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Report on Trend and Progress of Banking in India – 2011-12

The Reserve Bank of India today released the statutory [Report on Trend and Progress of Banking in India 2011-12](#). This Report presents the performance and salient policy measures relating to the banking sector during 2011-12. The Report also provides an analysis of the co-operative banks and non-banking financial institutions.

The key messages of the Report are set out below:

Perspectives on the Indian Banking Sector

- The financial system of the country remains robust. Risks to stability are, however, elevated due to global and domestic macroeconomic factors (para 1.27, page 8).
- The strategic and operational responses during the year pertained to policy initiatives with regard to enhancing co-ordination among regulators and positioning of banks to meet the needs of inclusive growth, besides a review of the regulatory framework for the microfinance sector (para 1.13-1.19, pages 3-6).
- At the present juncture, the key issues related to the Indian banking sector include:
 - prospective migration to Basel III which will increase the capital requirements on Indian banks;
 - need to achieve meaningful financial inclusion through the evolution of sustainable business and delivery models;
 - slippage in asset quality needs to be contained; and
 - need to tap untapped business opportunities for resources to power the growth engine. The challenge for Indian banks is to reduce costs and pass on the benefits to both depositors and lenders (para 1.21-1.23, pages 6-7; para 1.26, page 7; para 1.29-1.30, pages 8-9; para 1.34, page 9).
- Notwithstanding the multitude of challenges, the regulatory responses and the inherent strengths underlying the Indian economy should ensure that the banking system continues to play a positive role in supporting the financing needs of our growing economy (para 1.35, page 9).

Global Banking Developments

- The global banking system faced a number of challenges during 2011-12, such as weakening global growth, escalation of the sovereign debt crisis and related funding and deleveraging risks, especially for European banks (para 2.1, page 10).
- Global credit growth exhibited a divergent trend across economies. The Return on Assets (RoA) improved for banks in the US and some EMEs, but declined in European countries (para 2.2, page 10; para 2.8-2.9, pages 12-13).
- Significant progress has been made on the regulatory front with several initiatives, such as formulation of Basel III framework, framework for Global-Systemically Important Financial Institutions (G-SIFIs) and Domestic-Systemically Important Financial Institutions (D-SIFIs) but implementation challenges remained (para 2.32-2.40; pages 24-25).

Policy Environment

- The major initiatives in the area of regulation and supervision of banks during the year include the migration to Basel II advanced approaches, setting out the roadmap for phased implementation of Basel III norms, efforts to move towards dynamic provisioning framework/ counter-cyclical capital buffers, adoption of securitisation norms in line with international best practices, sound compensation practices and adoption of a risk-based supervisory approach for banks (para 3.34, 3.36, pages 35-38; 3.58, page 41).
- Several policy measures were undertaken to improve the credit delivery system, such as revision of priority sector norms to refocus direct agricultural lending by banks, modification of the Kisan Credit Card (KCC) Scheme to suit the current requirements of farmers and a special and concessional refinancing facility to improve the flow of credit to agriculture (para 3.13-3.16, page 30; para 3.22, page 32; para 3.18-3.20; page 31).
- The Reserve Bank continued to spearhead the agenda of financial inclusion through policy initiatives combined with its outreach visits (para 3.28-3.32, pages 34-35).

Operations and Performance of Commercial Banks

- Performance of banks during 2011-12 was conditioned by overall slowdown in the domestic economy. The consolidated balance sheet of scheduled commercial banks (SCBs) recorded slower growth during 2011-12, as compared with the previous year (para 4.3, page 54).
- The growth in net profit of SCBs slowed down, mainly due to steep increase in interest expenditure. Consequent to the slowdown in net profit, Return on Assets (RoA) and Return on Equity (RoE) dipped marginally. Also, Net Interest Margin (NIM) declined marginally during 2011-12 as compared with the previous year (para 4.17-4.21, pages 60-61).
- The Capital to Risk-weighted Asset Ratio (CRAR) remained well above the stipulated minimum for the system as a whole as well as for all bank groups during 2011-12, indicating that Indian banks remained well-capitalised. As at end-March 2012, Tier I capital accounted for more than 70 per cent of the total capital of Indian banks (para 4.25-4.26, pages 64-65).

- During 2011-12, the deteriorating asset quality of the banking sector emerged as a major concern, with gross Non-Performing Assets (NPAs) of banks registering a sharp increase (para 4.29-4.30, page 66).
- On a year-on-year basis, the progress made by banks under Financial Inclusion Plans (FIPs) was found to be satisfactory. The process of providing banking outlets in all villages with population more than 2,000 is almost complete (para 4.78-4.84, pages 85-87).

Developments in Co-operative Banking

- Urban Co-operative Banks (UCBs) posted double-digit growth in assets and showed an improvement in profitability and asset quality in 2011-12 (para 5.13, page 97; para 5.17-5.18, pages 99-100).
- As a fall-out of consolidation, the sector witnessed a rise in the number of financially stronger UCBs and the exit of weaker UCBs. About 61 per cent of these institutions, accounting for 78 per cent of the total banking business of the UCB sector, had ratings of 'A' and 'B' as per the new CAMELS rating model (para 5.5, page 94; para 5.8, page 95).
- As regards rural co-operatives, State Co-operative Banks and District Central Co-operative Banks showed some signs of improvement in profitability and asset quality in 2010-11, partly attributable to the prudential regulatory reforms and revival package being implemented for these institutions. However, this revival was yet to spread to the Primary Agricultural Credit Societies (PACS). PACS remained the weakest spot in this structure, reporting high levels of overdues and losses (para 5.33, page 106; para 5.34, page 107; para 5.38, page 108; para 5.44, page 111).
- Unlike the revival witnessed in short-term rural co-operative structure, the long-term rural co-operative structure continued to post losses and also exhibited weak asset quality in 2010-11, as in the past (para 5.48, page 112; para 5.52, page 112).
- Going forward, it is necessary to persevere with recapitalisation and regulatory reforms for the entire rural co-operative sector so that the sector can lend support to financial inclusion and agriculture (para 5.72, page 119).

Non-Banking Financial Institutions

- The financial performance of Financial Institutions (FIs) in terms of both operating and net profits improved substantially during 2011-12 (para 6.10, page 123).
- The financial performance of Non-Banking Financial Companies - Deposit taking (NBFCs-D) witnessed improvement as reflected in the increase in their operating and net profits during 2011-12 mainly emanating from fund-based income (para 6.31, page 131).
- The financial performance of Non-Banking Financial Companies – Non-Deposit taking Systemically Important (NBFCs-ND-SI) showed marginal deterioration in their net profits during 2011-12. Besides, the increase in impaired assets was a cause of concern (para 6.42, page 137).