Performance of the Indian Banking Sector in the Basel Regime

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List of Abbreviations

AGTA: Advances to government undertakings to total advances

AMA: Advanced Measurement Approach

ANBC: Adjusted Net Bank Credit

ASTTA: Advances secured by tangible assets to total advances

BCBS: Basel Committee on Banking Supervision

BIA: Basic Indicator Approach

BPE: Business per Employee

CAR: Capital Adequacy Ratio

CCB: Capital Conversion Buffer

CDO: Credit Debt Obligation

CDS: Credit Default Swap

CRAR: Capital to Risk weighted Asset Ratio

CRR: Cash Reserve Ratio

DEA: Data Envelopment Analysis

DMU: Decision Making Units

FE: Fixed Effects

GSTI: Government securities to total investments

NFSR: Net Stable Funding Ratio

NPA: Non Performing Assets

NPANA: Non Performing Assets to Net Advances

OBALEX: Off balance Sheet Exposure

OPRTA: Operating Profit to Total Assets

OTE: Overall Technical Efficiency

PLR: Prime Lending Rate

PSATA: Priority sector advances to total advances

PSB: Public Sector Banks

PTE: Pure Technical Efficiency

RBI: Reserve Bank of India

RE: Random Effects

ROA: Return on Assets

ROE: return on Equity

RWA: Risk Weighted Assets

SA: Standardised Approach

SBI: State Bank of India

SE: Scale Efficiency

SFA: Stochastic Frontier Approach

SLR: Statutory Liquidity ratio

TA: Total Assets

TE: Technical Efficiency

TTE: Transformed Technical Efficiency

UATA: Unsecured advances to total advances

VAR: Value at Risk

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ABSTRACT

With the liberalization of the Indian economy in 1991 and the banking sector reforms of 1998, the Indian banking sector witnessed an implementation of credible paradigm shift. Ever since the Indian banking sector has been engineered towards compliance to the Basel Accords with the authoritative assertiveness of the RBI. These regulation aimed at easing directed credit restrictions under the priority sector lending arrangements, reduction of statutory pre-emptions, deregulation of the interest rates and fostering prudential norms.

In this era of holistic convergence to the Basel norms, the weakening of the entry barriers due to the financial liberalization brought in the inception of competition in the sector along with technological advancements and challenged the adaptive potential of the existing banks. Compliance to these norms and in the run for its existence in the competitive environment, the banks objectively incubated diverging portfolio of products and services leading to a change in the capital allocation and business operations of the banks.

Adherence to the capital adequacy standards measured in terms of the Capital Adequacy Ratio (CAR) prescribed by the Basel accords to balance the profitability and stability of the banks brought about significant shift in the portfolio composition of the banks. In our study we examine the changes in the asset and investment composition of the banks in the pre-Basel era, Basel I era and Basel II era in the Indian banking sector. Further, we also analyse the impact of CAR on the performance of the Indian Banking sector measured in terms of profitability, efficiency, productivity and asset quality.

The global financial crisis of 2007-2008 has paved the way for the Basel III norms with more emphasis on the quality of capital in the bank's balance sheet and by introducing buffers to withstand situations arising out of financial distress. Adherence to the Basel III capital adequacy norms has again posed new challenges for the banks to make necessary adjustments in their capital base. With the RBI's announcement of adherence to the Basel III capital adequacy norms in the year 2010 by 2013, we analyse the preparedness of the banks to adopt the Basel III norms by studying the different elements of the capital of the banks.

Keywords: *Basel Accords, Basel III, Capital Adequacy Ratio, Bank Performance*