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COMPARATIVE STUDY OF INDIAN AND CHINESE BANKING SECTOR AND ITS ROLE IN THEIR ECONOMIC GROWTH AND DEVELOPMENT

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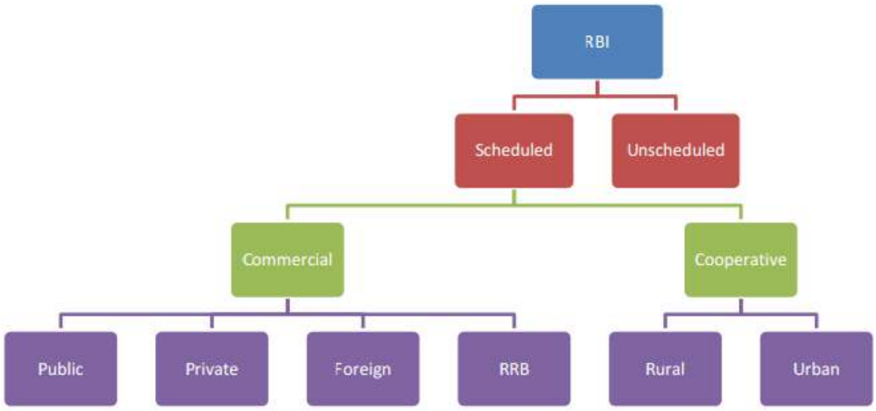
Abstract : This paper compares the operative performances of the banking institutions in China and India, taking into account the contentious issue of institutional differences in banking sectors in these two economies. The historical frequency of banking crises is similar in advanced and developing countries, with quantitative parallels in both the run-ups and the aftermath. We establish these regularities using a dataset spanning from the early 1800s to the present. Banking crises weaken fiscal positions, with government revenues invariably contracting. Three years after a crisis central government debt increases by about 86%. The fiscal burden of banking crisis extends beyond the cost of the bailouts. The study also examines the issue of the use of banks to provide countervailable subsidies to exporting organizations. Our results show that the efficiency differences between banks in these two countries can be directly related to their institutional differences.

KEYWORDS: Banking; Financial crises; Recessions; Real estate; Debt; Historical and Subsidies

INTRODUCTION

India's largest bank, SBI, got a credit rating downgrade this week from Moody's. This comes on top of worries about the quality of bank assets in India in a slowdown. China's banks are not having a great time either. Here's a head-to-head comparison of the banking sectors of the world's fastest growing major economies. India's banks are smaller, more conservative and potentially in much less trouble than China's. The financial sector played an important role in the economic growth. In financial Sector, Banking system may directly affect growth by improving the access to financial services and indirectly by improving the efficiency of financial intermediaries, both of which reduce the cost of financing, and in turn, stimulate capital accumulation and economic growth. Due to their influence within a financial system and an economy, banks are generally highly regulated in most countries. India has the Seventh largest geographic area of 32, 263 sq kms, whereas China has Third Largest area of 9,596,961 sq. km.

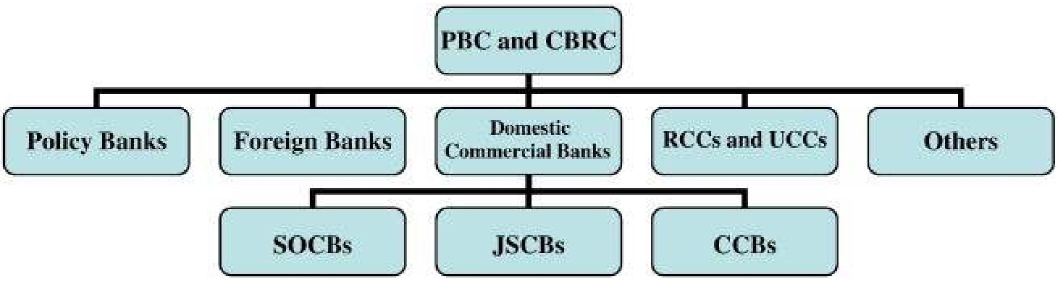
The two countries have similar labor endowments and development lags due to government controls and protected nature of their economies. The Chinese culture is more homogeneous and Indian culture is great diversified. India lags behind china in infrastructure. Primary, secondary education, vocational education training in china results in 99.1% literacy rate, where as in India it is 50 to 60 %.



The Reserve Bank of India, the nation's central bank, began operations on April 01, 1935. It was established with the objective of ensuring monetary stability and operating the currency and credit system of the country to its advantage. The scheduled bank are scheduled by Reserve Bank of India and they are fully authorized to do banking business in India. Reserve Bank of India directly control over it.

Non-scheduled are not scheduled by Reserve Bank of India they do work under Banking Regulation Act of India.

2 CHINA BANKING SYSTEM:

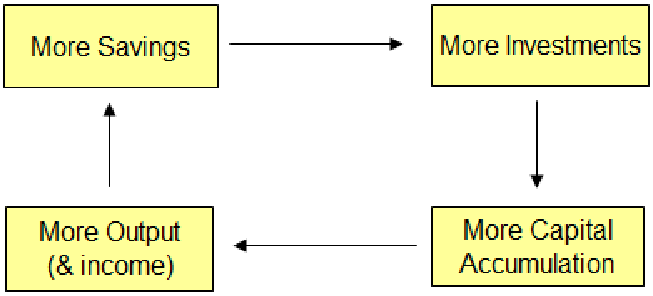


The People's Bank of China (PBOC) is China's central bank, which formulates and implements monetary policy. The PBOC maintains the banking sector's payment, clearing and settlement systems, and manages official foreign exchange and gold reserves. The banking sector in China primarily comprises of state-owned commercial banks and policy banks, the banking segment is mostly controlled by 4 state-owned banks namely the Industrial & Commercial Bank of China (ICBC) specialized in lending to industrial sector, China Construction Bank (CCB) traditionally focused on infrastructure development, Bank of China (BOC) conventionally responsible for foreign exchange and financing of imports & exports and Agricultural Bank of China (ABC) primarily focused on lending to agriculture and rural development contributing about 60-70% of the domestic banking business.

3 OBJECTIVES:

1To Study the impact of banking sector on Economy.
2Comparison of India and China on the basis of banking system and its role in economic growth and development.

4 RELATION BETWEEN SAVINGS AND ECONOMIC GROWTH:



5 THE GROWTH DRIVERS OF INDIAN BANKING SECTOR:

- High growth of Indian Economy: The growth of the banking industry is closely linked with the growth of the overall economy
- Rising per capita income: The rising per capita income will drive the growth of retail credit.
- New channel – Mobile banking is expected to become the second largest channel for banking after ATMs: New channels used to offer banking services will drive the growth of banking industry exponentially in the future by increasing productivity and acquiring new customers.

6 MAJOR CONCERN OF INDIAN BANKING SECTOR:

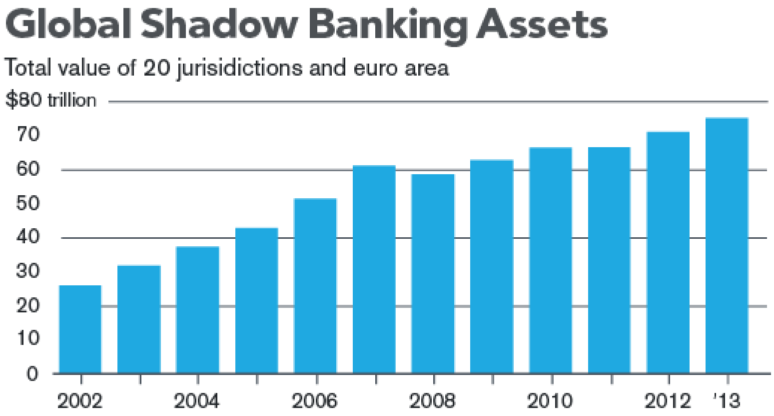
1)Intensifying competition: Due to homogenous kind of services offered by banks, large number of players in the banking industry and other players such as NBFCs, competition is already high.
2)Managing Human Resources and Development: Banks have to incur a substantial employee training cost as the attrition rate is very high. Hence, banks find it difficult manage the human resources and development initiatives.
3)Increasing non-performing and restructured assets: Due to a slowdown in economic activity in past couple of years and aggressive lending by banks many loans have turned non-performing. Restructuring of assets means loans whose duration has been increased or the interest rate has been decreased. This happens due to inability of the loan taking company/individual to pay off the debt.

7 SHADOW BANKING:

The scale of it is almost unfathomable: $75 trillion worldwide. The Financial Stability Board says it poses “systemic risks” to the global financial system. It’s growing at phenomenal rates in China and India and booming in Western banking capitals as well. The catchall phrase “shadow banking” encompasses risky investment products, private lending between individuals, pawnshop and loan-shark operations in emerging markets, as well as more respectable activities like derivatives, money-market funds, securities lending and repurchase agreements at financial institutions in Europe and the U.S. The common denominator is that these activities flourish outside the regular banking system and often beyond the control of regulators and monetary policy. Together they show how hard it is to restrict risky lending without causing harm.

THE SITUATION:

Some risk-taking by banks has been reined in since the 2008 financial crisis. The global rise of shadow banking has not. The FSB said the sector grew to $75 trillion in 2013, an increase of $5 trillion from the previous year. The board earlier found increases in almost three-quarters of the economies it surveyed. The situation is most pressing in Argentina, where the FSB reported a 50 percent increase in 2013, and in China, with a 30 percent increase. In June 2013, a Chinese government effort to curb wealth-management products resulted in the worst cash crunch in at least a decade. The value of these investments, which offer high short-term interest rates and are not guaranteed, had surged to 9.1 trillion yuan (about $1.5 trillion) — almost the size of the Australian economy. Their growth caused the man who is now China’s top securities regulator to label the off-balance-sheet products a “Ponzi scheme,” because banks have to sell more each month to pay off those that are maturing. But China’s savers responded to the crackdown by scooping the products up in record numbers. Another threat to stability is China’s loosely regulated $2 trillion trust industry, made up of 68 companies that sell high-yield investments to wealthy customers, frequently through banks, that are often based on risky loans to such industries as energy and property. In April, 2014, after one trust almost defaulted and at least 20 others were reported to have run into difficulty making repayments, the banking regulator ordered trusts to be prepared to make good on the investments in the event of losses, and announced a “strict” approval process for new products. About $853 billion worth of trust products matured in 2014, 50 percent more than the year before.



THE BACKGROUND:

With so much money sloshing around outside the official system, shadow banking makes it harder for countries like China and India to control their economies by changing interest rates or jiggering the money supply. In India, the inflation rate stayed higher than 8 percent in 2012 and 2013 despite 13 interest rate hikes by the central bank. Government officials simply don’t have enough control over the economy to make an impact. In China, savings deposit rates of 3 percent, lower than the target for inflation, combined with the inability of at least 90 percent of small businesses to get bank loans (forcing them to turn to other sources of lending) have propelled the shadow-banking sector to an estimated $6 trillion, or 69 percent of the economy. Shadow banking raises the risk of public unrest because the government can’t provide a bailout, as it could if a bank collapses when a loan isn’t repaid. There’s no place to put the money. American and European regulators have warned of risks arising from banking activities by lightly regulated financial companies that lack access to deposit insurance and other protections.

THE ARGUMENT:

Why don’t governments crack down? Seize control? Get a grip on all this money outside their purview? In Europe and the U.S., regulators’ concerns have been offset by fierce lobbying by the financial industry. In the developing world, the shadow-banking sector provides grease to keep economies functioning smoothly. Small businesses get the loans they need; savers get investments yielding more than inflation. And in economies with underdeveloped financial systems, like China’s and India’s, shadow banking fills a vacuum. Reining it in can be the right long-term policy, but can slow growth and raise risks in the short term. Government officials know that shadow banking presents a danger — and that they attack it at their peril.

8 CONCLUDE:

China and India both have accomplished a great deal in reforming and improving their banking industries in recent years. Because state ownership will continue to dominate the banking sector in each country, the major challenge for the governments in China and India will be to ensure that banks can operate as genuinely commercial businesses by striking a proper balance between their roles as owners and as supervisors of banks. Following foreign equity participation and the public listing of China’s state-owned banks, corporate governance of these banks is changing dramatically. Public sector banks in India should presumably move more quickly in improving their governance, because they have been listed for quite some time already, although domestically. Despite supportive government policies toward the banking sector and an extensive branch network, both China’s reforming state-owned banks and India’s public sector banks still need to demonstrate that they are the right mechanisms to deliver and maximize shareholders' value, which in turn fosters the development of the national economies going forward.

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