive to reputational risk. Like all other economic activities, the banking sector also has various risks in its operations. It is utmost importance to ensure that the banking sector stays safe and sound. At present, banks highly focus on strengthening the balance sheet and improving the stakeholders' value. Thus, it becomes important to analyze the financial performance of banks to get insight into the operational activities of business.

1.1 EVOLUTION OF BANKING SECTOR IN INDIA

Banking is crucial to a well-functioning economic system. Banking sector in India has passed through different phases over the centuries. The Indian Banking system classifies the changes into three phases.

Phase 1

The first phase of banking system in India was initiated during 1786 to 1969. This period was marked as the establishment of Indian banks and more banks were introduced. When the English traders came to India, they faced the problem of raising working capital due to language barrier. Therefore, they established Agency House, which combined trading with banking. The Agency House established the first bank in India called the Bank of Hindustan in 1770. This bank said to be the first commercial bank in India, followed by General Bank of India in 1786. Later on, many banks were established. However, liquidation proceedings were also started in the year 1829 for winding up Bank of Hindustan and finally it was liquidated in 1832. The East India Co., the ruler of India, took initiative in establishing Presidency Banks by contributing capital to meet its own demand for funds. Accordingly, Bengal Presidency established a bank called Bank of Calcutta in the year 1806. This was later rechristened as Bank of Bengal in 1809 and two more presidency banks namely Bank of Bombay and Bank of Madras were established in the year 1840 and 1843 respectively. All three Presidency banks were incorporated as joint stock banks. In due course, this encouraged them to establish more banks in India. By the turn of the century, many banks were established by Indians, namely, Punjab National Bank, Allahabad Bank, Bank of Baroda, etc. As the British rule flourished in India, the three Presidency Banks were amalgamated and a powerful Imperial Bank was established in 1921 as Bank of India. This was renamed as State Bank of India in 1955. The growth

was very slow in this phase, and the banking industry experienced failures between 1913 and 1948. During this phase, public had lesser confidence in banks, and post offices were considered as the safest form to deposit funds. Until the birth of Reserve Bank of India in 1935, the Presidency Banks and later Imperial Bank of India were acting as sort of bankers to the Government of India. Due to absence of regulation and facilities to provide timely assistance, there were recurrent bank failures. This resulted in suspicion about banks in the minds of the people. Hence, the need for a separate Central Bank was emphasized. Accordingly, the RBI came into existence in 1935 to perform all the functions of a Central Bank. To assist the functions and activities of commercial banks, the Government of India came up with the Banking Companies Act in 1949. Later it changed as Banking Regulation Act in 1949, by amending the Act in 1965.

Phase 2

During second phase, the banking sector faced several major changes in between 1969 to 1991. The RBI and the Banking Regulation Act had taken strides to promote macro-economic objectives such as economic growth, better regional balance of economic activities and the diffusion of economic power. Immediately after independence, wide power of regulation and control was given to the RBI. By making use of those powers, the RBI was successful in making Indian banking system trustworthy. Shortly, bank failures were reduced and Indian banks had shown progress under the guidance of the RBI. Many malpractices, deficiencies and drawbacks were sought to be removed by the RBI. Another significant step was taken in 1969 by nationalizing 14 commercial banks in India. They are Central Bank of India, Syndicate Bank, Union Bank of India, Bank of Baroda, Canara Bank, Indian Bank, UCO Bank, Bank of India, Bank of Maharashtra, Dena Bank, Punjab National Bank, Indian Overseas Bank, Allahabad Bank and United Bank of India. Then, six more banks were nationalized in 1980. The major objectives of nationalization were to widen the branch network of banks, particularly in the urban and semi-urban areas. It would help in greater mobilization of savings and flow of credit to all sectors. In 1975, Regional Rural Banks were established for the development of rural areas.

The following are the steps taken by Government of India to regulate Banking Sector in India.

- 1921: Imperial bank was the only bank exist,
- 1935: Reserve Bank of India was established as central bank of India,
- 1949: Enactment of Banking Regulation Act,
- 1955: Imperial bank was converted into State Bank of India,
- 1969: Nationalization of 14 commercial banks,
- 1975: Regional Rural Bank was established,
- 1980: Nationalization of six more banks with deposit of above Rs. 200 Crores, and
- 1984: Core Banking Solution was created to establish a single large database through networking.

In this phase people started having enough faith and confidence on the banking system, deposits & advances and it started to grow further.

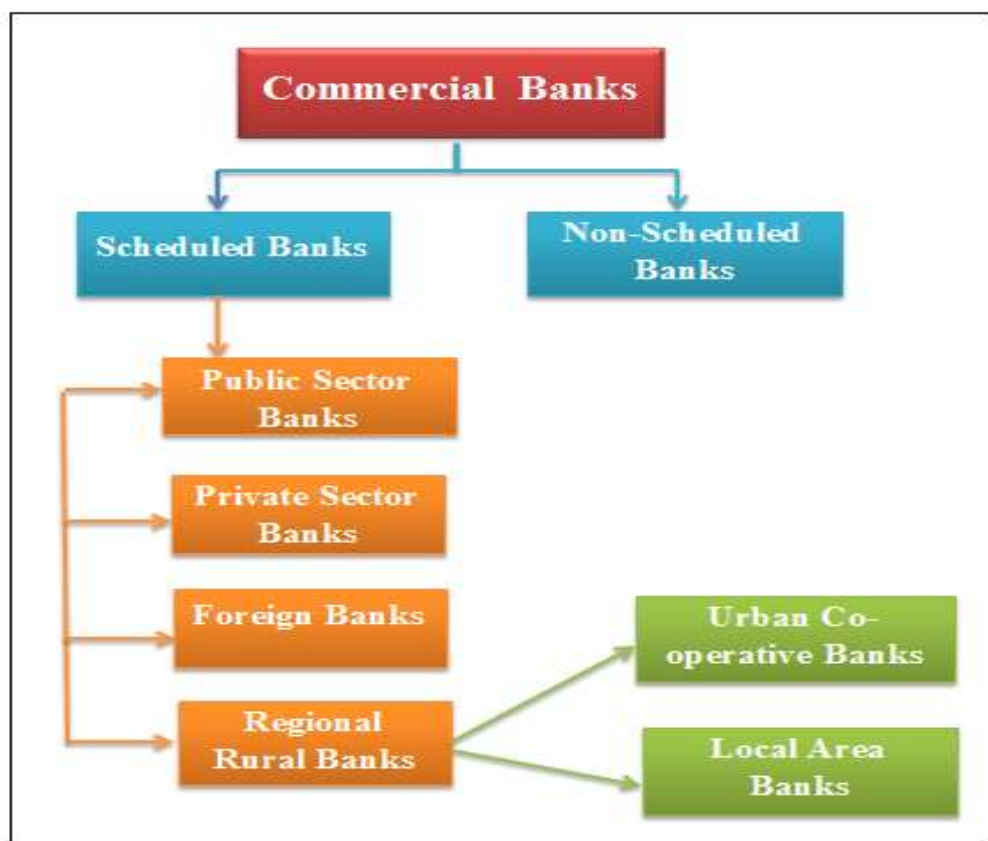
Phase 3

The third and the most exciting phase of Indian Banking system was commenced with the process of economic liberalization in 1991. The reforms in the commercial banking sector had two distinct phases. The first phase of reform was introduced subsequent to the release of the Report of the Committee on Financial System (Chairman: M. Narasimham), 1992 mainly focused to create a viable and efficient banking system, which would thereby improve the productivity and efficiency of the financial system. The second phase of reforms, introduced subsequent to the recommendations of the Committee on Banking Sector Reforms (Chairman: M. Narasimham), 1998 directs to strengthen the banking sector through rigorous operations, prudential and accounting norms, improvements in the credit delivery system. It had greater emphasis on structural measures, improvement in standards of disclosure and levels of transparency in order to align the Indian standards with international best practices. Reforms have brought about considerable improvements as reflected in various parameters relating to capital adequacy, asset quality, income recognition, profitability, gradual reduction in Statutory Liquidity Ratio (SLR) and Cash reserve Ratio (CRR), norms for investment and operational efficiency. RBI periodically revising the rates of SLR and CRR to ensure funds in commercial banks. The rate of SLR was reduced from 25 percent in 2004 to 19.5 percent in 2018. The CRR rate was reduced from 4.75 percent in 2004 to 4 percent in 2018. In December 2021, the rate of SLR and CRR was reduced at 18 percent and 4 percent respectively.

During this phase, banking sector took a U-turn through strategic initiatives such as adopting new business models, expanding scope of their activities and embracing new technology through the introduction of various delivery channels. The beginning of the new century brought more innovations in line with the global developments. The ongoing phase witnessed the launch of more ATMs, which made cash withdrawals easier. This phase also brought in internet banking and mobile banking for easier financial transactions from anywhere at any time. Banks have been attempting to provide better services to provide financial transactions faster and more efficiently. During October 2021, RBI increased per transaction limit of Immediate Payment Service (IMPS) from Rs. 2 lakhs to Rs. 5 lakhs. Positive Payment System have been introduced with effective from 1st January 2021, to prevent the interest of account holders.

1.2 THE STRUCTURE OF COMMERCIAL BANKS IN INDIA

The commercial banks in India are functioning under the supervision and control of the RBI.



Source: Based on the information from RBI (2018-2019)

Figure 1
Structure of Commercial Banks in India

In terms of ownership and function, commercial banks operating in India consist of the following:

- i. Public Sector Banks – 21 (as on March 2018),
- ii. Private Sector Banks – 19,
- iii. Foreign Banks (44 as on March 2018) and
- iv. Regional Rural Banks (56).

On, 30th August 2020, Finance Minister Nirmala Sitharaman announced the mega merger of 10 public sector banks into four large entities. The consolidation of 10 public sector banks involved integration of six exhaustively performing banks with four better performing banks. The merger reduced the number of state run banks as 12. The four sets of mergers are as follows:

1. In the first set of consolidation, Oriental Bank of Commerce and United Bank of India amalgamated with Punjab National Bank. It becomes the second largest public sector bank in terms of business and branches,
2. In the second set of consolidation, Syndicate Bank amalgamated with Canara Bank to form the fourth largest in terms of business and the third largest in terms of branch network,
3. In the third, Andhra Bank and Corporation Bank joined with Union Bank of India and the new entity became fifth largest in terms of business and fourth largest in terms of branches, and
4. Finally, Allahabad Bank amalgamated with Indian Bank, forming the seventh largest entity in terms of business.

The banks are divided into Scheduled and Non-Scheduled banks as detailed below.

Scheduled Banks

Scheduled banks in India are the banks which are included in the Second Schedule of Reserve Bank of India Act, 1934. They must have a minimum capital of Rs. 5 lakhs and maintain reserves as per the directions of RBI. Scheduled banks can borrow money from RBI based on stipulated conditions. They can become full-fledged members of clearing

houses in various centers. In addition to commercial banks, cooperative banks also entitled to become scheduled banks only if they fulfill the criteria which is stipulated by RBI.

Non-Scheduled Banks

Non-scheduled banks are those banks which are not listed in the Second Schedule of Reserve Bank of India Act, 1934 and having a reserve capital of less than Rs. 5 lakhs. Unlike scheduled banks, they are not entitled to borrow money from the RBI for normal banking purposes, except, in emergency situations. They can maintain the reserves with RBI or they can maintain the same with themselves. After May 1977, no more non-scheduled commercial banks are in existence. However, there are small non-scheduled urban cooperative banks, which are operating under RBI.

Public Sector Banks

In Public sector banks, majority/full stake of share capital is with the Government of India. Public Sector banks consist of State Bank of India (SBI) and other public sector banks. SBI itself emerged as a successor of Imperial Bank of India, which in turn emerged out of the unification of Presidency Banks under the British regime. The public sector banks came into existence in two phases. In the First phase 1969, the Government of India nationalized 14 commercial banks as public sector banks. In the Second phase, in April 1980, six more commercial banks (with deposits of above Rs. 200 Crores) were nationalized. All the nationalized banks were fully owned by Government of India in 1990s. After the merger of 7 associate banks of SBI with State Bank of India on 1st April, 2017 and declaring IDBI bank as a private sector, the total number of banks under public sector stands at 21 as of March 2018.

Private Sector Banks

Private sector banks are banks where the majority of share capital and the ownership of the banks are held by private individuals or corporates. The banks are owned, managed and controlled by private promoters, and they undertake all types of banking transactions by themselves. The private sector banks, which were operating in India prior to the liberalization year of 1991, are considered as Old Generation private sector banks. The banks that came into existence subsequent to Narasimham Committee Report I and revised RBI guidelines in 1993 are called as New Generation private sector banks. The total number of private sector banks as of March, 2018 was 19.

Foreign Banks

Foreign banks are those banks, which are registered and have their headquarters in a foreign country, but entitled to operate their branches in India. These banks were allowed to operate through a network of branches. According to the policy of RBI, foreign banks were allowed to open branches in India and they were to be treated the same way as Indian banks are treated in the respective countries. While opening branches in India they have to adhere the guidelines issued by RBI with regard to capital structure, maintaining reserves with RBI and prudential norms to the satisfaction of the authorities. Foreign banks must have a minimum capital of US \$ 25 millions to open 3 branches. The first and second branches must have a minimum of US \$ 10 millions each. The third branch should have US \$ 5 millions. As of March 2018, 44 foreign banks were operating in India.

Regional Rural Banks

RRB banks are established “with a view to developing the rural economy for the purpose of the development of agriculture, trade, commerce, industry and other productive activities in the rural areas, credit and other facilities, particularly to the small and marginal farmers, agricultural laborers and artisans and small entrepreneurs”. The main businesses of RRBs were to “mobilize deposits primarily from rural/semi-urban areas and provide loans and advances to rural areas. In short RRBs can be called “By the rural, of the rural and for the rural”. It was being set up to increase the flow of credit to smaller borrowers in the rural areas. On 2nd October 1975, the first RRB the Prathama Bank were started with authorized capital of Rs. 5 Crores. Further, five regional rural banks were set up with a total authorized capital Rs. 100 Crores which was later augmented to Rs. 500 Crores (\$50 million). Over the years nationalized banks had established 196 RRBs in different parts of India. However due to viability problem, only 56 RRBs exist as of 31st March 2018. On behalf of RBI, RRBs are regulated by National Bank for Agriculture and Rural Development (NABARD).

1.3 ASSET QUALITY OF SCHEDULED COMMERCIAL BANKS IN INDIA

The quality of assets held by banks is a critical indicator of the health of the financial system. It reflects the level of banks credit risk and efficiency of banks in allocation of resources for productive purpose. Currently, the bank lending has gained more attention because of mounting Non-Performing Assets (NPAs). The net NPA of

Scheduled Commercial Banks have increased from Rs. 2,43,960 Crores in March 2005 to Rs.5,20,838 Crores in March 2018. The high level of NPA indicates that the banks have huge number of credit defaulters that ultimately disturbs the profitability and liquidity of the banks. Thus, it becomes an area of due concern.

CLASSIFICATION OF ASSETS

The banks classify their advances into two groups based on the record of borrowers regarding the repayment of principle and interest:

1. Performing Assets, and
2. Non-Performing Assets.

The Non-Performing Assets is again classified into three groups. They are Sub-Standard Assets, Doubtful Assets and Loss Assets.

PERFORMING ASSETS

Performing assets are those assets, which generate income and do not carry any problem in repayment of interest and principle. It does not carry more than normal risk attached to the business. These assets are considered as performing assets or standard assets.

NON-PERFORMING ASSETS (NPA)

An asset, including a leased asset, becomes non-performing assets when it ceased to generate income for the banks. An advance is considered as NPA when the interest or principle remain overdue for a period of more than 90 days in respect of term loan and cash credit.

As per the norms prescribed by RBI, Non-Performing Assets shall be a loan or an advance where:

- Interest or principal remains overdue for a period of more than 90 days in respect of term loan,
- The account remains 'out of order' more than 90 days in case of an Overdraft/Cash Credit,
- The bills remained unpaid for a period of more than 90 days in the case of bills purchased and discounted,
- The installment of principal or interest remains overdue for two crop seasons for short duration crops,

- The installment of principal or interest remains overdue for one crop season for long duration crops, and
- The amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitization transaction as on February 1, 2006.

Sub-standard assets

Sub-standard assets are those assets which remains NPA category for a period of less than or equal to 12 months from the due date.

Doubtful assets

An assets would be classified as doubtful if it has remained sub-standard category for a period of 12 months from due date.

Loss assets

A loss asset is an asset where the loss has been identified by the banks internal or external auditor or through inspection, but the amount has not been written off wholly or partially. An asset will become loss, if the doubtful asset exceeds the period of 3 years from the due date.

From the time of loan account becomes NPA and till the time of recovery of dues, banks are required to make provisions. RBI has prescribed certain percentage of provisions under each category, as presented in Table 1.

Table 1 Asset Classification and Provisioning Norms of NPAs

Type of Asset	Interval period	Provisions
Standard assets	On time collectable assets	0.40 percent of standard assets
Sub-standard assets	less than or equal to 12 months from due date.	15 percent of total outstanding
Doubtful assets	Remain substandard category for 12 months from due date.	
	Up to 1 year	100 percent for secured and 25 percent for unsecured portion
	1 to 3 years	100 percent for secured and 40 percent for unsecured portion
	More than 3 years	100 percent for secured and 100 percent for unsecured portion
Loss assets	Written off and uncollectable assets	100 percent for both secured and unsecured portion

Source: dbie.rbi.org.in

CAUSES OF NON-PERFORMING ASSETS

The following are the main reasons for growing NPAs.

- Willful default by customers. i.e., they can able to repay but purposively not paying their debt,
- Diversifying funds for purposes other than the real intention mentioned in loan document,
- Inadequate credit appraisal system and improper debt management by the banks, which leads to massive increase in NPAs,
- Absence of regular inspections by bank officials to follow the debtors' activities regarding the usage of loan amount,
- Political pressure for sanction of loans to corporate sectors,
- Frequent changes in government policies,
- Excessive overdraft lending, and
- Improper execution of commands, which are issued by a legal authority.

RECOVERY CHANNELS OF NPAs

Different channels were introduced to recover the amount of NPA namely, Lok Adalats, DRT Act, SARFAESI Act and Insolvency and Bankruptcy Code, in order to strengthen the credit discipline of the banks.

Lok Adalats

Lok Adults were set up under Legal Service Authority Act, 1987. It was mainly to resolve disputes between parties which are under “doubtful” and “loss” category with an unpaid due amount up to Rs.20 lakhs.

DRT Act

DRT (Debt Recovery Tribunal) was set up under The Recovery of Debts in Banks and Financial Institutions Act, 1993. DRT has been authorized to consider cases, which have advance of Rs.10 lakhs and above. The recovery amounts which are below Rs.10 lakhs are sent to civil court.

SARFAESI Act

SARFAESI (Securitization and Reconstruction of Financial Assets and Enforcement of Securities Interest) Act 2002, aims at realization of interest due without the intervention of court or tribunal. It deals only with Securitization, Asset Reconstruction and Security Enforcement aspects. This Act is not applicable to unsecured loans, the amount of loan which are below Rs.10 lakhs and the loans where the remaining principal due is less than 20 per cent of the advances.

Insolvency and Bankruptcy Code (IBC)

In 2016, Government of India introduced IBC as consistent recovery channel to improve the asset quality of banks. The rates of recovery in the existing channels were declined over the period of time. To resolve the issue and to find solution to recover NPAs, the IBC resolution process has been enacted. It is expected to result in better recovery as compared to existing channels.

1.4 ISSUES AND CHALLENGES OF BANKING SECTOR

A balanced and vigil regulation has mandated to ensure the transparency of banking sector. The banking sector provides finance to various segments of the economy and helps in sustainable socio-economic growth. Apart from traditional business activities, banks are offering diversified financial services such as mutual funds, merchant banking, venture capital, etc. Besides, banks have introduced e-banking and e-payment system through electronic means such as e-cheque, card based payments (credit card, debit card and smart cards) and Electronic Fund Transfer (EFT) Structured Financial Messaging Solution (SFMS), Unified Payment Interface (UPI) and Bharat Interface for Money (BHIM). Therefore, there is a need for understanding the challenges, which are associated with different banking activities to address the issue of deteriorating capital, growing NPAs and declining profitability. At present, the Indian banking sector is facing several challenges to stabilize the economy. Some of the critical aspects are discussed below.

Capital Adequacy

As per the capital adequacy requirements laid out by the Basel Committee on Banking Supervision (BCBS), banks are required to maintain an adequate ratio to support banking business. Due to increasing level of NPAs, higher capital adequacy is required in the banking industry to ensure their survival. In the light of Basel III norms, RBI monitors

compliance of risk under risk based supervision framework, especially to meet the credit demand and to prevent the banks from becoming bankrupt. The ratio of CAR has been significantly declining from 12.91 percent at March, 2004 to 11.98 percent at March,2018.

Bank Recapitalization Plan

The public sector banks are saddled with high non-performing assets (NPAs) and facing risk on granted loans, which are in insolvency proceedings. As a result, Central Government had announced to infuse Rs. 70,000 crores under Indradhanush Scheme in 2015, to public sector banks over four successive years to meet the capital requirement in line with global risk Basel-III norms. Again, to revamp the functioning of public sector banks the Government has announced to infuse Rs. 2.11 lakh crores (\$32.4 billion) capital over two years into public sector banks. The Banks received Rs. 1.35 lakhs crores through Recapitalization Bonds, Rs. 18 lakh crores from budgetary support and remaining Rs 58 lakh crores raised through the sale of shares of the banks. It will increase lending capacity of PSBs, which in turn boost the economy.

Non-Performing Assets (NPA)

The commercial banks continue to face the problem of non-performing assets (NPAs), which attribute to other factors such as weak debt recovery mechanism, non-realization of security and poor credit appraisal techniques. The recovery channel Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002 and the enactment of Insolvency and Bankruptcy Code (IBC) Act, 2016 has increased the momentum for the recovery of NPAs. However, banks need to intensify their efforts to recover their overdue and has to prevent generation of fresh NPAs further.

Prompt Corrective Action (PCA) framework for NPAs

Reserve Bank of India has issued regulatory trigger points as prompt corrective action framework in terms of three parameters, i.e., capital to risk weighted assets ratio (CRAR), net non-performing assets (net NPA) and return on assets (RoA). RBI issued mandatory and discretionary restrictions, when certain risk thresholds are breached. It is mainly to facilitate the banks to take corrective measures in a timely manner to realize the financial health. The framework of the PCA are as follows.

Table 2 Prompt Corrective Action (PCA) Framework

Area	Indicator	Risk Threshold 1	Risk Threshold 2	Risk Threshold 3
Capital	Capital to risk weighted asset ratio or Common Equity Tire 1 ratio (CET 1)	< 10.25 % but \geq 7.75 % or < 6.75 % but \geq 5.125 %	< 7.75 % but \geq 6.25 % or < 5.125 % but \geq 3.625 %	< 3.625 %
Asset Quality	Net Non-Performing Advances (NNPA) ratio	\geq 6.0 % but < 9.0 %	\geq 9.0 % but < 12.0 %	\geq 12.0 %
Profitability	Return on Asset (RoA)	Negative RoA for two consecutive years.	Negative RoA for three consecutive years.	Negative RoA for four consecutive years.

Source: dbie.rbi.org.in

Note:

CET 1 ratio: The percentage of core equity capital, net of regulatory adjustments to total risk weighted assets as defined in Basel III guidelines.

NNPA ratio: Net NPAs to net advances ratio.

RoA: Profit after tax to average total assets ratio.

Table 3 Mandatory and Discretionary actions under PCA framework

Specifications	Mandatory actions	Discretionary actions
Risk Threshold 1	Restriction on dividend distribution/remittance of profits	Special audit/ inspection of the banks, Strategy related, Corporate Governance related
Risk Threshold 2	In addition to mandatory actions of Threshold 1, Restriction on branch expansion and Higher provisions as part of coverage regime.	Capital related, Credit risk related, HR related, Profitability related, Operation activities related.
Risk Threshold 3	In addition to mandatory actions of Threshold 1, Restriction on branch expansion Restriction on management compensation and directors fees as applicable.	Any other

Source: dbie.rbi.org.in

Technology and its Impact on Banking

Banking sector has been transformed into an Information Technology (IT) intensive operation. It helped them to have efficient customer service, better financial transaction with improved internal controls and productivity. On the other side, IT based products and services have their inherent risks, which need to manage through preventive and corrective measures. Majority of commercial banks offer CORE banking based services to customers across various geographical locations with the help of Central Data Centers. CORE banking has enabled banks to generate various Management Information System reports for decision making, as well as for analysis with a view to improve various products and services offered to customers. Technology will act not only as the facilitator but a catalyst to reach out and meet the expectations of customers.

Banks and technology are evolving so rapidly that bank staffs must continually seek new skills that enable them not only to respond the change, but also to build competence in handling various queries raised by customers. Therefore, there is a need to keep them updated with a new set of skills and knowledge.

1.5 SCOPE OF THE STUDY

The current study focused on assessing the financial soundness of scheduled commercial banks (Public sector, Private sector and Foreign banks) by measuring their Capital Adequacy, Asset Quality, Management Ability, Earning Efficiency, Liquidity and Sensitivity to Risk. The study covers a period of 15 years from 2003-2004 to 2017-2018. Since the scope is broader, a systematic approach is used to select the components. Multi Criteria Decision Making Approach is employed to rank the banks. The study used survival analysis to investigate the financial condition of the banks and to predict the financial variables, which will signal financial distress condition of the banks.

1.6 STATEMENT OF THE PROBLEM

The Indian Banking Industry has undergone noticeable changes, which are underpinned by competitive operating environment and financial inclusion through technological advancement. In the liberalization era, Narashimham Committee (1991) examined all aspects relating to structure, organization and functioning of the Indian banking sector. Based on the recommendations of the committee, Reserve Bank of India (RBI) issued various measures which include capital adequacy, income recognition, asset

classification, reduction of Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) to strengthen the banking system. The RBI has initiated various measures to improve the payment and settlement system. These measures include Electronic Fund Transfer (EFT), Real Time Gross Settlement (RTGS), Structured Financial Messaging Solution (SFMS), Unified Payment Interface (UPI) and Bharat Interface for Money (BHIM). To argument the growth of industrial and agricultural sector, the loans and advances granted by the banks have increased from Rs. 11,50,836 Crores in March, 2005 to Rs. 87,46,000 Crores in March, 2018. But, the major problem faced by the banks is growing NPAs. The ratio of gross NPA to gross advances of scheduled commercial banks sharply increased from 7.2 percent in March, 2004 to 11.2 percent in March 2018. The banking sector is facing a problem of increasing level of non-performing asset and it is more in public sector banks. The gross NPA of scheduled commercial banks have increased from Rs.3,23,464 Crores in March, 2015 to Rs.10,39,787 Crores in March, 2018. The banking sector has been under strong pressure to become more competitive and efficient. The sustainability continues to be a major challenge to the banks, because of growing NPAs and deteriorating profitability, cash flow and liquidity. With a view to investigate the financial distress condition of the select scheduled commercial banks, the study entitled “Prediction of Financial Distress of Scheduled Commercial Banks in India – An Application of Survival Analysis” was carried out.

1.7 RESEARCH QUESTIONS

The present study aims to examine the financial soundness of scheduled commercial banks using CAMELS approach and to identify the variables, which influence financial distress condition of banks in India. Thus, the following research questions were framed.

1. Are the scheduled commercial banks financially sound?
2. Where do they stand in terms of their performance? Are the banks consistent in their performance?
3. What is the level of non-performing assets of the banks? Do the public sector banks face financial crisis more severely than other bank groups? and
4. What is the level of distress condition of scheduled commercial banks in India?

1.8 RESEARCH OBJECTIVES

In order to address the above mentioned research questions, the following objectives were framed:

- To evaluate the performance of select scheduled commercial banks,
- To analyze the trends in non-performing assets of the banks,
- To rank the banks based on multi-criterion approach (VIKOR), and
- To predict the financial distress condition of select banks using survival analysis.

1.9 RESEARCH HYPOTHESES

The following null hypothesis were framed to support the study

H₀₁: There is no significant mean difference of select scheduled commercial banks in respect of Capital Adequacy, Asset Quality, Management Ability, Earnings Efficiency, Liquidity Management and Sensitivity to Risk of select scheduled commercial banks.

H₀₂: There is no significant mean difference in trends of non-performing assets of select scheduled commercial banks.

H₀₃: There is no link between credit risk variables with operational risk, profitability and other specific variables.

H₀₄: There is no link between operational risk variables with profitability and other specific variables.

H₀₅: There is no link between profitability variables and other specific variables.

H₀₆: There is no significant relationship between predictor variables and financial distress condition of Indian scheduled commercial banks.

1.10 LIMITATIONS OF THE STUDY

The limitations confronted while carrying out the research are as follows:

- The study focused only on quantitative aspects of financial data and the qualitative aspects are not analyzed,

- The study was based on the data collected only up to 2017-2018, to ensure comparison between the banks. This is due to merger in public sector banks.
- State Bank of India Group was completely excluded because of consolidation of all the subsidiary banks into State Bank of India on 1st April 2017.

1.11 CHAPTER SCHEME

The study is organized under the following five chapters.

Chapter 1: Introduction

This chapter provides a detailed background of the study, Statement of the Problem, Scope of the Study, Objectives, Hypothesis, Limitations of the Study and Chapter Scheme.

Chapter 2: Review of Literature

This chapter reviews various research studies, which are related to the research problem and indicates the Research Gap.

Chapter 3: Research Methodology

This chapter explains the methodology adopted for the study and enlightens the Method of Data Collection, Period of Study, Sample Selection and Statistical Tools applied for the study.

Chapter 4: Results and Discussions

This chapter focuses on analysis of data collected and interpretation of the results. The results are inferred based on the objectives of the study.

Chapter 5: Summary of findings and Conclusion

This chapter presents the summary of findings of the study, suggestions to the banks and lists the areas of study for further research.