<u>Porter's Five Force Analysis</u>

<u>SECTOR-BANKING/FINANCE</u>

The Banking Sector is one of the most important economic sectors. The Indian banking sector is broadly classified into scheduled and non-scheduled banks. As per the Reserve Bank of India (RBI), India's **banking sector** is sufficiently capitalised and well-regulated. The overall banking industry is now going through a phase of modernisation in which a migration from physical banks to online banks is being seen.
The five porter's analysis for this sector is listed below-

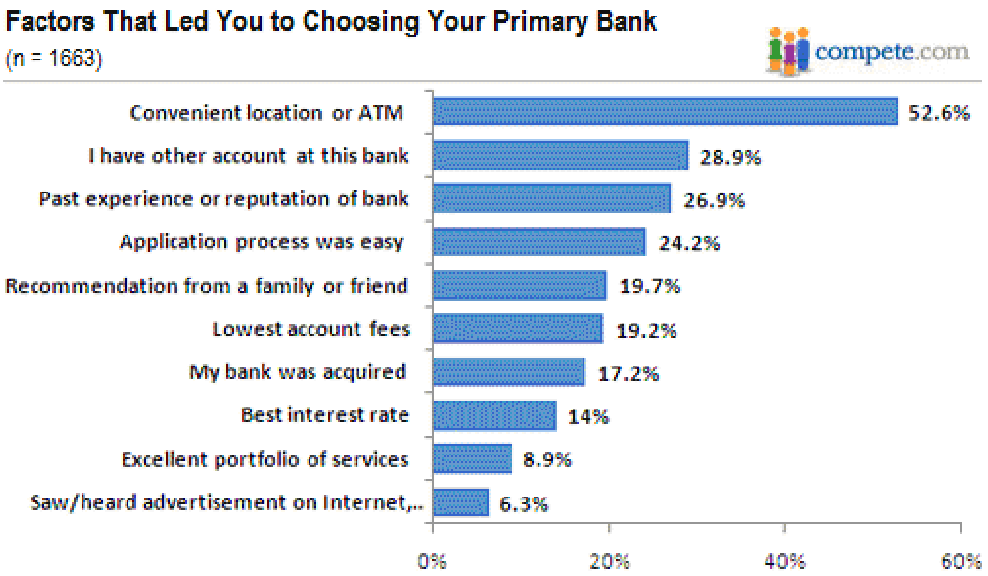
<u>Bargaining power of Buyers:</u> The individual doesn't pose much of a threat to the banking industry, but one major factor affecting the power of buyers *is relatively high switching costs.* If a person has one bank that services their banking needs, mortgage, savings, checking, etc, it can be a huge hassle for that person to switch to another bank.
To try and convince customers to switch to their bank they will often times lower the price of switching, though most people still prefer to stick with their current bank.
The internet has greatly increased the power of the consumer in the banking industry. The internet has greatly increased the ease and reduced the cost for consumers to compare the prices of opening/holding accounts as well as the rates offered at various banks.
ING Direct introduced high-yield savings accounts to catch the buyers' attention, then they went a step further and made it very easy for customers to transfer their money from their current bank to ING. *ING was successful in its attempt because it managed to make switching costs very low in terms of time and capital.*
However, Internet Banking has made it easy, both in terms of money and time, for consumers to switch from one bank to another.

<u>Bargaining power of Suppliers:</u> Capital is the primary resource of any bank and there are four major suppliers of capital in the industry.
1. Customer deposits.
2. mortgages and loans.
3. mortgage-baked securities.
4. loans from other financial institutions.

By utilizing these four major suppliers, the bank can be sure that they have the necessary resources required to provide service to their customers' borrowing needs while maintaining enough capital to meet withdrawal expectations.
The power of the suppliers is largely based on the market, their power is often considered to fluctuate between medium to high.

<u>Rivalry amongst existing competitors:</u> The banking industry is considered highly competitive. The financial services industry has been around for hundreds of

years, and just about everyone who needs banking services already has them. Because of this, *banks must attempt to lure clients away from competitor banks. They do this by offering lower financing, higher rates, investment services, and greater conveniences than their rivals.* The banking competition is often a race to determine which bank can offer both the best and fastest services but has caused banks to experience a lower ROA (Return on Assets). Given the nature of the industry, it is more likely to see further consolidation in the banking industry. Major banks tend to prefer to acquire or merge with other banks than spend money on marketing and advertising.
The various reasons for competition in the industry can be seen in this bar graph.



<u>Threat of substitutes products:</u> Some of the banking industry's largest threats of substitution are not from rival banks but from non-financial competitors. *The industry does not suffer any real threat of substitutes as far as deposits or withdrawals, however, insurances, mutual funds, and fixed income securities are some of the many banking services that are also offered by non-banking companies.* There is also the threat of payment method substitutes and loans are relatively high for the industry. For example, big-name electronics, jewelers, car dealers, and more tend to offer preferred financing on "big ticket" items. Often times these non-banking companies offer lower interest rates on payments than the consumer would otherwise get from a traditional bank loan.

<u>Threat of New Entrants:</u> Despite the regulatory and capital requirements of starting a new bank, between 1977 and 2002 an average of 215 new banks opened each year according to the FDIC. *With so many new banks entering the market each year the threat of new entrants should be extremely high.* However, due to mergers and bank failures, the average number of total banks decreases by roughly 253 a year. A core reason for this is, what is arguably, *the biggest barrier to entry for the banking industry, trust.*

Because the industry deals with other people's money and financial information new banks find it difficult to start up. Due to the nature of the industry people are more willing to place their trust in big-name, well-known, major banks that they consider to be trustworthy.

The banking industry has undergone a consolidation in which major banks seek to serve all of a customer’s financial needs under their roof. This consolidation furthers the role of trust as a barrier to entry for new banks looking to compete with major banks, as consumers are more likely to allow one bank to hold all their accounts and service their financial needs.

Ultimately the barriers to entry are relatively low for the banking industry. While it is nearly impossible for new banks to enter the industry offering the trust and full range of services as a major bank, it is fairly easy to open up a smaller bank operating on the regional level.