



Ad<sup>v</sup>anced  
Leadership  
Programme

# **Challenges for Indian banks during the next decade**

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November 26, 2012

# AGENDA

**The last two decades: a quick recap**

**A transforming India: driving the banking sector**

**Looking ahead**

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# India's transformation

Transition to a global economy		
Pre-1990	The 1990s	Since 2000
<ul style="list-style-type: none"><li>• High regulation &amp; protectionist policies</li><li>• Import-substitution strategy</li><li>• Focused on agriculture and industry</li></ul>	<ul style="list-style-type: none"><li>• Open to foreign investments &amp; competition</li><li>• Extensive reforms</li><li>• Corporate &amp; financial sector restructuring</li></ul>	<ul style="list-style-type: none"><li>• Growth of knowledge economy</li><li>• Global competitiveness</li><li>• Strong domestic savings &amp; consumption</li></ul>

# Knowledge and innovation led growth

Structural shift from an agrarian/ manufacturing to a services-led economy

*Built on multiple drivers*

Knowledge  
based  
business

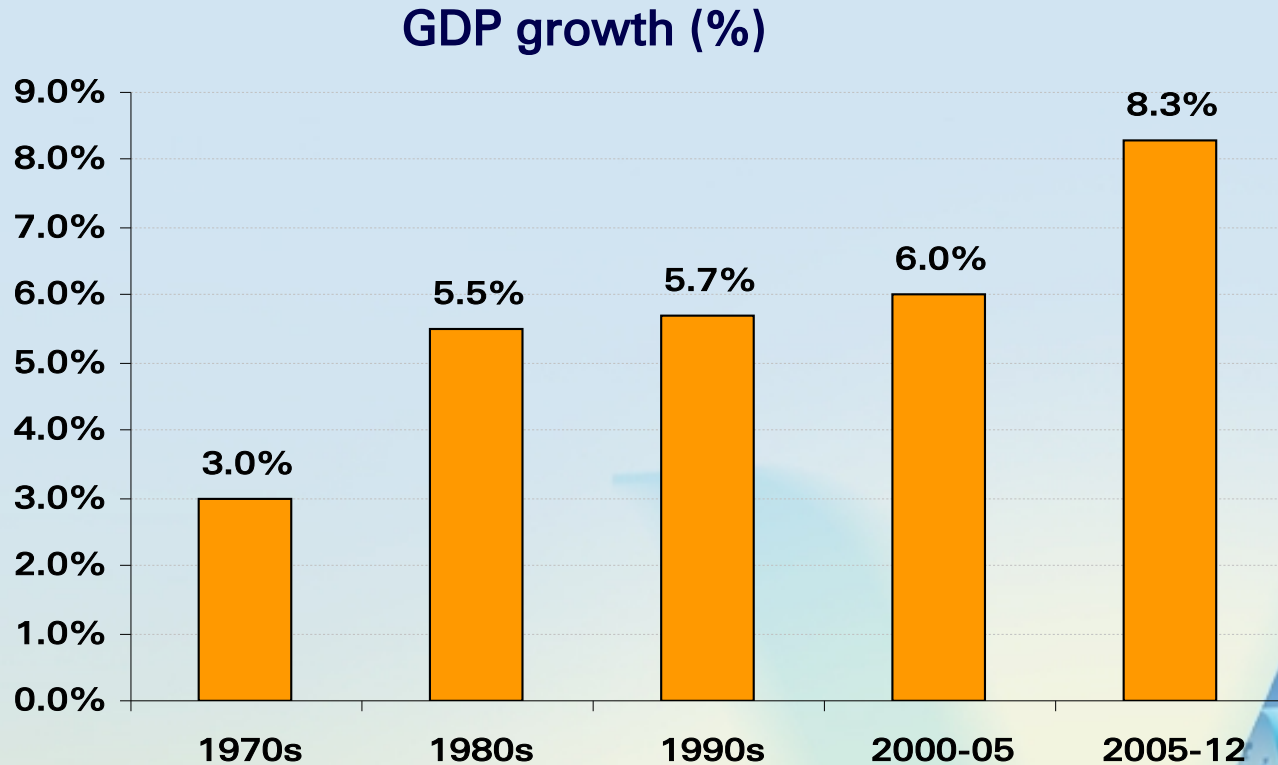
Domestic  
consump-  
tion

Global  
competi-  
tiveness

Investment

**Virtuous cycle of a growing consumer class and a resurgent corporate sector**

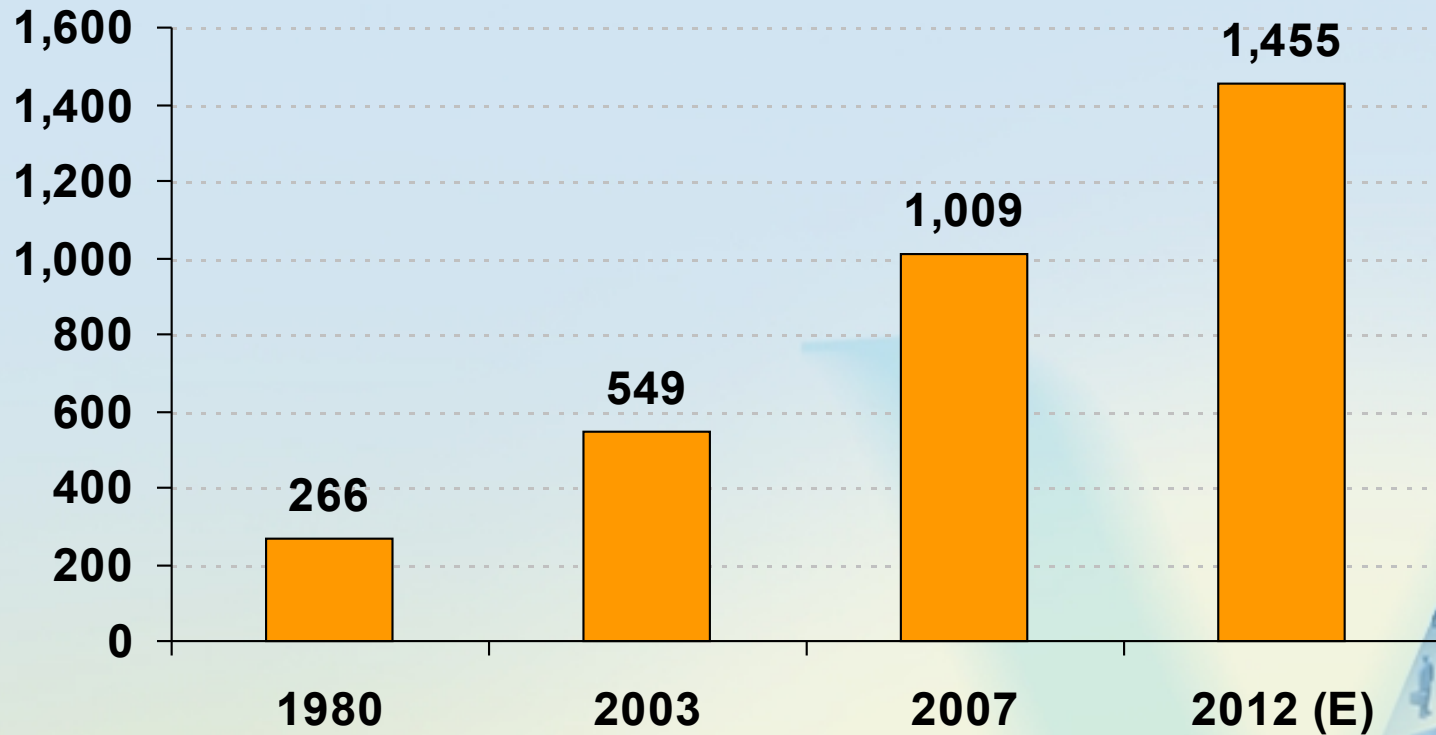
# Leading to a step change in growth rates



*India has moved to a higher growth trajectory*

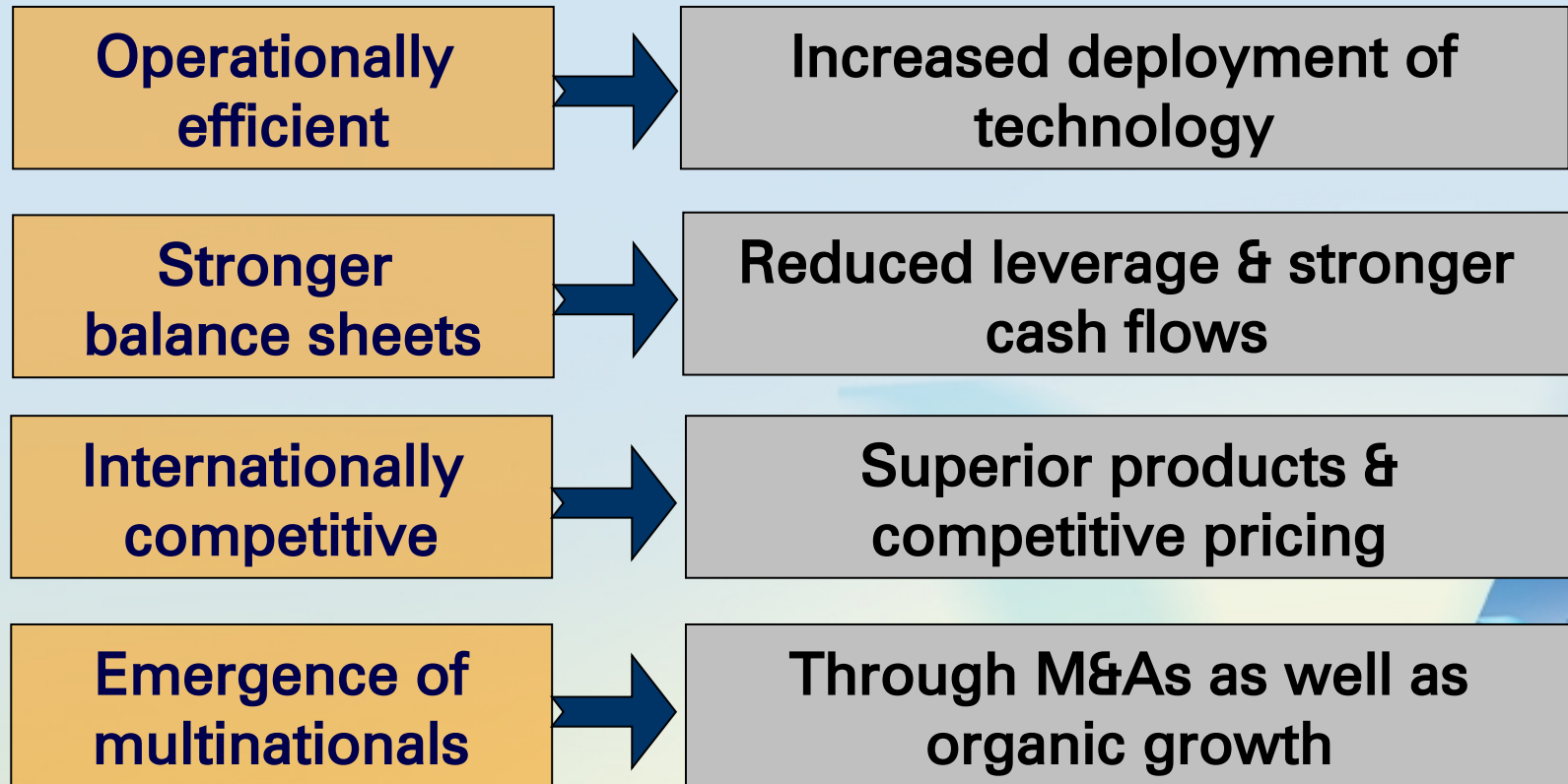
# ...rapidly growing household incomes

Per capita GDP (USD)

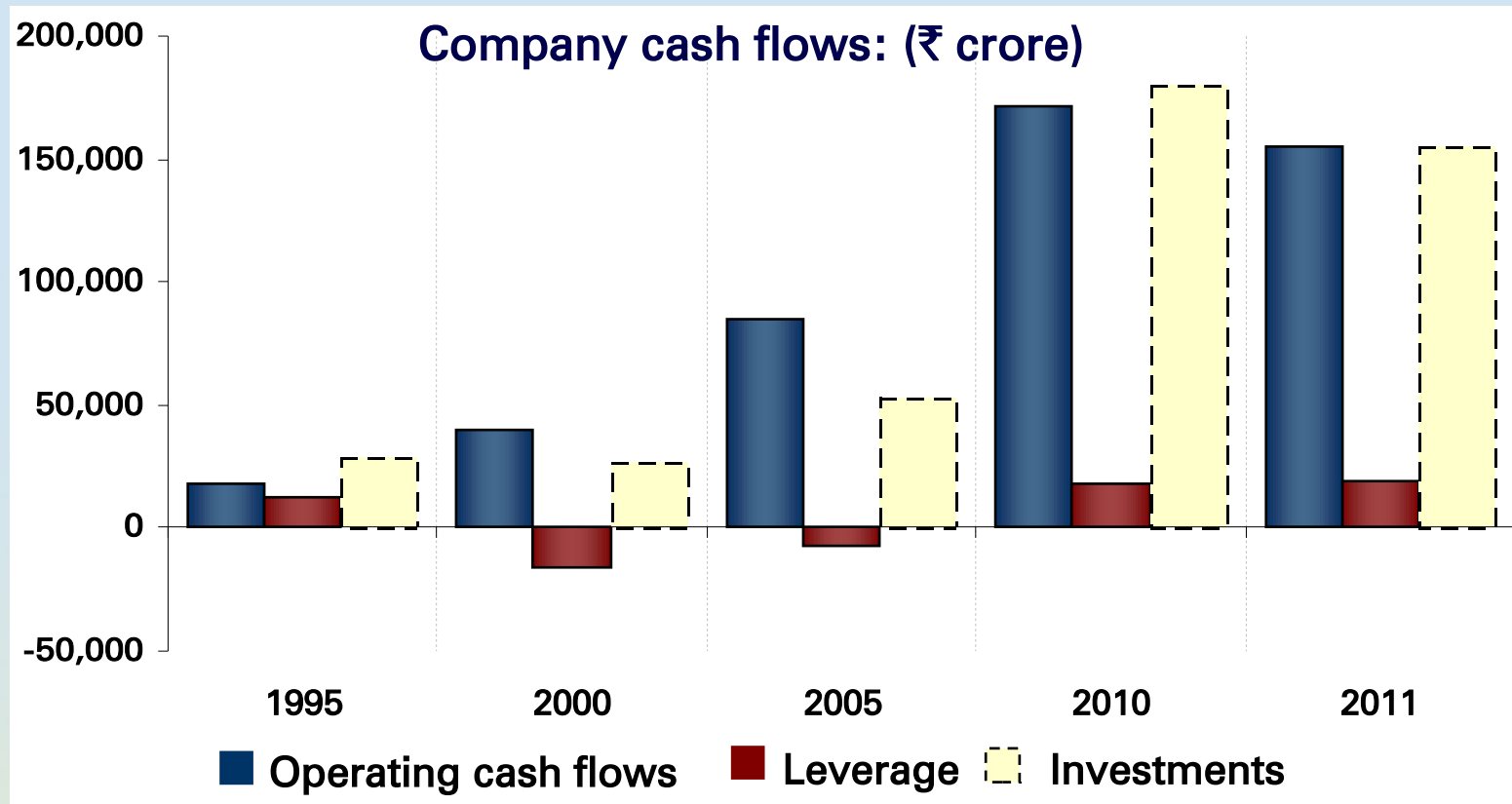


Source: IMF, McKinsey & Co.

# ... and a resurgent corporate sector



# ...with growth ambitions on a sound footing



**Nine fold rise in operating cash flows from 1995-2010**

Sample of 1,050 manufacturing companies

Source: CMIE Prowess

# Banking has transformed in this period

- ✓ **Advent of retail banking**
- ✓ **Growing presence of foreign banks**
- ✓ **Emergence of a universal banking model**
- ✓ **Banks and non banks competing to serve similar customer needs**
- ✓ **Technology driven innovation in products and access to services**
- ✓ **Focus shifting to inclusive banking**

# Driven by the impact of technology

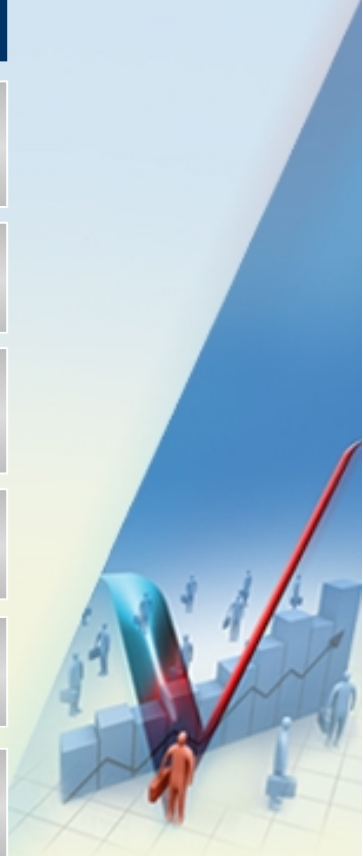
## Technology driven banking infrastructure

- RTGS<sup>1</sup>
- NEFT<sup>2</sup>
- Interbank Mobile Payments System
- ATM installed base of over 100,000 (over 27% compounded growth from 2006 to 2012)
- POS terminals over 700,000

1. Real time gross settlement system
2. National electronic funds transfer

# The disruptive power of technology

ICICI Bank	Share of transactions in 2001	Share of transactions in 2012
Branches	94%	12%
ATMs	3%	41%
Internet	2%	35%
POS	-	7%
Call centre	1%	2%
Mobile	-	2%



# Decadal growth in banking: five times

	1970	1980	1990	2000	2010	2011
Scheduled commercial banks <sup>1</sup>	72	148	270	297	165	163
Branches and offices	10,131	32,419	59,756	65,412	85,393	93,080
Deposits (₹ bn)	53	334	1,735	8,516	44,928	52,080
Advances (₹ bn)	42	221	1,055	4,541	32,448	39,421

- Deposits and advances grew about 5x per decade (18% CAGR)
- Advances growing faster since 2000 (>20% CAGR)

1. Consolidation from the year 2000 was due to a reduction of regional rural banks (RRBs) from 196 to 82, and the reduction in foreign banks and other domestic banks from 101 to 83
2. Includes public sector banks, private sector banks, RRBs and foreign banks

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# India's key competitive strengths

- ✓ **A large domestic consuming market with a favourable demographic profile**
- ✓ **An entrepreneurial talent pool with innovation capabilities**
- ✓ **Cost competitiveness**
- ✓ **Potential for improving productivity with easing infrastructure bottlenecks**

# Demographic advantage

- ✓ **A young population with median age of 25 years**
- ✓ **Median age would be 30 years in 2025**
- ✓ **Rising share of working age population**
- ✓ **Addition of around 11 million to the workforce every year for next five years**
- ✓ **Working age population to exceed 50% of total population in 2025**
- ✓ **India to account for around 25% of the global workforce by 2020**
- ✓ **Dependency ratios to remain low till 2040**

Source: United Nations

# Increasing prosperity

## Upward migration of household incomes

- Households with incomes of over USD 10,000 per annum to increase to ~82 million by 2018 from current ~34 million
- ~40 million households will move out of the deprived category (household income < USD 4,000 per annum)

# Rise in per capita GDP to drive growth

Per capita  
GDP < US\$ 500

- Limited aspirations
- Low affordability

Early 2000

Per capita  
GDP at US\$  
500 -1,500

- Increased affordability
- Aspirations of a better lifestyle

2002-2011

Per capita  
GDP at US\$  
1,500 -2,500

Demand for  
better living  
environment

2012-2017

Per capita  
GDP at US\$  
2,500-4,000

Accelerating  
consumption  
cycle

2018-2021

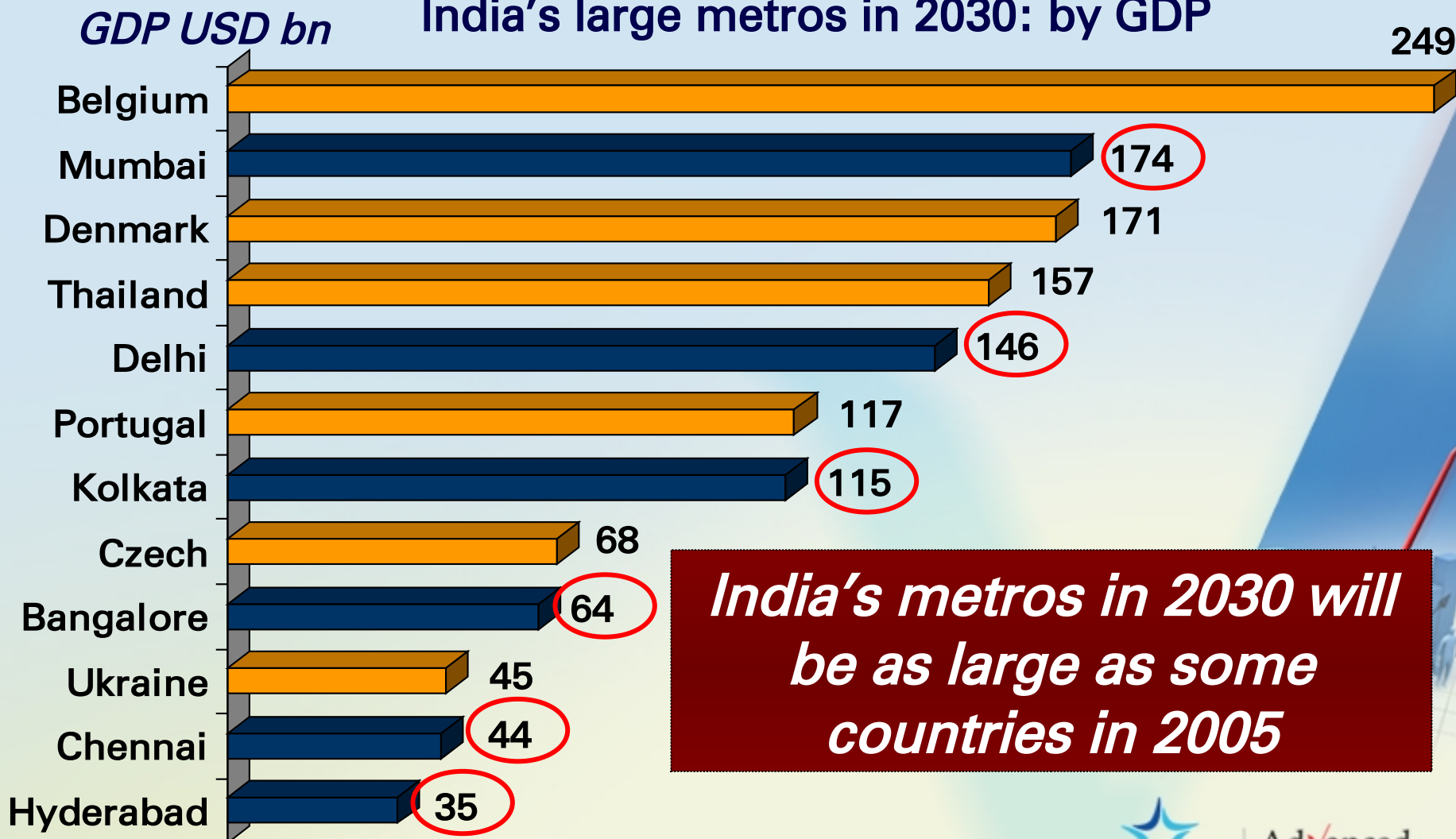
# Infrastructure investments

**Meeting existing shortages and hence highly viable**

- ✓ **Economic growth and rising per capita income leading to:**
  - ✓ **Demand for better infrastructure**
  - ✓ **Growing ability to finance projects**
  - ✓ **Willingness to pay for infrastructure facilities**
- ✓ **Infrastructure development a key priority**
  - ✓ **Major areas of development being roads, power, ports, airports, rural & urban infrastructure**
  - ✓ **Infrastructure spending as a percentage of GDP is expected to exceed 10.5% by the end of the 12th Plan period**

# Rapid Urbanisation

## India's large metros in 2030: by GDP



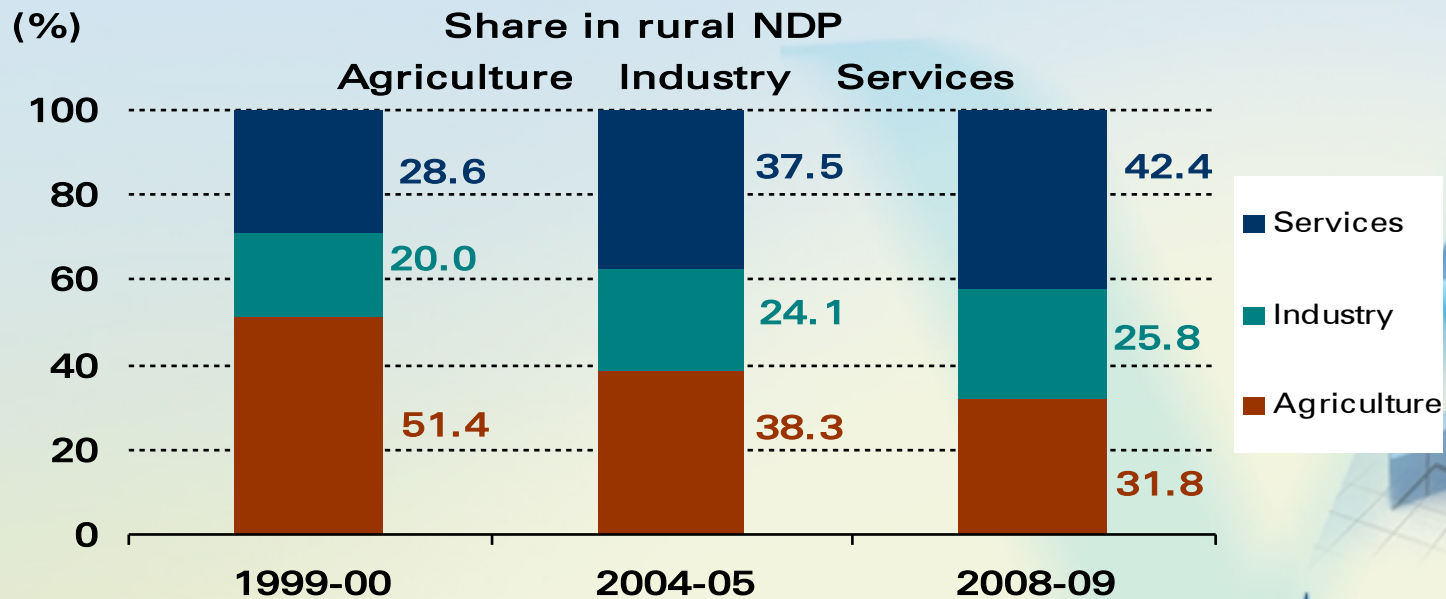
*India's metros in 2030 will be as large as some countries in 2005*

Assuming an annual GDP growth of 8.0% between 2009-2018 and 7.0% between 2018-2030

Source: Mckinsey

# Resurgent rural India

- ✓ **Over 700 mn people across 600,000 villages**
- ✓ **Rural growth supported by:**
  - ✓ **Changing characteristic of rural economy with reduced dependency on agriculture**
  - ✓ **Rising wealth creation with estimate of 40 mn middle & high income households by 2010**



# The China proxy

China (USD)	2003	2005	2010	2012 (E)
GDP (bn)	1,641	2,257	5,930	7,992
Per capita GDP	1,270	1,726	3,738	5,899
Population (bn)	1.29	1.31	1.34	1.35

India (USD)	2003	2005	2010	2012 (E)
GDP (bn)	590	808	1,598	1,779
Per capita GDP	549	729	1,342	1,455
Population (bn)	1.07	1.11	1.19	1.22

- China's evolution is an indication of future progress in India

(E) - estimate

Note: GDP is on nominal basis

Source:IMF

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# Key themes for the banking sector

**Scale**

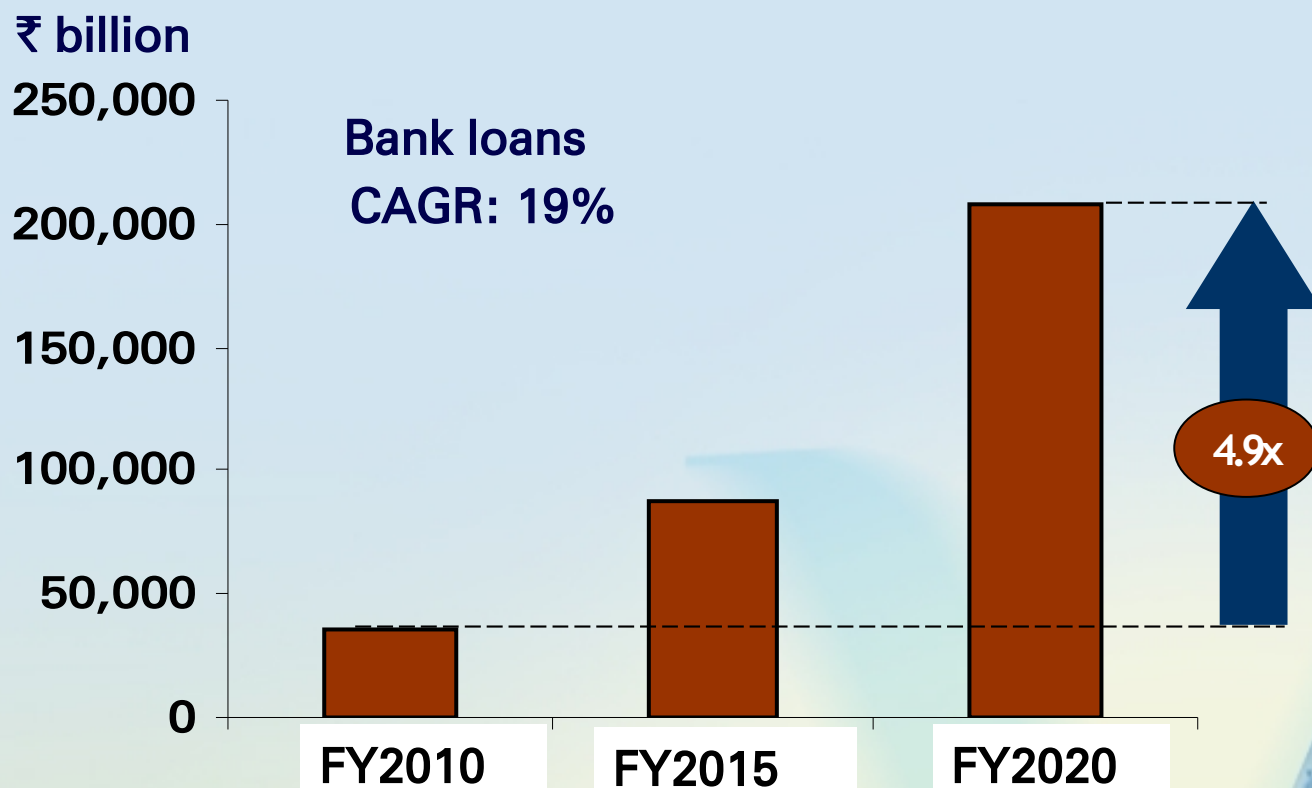
**Customer engagement**

**Technology**

**Inclusion**

**Regulation**

# Scale: Indian banking in 2020



- Indian banks need to prepare for multifold increase in scale

# Customer engagement

## *Customer acquisition and on-boarding*

Branches

ATMs

Connected  
marketplace

- Products that address needs of diverse customer segments
- Strong distribution backing products
- Development of new channels by leveraging technology
- Consistency in experience across channels
- Mobile technologies

# Customer engagement

*Servicing customers through the life cycle*

## Analytics



- Consistency of customer experience across channels of distribution
- Analytics to understand and address customer needs across diverse segments
- Development of banking history for underbanked and unbanked customers for cost effective credit

# Technology continues to be in flux

From mainframe to  
minicomputer to  
desktop PC

*And now, mainframe  
in a pocket*

- Higher capacity and processing capability
- Software to run the devices
- Ability to connect through broadband and wireless
- Mobility, new platforms and the ecosystems in handheld devices

**New platforms such as for payments are now challenging the traditional bank channels**

# The next wave: being connected

- 2.25 bn (32%) of world population is online today, and 1.10 bn users are on 3G
- Mobile internet is ramping up dramatically
  - 57 mn 3G users in China, y-o-y growth of 115%
  - 39 mn 3G users in India, y-o-y growth of 840%
- Mobile internet makes up 50% of internet traffic in India

Source: KPCB

- Out of 1.80 bn mobile users in China and India
- One billion will go online in two years

# Connectivity in India ..

**Third largest  
internet user base**

**Second largest  
mobile subscriber  
base**

- 120 mn internet users, 800 mn mobile subscribers
- Broadband connectivity a catalyst
- Consumers are becoming part of the cloud seamlessly without consciously realising it
- Device costs will continue to drop
- More and more capabilities would be available at lower costs

***.. would have a significant impact on banking and the ability to leverage this opportunity will be a key success factor***

# Inclusion: enablers

Technology

Unique identity number

Simplified banking

# Channel innovation

## Driving scale and profitability

### Smart cards

- Opening and operating savings accounts
- Easy KYC

### POS machines

- Used by branchless banking channels

### Low cost branch

- Resource efficient branches

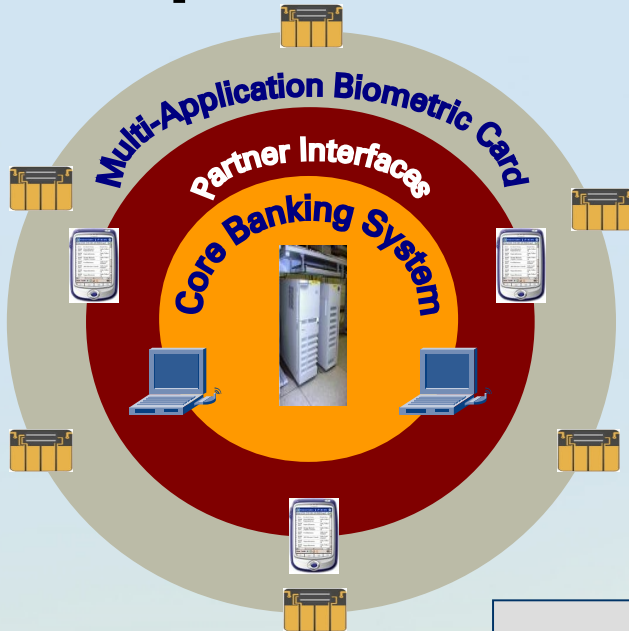
### Low cost ATMs

- To bridge distance and ease transactions

### Mobile phones

- For all banking operations
- Steadily gaining traction

# Smart cards have simplified data capture



## Biometric Transaction Card



- Biometric smart card for secure validation
- Overcome distance by setting up service points close to customers
- Most effective for the poor and uneducated

# Branch in a box



- POS based solution offering banking transactions like balance enquiry, cash withdrawal, deposit
- Cheque payment (with capability to display signatures for verification)
- RTGS<sup>1</sup>/ NEFT<sup>2</sup>
- Can support transactions like pass book printing, opening of fixed deposits and bill payment
- Low bandwidth
- GPRS connectivity

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# Unique identity number

## Preliminary KYC and wider acceptance

- Instant identity verification
- Basis for Know Your Customer
- Build credit history
- Improve service delivery to the poor
- Customer management to avoid issues of over-leveraging

# Financial services for all

## Subsidy transfer

- Direct payment of benefits such as NREGA, Social Security Pension schemes

## Payment ecosystem

- Cashless payments through mobile wallets

## Credit

- Account history from electronic transactions for data driven lending

# Regulatory developments

- ✓ **While Indian banks need to focus on growth and scale they are also part of the global regulatory framework**
- ✓ **Globally there is regulatory focus on complexity and consequently on making banks simpler**
- ✓ **Regulators seeking granular insight into each business and an understanding of the risks**
  - ✓ **Resulting in more intensive supervision**
- ✓ **Emphasis on capital and risk management**
  - ✓ **Rising capital requirements**
  - ✓ **De-risking business means lower returns**
- ✓ **This is the environment in which Indian banks have to achieve growth**

# In summary

- ✓ **The next decade for Indian banking will be more transformational than the last decade**
- ✓ **Economic growth and shifts in technology will drive this transformation**
- ✓ **Banks will need to be cognisant of evolving regulations and regulatory expectations as they build out their business**

**Thank you**