

Growth of Financial Service Sector in India

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I. 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.

II. Market Size

Total outstanding credit by scheduled commercial banks of India stood at Rs 72,606.11 billion (US\$ 1.08 trillion)!. The Association of Mutual Funds in India (AMFI) data show that assets of the mutual fund industry have reached a size of Rs14.21 trillion (US\$ 210 billion)@.

During April 2015 to March 2016 period, the life insurance industry recorded a new premium income of Rs 1.38 trillion (US\$ 20.54 billion), indicating a growth rate of 22.5 per cent over the previous year. The general insurance industry recorded a 12 per cent growth year-on-year in Gross Direct Premium underwritten in April 2016 at Rs105.25 billion (US\$ 1.55 billion).

India's life insurance sector is the biggest in the world with about 360 million policies, which are expected to increase at a Compounded Annual Growth Rate (CAGR) of 12-15 per cent over the next five years. The insurance industry is planning to hike penetration levels to five per cent by 2020, and could top the US\$ 1 trillion mark in the next seven years. The total market size of India's insurance sector is projected to touch US\$ 350-400 billion by 2020.

India is the fifteenth largest insurance market in the world in terms of premium volume, and has the potential to grow exponentially in the coming years. Life insurance penetration in India is just 3.9 per cent of GDP, more than doubled from 2000. A fast growing economy, rising income levels and improving life expectancy rates are some of the many favourable factors that are likely to boost growth in the sector in the coming years.

Investment corpus in India's pension sector is expected to cross US\$ 1 trillion by 2025, following the passage of the Pension Fund Regulatory and Development Authority (PFRDA) Act 2013.

Investments/Developments

- International Finance Corporation (IFC), the investment arm of The World Bank, plans to invest around Rs 135 crore (US\$ 20.3 million) via non-convertible debentures (NCD) in GrameenKoota, a Bangalore-based microfinance company
- Synchrony Financial, a US-based consumer financial services company, plans to expand its operations in India by investing US\$ 12 million to set up centres of excellence, which can develop finance, analytics and information technology solutions.
- Thomas Cook India, an integrated travel and travel related financial services company, has entered into a partnership with Western Union Business Solutions, with a view to assist Small and Medium-sized Enterprises (SMEs) in India with their trade payments across borders.

- Kotak Mahindra Bank Limited has bought 19.9 per cent stake in Airtel M Commerce Services Limited (AMSL) for Rs 98.38 crore (US\$ 14.43 million) to set up a payments bank. AMSL provides semi-closed prepaid instrument and offers services under the 'Airtel Money' brand name.
- Tata Capital, the financial services arm of Tata Group, plans to raise Rs 2,000 crore (US\$ 293.4 million) for its real estate fund, from State General Reserve Fund (SGRF), the sovereign wealth fund of Oman.
- Ujjivan Financial Services Ltd, a microfinance services company, has raised Rs 312.4 crore (US\$ 45.84 million) in a private placement from 33 domestic investors including mutual funds, insurance firms, family offices and High Net Worth Individuals (HNIs), ahead of its planned Initial Public Offering (IPO).
- Insurance firm AIA Group Ltd has decided to increase its stake in Tata AIA Life Insurance Co Ltd, a joint venture owned by Tata Sons Ltd and AIA Group from 26 per cent to 49 per cent.
- Canada-based Sun Life Financial Inc plans to increase its stake from 26 per cent to 49 per cent in Birla Sun Life Insurance Co Ltd, a joint venture with Aditya Birla Nuvo Ltd, through buying of shares worth Rs 1,664 crore (US\$ 244.14 million).
- Nippon Life Insurance, Japan's second largest life insurance company, has signed definitive agreements to invest Rs 2,265 crore (US\$ 332.32 million) in order to increase its stake in Reliance Life Insurance from 26 per cent to 49 per cent.
- The Reserve Bank of India (RBI) has granted in-principle licenses to 10 applicants to open small finance banks, which will help expanding access to financial services in rural and semi-urban areas, thereby giving fillip to Prime Minister's financial inclusion initiative.
- The Reserve Bank of India (RBI) has also given in-principle approval to 11 entities to open payment banks which are expected to result in widening the reach of banking services and thereby improve the extent of financial inclusion as envisaged by the government. The setting up of 11 new payments banks can potentially free up Rs 1,40,000 crore (US\$ 205.4 billion) per annum to fund the infrastructure sector, as per a study by the State Bank of India.
- India's largest microfinance company Bandhan has set up Bandhan Bank Ltd, banking and financial services company, post the receipt of license from RBI.

Government Initiatives

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 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.

Road ahead

India is today one of the most vibrant global economies, on the back of robust banking and insurance sectors. The country is projected to become the fifth largest banking sector globally by 2020##. The report also expects bank credit to grow at a Compound Annual Growth Rate (CAGR) of 17 per cent in the medium term leading to better credit penetration. Life Insurance Council, the industry body of life insurers in the country also projects a CAGR of 12–15 per cent over the next few years for the financial services segment.

Also, the relaxation of foreign investment rules has received a positive response from the insurance sector, with many companies announcing plans to increase their stakes in joint ventures with Indian companies. Over the coming quarters there could be a series of joint venture deals between global insurance giants and local players. The relaxation in the foreign direct investment (FDI) limit to 49 per cent can result in additional investments up to Rs 60,000 crore (US\$8.81 billion).

III. Conclusion

The Indian financial services sector is one of the most complex, yet one of the most robust service segments of the Indian economy. Spanning from insurance to capital markets, banking to foreign direct investments (FDI) and from mutual funds to private equity (PE) investments, the financial services sector covers all related segments under its umbrella. Having major effects in its abstract as well as physical form post liberalisation, the financial services segment is undoubtedly the mainstay of Indian economy.

References:

- [1]. Media Reports, Press Releases, IRDAI, General Insurance Council, Reserve Bank of India
- [2]. Exchange Rate Used: INR 1 = US\$ 0.0149 as on May 16, 2016