

A Study on Effectiveness and Constraints in Accessing Financial Services in India

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ABSTRACT

India has a diversified financial sector undergoing rapid expansion, both in terms of strong growth of existing financial services firms and new entities entering the market. The sector comprises commercial banks, insurance companies, non-banking financial companies, co-operatives, pension funds, mutual funds and other smaller financial entities. The present growth rate of financial sector in India is about 8.5% p.a. An increase in growth rate is equivalent to growth of our economy. Over the past few years, there have been reforms in monetary policies, economic policies, opening up of financial markets, development of other financial sectors etc. In present times, a wide variety of financial products and services are offered to consumers to keep them satisfied. The Reserve Bank of India has also played a major role to help in growth of financial sector of India. The paper aims at trends, effectiveness and constraint in issuing financial services in India.

1. Introduction

India has a diversified financial sector undergoing rapid expansion, both in terms of strong growth of existing financial services firms and new entities entering the market. The sector comprises commercial banks, insurance companies, non-banking financial companies, co-operatives, pension funds, mutual funds and other smaller financial entities. The banking regulator has allowed new entities such as payments banks to be created recently thereby adding to the types of entities operating in the sector. However, the financial sector in India is predominantly a banking sector with commercial banks accounting for more than 64 per cent of the total assets held by the financial system.

The Government of India has introduced several reforms to liberalise, regulate and enhance this industry. The Government and Reserve Bank of India (RBI) have taken various measures to facilitate easy access to finance for Micro, Small and Medium Enterprises (MSMEs). These measures include launching Credit Guarantee Fund Scheme for Micro and Small Enterprises, issuing guideline to banks regarding collateral requirements and setting up a Micro Units Development and Refinance Agency (MUDRA). With a combined push by both government and private sector, India is undoubtedly one of the world's most vibrant capital markets. In 2017, a new portal named 'Udyami Mitra' has been launched by the Small Industries Development Bank of India (SIDBI) with the aim of improving credit availability to Micro, Small and Medium Enterprises' (MSMEs) in the country. India has scored a perfect 10 in protecting shareholders' rights on the back of reforms implemented by Securities and Exchange Board of India (SEBI).

2. Growth of financial sector in India

The present growth rate of financial sector in India is about 8.5% p.a. An increase in growth rate is equivalent to growth of our economy. Over the past few years, there have been reforms in monetary policies, economic policies, opening up of

financial markets, development of other financial sectors e.t.c. In present times, a wide variety of financial products and services are offered to consumers to keep them satisfied. The Reserve Bank of India has also played a major role to help in growth of financial sector of India.

The diversified financial sector of India comprises of banks, mutual funds, insurance companies, pension funds e.t.c. Do you know that the banking sector in India holds more than 60% of the total financial assets of the country? At present, India is without any doubts one of the world's most vibrant capital market. Let's take a look at growth of some of the financial sectors of India one by one-

Growth of the Banking Sector

Being one of the most extensive, the entire Indian banking system has a total asset value of approximately US\$ 270 billion with total deposits being around US\$ 220 billion. The banking system in India is continuously advancing and transforming itself. The current development of Core banking, Internet banking e.t.c. has made banking operations easy and customer friendly.

Growth of the Capital Market in India

The capital markets in India have also witnessed changes. Some of them are-

- Stock exchanges facing privatization.
- Removal of ill-used forward trading mechanism
- In order to serve different investors in different locations, the introduction of InfoTech systems in National Stock Exchange.
- The increase in the ratio of transaction with deposit system and share ratio.

Growth in the Insurance sector in India

- The market potential in India is immense. But it is untapped. So now in order to utilize this opportunity,

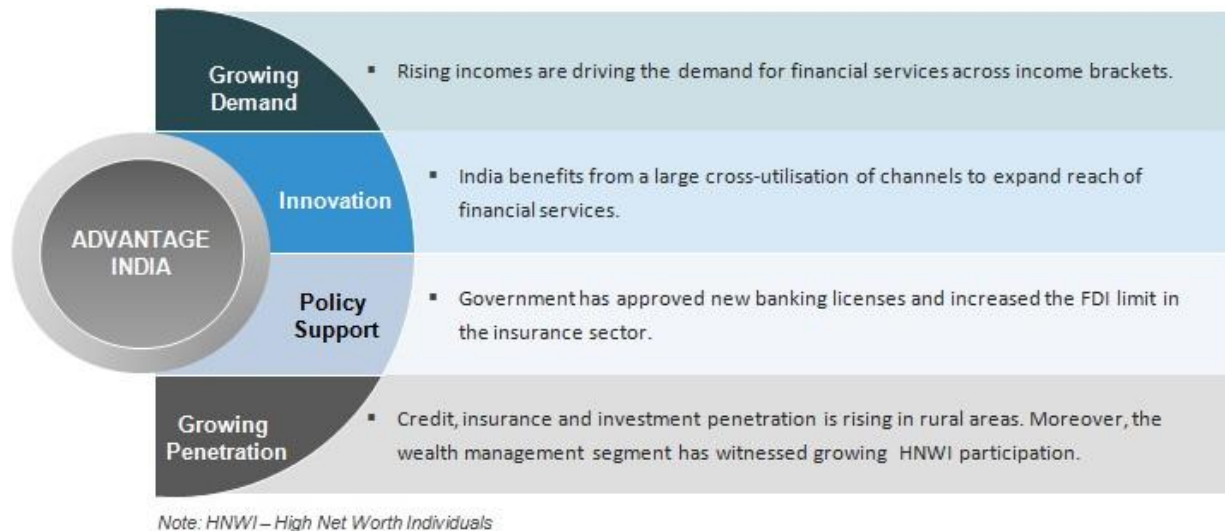
both foreign and Indian private players are providing tailor made products with opening of the market.

- Because of huge competition and entry of new players, the insurance sector has also witnessed innovations like innovative insurance based products, services and value.
- Many foreign companies like New York Life, Aviva, and Standard Life have also entered this sector.
- Now days, the insurance companies are engaged in aggressive marketing, selling and distribution techniques because of the extreme competition that they face from each other...

- The credit for the development of this sector also goes to the active part of the regulatory body – Insurance Regulatory and Development Authority.

Growth of the Venture Capital Market in India

- Inspire of the hindrances by the external setup, the venture capital sector in India is a very active financial sector.
- In India, currently, there are around 2 international and 34 national venture capital funds registered by SEBI.



The country's financial services sector consists of the capital markets, insurance sector and non-banking financial companies (NBFCs). India's gross national savings (GDS) as a percentage of Gross Domestic Product (GDP) stood at 30 per cent in 2017. The total amount of Initial Public Offerings increased to Rs 84,357 crore (US\$ 13,089 million) by the end of FY18. The total number of IPO's reached 161 and amounted to US\$ 5.52 billion between January-November 2018. @ In FY17, individual wealth in India expanded to Rs 344 lakh crore (US\$ 5,337.47 billion) from Rs 310 lakh crore (US\$ 4,620.66 billion) in FY16.

Financial industries in India are considered to be the lifeline of the economy. They play a catalytic role in activating and sustaining economic growth. As per report, India's banking sector is expanding rapidly and has the potential to become **the fifth largest banking industry in the world by 2020** and third largest by 2025.

India has a diversified financial sector undergoing rapid expansion, both in terms of strong growth of existing financial services firms and new entities entering the market. Many emerging trends in financial services sector like digital payment, security, robo-trading, artificial intelligence, is helping financial institutions in providing innovating solutions.

There are 6 core functions which are witnessing emerging trends in financial services sector are:

- Payments
- Market Provisioning

- Investment Management
- Insurance
- Deposits and lending
- Capital Raising

3. Emerging trends in financial services sector and its implications

Payments

Within payment there are two cluster of innovation that is Cashless world and New Emerging payment rails. Key emerging trends include **mobile payments, streamlined payments, integrated billing, next generation security, mobile money, cryptographic protocols and p2p transfers**. New consumer functionalities are being built on existing payment systems and will result in meaningful changes in customer behavior. Also the greatest potential for crypto currencies may be to radically streamline the transfer of value, rather than as store of value.

Implications for Financial Institutions

- Financial institutions may lose control over their customers' transaction experience as payments become more integrated
- With reduced visibility, becoming the default card among specific customer segments will become critical
- Winning issuers will be able to gain visibility into more of customers' spending patterns, build more holistic

understanding of customers, and create more competitive offerings

- As more efficient alternative rails are adopted, the role of traditional intermediaries as a trusted party may diminish
- Financial institutions may face a new set of risks (e.g., reputation, security) and regulatory issues as they participate in new rails
- Applications of these technologies can expand beyond money transfer to modernize other financial infrastructures

Market Provisioning

Within market provisioning, the two cluster of innovation are Smarter, Faster Machines and New market platforms. The major emerging trends include **machine accessible data, artificial intelligence / machine learning, big data, fixed income platform, funds / fund of funds, private equity / venture capital shares, private company shares and commodities & derivative contracts**. As the popularity of high frequency trading declines, the focus of algorithmic trading may shift to smarter, faster response to real-life events. And new information platforms are improving connectivity among market constituents, making the markets more liquid, accessible, and efficient.

Implications for Financial Institutions

- The impacts of event-driven algorithmic trading on liquidity, spread and systemic stability are unclear
- With end-to-end trading activities automated, even small errors in data integrity, trade strategy, and execution will lead to large impacts
- Regulators have the potential to significantly alter the course of developments in this area
- As traditional differentiators among intermediaries (e.g., ability to discover counterparty) become commoditized, the importance of advisory services will increase
- Information platforms will evolve the standards for best-execution from a best-efforts basis to more quantifiable and comparable metrics

Capital Raising

The cluster of innovation among capital raising is **Crowd Funding**. The major trends among crowd funding includes **empowered angel investors and alternative adjudication**. Crowd funding platforms are widening access to capital raising activities, making the overall ecosystem richer.

Implications for Financial Institutions

- Access to more diverse funding options allow new companies to grow at a quicker pace and shorten the average time between early funding stages
- Distribution platforms create a venue for investors to tailor their investment portfolio across dimensions beyond financial return
- As the barriers to enter the asset class fall, it becomes ever more important for traditional

intermediaries' profitability to find undiscovered "start" investments

Investment Management

Within investment management, the two major cluster of innovation are Empowered Investors and Process Externalization. The major trends include **social trading, automated advice & wealth management, retail algorithmic trading, process-as-a service, advanced analytics, natural language and capability sharing**. Robo-advisors are improving accessibility to sophisticated financial management and creating margin pressure, forcing traditional advisors to evolve. Also, the scope of externalizable processes is expanding, giving financial institutions access to the new levels of efficiency and sophistication.

Implications for Financial Institutions

- New entrants will place pressure on margins and intensify competition among traditional players in more specialized segments
- As more advisory functions become automated, distributing wealth products via proprietary advisory channels will become less effective
- As new entrants widen the access for mass customers, they will compete for customers' traditional savings deposits
- The ability to access sophisticated capabilities without large infrastructure investments flattens the playing field for mid-sized institutions
- Organizational agility will become critical to sustain competitiveness as high-value capabilities are continued to be commoditized
- Externalization of capabilities may result in workforce skill loss by preventing the development of a holistic view of operations

Insurance

Within insurance, there are two clusters of innovation which are Insurance Disaggregation and Connected Insurance. The major trends in industry includes **disaggregated distribution, sharing economy, 3rd party capital, smarter & cheaper sensors, internet-of-things, wearables, standardized platforms and self-driving cars**. Emergence of online insurance marketplaces and homogenisation of risks will force big changes in insurers' strategies. And, Ubiquity of connected devices will enable insurers to highly personalise insurance and proactively manage clients' risks.

Implications for Financial Institutions

- In an increasingly commoditised environment, the risks of customers being more fickle will increase and creating loyalty through innovation will become more important
- Insurers' ability to benchmark against competitors will become more important as customers gain ability to comparison-shop
- With increased margin pressure, insurers will need to increase their size by expanding either scope or scale

- As customer relationships evolve from short-term product-based to long-term advisory, capturing customers early on becomes critical
- As insurers become a hub for customer data, their strategic value within full-service financial institutions will grow
- Forming partnerships with data providers, device manufacturers and other ecosystem participants will be critical to enable connected insurance

models, and the long-term structure of the financial services industry.

4. Government initiatives for financial services industry in India

- Several measures have been outlined in the Union Budget 2016-17 that aim at reviving and accelerating investment which, inter alia, include fiscal consolidation with emphasis on expenditure reforms and continuation of fiscal reforms with rationalization of tax structure. The Union Budget 2016-17 has allowed foreign investment in the insurance and pension sectors in the automatic route up to 49 per cent subject to the extant guidelines on Indian management and control to be verified by the regulators.
- Service tax on service of life insurance business provided by way of annuity under the National Pension System regulated by Pension Fund Regulatory and Development Authority (PFRDA) being exempted, with effect from April 01, 2016.
- Capital gains tax exemptions have been extended to merger of different plans within a mutual fund scheme, which is expected to benefit investors in case of merger of mutual fund schemes. The Government of India plans to revise and improve few of its flagship schemes such as the Atal Pension Yojana (APY), aimed at providing pension coverage, and Pradhan Mantri Mudra Yojana, which funds small entrepreneurs, in Union Budget 2016-17 in order to increase the number of beneficiaries covered by these schemes and overcome shortcomings in implementation.
- The Government has also announced several schemes to improve the extent of financial inclusion. The Prime Minister of India has launched the Micro Unit Development and Refinance Agency (MUDRA) to fund and promote Microfinance Institutions (MFIs), which would in turn provide loans to small and vulnerable sections of the business community. Financial Services Secretary Mr Hasmukh Adhia has announced that the ministry will launch a campaign for loans under Pradhan Mantri Mudra Yojana (PMMY) in order to double loan disbursement to the small business sector to over Rs 100,000 crore (US\$ 14.67 billion).
- Government of India's 'Jan Dhan' initiative for financial inclusion is gaining momentum. Under Pradhan Mantri Jan Dhan Yojna (PMJDY), 217 million accounts# have been opened and 174.6 million RuPay debit cards have been issued. Government of India aims to extend insurance, pension and credit facilities to those excluded from these benefits under the Pradhan Mantri Jan Dhan Yojana (PMJDY). The Union Cabinet Minister has also approved the Pradhan Mantri Suraksha Bima Yojana which will provide affordable personal accident and life cover to a vast population. The Union Cabinet has approved 100 per cent Foreign Direct Investment (FDI) under the automatic route for non-bank entities that operate

Deposits and Lending

The clusters of innovation in this sector are Alternate lending and Shifting Customer Preferences. The key market trends include **P2P lending, lean & automated processes, alternative adjudication, virtual banking 2.0, banking as platform (API) and evolution of mobile banking.** New entrants will make meeting customer demands more important, creating an imperative for banks to reconsider their roles. Also, new lending platforms are transforming credit evaluation and loan origination as well as opening up consumer lending to nontraditional sources of capital.

Implications for Financial Institutions

- Intensified competition will narrow spread between deposits and loans, decreasing financial institutions' profitability
- As savers turn to alternative platforms, traditional deposits and investment products will be eroded
- Distribution of customers' credit portfolio over a large number of alternative platforms may make it difficult to measure customer's creditworthiness
- Financial products will increasingly be offered on a stand-alone basis limiting incumbents' ability to competitively cross-subsidize
- Financial institutions' ability to collaborate with non-traditional players and other institutions will become essential
- Financial institutions will need to choose where they will specialize and where they will leverage external partners (e.g., product manufacturing vs. creation of customer experience)

Innovation in financial services is deliberate and predictable; incumbent players are most likely to be attacked where the greatest sources of customer friction meet the largest profit pools. Innovations are having the greatest impact where they employ business models that are platform based, data intensive, and capital light. The most imminent effects of disruption will be felt in the banking sector; however, the greatest impact of disruption is likely to be felt in the insurance sector. Incumbent institutions will employ parallel strategies; aggressively competing with new entrants while also leveraging legacy assets to provide those same new entrants with infrastructure and access to services. Collaboration between regulators, incumbents and new entrants will be required to understand how new innovations alter the risk profile of the industry – positively and negatively. Disruption will not be a one-time event, rather a continuous pressure to innovate that will shape customer behaviours, business

White Label Automated Teller Machine (WLA), subject to certain conditions.

- Minister of Finance Mr ArunJaitley has formally declared the merger of Forward Markets Commission (FMC) with Securities and Exchange Board of India (SEBI), which help convergence of regulations in the commodities and equity derivatives markets. The Insurance Regulatory and Development Authority of India (IRDA), as part of its endeavour to increase insurance sector growth, has allowed a new distribution avenue called the 'point of sale' person, who will be allowed to sell simple standardised insurance products in the non-life and health insurance segments, which are largely pre-underwritten. The Department of Industrial Policy and Promotion (DIPP) has allowed 100 per cent Foreign Direct Investment (FDI) in asset reconstruction companies (ARC) under automatic route, which will

help to tackle the issue of declining asset quality of banks.

5. Conclusion

In order to achieve the goal of faster and inclusive growth, it is high time the government and banking industry undertake a comprehensive relook into the existing policies and structures. In our country, need for qualitative banking surpasses the conservative economic or financial logic as the **financial inclusion** is still a distant dream. In addition to the provision of traditional services, many social functions are attached to the banking system financial inclusion and inclusive growth. Banks are at the core of any economic system whether developed or developing. Essentially, a technologically advanced, transparent and efficient banking system is the need of the hour for the growing economy like India.

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