Project Blue:
Assessing the future trends for financial services in India
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Introduction

Welcome to Project Blue: Assessing the future trends for financial services in India.

As the financial services industry continues to recover from the economic crisis, it is critical that financial institutions deal with the longer term trends that are transforming the market and competitive environment. It is of utmost importance, market players in the industry identify risks and threats to their business and capitalise on the opportunities presented by the continuously evolving landscape.

To help financial services businesses develop effective strategies to respond to these changes, we have developed a global framework, called Project Blue (refer to appendix). Project Blue sets the forward looking agenda for leaders of financial institutions, regulators and policy makers. This framework can be used to systematically and comprehensively identify the issues that should be addressed related to such areas as market strategy, organisation, operating models and risk.

Our development of Project Blue drew on our interactions with various players in the financial services sector: customers, businesses, regulators and government. We believe that Project Blue will help financial services businesses as they deal with the impact of new technology, demographics, social changes and mounting pressures on the world’s most critical natural resources.

Although the Project Blue global framework is all encompassing, we realise that this framework needs to be customised to function effectively in different markets. This is particularly the case with respect to India, which offers huge opportunities for growth. Thus we have developed a unique framework for India, keeping in mind the regulatory, fiscal and political environment. The Project Blue framework for India is represented in Figure 1.

![Figure 1: Project Blue Framework for India](source: PwC Project Blue analysis)
Rather than offering one single way forward, the Project Blue framework is flexible enough to be applicable to the many different organisations within the financial services sector for their strategic assessments and is adaptable to the unique challenges faced by all organisations.

Using the Project Blue framework will help your business to target investment, identify talent requirements and develop the necessary operational capabilities needed to make the most of your competitive potential.

In this document we will discuss the challenges and opportunities by expanding upon each of the individual components of the Project Blue framework.

We hope you find this document insightful and useful and we would be pleased to discuss this framework in more detail as the Indian economy continues to evolve.
Adapting to challenges and opportunities

Against the backdrop of a complex and uncertain economic environment, financial service institutions in India are struggling to retain their competitiveness and to align their business models to the rapidly changing circumstances. Forward-looking organisations are seeing the shake-up as a once in a generation opportunity to redefine their strategies and business models, when the competitive structure of their industries are relatively open to change.

The Project Blue framework has been designed to help industry executives organise their assessment of a world in flux, debate the implications for their business, rethink their strategies and, if necessary, reinvent their organisation. Seeing the future clearly, being first to adapt strategies and business models, and breeding a culture that shapes, rather than reacts to, the changing business environment will be the building blocks of sustainable competitive advantage in the future.

The Project Blue framework for India draws on the experience of the PwC global network and has been developed considering the major trends that are reshaping the economy and transforming the behaviour of consumers, businesses and regulators. The India growth story, although impacted to a great extent by international factors, is equally driven by domestic factors, like changing consumer behaviour, falling investment, the increasing trade gap and current account deficit. In view of the growing integration with global markets, India needs to have a strong regulatory framework to prevent and protect against external threats. Being a hugely under-penetrated financial market, India presents immense opportunities to tap investors’ savings and channel them into the financial markets. However, regulatory changes, fiscal pressures and political and social instability all mean India’s is a complex business environment.

These complexities in the Indian business environment make the future of financial services difficult to predict. They also mean that a significant amount of management time is consumed in a focus on short-term optimisation, and in some cases survival, at the expense of long-term strategy and execution.

Regulatory environment

Regulatory change will be a way of life for the foreseeable future, driven by the requirement to better manage risk in the financial system. The multiple changes taking place in the financial services domain are resulting in greater uncertainty and complexity, with the prospect of further industry restructuring ahead. While the reforms are still in the early stages of development, they will come to redefine the role of financial institutions and with it, their strategies and business models. It’s vital to look beyond compliance to understand how these developments will affect product and business portfolios, how they will determine the allowable cost structure of your organisation and ultimately how they will influence the fundamental design and strategy of your organisation.
Regulatory change will challenge you to identify which areas of your business offer the greatest potential and to identify the core attributes on which to establish sustainable competitive advantage.

Globally, a regulatory reform agenda has taken a definitive shape, and efforts are now being made to standardise these measures across countries, so that there is no window of regulatory arbitrage. A strong regulatory framework entails strengthening liquidity conditions, enhancing risk coverage, reducing leverage, recognising systemic risk and maintaining financial stability. Across the US and Europe the regulatory developments which CEOs are responding to include Foreign Account Tax Compliance Act (FATCA), Dodd-Frank, Alternative Investment Fund Managers Directive (AIFMD), the Volcker rule and Over the Counter (OTC) derivative market reforms to mention a few. Also, the need to maintain higher capital standards under Basel III, which aims to ensure better financial stability, are affecting investment strategies, while increasing the regulatory burden for banks and other financial services institutions.

In India also, the regulatory landscape is undergoing a shift, as a result of global reforms related to Basel III, OTC derivative reforms, and the development of an effective anti money laundering (AML) framework, amongst others. One of the most recent regulatory developments, which presents huge opportunity in the banking sector, has been the issuing of new banking licenses to corporate houses.

Regulatory change is aimed at bringing about uniformity in regulatory reform, minimising regulatory overlap and developing new markets. In recent years, advances in technology, innovations in processes and the need to manage the rise in flow of capital have led to a need for a stronger and more resilient regulatory framework. Indian regulators are playing a key role in the region, and learning from their counterparts in other parts of the world, in continuing to strengthen the regulatory framework in India.

“The global community of regulators – as well as the political classes – are keen on ensuring the stability of the financial system. And that implies a completely new order, a new set of rules to play by. In these cases, it’s not uncommon to wind up in a situation of regulatory overreach”

Piyush Gupta
CEO & Director, DBS Group
16th Annual CEO Survey, PwC India
“I think the level of external threats has increased with every passing decade. And as the pace of change has increased, organisations like ours have to be a lot more flexible than we might have been in the past.”

Shikha Sharma
MD & CEO, Axis Bank
16th Annual CEO Survey, PwC India

**Fiscal pressures**
The Indian economy is in need of fiscal consolidation to boost capital expenditure. Fiscal reforms have been undertaken, aimed at cutting down spending on subsidies and increasing revenues.

Fiscal pressures

<table>
<thead>
<tr>
<th>Year</th>
<th>Fiscal deficit</th>
<th>Savings rate (Lhs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>38%</td>
<td>38%</td>
</tr>
<tr>
<td>2008-09</td>
<td>37%</td>
<td>37%</td>
</tr>
<tr>
<td>2009-10</td>
<td>36%</td>
<td>36%</td>
</tr>
<tr>
<td>2010-11</td>
<td>35%</td>
<td>35%</td>
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<tr>
<td>2011-12</td>
<td>34%</td>
<td>34%</td>
</tr>
<tr>
<td>2012-13</td>
<td>33%</td>
<td>33%</td>
</tr>
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</table>

Source: Economic Survey 2012, Planning Commission

Not just net tax revenue, but overall revenue receipts have been lower than expenditure

<table>
<thead>
<tr>
<th>Year</th>
<th>Total revenue receipts</th>
<th>Total expenditure</th>
<th>Net tax revenue</th>
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<tbody>
<tr>
<td>2007-08</td>
<td>18.0%</td>
<td>18.0%</td>
<td>18.0%</td>
</tr>
<tr>
<td>2008-09</td>
<td>16.0%</td>
<td>16.0%</td>
<td>16.0%</td>
</tr>
<tr>
<td>2009-10</td>
<td>14.0%</td>
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<tr>
<td>2010-11</td>
<td>12.0%</td>
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<tr>
<td>2011-12</td>
<td>10.0%</td>
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</tr>
<tr>
<td>2012-13</td>
<td>8.0%</td>
<td>8.0%</td>
<td>8.0%</td>
</tr>
</tbody>
</table>

Source: Economic Survey 2012, Planning Commission
Reducing India’s deficit is proving difficult in the face of low tax receipts and subsidies in areas such as petrol and cooking fuel. Tax receipts as a percentage of GDP were 9.6% in India in 2011, the lowest level of any major economy (the world average was 29.5%) (See Figure 2). This low level of tax revenue and the parallel economy that underpins it depletes the funds available for much needed infrastructure investment and broader economic development.

The government announced an ambitious Union Budget in February 2013 in an effort to control the rising fiscal deficit. It set a target of a fiscal deficit of 4.8% of GDP in financial year 2013-14; an improvement from 5.1 and 5.7% in the previous two years. The projection for a lower fiscal deficit is based on the encouraging forecast for growth between 6.2 and 6.7% during the same year. Increased growth is a prerequisite for higher revenue collections.

The goal of controlling the fiscal deficit has not deterred the Finance Ministry from increasing overall expenditure while trying to rein in certain subsidies. The Budget made provisions for a 16% increase in overall expenditure, up from 10% and 9% in the previous two financial years. Revenue targets, on the other hand, remain high.

Defining his efforts to contain the fiscal deficit through rationalising expenditure, the Finance Minister said: “We took a dose of bitter medicine. It seems to be working.” The dose has certainly evoked positive sentiments among ratings agencies. Moody’s for instance, called the Budget ‘credit positive’, being convinced by its efforts for modest fiscal consolidation. However, it is only with time that we will know if the government will meet its food and fuel subsidy targets successfully, generates enough earnings from divestment and telecom fees and if the economy will grow enough to fill the government’s coffers with additional revenues from income tax.

“\textit{We ensure that we are prepared for potential adverse scenarios by making sure that we are well capitalised, that we are watching our risk processes and that we have a fairly diversified portfolio in terms of the risks that can come and hit us. And that immunises us a bit from some of these threats.}”

\textbf{Shikha Sharma}

\textbf{MD & CEO, Axis Bank}

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\textbf{Political and social instability}

The political and social scenario has become increasingly unstable in recent years. Factors ranging from corruption and citizen activism to fiscal austerity, unemployment and rising food prices are igniting ever-more frequent social and political unrest. In addition, the advent of social media is making it easier to communicate information, circumvent censorship and coordinate action.

The 16th Lok Sabha elections which will be held in 2014 may lead to instability, given the high rates of inflation, sluggish growth and conservative policies which were laid down by India’s United Progressive Alliance (“UPA”) government.

On the social welfare front, there is a need to boost the pension market to make up for the inadequacies of social welfare and help support an increasingly longer lived and growing population. There is a lack of tax incentives to help spur higher take-up of pensions. India has the second largest population of people over 60 in the world, and this number is expected to touch 173 million in 2026, from 71 million in 2001. It is clearly imperative that this segment is adequately covered under some kind of pension or other social welfare scheme.

The government has taken a huge step forward with the UID (Aadhaar) project which provides a unique identification to all residents across the nation. This is used primarily as the basis for efficient delivery of welfare services. Like other businesses, financial services companies will need to navigate the challenges presented by social and political instability. The Project Blue framework can help businesses address these challenges and identify opportunities to pursue further growth.

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1 CIA World Factbook 2011 estimates
2 Economic Times, 28.02.13
3 Reuters, 04.03.13
Planning for transformation

The rise and interconnectivity of emerging markets

India’s drive to boost exports and address its continuing current account deficit (see Figure 3) builds on its historic ties and strong trading relationships, both regionally and globally. One clearly emerging opportunity is tapping into the rapid expansion and increasing interconnectivity of the fast-growth markets of South America, Asia, Africa and the Middle East (together forming what PwC terms ‘SAAAME’). Trade between the SAAAME markets already accounts for around 30% of global commerce and this intra-SAAAME trade is growing at around 20% a year (see Figure 4). This is much faster than trade between developed-to-developed and developed-to-emerging markets. Eventually, we predict that SAAAME trade will be the dominant trade activity in the world.

Figure 3
Imports have continued to outpace exports, leading to a trade deficit

As a consequence, the current account deficit has also worsened

Source: Economic survey, Planning commission
South America, Africa, Asia and the Middle East (SAAAME) are emerging as an increasingly important network for International Trade

The growth in India’s economy since the advent of liberalisation in the early 1990s (an average growth of 8% a year over the past ten years) has transformed the country into an economic superpower. While remaining strong in comparison to most developed and SAAAME economies (see Figure 5), growth in India has, however, recently slowed. India is estimated to achieve a growth rate of 4.9% (IMF) or 5.0% (RBI) in 2012-13, reflecting continuing uncertainty over the Eurozone sovereign debt crisis and other impediments to global economic prospects.

Figure 4

Source: WTO, PwC Analysis

5 Economist online statistics, updated 27.09.12
6 International Monetary Fund (IMF) World Economic Outlook, October 2012
7 The RBI, [2012]
The UAE has recently emerged as India’s largest trading partner, pushing China to second position. India had a trade deficit of only $2,113 million USD with the UAE, while with China the figure was $31,492 million USD. Out of India’s top ten trading partners, seven were from the SAAAME market (UAE, China, Saudi Arabia, Iraq, Singapore, Indonesia and Hong Kong).

Figure 5
India’s GDP versus GDP of other emerging markets and advanced economies

Source: IMF, World Economic Outlook (October 2012)
India’s longer term economic prospects are strong. Our latest projections anticipate that the size of India’s economy will be similar to that of the US by 2050 (see Figure 6).

India’s ability to serve all time zones and longstanding trading and cultural ties with markets around the world have provided a strong foundation for its growing place at the centre of intra-SAAAME and wider global commerce. One of India’s fastest-growing investment relationships is with Japan, with India and Japan seeing each other as economic and political counterweights to an increasingly powerful China.

From a westward-looking perspective, the colonial legacies of India’s common law, wide use of the English language and a British-influenced education system have helped to provide a familiar environment for inbound investors from the UK, UK and wider EU, and to open the way for Indian businesses to establish strong presences in these markets⁹.

In turn, the Indian diaspora in both SAAAME and non-SAAAME markets have provided a useful bridgehead for trading ties and business development.

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<tbody>
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<td>4</td>
<td>Japan</td>
<td>4,381</td>
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</tr>
<tr>
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<td>Germany</td>
<td>3,221</td>
<td>Russia</td>
<td>5,308</td>
<td>Japan</td>
<td>8,065</td>
</tr>
</tbody>
</table>

Source: World in 2050 by PwC, January 2011 update

⁹ In relation to the UK, for example, India is the third largest investor in the UK and the largest market for British goods outside the EU (BBC News, 09.11.12)
Another aspect to note is that although the strength of the SAAAME markets is increasing, there is a huge amount of credit flow from the west to the SAAAME region (see Figure 7). Much of this SAAAME capital is still managed in the west. These anomalies are unlikely to endure and the eventual re-balancing will have a strong impact on financial markets and other businesses that operate within them.

Figure 7: Foreign Direct investment

FDI from non-SAAAME countries to SAAAME countries, US$ billions, 2003–2011*

Largest 12 destination countries for FDI to SAAAME, US$ billions, 2010

Largest 12 source countries for FDI to SAAAME, US$ billions, 2010

Sources: The Financial Times and PwC analysis
Notes: *2011 data is year to date, available as of 7 December 2011
The primary focus for most financial services institutions in India will remain the domestic market. But an international presence may still be needed to support their domestic clients’ overseas expansion plans. Financial services institutions are under particular pressure to extend their reach into Africa, Latin America and other parts of Asia, to keep pace with the growth in intra-SAAAME commerce and to make up for the slowdown in western economies. As many US and EU banks, insurers and asset managers continue to scale back their overseas holdings and operations, there could be openings for Indian institutions to move in and fill the gap, creating new relationships in SAAAME markets for investment opportunities in India.

While Singapore and Hong Kong are now home to a significant number of overseas Indian banking offices (second and third on the list of overseas offices respectively), Indian institutions are less well represented in Africa and Latin America. (The UK still has the largest number of overseas Indian banking offices). Indian banking offices in the UK are currently facing challenges as regulation continues to tighten, making it more expensive to do business. Further development of overseas presence may be especially important in supporting mid-size companies that do not have access to the capital market and foreign bank funding enjoyed by their larger counterparts. An outbound banking model that has primarily focused on deposits and remittances may also need to be extended to take in more acquisition and trade support.

It is therefore going to be important for financial services organisations to take a forward-looking view, liaising with clients on their long-term ambitions and ensuring that the necessary finance and advice are available on the ground. Indian institutions can’t be everywhere, so reciprocal arrangements with domestic partners that provide services for Indian businesses in return for support for their clients here in India are going to be an important element of this development.

India’s large and increasingly affluent millennial generation is changing the outlook and opportunities for financial services businesses in the country. A key opportunity is developing investment products for a generation that may be prepared to take more risk than their older and more conservative counterparts. The challenge is how to make sure that pursuit of these

Our latest research anticipates that domestic credit in China could overtake the US by 2023 and India will become the third largest domestic banking sector after China and the US by 2050

10 Economic Times, 03.11.12
opportunities doesn’t lead to mis-selling, or risk, creating a market bubble. This will require both effective regulatory controls and a more mature distribution structure led by a well-supported independent financial adviser network. The underlying requirement is for a deeper and broader-based capital market, with a robust governance architecture encouraging retail investors to access these markets.

Further opportunities could lie in the development of Mumbai and other major Indian cities as international financial centres (“IFCs”). The potential benefits include providing a focus for innovation, a broader and more sophisticated range of financial services advice and services for Indian corporations and the ability to turn financial services into a significant source of export earnings over the long-term. But an IFC cannot be created as an isolated offshore entity reliant on outside capital and expatriate personnel. To deliver benefits for the country, an IFC needs to be rooted in, and a mechanism needs to be created for developing the capabilities within the domestic financial services market. This will require talent, capital, world class infrastructure and regulatory best practice.

**What you need to think about**

- **Do you need to rethink your global strategy to tap into the increasing strength of the SAAAME markets?**

- **Will you need to adapt your operating model to the different SAAAME business environments?**

- **How can primarily domestically focused groups develop or acquire the necessary capabilities including talent, strategic agility and deep cultural understanding to operate effectively across multiple territories?**

- **How can financial institutions in India make inroads into intra- SAAAME trade flows? What can they offer in the SAAAME region that their competitors can’t?**

- **What is the best model of governance to follow in each SAAAME market?**
**Demographic change**

Customers and their demands are changing. Population growth in different countries, combined with an ageing population around the world, will create a markedly different consumer market by 2050.

While much has been made of the impact of ageing in the western world, the most dramatic changes will be seen in emerging markets as birth rates and life expectancy around the world begin to converge (see Figures 8 and 9).

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**Figure 8: Asia – Total Population against mortality & fertility rates 2000-2050**

![Graph showing total population against mortality & fertility rates from 2000 to 2050.](image)

- **Population size, five-year average, millions**
- **Rate, per 1,000**

- **Population CAGR 2000-2010: 1.14%**
- **Population CAGR 2010-2050: 0.53%**

**Source:** United Nations Population Division
Figure 9: The impact of demographic change will be felt in every region, but in different ways.

Sources: United Nations Population Division; PwC analysis
Notes: World population and median age based on UN population figures for 2010 and medium variant projection for 2050.

Figure 10: Comparison of working age population (16 to 65)

One of India’s great economic advantages is its demographic dividend, though it will face competition for investment and development from the even more swiftly expanding population in Africa.

Figure 10 shows the rapid increase in India’s working age population, as compared to other countries like China, US and Brazil.

In India, the family structure is also undergoing a transformation, with the number of nuclear families on the rise. According to the census conducted in 2011, 56% of households in urban India have four members or fewer, whereas ten years ago the median household size in urban India averaged four to five members. Even in rural India, the median household size is closer to four members. This strongly indicates a shift in the needs and preferences of the Indian middle-class family.

The shift in India’s demographics has led to significant changes in customer preferences and trends, for instance, the evolution in media and technology has set a higher bar of expectation for customer experience. Enhancing customer experience can eventually translate into incremental revenue from improvement in retention of customers. Hence, businesses need to continuously adapt and evolve their strategy to cater to their customer base.

Social and behavioural change

Social and behavioural change is occurring at a faster pace than at any time in history. Consumers are more informed and empowered than ever before, and old notions of value and loyalty are breaking down as digital technology allows consumers to both compare value and expand their choices. Continuing digital transformation is also changing the way people interact, share ideas and access products and services, with social networking now accounting for one in every six minutes spent online.¹¹

One of the classic examples of how social and behavioural change is being brought about is influencing of buying behaviour. India is characteristic of having a consistently high level of savings and investment (See Figure 11), but most of the savings of the household sector is going into buying gold and real estate. These savings need to be channelled into the capital market, providing attractive investment options to the investor.

Have you considered this?

- How can you capitalise upon India’s demographic dividend?
- How can the savings of the young working age population of India be directed to the capital market for increased investment and growth?
- How do your operating models and products need to evolve to cater to the rising and diverse consumption needs of the Indian population?

¹¹ comScore report, 2011
Reaching out to customers with no savings, pension or other engagement with financial services is a key focus of the government’s ‘inclusive growth agenda’. Bringing a larger number of people under the financial services net in the rural compared to urban areas is a priority for the government. Looking ahead, the rural segment will emerge as a green field for businesses, with expected burgeoning demand from this segment. With fewer bank branches, insurance and mutual fund agents than urban areas, the rural market is also far more open to competition.

The government’s ‘Aadhaar’ initiative will help reduce the percentage of the population which does not hold a bank account, helping them access a wide variety of financial products and services.

How financial services institutions respond to these social and behavioural changes could define their market position for decades to come. If they judge the implications of the current moment correctly, financial services institutions might be facing a once-in-a-generation opportunity to put a clear distance between themselves and their rivals. If they do not, they may face a mortal threat. The key differentiator will be an organisation’s ability to anticipate where the market is going on the back of these changes and to get ahead of its competitors.

In emerging markets, increasing affluence and urbanisation are creating new and expanding markets for financial institutions (see Figure 12). City dwellers’ average wealth and demand for financial products and services are generally much higher than their rural counterparts. Indeed, some observers now see the real distinction in the financial services sector as being not between emerging and developed markets, but rather between city and rural areas. The rural market in India opens up a whole new window of opportunity to the financial services sector, as the market is under-penetrated to a great extent and there is scope to introduce an array of savings and investment products to this segment.

Figure 11: Gross domestic savings and investment as a percentage of GDP

![Figure 11: Gross domestic savings and investment as a percentage of GDP](image-url)

Underlying all these demographic developments is the need for smarter and more differentiated customer segmentation as financial services businesses seek to make sure that products are structured and targeted for the differing needs of a fast evolving society. Technology, education and mobility have not only raised the living standards of these customers but also their expectations and aspirations. They are price-conscious but also switched-on to quality, service and desirability.

The emerging potential includes creating affordable products for what we call the global emerging middle (“GEM”). With more than two billion consumers, the global emerging middle (income $996 - $3,945) sits just below the conventional middle class ($3,946 - $12,195) in income terms. But its aspirations for the quality and performance of its products are in sync with higher-earning segments. Globally, we estimate that this will be a $6 trillion market by 2020.

By 2030, Asia will account for 66% of the global middle-class population and 59% of middle-class consumption.
India’s working-age population, in the age bracket of 15-59 years\textsuperscript{12}, accounts for 57% of the overall population. This means they are more open to media influence and rising expectations. However, the population is still predominantly rural (over two-thirds), with all the challenges that entails for sales, marketing and distribution strategies. Indeed, many of India’s large domestic companies and home-grown multinational corporations have been among the first and, in some cases, the most successful in creating value for and from India’s emerging middle class, especially in the challenging rural markets.

Financial services businesses will need to anticipate these developments and bring products and services in line with the changing customer base in the markets they serve.

The combined market potential of India’s ‘emerging middle’ is expected to cross the $1 trillion threshold by 2021 as its ranks swell to 570 million, from 470 million in 2010 (see Figure 13)

\textsuperscript{12} [Census of India]
PwC’s 16th CEO Survey indicates that Indian CEOs are pursuing three pathways to creating value:

1. Targeting pockets of opportunities
2. Concentrating on the customer
3. Improving operational effectiveness

Where does your opportunity lie.

- The global emerging middle, with a larger amount of disposable income, a huge window of opportunity to businesses
- Creating a competitive edge by strengthening customer relationships and providing personalised services to customers
- The rapid speed of urbanisation, creating housing and infrastructure investment opportunities for financial institutions
- Investing in the talent pool to develop the right kind of skill sets to aid your business growth
**Technological change**

Technology has always shaped society and commerce in unpredictable ways, changing customer behaviour, spawning new enterprises and wiping out existing businesses that are unable to keep pace. As the speed of technological development accelerates, the risk of falling behind becomes more acute.

In the digital world, the internet, mobile phones, data analytics and cloud computing are well established.

Yet, many companies across all sectors are still grappling with how these developments will affect consumer expectations, the way they interact with their customers and the underlying business models.

The development of digital financial services offers a valuable opportunity to engage more closely with younger and more affluent consumers. It is also necessary to expand the availability of services in rural areas without the need for expensive and slow-to-develop branch and agency networks. Successful models in other countries include Kenya’s M-Pesa, which now has 15 million customers, more than all of the country’s banks put together.

Figure 14 below shows the 2011 income split of those who currently use a mobile to purchase financial services in the geographies surveyed. The figure shows that across all segments of the population, irrespective of the level of savings, there exists a significant demand for branchless banking.

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**Figure 14: The demand for branchless banking is significant in all segments of the population, regardless of geography**

<table>
<thead>
<tr>
<th>Proportion of responses, %</th>
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<tbody>
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<tr>
<td>Savings &gt;£25,000</td>
</tr>
<tr>
<td>Savings &gt;£50,000</td>
</tr>
</tbody>
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Sources: PwC Digital Tipping Point Survey 2011; (Based on approximately 3,000 responses) PwC analysis
Notes: *Geographies surveyed were United Kingdom, United Arab Emirates, Poland, Mexico, India, Hong Kong, France, China and Canada

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In India, technology has helped to stimulate the financial services sector, by overcoming physical and geographical barriers. Technology has helped automate processes, facilitated branchless banking, enabled product innovation and helped allow real-time service delivery across the financial services sector. The mobile revolution has played a huge role in taking banking to India’s un-banked population and it continues to be the one of the most critical pillars supporting the overall structure of the financial services sector in India. Mobile technology is low cost, affordable and easily available and can help financial service providers penetrate markets and increase their customer base. It also provides customers the option to pay for products in multiple ways.

Digital development will also make it easier for telecommunication companies and other new entrants to break into the market by leveraging their existing platforms at relatively lesser cost, highlighting the importance of looking beyond existing peers to identify the biggest potential threats to the business in the coming years.

It is interesting to note that even though India is an emerging technology hub, the country’s IT spend as compared to other countries is quite low. As forecasted for 2013, US IT spend will reach $634 bn and China will be around $173 bn.

Young urban consumers are already a key part of the aspirational emerging middle. The challenge will be how to engage with a digitally-enabled consumer segment that is creating new rules for choice, interaction and demand. In a society polarised between tech-savvy consumers and people with little or no familiarity with technology, the other main challenge is how to develop the access and vocational training needed to extend these openings to all.

The rapid emergence of social media in parallel with the rise of mobility has seen customers increasingly turn to their peers for information and advice, rather than to financial experts. As more financial services customers become ‘self-directed’, they are coming to rely less upon traditional sources of financial advice.

Business heads will need to work out how best to engage with and sell to the emerging middle and wider millennial generation in both rural and urban markets. This entails developing the digital distribution and social media presence to reach this highly networked segment. But the demands go further as businesses will need to find ways to tap into the mindspace of a segment that has little loyalty to traditional brands and looks to its virtual peers to provide key product assessment and recommendations.

Financial service institutions also need to develop innovative business models to tap into the ‘ecosystems’ of these customer segments and make maximum use of technology to gauge demand, communicate and distribute.

Firms are hesitant to make strong use of social media due to the challenges posed by information security and compliance with IT regulations

In a digital world, it will be harder for financial services businesses to differentiate themselves, as competition intensifies. The ease of switching afforded by digital technology could also drive down margins and profits. Some organisations could be strained to breaking point. In such a competitive scenario, it is necessary for business leaders to develop a vision and strategy to understand how digital transformation will impact customer demands. New operating models and means of interaction will be required to be successful in this changing business context. In most cases, it will prove more effective to work successfully with innovators from technology, telecommunications and other non-traditional banking providers, than to go at it alone. Identifying partners to acquire or help deliver the vision will be of critical importance.

Indian IT spending is projected to reach $71.5 billion in 2013, growing 7.7% from the $66.4 billion forecast for 2012.
What are the opportunities and challenges you are likely to face?

• Increasing reach and scalability of financial services businesses beyond Tier 1 and Tier 2 cities, with the use of technology

• Creating efficiency in operations and extending an enhanced customer experience

• Using the social media platform judiciously to discover new opportunities

• Creating a resilient risk management framework with the support of technology
The ‘war’ for natural resources

The expanding size and prosperity of the global population is leading to rapidly rising consumption and putting unsustainable pressures on the world’s most critical natural resources. Even basic commodities such as water are now in increasingly short supply, providing a spur for the development of new markets, technologies and investments on the one side and the potential for unrest, commercial disruption and protectionist behaviour on the other. The growing shortage of resources will be exacerbated by climate change, heightening catastrophe risk and putting further pressure on land, water supplies and food production. The ‘war’ for natural resources is likely to play out on multiple fronts. Examples include responses to the increase in water withdrawals, which are forecast to rise dramatically. Food production will naturally gravitate to locations with more plentiful sources of water, which may be outside a country’s border. This would have the effect of extending the supply chains for, and potential cost of, food production.

Scarcity of energy is a critical issue especially in South Asia. Around 400 million of Indians are without electricity, and there is a huge need to supply power to the residents of India, especially in the rural areas. Although generation capacity has increased each year, the rise in demand has outpaced the supply. This is clearly an area of concern as lack of electricity hampers the growth of the economy, limiting industrial output.

India faces the challenge of how to secure the oil, minerals and other natural resources it needs to meet rising demand and sustain expansion. The US is heading for energy independence by 2030, but India is still going to face a major deficit. India needs to find ways to secure strategic supplies. Notable developments include Reliance Industry’s investment in US shale gas and Adani Group’s coal mining ventures in Australia, which have made it India’s largest investor in the country. The further development of alternative energy sources and more efficient use of existing resources are also going to be crucial as India seeks to meet demand and manage its carbon footprint.

As countries vie to secure oil, minerals and other natural resources, an international financial services presence may be needed to support the investment and development projects that would allow India to compete for these resources. Notably, this would appear to be part of the rationale for Chinese banks’ investment in, and tie-ups with, a number of South African banks.

India’s approach to a lower-carbon growth strategy involves ensuring that policies are inclusive and span all national sectors, in order to reduce the transaction costs of implementing the policy. As countries vie to secure oil, minerals and other natural resources, an international financial services presence may be needed to support the investment and development projects that would allow India to compete for these resources. Notably, this would appear to be part of the rationale for Chinese banks’ investment in, and tie-ups with, a number of South African banks.

The potential ‘war’ for natural resources and the impact of climate change are phenomena that will have a fundamental impact on the way people live and companies do business. It’s likely to become one of the main, if not the key driver of, government policies. It will also open up new markets and business models for organisations that both understand the changing dynamics of supply and demand, and know how to mitigate the risks.
What you need to think about

• Increased pace of urbanisation is exerting pressure on the availability of natural resources like water, land, energy and clean air

• Helping businesses manage commodity, supply chain and other risks provides an opportunity and financial services businesses need to factor in shifts in investment risk and asset prices.
State-directed capitalism

Historically, India has always operated within a state-directed framework, unlike certain other countries. Globalisation is intensifying the competition between countries and cities. Local leaders are ever more aware of their sources of competitive advantage and how to attract the businesses, facilitate investment in infrastructure and the secure supply chains needed to make the most of this potential.

The five year plans play an important role in creating strategies for India’s growth going forward. One of the focus areas in these plans is infrastructure. In the twelfth five year plan (2012-17), infrastructure requirements have been projected to increase to Rs 41 lakh crore (10 per cent of GDP in 2016-17, from 8 per cent in 2011-12). This is intended to support economic growth. Over the plan period as a whole, infrastructure investment is estimated to be about 9.95 per cent of GDP. Financing of this investment will require a bulk contribution from the public sector, but this will have to be coupled with increased private investment. The share of private investment in infrastructure may need to increase to 50 per cent for the Twelfth Plan to be realised.

Financial institutions will be expected to play a key role in attracting and channelling the funds needed to meet the government’s private sector investment targets. At present, financial institutions only provide around a quarter of infrastructure investment – there is a particular need for more funding from the insurance and pensions sectors (these provide only 7% of total investment at present). India lacks depth in its debt, currency and derivative markets to create the necessary support and channels to meet investment priorities. The government and RBI have acknowledged that India’s corporate debt market lags behind other leading economies and that development of this market should be a priority.

At present, too little of the country’s vast savings are being channelled into the capital markets to support investment in infrastructure, business growth and other development opportunities. Tax breaks would help to stimulate greater consumer interest, though as outlined earlier this may be difficult in the current fiscal situation. Financial services businesses could themselves do much more to develop attractive products, distribution capabilities and investor confidence to build up capital market investment. They will, however, need the support of regulators and policymakers to make this happen.

India is under-penetrated in terms of banking – 40% of households have no bank account and the ratio of bank credit to GDP is less than 60%, compared to around 140% in East Asia. There is a similar picture in insurance, with premiums per capita of $64 in 2010, compared to a global average of $627 and the emerging market average of $110. In value terms, growth in the financial services sector has been primarily urban. The challenge is how to promote financial inclusion and develop a profitable model outside the main urban areas. This in turn demands simpler products, smart use of technology and support for greater financial literacy.

Encouraging savers to move funds to capital market investments is the overriding key to generating more finance for infrastructure and other key economic priorities. India’s savings rate is more than 30% of GDP, one of the highest in the world. But pension and fund management firms are finding it very difficult to attract these savings.

It is becoming immensely critical for industry and consumer groups to work together to influence and shape government policies. It will also be important for financial services businesses to develop a strong relationship with government to make sure their business strategy anticipates and is aligned to government priorities and investment plans.

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19 Twelfth Five Year Plan in India (2012-17): Instruments and approach, presentation by Rajib Das, Senior Research Fellow at the Institute for Indian Economic Studies, to the Policy Research Institute, Ministry of Finance, Japan, 07.02.12
20 Economic Times, 10.11.12
21 Twelfth Five Year Plan (2012-2017), Planning Commission, Government of India
22 Swiss Re Sigma World Insurance in 2010
23 Reserve Bank of India, 30.05.12
Aligning your growth plans

• Can you align your strategy to move towards the governments’ goal of financial inclusion with a low-cost distribution model?

• How can you operate efficiently in a constantly changing regulatory environment?

• Do the five year plans and annual financial budgets create opportunities for your business?

• To what extent does opportunity lie in establishing public-private partnerships to fund infrastructure development in India?
PwC’s Project Blue framework for India is designed to provide your business with a framework for organising your views on the global developments ahead, the implications for your business and your resulting vision for the future.

During our development of Project Blue, we’ve spoken with business leaders around the world to assess how these drivers will affect them. Drawing on these discussions and our research into the impact of the main forces of change highlights the key areas that boards will need to assess and address as they look to sustain and sharpen competitive relevance.

As the summary of a CEO’s agenda in the diagram above highlights, the underlying considerations CEOs will need to ponder include: what kind of leadership is required in this complex and uncertain environment, how their risk profile is likely to change, and what kind of governance and reporting systems will be required to plot a successful course through the changes ahead.

The businesses that come out on top will have a superior capacity for innovation and constant reinvention, will be agile enough to quickly capitalise on emerging opportunities and will have the strategic approach to talent needed to make sure that the right people are available in the right places at the right time. If your business is constantly scrambling to keep pace with unfolding events, it’s going to find itself on the back foot competitively and risks losing out.

We will continue to meet with the leaders of financial service institutions to help them respond to the fast changing environment in India and to assess their strategies. We believe that the Project Blue framework will significantly enhance our conversations.
Looking ahead

- How are you responding to the shift in the focus of global power and how can you develop your services and geographical reach to support this growth?

- How can you make your products and services relevant to a new consumer generation to increase financial activity?

- How will your marketing and distribution models need to evolve and how can you move to the next level of growth?

- Who will be your competitors ten years from now, and will your business model still be relevant?

We will continue to meet with the leaders of financial service institutions to help them respond to the fast changing environment in India and to assess their strategies. We believe that the Project Blue framework will significantly enhance our conversations.
# Appendix

## Global Project Blue Framework

<table>
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<tr>
<th>Adapt</th>
<th>Global instability</th>
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<tr>
<td>Regulatory environment</td>
<td>Fiscal pressures</td>
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### Project Blue Framework

<table>
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<tr>
<th>Rise and interconnectivity of the emerging markets (SAAAME)</th>
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<tbody>
<tr>
<td>• Economic strength</td>
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<tr>
<td>• Trade</td>
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<tr>
<td>• Foreign direct investment</td>
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<tr>
<td>• Capital balances</td>
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<tr>
<td>• Resource allocation</td>
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<tr>
<td>• Population</td>
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<table>
<thead>
<tr>
<th>Demographic change</th>
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<tbody>
<tr>
<td>• Population growth discrepancies</td>
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<td>• Ageing populations</td>
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<tr>
<td>• Changing family structures</td>
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<tr>
<td>• Belief structures</td>
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<table>
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<tr>
<th>Social and behavioural change</th>
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<tbody>
<tr>
<td>• Urbanisation</td>
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<td>• Global affluence</td>
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<tr>
<td>• Talent</td>
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<tr>
<td>• Changing customer behaviours – social media</td>
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<tr>
<td>• Attitudes to financial institutions</td>
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<table>
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<tr>
<th>Technological change</th>
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<tbody>
<tr>
<td>• Disruptive technologies impacting FS</td>
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<tr>
<td>• Digital and mobile</td>
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<tr>
<td>• Technological and scientific R&amp;D and innovation</td>
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<tr>
<th>War for natural resources</th>
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<tbody>
<tr>
<td>• Oil, gas and fossil fuels</td>
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<tr>
<td>• Food and water</td>
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<tr>
<td>• Key commodities</td>
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<tr>
<td>• Ecosystems</td>
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<tr>
<td>• Climate change and sustainability</td>
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<tr>
<th>Rise of state-directed capitalism</th>
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<tbody>
<tr>
<td>• State intervention</td>
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<tr>
<td>• Country/city economic strategies</td>
</tr>
<tr>
<td>• Investment strategies</td>
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<tr>
<td>• SWFs/development banks</td>
</tr>
</tbody>
</table>

Source: PwC Project Blue analysis
Notes
About PwC

PwC* helps organisations and individuals create the value they're looking for. We're a network of firms in 158 countries with more than 180,000 people who are committed to delivering quality in assurance, tax and advisory services.

PwC India refers to the network of PwC firms in India, having offices in: Ahmedabad, Bangalore, Chennai, Delhi NCR, Hyderabad, Kolkata, Mumbai and Pune. For more information about PwC India's service offerings, please visit www.pwc.in.

*PwC refers to PwC India and may sometimes refer to the PwC network. Each member firm is a separate legal entity. Please see www.pwc.com/structure for further details.

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