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ANALYSIS OF NON-INTEREST INCOME AN OPPORTUNITY & SUCCESS OF BANKS IN INDIA

MEENA KUMARI
RESEARCH SCHOLAR
DEPARTMENT OF A.B.S.T.
UNIVERSITY OF RAJASTHAN
JAIPUR

ABSTRACT

Non-interest income is the income of a bank arising from non-traditional of Indian banking industry is slowly and shifting its revenue base from traditional to nontraditional activities that generate income, fee service charges and other types of non interest income. The shift toward non-interest income has been perceived to reduce the volatility of bank's revenues and reduce the risks, as noninterest income is less dependent on overall business conditions than traditional income. Over the years in general and post financial crisis 2008 in particular, non interest income has come under a lot of scrutiny all over the world. The present study is aimed to understand the contribution of non-interest income over the years and the risks associated with its additional, we study the result of stress test on the banks when this non-interest income dries up using the sample of banks in India during 2008-09 years to 2015-16.

KEYWORDS
Indian bank's interest risk, non-interest income.

1.1 INTRODUCTION OF NON-INTEREST INCOME

Non- interest income is define as income of a bank to arising from non-traditional banking as banks are increasingly squeeze in their detection of profitability; one strategy to increase income is to diversify away from traditional sources of revenue like loan making and toward activities that generate fee income, charges, service trading revenue, and other types of noninterest income.

Commission, exchange and brokerage are includes on all remuneration on services such as commission on collections commission/exchange on remittances and transfers, the commission on controlled through four holding companies, letter of letting out lockers and guarantee, commission on government business, commission on other that permitted agency business including consultancy and other services, brokerage on securities etc. but, in does not include foreign exchange income. Profit Net on sale of Investments the net position of gain and losses from sale of securities held on maturity shown under the particular head. Profit net revaluation of investments on the net position of revaluation on investment is shown under this particular head and if any loss occurs after the revaluation of investment it will shown as a deduction. Profit net on sale of land, building and other assets, net position of gain and losses from sale of furniture, land and building, motor vehicle silver, gold, etc. shown under this head.

Net profit on exchange transactions: includes profit or loss dealing in foreign exchange, all income earned by way of foreign exchange commission and charges on foreign exchange transactions, interest the income recorded here will be shown after setting off losses on exchange transactions. Miscellaneous income: all residual income arising out of miscellaneous sources such as: income from bank owned property; recoveries from constituents for go down rents, charges, security insurance etc. The major difference between interest income and non-interest income apart from latter non-traditional arising from activities is that there is higher operating this as the bank is exposed to a higher fixed income and the ups and downs of the business cycle.

Banks are very important to the organizations, which aid in the execution of the economic activities by individuals, business organizations and even the sovereign states. They serve primarily as a medium, which bridges the gap between surplus and deficit spending units in an economy this fundamental function of banks generate interest income which has over the years being their major source of revenue, since loans form a greater portion of the total assets of banks. These assets generate huge interest income for banks, which to a large extent determines their financial performance (mabvure et al., 2012). however, in the recent times to advancements in information and communication technology, increased competition in the middle of banking companies as well as the diversity and the complexity of businesses and their Demands for the financial services have constrained banks to consider other banking activities which offer diverse services to clients and beef up revenue generation through fee income.

The Non-interest incomes are basically incomes earned from sources other than the returns on advances to bank clients. They are usually fee-generating activities which range from underwriting activities to cash management and custodial services as well as derivative arrangements.

1. 2. REVIEW OF LITERATURE

The banking system in India is complex in that it comprises public and private firms with the latter including foreign firms. as in many other emerging economies, India until recently was heavily regulated with the banking sector aligned to meet social and economic development. The institutional structure of the financial system is by sociologists since communication

1. The banks either owned by the government, or private sector (RBI foreign) or regulated by the RBI
2. The financial development institutions and refinancing institutions, set up either by a separate statute or under companies act, either owned by government, RBI, private or other development financial institutions and regulated by the RBI; non-bank financial companies
3. The (NBFCS), owned privately and regulated by the RBI. The legislative framework governing public sector banks (PSBS) was amended in 1994 to enable them to raise capital funds from the market by way of public issue of shares.

Incomes from the nontraditional activities have played a more important role in improving total bank operating income (lepetit et al., 2013) are Barnes becoming increasingly reliant on fiduciary income, fees, service charges, revenue, trading and other types of non-interest Income. they reported that the industry as a whole, earned 42% of its net operating revenue from noninterest sources in 2014, a marked increase from 32% in 1990 and 20% in the recent renegotiation" in the banking business dynamics have made it necessary for banking companies to be proactive and innovative in their operations in the view of nachane and ghosh (2014), an important dimension of this financial innovations is a process which has been an upsurge in off-balance sheet (OBS) activities of banks. Such activities, though not entirely new from a historical edited by Francisco orrego vicuña have expanded considerably in range and scope in recent years.

Whereas the basic functions of banks and other financial service companies have remained relatively constant over time, the specific products and services through which these functions are provided have changed. The Component of total bank earning, non-interest Generating activities may increase the overall risk of banks via volatility. huizinga (2009) found that Income and banks with relatively high non-interest earning assets are less profitable and

Banks that rely largely on deposits for their funding are also less profitable. as late as 2000, many bankers (continued to believe that fee income would be a stable income stream; indeed, and analysts fond of the earnings growth potential, diversity and market insulation that fees provide (engen, 2010). this view is not very conclusive as recent evidence using accounting data (e.g. stiroh, 2016) suggests that an increased reliance on non-interest income raises the volatility of profits without raising profits. average

Deyoung s. and roland (2011) suggested and explained the three reasons why non-interest income may increase the volatility of bank earnings. first, loans that are held in a bank's portfolio especially loans to businesses - are relationship based. second (a bank that shifts its product mix from traditional to nontraditional asset-based interest-generating activities fee-based activities tends to increase its "degree of operating this". productivity obviously for most fee-based activities require banks to hold the little or no fixed assets, so unlike interest-based activities like portfolio lending, fee-based activities like trust services, mutual fund sales and cash management require little or no regulatory capital. them, according to this allows banks to finance a greater amount of their income-generating activities with presented which increases the fixed interest expenses.

1.3 CONTRIBUTION OF THE RESEARCH PAPER
Most of the existing literature on the banking sector relates to the private and public sector banks. There is not much literature available on banking sector, and more specifically in comparison with the private sector banks. The present study adds to the existing literature on banking and finance, private sector banks operating in rural areas with special focus on non-interest income share on risk in the Indian banking sector services offered by both types of banks.

1.4 OBJECTIVES
1. To conduct a detailed study of retail liabilities, products and services of Public Bank and Private Bank.
2. Comparative Analysis of products and services of both banks to find differential features and benefits of products and services of both banks and their advantages and disadvantages.
3. To recommend some strategies to both type of banks to enhance the marketability of their non-interest income, liability of products.

1.5 METHODOLOGY
In this research paper, we examine the impact of banks' non-interest income share on risk in the Indian banking sector for the period between 2008-09 and 2015-16 for sample of the banks. Comprises the sample of six banks two each from public sector, the private sector and foreign banks. The banks that are considered in the paper are state bank of India and bank of Baroda from Public sector, ICICI Bank and HDFC bank from the private sector, HSBC bank and SCB (Standards Charted Bank) bank from foreign banks. In this paper, we observe the trends in non-interest income in these banks and document the long-term trends in the amount and composition of non-interest income in Indian banks. Further, we also look into instability of Non-interest income.
We obtain our initial sample from the RBI database and augment this data with the center for monitoring the Indian economy's (CMIE) prowess database we include only public sector banks in our sample,: eliminating cooperatives and other state commercial enterprise banks. Our final sample comprises of 28 banks spanning the period 2004 2014 and which includes only public sector banks. Classifies the prowess database in two ways. Income the first definition of income divides into income interest income and interest on income. non-interest (loans) advances and investment activities is classified as interest income comprises income, while non-interest income from sources the interest earned on advances, deposits with the RBI, and deposits with other banks. Therefore, non-interest income Comprises profit on trading, gains from foreign exchange activity, income from fiduciary activities, fees and commissions for services related to issuing letters of syndication, underwriting, controlled through four holding companies, derivatives transactions, etc.

1.6 DATA ANALYSIS
Indian banks are growing at a very fast pace since the 6-11 of the early 1990s, and both interest income and non-interest income have risen over our sample period. The following table summarizes the figures of interest and non interest incomes of all scheduled commercial banks during the period of financial years 2008-09 to 2015-16. The figures in the table clearly indicate consistent growth in both interest and non-interest income over this time period, but the growth of non-interest income outpaces that of the growth of interest income.

TABLE 1: SHOWING THE FINANCIAL PERFORMANCE OF PUBLIC SECTOR BANKS IN INDIA (2008-09 TO 2015-16) (Amount : Rs. in Crore)

Items	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16
A. Income (i+ii)	147486.32	189289.69	204764.56	188889.39	245872	315608	354979	414288
	-100	-100	-100	-100	-100	-100	-8.10	-7.84
i) Interest Income	111647.38	157831.69	182273.7	164198.96	213075	273428	305899	366401
	-78.69	-83.87	-84.43	-87.39	-86.7	-86.6	-6.90	-6.93
of which: Interest on Advances	48944.25	76985.89	101402.86	110554.5	154101	204709		
Income on Investments	54107.99	62922.36	63293.87	47239.79	53119	63080	-	-
ii) Other Income	28149.85	30569.11	32599.85	23785.48	32797	42180	48898	478674
	-20.39	-17.26	-15.88	-11.98	-13.3	-13.4	-1.2	-0.8
of which: Commission & Brokerage	7923.23	12639.75	15778.2	12545.58	14799	18475		
B. Expenditure (i+ii+iii)	1321401.96	158233.76	182859.58	167801.23	219280	281215	3156728	369183
	-100	-100	-100	-100	-100	-100	-7.16	-6.97
i) Interest	64879.56	85039.72	101859.83	101898.8	148902	193447	211951	230856
Expended	-55.35	-53.78	-55.65	-61.89	-67.9	-68.8	-4.78	-4.38
of which: Interest on Deposits	63274.64	74668.29	86189.45	88868.29	132718	174313		
ii) Operating Expenses	-	-	-	-	-	-	66076	82966
	-	-	-	-	-	-	-1.59	-
iii) Provisions and Contingencies	23744.79	27471.16	28276.49	22612.76	23715	32578	37615	55165
	-18.88	-17.38	-15.58	-13.49	-10.8	-11.6	-0.86	-1.05
of which: Provision for NPAs	15199.15	57.25	39.66	61.99	80	93		
iii) Operating Expenses	33533.69	45715.94	53105.48	43256.59	46663	55190	-	-
	-27.89	-28.89	-28.99	-25.81	-21.3	-19.6	-	-
of which : Wage Bill	23582.26	28124.5	31457.83	27812.89	28660	34250	-	-
C. Profit								
i) Perating Profit	38389.3	46455.92	49798.65	42655.96	50307	66972	76872 -1.75	100066 -1.90
ii) Net Profit	1756840	18975.81	21493.98	20151.28	26592	34394	39258 -0.89	44911 -0.86

It appears that the more efficient banks pursue such diversification strategies. We also find that efficient banks as measured by profit per employee claim a bigger non-interest income. Similarly, at of banks with poor loan quality as assessed by net non performing advances to total advances, non-interest seeks sources of income. Larger banks are marginally associated with increased non-interest income. we find that business per employee to be negatively related to non-interest income; as employees pursue new business sources, these sources appear to be the more traditional, interest based source that you use this is consistent with the view that non-interest income improves income diversification and makes a bank less dependent on overall economic conditions that affect their loan portfolio (stiroh, 2014).
Composition of non interest income for the individual banks are given in figure 1 to 6 in number.
➢ About here figure 1. – the components of non interest income in state bank of India
In case of state bank of India, the income due to fees, commission and brokerage has been constant over the time. Income due to insurance premium increasing. Is the component due to exchange rate has been constant contributor the transactions
➢ About here figure 2.- The components of non interest income in the Bank of Baroda
In case of Baroda, bank of the income due to fees, commission and brokerage has increased over the time. The component due to exchange rate has increased the transactions

- About Here Figure 3.- The components of non interest income in ICICI Bank In case of ICICI Bank, the income due to fees, commission and brokerage has been volatile. The component due to exchange rate transactions has shown an increasing pattern.
- About Here Figure 4. – components of non interest income in HDFC bank in case of HDFC bank, the income due to fees, commission and brokerage volatile has been the component due to exchange rate transactions has shown an increasing pattern.
- About Here Figure 5. – components of non interest income in HSBC bank

In case of HSBC bank, the income due to fees, commission and brokerage has come down. The component due to exchange rate transactions has shown an increasing pattern.

- About here figure 6. – Components of non interest income in HSBC bank
- About here figure 7. – Component of non interest income in deutsche bank.

In case of deutsche bank, the income due to fees, commission and brokerage has come down. The component due to exchange rate transactions has shown an increasing pattern.

1.7 RISKS ASSOCIATED WITH NON INTEREST INCOME

The risks associated with non interest income can be summarized by the increasing contribution toward revenue.

In case of state bank of India, non interest income contributed to around 17% of revenue. in case of bank of Baroda, it contributed around 13% of revenue. In case of ICICI Bank, it contributed around 20% of revenue. In case of HDFC bank, it contributed around 18% of revenue. In case of HSBC bank, it contributed around 29% of revenue, earlier it contributed around soaring in case of deutsche bank, non interest income contributed to 36% of revenue. As one can observe, foreign banks are more read susceptible to volatility in non-interest income than private banks and public sector banks are highly immune to volatility of non interest income.

The instability of operating revenue due to non interest the income and net interest income is given by the following formula:

$^{\sigma 2}$ ddlnOPREV = $^{\alpha 2}$ $^{\sigma 2}$dlnNON+(1-α)2 $^{\sigma 2}$dlnNET+2*α*(1-α)*Covar(dlnNON,dlnNET)

Where a is defined as (volatility in non-interest income) / (instability of non interest income instability of net interest)

The following table presents the instability in operating revenue for all the banks considering the stable part of non interest income which is calculated by removing instability factor from non interest income

- About here Table 2. – instability in operating revenue for all the banks
- About here Table 3. – instability in non-interest income for all the banks
- About here Table 4. – standard deviation of the non interest income for all the banks

1.7.1 COLLISION ANALYSIS

By using the standard deviation as instability or volatility in the non interest income the stable par of non interest income is calculated as (1-stdev)*non income Interest

The following set of tables give the impact of instability of non interest income on different profitability ratios

- About here Table 5. – return on equity
- About here Table 6. – return on assets

The profitability ratios suggest that, instability of non interest income has not affected public sector banks but the profitability ratios of private banks and foreign banks are affected by a greater extent.

- About here Table 7. – burden ratio
- About here Table 8. – (expenses – non- interest income)/net interest income even after factoring in instability, deutsche bank was able to compensate its operating expenses with its non interest income and the performance of other banks was relatively good with respect to burden ratio.

1.7.2 STRESS TEST, WITH RESPECT TO CAPITAL ADEQUACY

In this paper, we have considered the non funded sources in off balance sheet which contribute to non interest income. The non funded sources contribute to credit risk to the bank. So in the paper, a scenario is created in which the bank has to pay off all the non funded sources at once all.

- About here Table 9. – the effect on capital adequacy ratio conclusion

Non-interest income has high operating this and low switching cost compared to interest income. Non-interest income is significant part of revenue for foreign banks whereas it forms less proportion of revenue to public sector banks commission, brokerage and exchange is significant part of private banks in India compared to public sector banks. This shows that private banks have more risk appetite than the public sector banks. Foreign banks have significant part of their income as profit from an exchange. reduction in non -interest income reduces ROE and ROA for the bank Burden ratio for foreign banks is good indicating that these banks have maintained their operating expenses and non-interest income to the comparable level. Stress test of capital Adequacy on banks has shown that foreign banks are read susceptible to non exposure of fund

Our preliminary results indicate that non-interest income is strongly and positively influenced by the return on a loan quality, profit per employee, and personalized customer service offered to bank customers. We find that foreign banks capture larger amounts of non-interest income. Furthermore, we find that as banks continue to develop traditional interest income sources, they international to diversify into non-traditional less sources of income, and we find that banks where employees generate more traditional business report significantly lower non-interest revenue.

1.8 CONCLUSION

Non-interest income is the income of a bank arising from non-traditional of Indian banking industry is slowly and shifting its revenue base from traditional to nontraditional activities that generate income, fee service charges and other types of non interest income. The shift toward non-interest income has been perceived to reduce the volatility of bank's revenues and reduce the risks, as noninterest income is less dependent on overall business conditions than traditional income. Over the years in general and post financial crisis 2008 in particular, non interest income has come under a lot of scrutiny all over the world. The present study is aimed to understand the contribution of non-interest income over the years and the risks associated with its additional, we study the result of stress test on the banks when this non-interest income dries up using the sample of banks in India during 2008-09 years to 2015-16.

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