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THE IMPACT OF DIGITALIZATION AND FINACIAL PERFORMANCE OF BANKING SECTOR IN INDIA

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ABSTRACT:

Data is digitized, adopting technology is digitalized, and Banking is also digitized. Every industry is becoming digitized, including the financial sector. Utilizing technology, banks are able to reach out to more clients and are able to provide better services in the form of E-banking which has reduced expenses and increased income. Various India's commercial banks have embraced technology with MICR-based cheque processing, thus, banks are mechanized & automated. EFT, interconnected bank branches, and ATM Channels provides 24/7 banking, these initiatives are strong and now the RBI has strengthened bank payment and settlement processes, so now Digital change undermines the stability and integrity of finance and consumer protection.

KEYWORDS: Banking, Digitalization, online Banking, Technology, Services

INTRODUCTION

There has been a marked increase in both the dissemination of digital technologies and the degree of trust with which governments and individuals have adopted them. The information and communication technology industry has not only revolutionised “the services sector in India” but also throughout whole world. The “digitalization of services” has had an impact on the lives of people of all socioeconomic backgrounds, transforming the way in which we bank, shop, travel, and learn, among other things. The implementation of information and communications technology into the banking industry has resulted in a shift in how financial institutions throughout the world conduct their business. The conventional approach to banking has been put to the test as a result of these new potential for the banking industry. To keep their current clients and get a larger portion of the market, financial institutions in India are rushing to adopt digital banking methods. This lightning-fast speed of digitalization in India's financial sector may be traced back to two primary drivers. First and foremost, Indian banks now have the opportunity to follow in the footsteps of their

worldwide competitors and pick up useful tips along the way. Second, they are in a position to capitalise on established technology and markets, which will ultimately lead to price reductions. The banking business in India has been able to reap the benefits of digitalization thanks to the increasing Internet penetration that has occurred there. These advantages are not limited to simply the economic elements; rather, it brings under its wing the happiness of both customers and employees, both of which are at the very heart of any corporate organisation. Customers' expectations about the security of their funds have evolved significantly in recent decades. They want to have constant access to the cash in their bank accounts as well as the capacity to fulfil their financial responsibilities in real time. The evolution of technology has made it possible for banks to fulfil the ever-increasing demands placed on them by their customers. Internet banking and the technologies that have developed from it, such as "ATMs, credit cards, debit cards, mobile banking applications & point-of-sale systems", have provided significant benefits to clients while simultaneously reducing the amount of labour required by bank staff. Internet banking and ATMs, in particular, have helped clients become less dependent on physical bank branches, which have led to higher productivity among bank personnel. It has been established that online banking is more effective in terms of operations ("Malhotra and Singh, 2006").

"Digital banking" has developed into strategic instrument that, on the one hand, may increase efficacy and operational control, and, on the other hand, can reduce costs by applying mechanised procedures, which contributes to improved production & profitability. Researchers intend an opinion that the internet fundamentally altered way that "banks" operate & completely transformed the sector. The internet has brought about a slow but steady transformation in the financial sector in India over the past two decades, and this transformation has been observed. The internet continues to reveal new facets, which makes it possible for financial institutions to broaden their scope of online-based services. The predictions made in the past by DeYoung (2001a) that the internet will significantly alter the method in which banks create their services are proving to be accurate. However, other writers have found that it works best as a supplement to traditional brick-and-mortar locations rather than as a replacement for them. The transformations that the internet has brought about in the banking business in India raise a few problems. To begin, it is important to determine whether or not these shifts in the banking business are being driven by either profitability or the desire to obtain a competitive advantage over their rivals. Are changes being made at banks in an effort to enhance their performance? This study provides answers to such queries and adds new information to the pool of previously accumulated knowledge.

TRANSFORMATION OF INDIA'S BANKING SECTOR INTO THE DIGITAL AGE

In the year 1996, ICICI –"first financial institution in India"- provided "banking services" through the internet. Other banks quickly followed following, despite the fact that the first years of digital banking were marked by limited accessibility due to the prohibitive cost of internet access. The transition toward digital banking began to gain steam as the price of internet access began to decrease and as the scope of services that could be obtained digitally grew. The public sector banks, which make up the majority of the banking industry, were slow to adopt digital banking services despite having the highest market share. As traditional financial institutions became more aware of the cost savings and income opportunities afforded by digital banking, they began to view it not as an "additional service" but rather as an "extension of conventional method of banking". Rise of "online banking" has resulted in the establishment of India's first bank that is dedicated only to digital transactions in the year 2016, under the name Digi bank. Since then, a great number of new banks that operate only online have opened their doors. The sheer volume of digital transactions carried

out in India over the course of several decades explains the country's rapid adoption of digital banking.

LITERATURE REVIEW

A discussion has been going on all over the world among academics concerning the implications that “digital banking” has on overall “performance of banks”. The following is a review of the previously published material:

“Keribal and Debener (2020)” conducted research on “bank performance” by employing “digitalization as a proxy” & used “text mining” as a method to “extract unstructured information” from “banks' annual reports”. They discovered that the phrase “digitization” was used more frequently than other terms, which suggests that there was greater investment in digital platform. A review of the current body of data demonstrates that experts have discovered that electronic banking may have both a beneficial and a negative influence on the functioning of banks. On the other hand, research paucity on implications of “digital banking” on the overall “performance of banks in India” is there. This work makes an effort to close the knowledge gap.

Shelar and Kumar (2019) analysed the impact that digitization, in the form of an increase in the volume of electronic payments, had on the “working capital of the Kotak Mahindra bank”, taking into account aspects such as profitability, liquidity, and efficiency. They came to the conclusion that although digitization has enhanced transparency, decreased the amount of paper work, and reduced the workforce, it has also increased costs (both maintenance and fixed). In addition, they came to the conclusion that in the short-run, profitability and efficiency would not be immediately impacted by digitization.

Kotarba, M. (2017) used these five measures to determine how far along the digitization process we are: “economy, society, industry, enterprise & customers”. Primary goal was to provide measures that could be utilised for the assessment of the progress made digitally. In addition, it was discovered that the economy, society, and industry do not have distinct boundaries; yet, in order to accurately measure efficiency, one must place their attention at “technologically oriented (internet-centric) & end user pleasure (client centric)”.

Malhotra & Singh (2010) - According to the findings of the study, online banks had lower rates of profitability compared to traditional banks, which led the researchers to conclude that “internet banking” is not a key factor in determining “profitability”. They said expansion of “online banking” was due to “private banks & banks” based in other countries.

RESEARCH OBJECTIVES

- To investigate how the digitalization of business may affect profits.
- To investigate how the digitalization of processes would affect the costs of such processes.
- To investigate if the adoption of digital technology has led to increased productivity among staff members.
- To investigate how the advent of digital technology has changed the prospects for company.
- To investigate the difficulties associated with using digital banking.
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RESEARCH METHODOLOGY

The survey was carried out to ascertain the perspectives of bankers on the effect that digitalization has on bank performance. The study is exploratory and descriptive in character, drawing on the insights gained from interviews with bankers. Interviews with bank workers with a semi-structured format were carried out in person and over the phone with the personnel. Interviews were conducted with thirty individuals working at ten banks. Depending on many “classifications of banks” that are active in “India”, this sample was

taken. “There are 1cooperative bank &1 regional rural bank together with 4 banks from the public sector &2 banks from the private sector”. There are also 2 banks from other countries. Banks from the public sector, private sector, and overseas were chosen based on their market capitalization. The researchers went with a cooperative and a regional rural bank since that was the most convenient option for them. “The State Bank of India, Punjab National Bank, Bank of Baroda & UCO Bank are the 4 public sector banks” that are taken into consideration for the study. 2 examples of private financial institutions are “HDFC Bank & ICICI Bank”. “Citi Bank & Standard Chartered Bank” are the 2 international financial institutions that will be analysed in this study. Within the category of cooperative and regional rural bank, the Kaira District cooperative and the Gramin Bank were chosen. The many financial institutions that were chosen each provide their customers with unique electronic banking options. Some companies dominate their field, while others are making rapid strides toward being competitive. In addition to questions concerning the interviewees' demographics, six primary questions were posed to them. In areas where there was a need, follow-up questions were asked. The answers to the six most important questions are as follows:

1. Do you believe that the rise of digital banking has led to increased profits?
2. Do you believe that the advent of digital banking has led to an increase in the operational efficiency of financial institutions?
3. Do you believe that the utilisation of digital platforms has resulted in a decrease in costs?
4. Do you believe that the advent of digital banking has made it possible for banks to increase their businesses?
5. Do you believe that the demand for financial services that are provided over the internet will continue to increase?
6. In your opinion, what are some of the obstacles that are preventing the expansion of digital banking in India?

RESULTS

The interview started out with the researchers asking questions that were connected to demographics. This has been done in order to acquire a rough idea of whether the responses varied according to gender, age, or experience in the workforce. In 2015, regional and rural banks were finally given permission to offer internet banking services (subject to certain requirements). The manager of the RRB that we spoke with confirmed that the organisation does not offer internet banking. On the other hand, he believed that in the not-too-distant future, they will be required to adjust to this novel financial occurrence.

In the first section, demographic information about the interviewees is presented (Table 1)

TABLE 1: DEMOGRAPHY OF INTERVIEWEES

DEMOGRAPHY	TOTAL
AGE	
Below 30 Years	12
30 – 45 Years	10
Above 45 Years	08
GENDER	
Male	16
Female	14
SECTOR	
Public Sector	16

Private Sector	08
Co-operative	01
Foreign Banks	04
Rural Regional Banks	01
DESIGNATION	
Non-managerial	08
Managerial	22
BANKING INDUSTRY WORKING EXPERIENCE	
Below 10 Years	06
10-20 Years	13
Above 20 Years	11

As can be seen from the table above, the interviewee panel consisted of persons from a variety of genders and types of banks, as well as people holding a variety of job titles. The researchers did not see any correlation between the respondents' age, gender, or work experience and the replies they provided. Only a portion of the comments that were given by respondents have been included in the next section's citations. In several instances, the replies were rethought so that they would be more relevant to the research that we are doing. However, in order to ensure that they were not misquoting anyone, the researchers made sure to get further confirmation from the respondents before quoting the respondent whose answer had been reframed.

Interview Snippets Relating to the Profitability Effects of Digital Banking are Presented in Section 2

In the 2nd section, some statements from the respondents about the profitability of banks as a result of digitization are shown.

A manager from the State Bank of India, when asked about the bank's profitability, says:

“Profitability is a difficult concept. It has different dimensions to it. Looking at the profitability parameters, they have certainly been on the up side in recent years. However, attributing it all to the digitalization in banks would not be correct. It played its part along with other factors.”

The following was stated by yet another management from HDFC banks:

“Apart from the regular economic factors. Digitalization probably has had the biggest impact on bank profitability in recent times. It might look farfetched but in my opinion financial statements of the banking industry would not have been close to what it is today if not for digitalization.”

The Manager of the Kaira District Cooperative has the following to say:

“Statistically speaking you will see an association between digital banking and bank profits. That might not be the case always. Banks with resources have definitely found digitalization to be profitable but the small banks have suffered the adverse effects of digitalization. For us it is more about retaining customers than profitability that is driving us towards digitalization.”

Excerpts from Interviews Relating to the Financial Impact of Digital Banking are Presented in Section 3.

In the 3rd section, some of the replies from those who were interviewed on the cost impacts of bank digitalization are shown.

When asked to describe the cost impacts, a management from Canara Bank said as follows:

“I see digitalization having two way effects on cost. First, the initial cost of setting up infrastructure for offering digital services and second maintenance cost of that infrastructure which are extra cost that we have to incur these days. However, we have certainly saved some cost due to digitalized services. I can’t say for sure if the cost saved is more or less than the cost incurred.”

The following is what one more management at ICICI has to say:

“On cost front I think we are saving a lot. We would have needed more branches to cater to the customers we have today if not for digitalization. Therefore, the number of branches has not increased proportionately to the number of customers. Requirement of office space has also shrunk as the number of customers visiting branches have come down. So we can now work with smaller branches.”

From the Citibank manager:

“Any organization before taking a decision takes into consideration two things which cost and customer satisfaction. Now a customer visiting a branch costs a lot of money and we are saving that by offering him services digitally. I think one of the reasons of our cost cuts is due to our global presence. We have been quick in adapting to best industry practices.”

Within the context of human resources, the manager of the Kaira District Bank said as follows:

“One of the biggest expenses that an organization has to incur is towards its human resource. To handle the growth in business that we have witnessed we would have needed more employees. Digital banking has allowed saving that cost. The cost that we save is a lot more than we have to incur on IT infrastructure and its maintenance.”

The manager at India's State Bank has said:

“A lot of money also went into cash handling earlier. The increase in digital transactions has brought down those expenses. In the initial years we did have incur cost for both digital platforms as well as cash handling. However, with rising internet users people are using more and more digital platforms. Risk relating to cash handling has also come down which effectively reduces premiums we pay for insuring our cash.”

The Interview (Section 4): Various excerpts connected to the topic of efficiency in digital banking

The following was stated by a manager of the Punjab National Bank:

“I feel our efficiency as an organization has improved tremendously. We can now do more work with less time and resources when compared to pre digitalization era. In the initial years we did face problems but as it all sorted out we have been doing well.”

Another one of Standard Chartered's managers had this to say:

“I see efficiency from two aspects. First the organizational or institutional efficiency. Second efficiency of the human resource. We have improved on both fronts. I will give an example to make you understand better. As making payments with cheques without any digital process took a lot of time with digital banking, you can make instant payments anytime of the day. Now efficiency of employees I can best explain with an increase in business per employee. It is true not only for us but everyone in the industry.”

This is what a management from the Kotak Mahindra bank has said:

“Going digital is cost saving and efficient that is the reason you see a shift from traditional brick and mortar based business models to internet based business models. Due to its efficiency, you see a rise number of banks that are only operating digitally. So yes digitalization has improved bank efficiency.”

Excerpts from Interviews Relating to the Effects of Digital Banking on Business Growth are Presented in Section 5.

The following was stated by a manager working for State Bank of India:

“Digital banking has allowed us to effectively increase our financial resources. Like earlier people would keep lot cash in hand to meet out their expenses. With digital transactions going up the use of cash has come down. So all the money stays in the bank which we then use for expanding our business”

The following was stated by an ICICI manager:

“Growth in banking business is the result of other economic factors. Though banks have themselves expanded their scope of operations. We now provide a range of other financial services that we did not offer earlier. I think digitalization has allowed us opportunities to get into those verticals.”

The following was stated by a manager of the Kaira District Cooperative:

“I don’t see the growth in banking business being related to the digitalization revolution. The growth of banking industry is the result of overall economic development. Government policies regarding financial inclusion and financial literacy is helped our business. The growth of digital banking is however linked to increased internet penetration.”

The following was stated by a manager at Citibank:

“I see growth of other digital services also contributing to the growth of banking business. From booking of train and air tickets to buying clothes can all be done online? In order to do these things online you need to pay digitally and to pay digitally you need a bank account. So the ease that digital banking provides has in my opinion some way contributed to growth in banking business.”

Excerpts from Interviews Regarding the Obstacles That Digital Banking Faces Section 6

A manager from HDFC had this to say:

“I see digital offerings from the likes of Google and Amazon a serious problem for us. We stand to lose digital product customers to them if we do not improve our products to their level. I also see convincing customers who are not literate and rural customers to use our digital platforms as a challenge. Internet penetration increasing in rural areas rapidly gives us a huge market in those areas. Though we are increasing our digital presence in rural areas, we still have a long way to go.”

The following was stated by a manager of the Punjab National Bank:

“Automated process has taken away a lot jobs. Now moving more towards automation we need to train our employees to help them transit into newer roles. Our public sector banks are one of the biggest employers not just in India but also across the globe. Therefore, we need to strike a balance between automation and employee welfare. I think to do that is a big challenge for us.”

One Allahabad Bank manager explains:

“I see security as the biggest the blockade in the growth of digital banking. Rising phishing frauds and data privacy issues that we face is a serious threat that we need to tackle. Both these issues affect the confidence that a customer places in us. Loosing customer confidence is eventually loosing customer. The challenges that we face in our growth can only overcome with our individual efforts. Right government policies and our sustained efforts will change forever how we see banks and banking.”

Conclusions drawn from the Interviews:

- The researchers could not detect any influence of respondents' sexual orientation on the replies they received. However, there were some disparities in the replies of the workers depending on factors such as their age and the amount of work experience they had. Due to the small size of the sample, it was not possible to determine whether or not there was a statistically significant gap in the replies provided by workers who varied in age and years of experience in the workforce.
- According to the findings of the researchers, regional rural banks do not offer digital services, with the exception of those that satisfy specific requirements set by the Reserve Bank of India. Even those RRBs, which allowed digital banking, cannot offer transactional services to its customers. The respondent however believes that RRBs will also provide digital based services in the near future.
- According to the findings of the research, the profitability of banks has increased thanks to digital banking. The beneficial function that digital banking may play in enhancing profitability indicators is a topic of consensus among all responders. The respondents also pointed out other reasons as well for increasing profits in the banking industry. Some respondents were of opinion that bigger banks enjoyed more benefits of digitalization due to their large customer base. Even among big banks private and foreign banks obtained better results of digitalization as their ratio digital banking users to total users were better than public sector banks.
- The financial services sector has been completely revolutionised as a result of the advent of digital technology. The notion that a client is a customer of a specific branch has been superseded by the notion that a consumer is a customer of the entire bank. In the initial years of digitalization, bank employees were averse to technology fearing job security. Acceptability among employee as well as customers has gone up in the recent years. Customers and employees are asking for more automated processes to reduce customer's branch dependency.
- Everyone who participated in the survey agreed that the adoption of digital technology had increased the productivity of both employees and institutions. Automated processes have brought down the level of manual labour and reduced errors. Although employee workload have not gone down its nature has changed over the years due to digitalization. Nature of work has evolved from transaction banking to business development. Post the digitalization era both business and profit per employee has been increasing consistently.
- All of the respondents are in agreement that the advent of digitization has helped banks significantly reduce their operating expenses. The infrastructure cost for offering digital services are in the opinion of majority respondents lesser when compared to branch based services. Banks that have a smaller customer base consider digital services to be an extra burden on their financials. Their limited number of branches are well placed to cater their small customer base but due competition they have to offer digital services. For example when a customer steps into a bank branch to withdraw money, it costs more than an ATM transaction. An ATM transaction also costs more than a transaction done on other digital platforms. As more and more

people shift towards digital services this cost may go down further owing to economies of scale. Benefits of these cost reductions have passed on to customers making them move towards conventional banks from local moneylenders.

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- Researchers discovered that banks are leveraging technology to diversify their offerings beyond traditional banking into other areas of the financial industry. Banks by providing all financial services under one-roof banks have increased their customers manifold. Using their digital platforms banks have been successful in cross selling other financial products. Bankers however also attribute rise in business and revenue of banks to other economic factors as well. Some bankers are of the opinion that as internet penetration increases in rural areas private and foreign banks will have more opportunities there. As maintaining a physical branch was costly, these banks hardly had any presence in these areas.
- The increasing digitization of banking systems has been shown to be motivated not just by a need for a competitive edge but also by a desire to maximise profits. Cooperative banks and Regional Rural Banks are lagging behind in terms of services provided digitally. However, they are slowly moving towards digital services allowing them to provide better services to their customers. Since internet penetration and literacy in rural areas is still low, RRBs are managing without it for now. They will have to start offering digital services in the future, if they are to survive the banking revolution.
- Challenges to digitization occur on both sides of the company. When seen from the standpoint of a bank, the most significant concern is security. Banks are suffering financial losses as a result of cyberattacks on their ATMs and websites. From the point of view of the client, issues such as awareness, education, and acceptance were recognised as problems that needed to be fixed. Bankers feel that these challenges cannot be address alone and banking industry will need government support to help overcome it. Banks are also facing stiff competition from tech giants such as Google and Amazon, who have better digital products than banks. To ward off this challenge they need to continuously upgrade their products and make it more users friendly.

CONCLUSION & DISCUSSION

The financial services sector has been completely revolutionised as a result of the advent of digital technology. The notion that a client is a customer of a specific branch has been superseded by the notion that a consumer is a customer of the entire bank. During the early years of digitization, top bank personnel were resistant to technology because of worry that they would lose their jobs and be unable to adjust to changing circumstances. In recent years, there has been a rise in the level of acceptance of automated operations not just among employees but also among customers. Customers and staff are expressing a desire for automated processes that will lessen their need on physical branches. Customers now have more freedom to satisfy their financial responsibilities at a time and place that is most convenient for them thanks to digitalization. The Indian banking sector is currently experiencing a price war as a result of the increasing competition. More than ever, financial

institutions concentrated on cutting their operating expenses. The adoption of digital technology in banking has shown to be an effective strategic strategy for lowering operating expenses. However, banks have incurred significant expenditures in the form of infrastructure and training costs in order to provide digital banking services. These costs have been borne by the banks. In most cases, these expenditures are repaid in a relatively short amount of time, and the company does not have to wait several years to do so. When more individuals switch to digital platforms, banks will reap the benefits of lower costs in greater amounts. The decline in the cost of technology will also help financial institutions like banks. The transition away from traditional banking and toward digital ways of delivering services has had a favourable impact on the profitability of banks. Clients that seek out digital services tend to be highly happy customers, which in turn makes them loyal to their banks, which would otherwise have to spend a lot of money to keep them as customers. As a result, the move to digital banking can result in an increase in profits. The pace of economic growth in India has helped banks in ways to migrate to digital services by helping to provide a consistent flow of revenue. This has made it possible for banks to advance in these directions. The fact that digital banking may generate a profit has encouraged non-traditional firms to enter the market and provide digital financial services. Since digitization was introduced, there has been an overall improvement in the efficiency of the financial business. It is expected that the system would become more efficient as a result of the concerted efforts of the business and the government to reduce the prevalence of cash in Indian society. An increase in employee productivity is possible through the use of employee training and feedback, both of which will make the employees' transition to the ever-evolving technology more seamless and straightforward. Because of the government's push toward a cashless society and the creation of a digital India, digital banking solutions are now absolutely necessary. Because a truly digital India is impossible to achieve without an advanced digital banking infrastructure. The rise of the digital banking system, which was already increasing rapidly, has been further complemented by technology efforts such as the Unified Payments Interface (UPI). In the future, financial institutions will not only need to fulfil the ever-increasing requirements of one billion consumers who are connected to the internet, but they will also need to ensure that they are leagues ahead of the new competitors. The difficulties associated with digital banking are constantly discussed by both the government and business participants in the industry. It's encouraging to see that digital banking is making headway in more remote locations as penetration increases there. Now, rural populations might be encouraged to adopt digital platforms through engagement efforts by banks. Customers will be more likely to become used to digital banking if they are offered increased incentives for adopting digital modes of transaction. Customers, particularly those living in remote regions, will get the confidence necessary to use digital platforms if they have access to high-speed internet and more awareness programmes.

SUGGESTIONS

This section offers some concrete recommendations for overcoming obstacles that stand in the way of the widespread adoption of digital banking in India. The proposals included in the next part include both the solutions developed by researchers themselves as well as those developed by bankers in order to overcome difficulties associated with digital banking in India. The following are some recommendations:

- The government should issue directives to banks requiring them to devote a greater portion of their corporate social responsibility (CSR) funding to resolving issues associated with digital banking.

- The ability to interact directly with consumers is a significant benefit enjoyed by banks. They need to participate in programmes designed to raise the consumers' level of awareness.
- It is necessary for the Reserve Bank of India to develop and implement policies that discourage the use of cash.
- In addition, in order for banks to increase the productivity of their workers, they need to bring in the most recent technology from other countries and provide ongoing training to workers at regular intervals. This will allow workers to more easily adjust to new circumstances.
- In order for financial institutions to lower their overall operating expenses, it is imperative that they devise plans to lessen the average number of customers served by each branch.
- It is recommended that monetary incentives be provided by both the government and banks in order to encourage cashless transactions.
- It is necessary for the sponsoring banks of RRBs to include the CBS of RRBs into their own core banking systems.
- It should be requested of firms who provide telecommunications services that they provide high-speed internet access to places that are rural.

INDICATIONS FOR FURTHER STUDY

The nature of this study was qualitative, and it used an exploratory approach. In the future, research may be undertaken utilising empirical data from the banking sector to investigate the influence that digitization has on the profitability of banks. For the purpose of determining how various factors, such as utilisation of automated teller machines, web-based transactions, return on investment, point-of-sale transactions, and so on, affect bank profitability; several factors can be taken into consideration.

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