

A CASE STUDY ON STRATEGIC MANAGEMENT OF NON PERFORMING ASSETS IN HDFC BANK: AN IMPLEMENTATION OF MCKINSEY 7S MODEL

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INTRODUCTION

The case explores and analyses management strategy employed by HDFC bank to cope up with the problem of Non Performing Assets using Mckinsey 7s model. The case also presents SWOT analysis for HDFC bank through the assessing lens of bank's NPA management. A brief profile of HDFC Bank has been presented in the case study along with key financial highlights and selected financial ratios of the bank for eight years period from FY 2011 to FY 2018. In the case study, light has been thrown on the strategic intent of HDFC bank to deal with Non Performing Assets with underlining of Bank's Mission and Vision. Case study also conferred HDFC Bank's business model in order to develop understanding about operational insights and business structure of the bank. In SWOT analysis, it has been observed that immense efforts has been made by HDFC Bank for management of NPA and maintain standard asset quality in the loan portfolio of the bank. A brief discussion on NPA statistics has been presented and case study concludes with comparative presentation of strategic management of NPA by HDFC bank and its private peers through Mckinsey 7s framework.

A BRIEF PROFILE OF HDFC BANK

Housing Development Finance Corporation Limited was the first financial company got approval from RBI to set up a private bank as a measure of liberalization of banking industry in India in 1994. The bank incorporated in August 1994 and started operations as a SCB (Schedule Commercial Bank) from January 1995 by the name "HDFC Bank Limited" had its registered office in Mumbai, India.

Housing Development Finance Corporation Limited is an Indian company dealing in banking and financial services sector. As of end of June 2019, it has a base of 1,04,154 permanent employee. It is country's largest private sector bank by its assets. It has been known for largest bank in India by market capitalization as on March 2020. Bank has started operations in January 1995 with a simple but strong mission: 'World Class Indian Bank'. HDFC banks focused on quality products and excellence in services. In today's banking scenario they succeeded in their goal. They are committed towards their efforts to satisfy customer in domestic and overseas market.

DISTRIBUTION NETWORK

Housing Development and Finance Corporation Limited is Indian company serves in banking and financial services sector headquartered in Mumbai. At present, bank has a network of 5326 branches spread among 2825 cities in India linked online and real time basis. The bank has also a network of 14996 ATMs across India. ATM network of the bank can be accessed by all domestic and International VISA/MasterCard/Maestro/American Express card holders. HDFC bank is also performs clearing/settlement functions to various stock exchanges viz. NSE and BSE.

PRODUCT Portfolio of HDFC Bank

The Bank provides various products and services to fulfill the need of their customers. Bank deals with both, individual and corporate customers along with small and medium enterprises. For individual customers, bank has a bunch of different accounts, schemes, investment plans, variety of loans and different cards. The customer can select the products/services as per their requirement. For corporate customers and organizations, the bank provides customized solutions categorized as fund based and fee based services, value addition, investment services etc. These products and services are offered by the bank to their customers at affordable price with custom services provides value in the long run to employees and help in ornamental goodwill of the bank. Various products and services offered by the bank are as follows:

- Loans.
- Accounts and deposits.
- Investments and Insurance.
- Cards.
- Forex and payment services.
- Customer center.

TECHNOLOGY

HDFC Bank functions in an extremely automatic atmosphere motorized by information technology and communication systems. All divisions and subdivision along with branches have online connectivity which permits immediate funds transfer to the customers. One retail Customer can avail banking services from other branches through the branch network and Automated Teller Machines (ATMs).

They have made extensive efforts and payments in obtaining the best technology available internationally to build infrastructure for a world class bank. HDFC Bank has prioritized its engagement in technology and the internet as one of its key goals and has already made significant progress in web-enabling its core businesses. In each of its businesses, the bank has succeeded in leveraging its market position, expertise and technology to create a competitive advantage and build market share.

Table 1: Financial Highlights

YEARLY RESULTS OF HDFC BANK (in Rs. Cr.)	MAR '19	MAR '18	MAR '17	MAR '16	MAR '15	MAR '14	MAR '13	MAR '12
INTEREST EARNED								
a)Int. /Disc. on Adv/Bills	77,544.19	62,661.79	52,055.26	44,827.86	37,180.79	31,686.92	26,822.39	20,536.60
b)Income on Investment	19,997.46	16,222.37	15,944.34	14,120.03	10,705.61	9,036.85	7,820.26	6,504.59
c)Int. on balances With RBI	635.7	523.88	532.02	361.61	517.1	355.99	281.63	137.14
d)Others	794.7	833.31	774.34	911.95	66.41	55.78	140.59	108.02
Other Income	17,625.87	15,220.31	12,296.49	10,751.72	8,996.34	7,919.64	6,852.62	5,243.69
EXPENDITURE								
Interest Expended	50,728.83	40,146.49	36,166.74	32,629.93	26,074.23	22,652.90	19,253.75	14,989.58
Employees Cost	7,761.76	6,805.74	6,483.66	5,702.20	4,750.96	4,178.98	3,965.38	3,399.91
Other Expenses	18,357.61	15,884.62	13,219.66	11,277.49	9,236.59	7,863.21	7,270.74	5,190.15
Operating Profit before Provisions and contingencies	39,749.72	32,624.81	25,732.39	21,363.55	17,404.47	14,360.09	11,427.62	8,950.40
Provisions And Contingencies	7,550.08	5,927.49	3,593.30	2,725.61	2,075.75	1,588.02	1,677.00	1,437.25
P/L Before Tax	32,199.64	26,697.32	22,139.09	18,637.94	15,328.72	12,772.07	9,750.62	7,513.15
Tax	11,121.50	9,210.57	7,589.43	6,341.71	5,112.80	4,293.67	3,024.34	2,346.08
P/L After Tax from Ordinary Activities	21,078.14	17,486.75	14,549.66	12,296.23	10,215.92	8,478.40	6,726.28	5,167.07
Net Profit/(Loss) For the Period	21,078.14	17,486.75	14,549.66	12,296.23	10,215.92	8,478.40	6,726.28	5,167.07

Table 2: Standalone key financial ratios

KEY PERFORMANCE RATIOS	Mar-19	Mar-18	Mar-17	Mar-16	Mar-15	Mar-14	Mar-13	Mar-12
ROCE (%)	3.34	3.2	3.18	3.17	3.11	3.18	3.12	2.97
CASA (%)	42.37	43.49	48.03	43.24	44.03	44.81	47.43	48.39
Net Profit Margin (%)	21.29	21.79	20.99	20.41	21.07	20.61	19.18	18.93
Operating Profit Margin (%)	3.48	2.82	3.25	2.56	2.51	1.35	-0.36	-0.28
Return on Assets (%)	1.69	1.64	1.68	1.73	1.73	1.72	1.68	1.52
Return on Equity / Networth (%)	14.12	16.45	16.26	16.91	16.47	19.5	18.57	17.26
Net Interest Margin (X)	3.87	3.76	3.83	3.89	3.79	3.75	3.94	3.63
Cost to Income (%)	38.41	39.62	37.84	36.69	36.84	36.53	36.02	38.03
Interest Income/Total Assets (%)	7.95	7.54	8.02	8.49	8.2	8.36	8.75	8.07
Non-Interest Income/Total Assets (%)	1.41	1.43	1.42	1.51	1.52	1.61	1.71	1.55
Operating Profit/Total Assets (%)	0.27	0.21	0.26	0.21	0.2	0.11	-0.03	-0.02
Operating Expenses/Total Assets (%)	2.09	2.13	2.28	2.39	2.36	2.44	2.8	2.54
Interest Expenses/Total Assets (%)	4.07	3.77	4.18	4.6	4.41	4.6	4.8	4.43

Table 3: NPA ratios

NPA RATIO	Mar-19	Mar-18	Mar-17	Mar-16	Mar-15	Mar-14	Mar-13	Mar-12
Gross NPA	11,224.16	8,606.97	5,885.66	4,392.83	3,438.38	2,989.28	2,334.64	1,999.39
Net NPA	3,214.52	2,601.02	1,843.99	1,320.37	896.28	820.03	468.95	352.33
% of GNPA	1.36	1.3	1.05	0.94	0.9	1	0.97	1.02
% of Net NPA	0.39	0.4	0.33	0.28	0.2	0.3	0.2	0.2

STRATEGIC INTENT OF THE BANK

The long-term intent of the bank is to partner with customers in their progress - fulfilling and enriching their financial journeys. The bank deliberates that to remain relevant in the financial services industry of the future; banks need to embrace Customer Experience design as a core component of their business model and that the Customers compare banks not with other banks, but with the most powerful experiences they have with any service provider across industries. And thus the core values of the bank are built upon —customer-first attitude.

1. HDFC banks states in the vision statement to be a preference of customer in providing financial solution and serve them with superior banking, enabled employees and better use of technology keeping in mind the core values of

- Ethics
- Transparency
- Customer Centricity
- Teamwork
- Ownership

2. Mission of the bank is to capture retail banking system by offering wide range of financial products and services, accounts, loans, schemes, investments delivered through all channels of distribution. It provides to end-to-end retail customer necessities through retail responsibilities, retail lending and investment products. The bank follows customer centric method in its banking business though pointing at the Life Cycle 'financial needs of the clientele through pioneering products and services. For the purpose of building of its Retail Deposit franchise the Bank follows customer division approach. The bank proposals whole bunch of financial services for its Non Resident Indians (NRI) and High Net worth Individuals (HNIs) through its holding companies such as providing Estate planning, insurance products, management of investment portfolio and credit cards. The bank provides complete and custom corporate or organization banking solutions.

MOGO – HDFC Musical Logo

MOGO is a registered trademark of Brand Music. HDFC Bank's MOGO is a lively appearance of the standards and values that have driven the Bank to become nation's best digital bank. It assistances to create a influential emotional connect with its customers and construct recall value amid patrons through all platforms viz. Automated Teller Machines, Mobile Banking, Applications and other touch-points. MOGO reproduces the two extents of bank: Reliance and Reformist modification. The musical piece is inspired on the one hand, by **Raag Bilawal** which couriers novelty and vitality, and on the other by **Raag Shudh Kalyan** which imitates the thoughtful nature of the Bank. One can find modern western music instruments such as the Piano and Guitar escorting with Sitar in order to create a healthy mixture of global ambition with Indian touch.

BUSINESSES OF HDFC BANK

HDFC Bank provides to an extensive variety of banking services including commercial banking and investment banking services on wholesale front and branch banking on the retail front. There are three segments where HDFC performs banking operations:

WHOLESALE BANKING

HDFC bank renders banking services in the target market where there are mainly large, companies belongs to Indian corporate sector and also at the smaller extent, small, medium size enterprises and agro-based businesses. For the fulfillment of banking needs of these sectors of the economy HDFC bank provides bunch of banking services comprising cash management, working capital finance, trade service and transactional services. Bank also provides customized solutions to the corporate customers. Bank offers superior financial products and services to their corporate clientele. It also renowned as premier service provider in banking for cash management and customized solutions of transactional banking for corporate houses, stock exchange, mutual funds and other banks.

TREASURY

In treasury business, HDFC has three segments- Money market & Debt securities, Foreign exchange and derivatives and equities. After the liberalization of Indian financial markets, large corporate customers seek for consultancy about more sophistication in risk management, consultancy and product structure. These segments of banking business are attended by HDFC's treasury team. For the fulfillment of obligatory reserve requirement mandated by Reserve Bank of India, the bank keeps 25 percent of its total deposits in liquid securities issued by government. Bank's treasury team deals in managing the risk and returns of such investment of the bank.

RETAIL BANKING

The objective of bank in retail banking segment is to render wide range of financial services to its customer through one stop window. All banking requirements of customers fulfilled by world class service delivered by increasing branch network and through other delivery channels viz. Phone banking, ATMs, Mobile banking and Net banking etc. The HDFC Bank have designed distinct financial solution programs for HNI customers viz. Investment advisory services programs and HDFC Bank Plus. These programs have been designed to fulfill the

needs of HNI customers who seek the information and advisory services for their investments.

The bank also provides wide range of retail loans comprising Personal loan, auto loan, mortgage loan, loan against marketable securities, and two wheeler loan. HDFC also provides services as Depository Participant (DP) to retail customers. HDFC bank is recognized as the first bank in India for launching an International debit card with VISA. Bank started to deal in credit card business in the year 2001. As on March 2015, the bank had total 25 million users of debit and credit cards. HDFC is the leading player in merchant acquiring business with 2,35,000 Point on sale (POS) for debit card and credit card acceptance. Bank also provides various internet based Business to Customer (B2C) services for deposits, utility payments and loans etc.

SWOT ANALYSIS (FY 2018)

STRENGTH

- Drivable key performance ratios
- Robust operating revenue growth
- Sustainable growth in operating profit
- Under control risk parameters
- Increasing Cash Flow and Cash from Operating activity
- Improving Net profit year on year
- Growing Net Profit with increasing Profit Margin
- high degree of customer satisfaction
- The attrition rate in HDFC is low

WEAKNESS

- Bank doesn't have sturdy presence in Rural areas
- HDFC lacks in aggressive marketing strategies
- Low size and less numbers of corporate loans in lending portfolio
- Restrained income from corporate franchise
- Eroding profits due to higher provisioning requirement

OPPORTUNITIES

- HDFC bank follows much better parameters for maintaining the asset quality comparatively than government banks, therefore the profit growth is expected to increase
- Small, Medium Enterprises are increasing with fast growth rate. HDFC bank has good standing in terms of upholding company's salary accounts
- Huge scope for acquisitions and alliances because of strong financial position of the bank
- Huge scope in cross selling of financial products aided by big data analytics of the retail customers.
- Sustainable growth from existing deposits customers along with viable growth in fee income from distribution of fee based products.

THREATS

- Minor increase in NPA in recent Results. Though it is minor but not a good insignia for the financial health of the bank.
- Steady profit has led to increase the number of competitors in the banking industry and consequently sales of financial products/services may be affected
- Technologies developed and adopted by the competitor could be a serious threat to the industry in long run
- Shortages of skilful workforce in global market is a threat to steady growth of profits for the bank.

CHALLENGES

- Navigation of HDFC Bank in a new landscape is required which is changing very fast with consolidation of public sector banks.
- Significant changes occurred in asset quality of corporate loans in the lending portfolio.
- Higher provisioning requirements for NPA may adversely affect the profitability of the bank.
- The Bank has to work upon and increase market share and revenue from rural and semi-urban branches.

NPA MANAGEMENT BY BANK

Management of HDFC Bank has published a watch list of those accounts which were the key source of potential bad impact on the asset quality of corporate

loans in lending portfolio in the beginning of financial year 2018. Major accounts belong to that list comprised those sectors (steel, power etc.) which were under stress due to several macroeconomic factors. To start with, majority of watch list account contained of sectors, which were under stress viz. steel and power with core fund based outstanding of ₹ 2861 crore. Further, non fund based outstanding remained ₹ 298 crore. During this year bank also added ₹ 21,51 crore of corporate slippage out of which ₹ 1763 crore belonged to the watch list. Although the magnitude of watch list has reduced significantly up to 41.2 % with core fund based outstanding of ₹ 1123 crore and non fund based outstanding of ₹ 197 crore as on March 2018. Aforesaid watch list, in proportion of total customer assets has reduced by 7.91% as on March 2017 to 3.19% as on March 2018. Material rise in asset quality metrics was an outcome of high slippages from the watch list. During this financial year (2018), bank observed an addition into Gross NPA of ₹ 2617 crore. Addition of fresh Net NPA of ₹ 613 crore was observed in the financial year end 2018. After consideration of necessary write offs, bank's Provision coverage stood at 59.24%. Further, net restructured loan book stood at ₹ 594 crore and net restructured asset ratio stood at 1.21%. Total outstanding value of underlying Gross NPA subjected to S4A and 5:25 redressal scheme reported at ₹ 271 crore and ₹ 319 crore respectively as on March 2019. Gross NPA of bank has increased with a very slow pace in recent years and stood at 1.36% as on March 2019 which is very little high then 1.30% as on March 2018. Net NPA has shown a decline as on March 2019 and stood at 0.39% as compare to 0.40% as on March 2018. Bank has managed their NPA account with a professional manner and also followed selective approach for the lending. Further, bank has focused more on preventive measures like, accurate & close appraisal of loan application, gathering correct information about borrower's repayment behavior etc.

THE MCKINSEY 7S ANALYSIS

Seven elements (Superordinate Goals, Strategy, Structure, Systems, Style, Staff and Skills) of McKinsey 7S Framework have been analyzed in the context of HDFC bank with respect to strategic management of NPA accounts. In order to make a comparison between McKinsey 7S elements of the HDFC bank with other private banks, 7 tables for each element of McKinsey 7S framework have been prepared. The compilation of the results based upon the annual reports of

HDFC bank and sample private banks (including Axis Bank, ICICI Bank, Indusind Banks, Kotak Mahindra Bank, Federal Bank) in India presented below

Table 4: Super ordinate goals

HDFC Bank	Private Sector Banks
1) Customer Centric Operations 2) Ethics 3) Transparency 4) Teamwork, and 5) Ownership	1) Maintain a healthy financial profile and diversify earnings across businesses and geographies. 2) Maintain high standards of governance and ethics.

Table 5: Strategy

HDFC Bank	Private Sector Banks
To calibrate our portfolio concentration a lot more tightly than in the previous years. Diversified our loan book materially and now have 45% of our loans in the Retail segment. Reduced concentration risk in corporate book significantly. Confined sanctions and keenly targeting to the pool of better rated corporates, we continue to drive the transition of our corporate franchise towards a more flow led, transaction banking oriented business.	(1) Proactive Monitoring; (2) Improving portfolio mix; (3) Reducing Concentration Risk and (4) Deleveraging stressed assets by sales or enforcing contractual rights

Table 6: Structure

HDFC Bank	Private Sector Banks
The independent risk management structure to monitor all risks including credit risk. The goal of credit risk management focuses on maintaining asset quality and concentrations at individual exposures as well as at the portfolio level. Internal rating forms the core of the risk management process for wholesale business with internal ratings determining the acceptability of risk,	Independent Risk Management Group formed. A separate Credit Monitoring Group formed for proactive resolution of recovery in SME segment.

<p>maximum exposure ceiling, sanctioning authority, pricing decisions, review frequency. For the retail lending portfolio comprising small enterprises and small agriculture borrowers, the Bank uses different product-specific scorecards. Big, risk weighted and complex exposures require to be independently examined by the concern department for each transaction whereas small, template exposures are extended within the approved product policies.</p>	
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Table 7: Systems

HDFC Bank	Private Sector Banks
<p>Credit models used for risk estimation are assessed for its discriminatory power, calibration accuracy and stability independently by a validation committee.</p>	<p>(1) Use of Predictive models for stress- identification. (2) Central Aberrant Database to review the borrower's profile before credit sanction</p>

Table 8: Style

HDFC Bank	Private Sector Banks
<p>The Bank's Structured Finance Group (SFG) is a specialized group focusing on resolution of non-retail impairments of the Bank. The team is based out of the Central Office in Mumbai, and oversees rectification and restructuring as well as recovery for the Western zone of the country. The central team is supported by three Regional Recovery Cells at Delhi, Kolkata and Chennai.</p>	<p>The Retail Credit and Policy Group is an independent unit focusing on policy formulation and portfolio tracking and monitoring and reports to a group of Executive Directors</p>

Table 9: Staff

HDFC Bank	Private Sector Banks
Independent Recovery Cells at central office and three other regional centres	Independent Groups deployed to recognize, measure and monitor the bank group's principal risks

Table 10: Skills

HDFC Bank	Private Sector Banks
Training intervention to strengthen the status of compliance standards as an important element of business and to communicate the message that the compliance and governance are most important and value driven.	(1) Structured hand-holding programs (2) Video based learning modules

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