“AN ANALYSIS OF RETAIL BANKING IN INDIAN BANKING SECTOR”

A Project Submitted to

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of Bachelor in Commerce (Accounting and finance)

Under the Faculty of Commerce

BY

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JNAN VIKAS MANDAL’S COLLEGE

Mohanlal Raichand Mehta College of Commerce

Diwali Maa College of Science

Amritlal Raichand Mehta College of Arts

Dr. R.T. Doshi College of Computer Science

NAAC Re-Accredited Grade 'A+' (CGPA : 3.31) (3rd Cycle)

Sector-19, Airoli, Navi Mumbai, Maharashtra 400708

Project Report On

FEBURARY 2024

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Certificate

This is to certify that **Miss. Hrashada Vasu Rangaswami** has worked and duly completed her/his project work for the degree of Bachelor in Commerce (Accounting and Finance) under the faculty of Commerce in the subject of **Accounting and Finance** and her / his project is entitled, "**AN ANALYSIS OF RETAIL BANKING IN INDIAN BANKING SECTOR**" under my supervision.

I further certify that the entire work has been done by the leaner under my guidance and that no part of it has been submitted previously for any Degree of Diploma of any University.

It is her/ his own work and facts reported by her/his personal findings and investigation.

Guidence Teacher

ASST. PROF. DR. KISHOR CHAUHAN

Date of Submission

DECLARATION

I the undersigned **Miss . Harshada Vasu Rangaswami** here by, declare that the work embodied in this project work title "**AN ANALYSIS OF RETAIL BANKING IN INDIAN BANKING SECTOR**", forms my own contribution to the research work carried out under the guidance of **ASST . PROF . DR . KISHOR CHAUHAN** is a result of my own research work has not been previously submitted to any other University for any other Degree / Diploma to this or any other University.

Wherever reference has been made to previous work of others, it has been clearly indicated as such and included in bibliography.

I, here by further declare that all information of this document has been obtained and presented in accordance with academic rules and ethical conduct.

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EXECUTIVE SUMMARY

Retail banking has been expanding in every economy and India is no exception. Availability of superior technology drives retail banking into greater heights. Retail lending gives fillip to consumer and manufacturing Industries.

Retail banking in India is growing at a great speed and major players in the banking and financial services sector are contending with each other to penetrate into the market with their competencies synergizing with software and the IT. The concept of retail banking is not new to Indian banks, as some nationalized banks have been giving a limited retail services. With the changing trends in the income patterns and distribution in the wake of liberalization and globalization, Indian banks are turning to be media-expansive, offering services through the ATMs, tele-banking and online banking.

As major players are exercising to cater to the retail banking needs of the second largest populated economy, more focus on local needs along with the developing trends in consumer spending is the need of the hour. As of now, customization of products to the local needs is less than the expectations of the customers. Focus on local needs may give an opportunity and access to the rural market where equivalent opportunity is available for immediate expansion.

About a decade of development in the banking sector as a consequence of reforms, a large pie of the economy is still untouched by the modern banking services. Retail banking is promising a future for the bankers, an opportunity for the unemployed, enhanced service to the consumers and boost-up to the consumer goods industry.

So keeping in mind the importance of the whole banking industry in Indian economy this report is divided into two parts. The first part of this report deals with The Indian banking Sector as a whole where we have included the basic functions of a bank, Banking in India, Basel accords and Asset-Liability management in banks.

The second and the major part of this report covers Retail Banking and concerned topics such as emerging trends in retail banking, products and services offered, NPAs in retail banking, SWOT and future of retail banking followed by a questionnaire which shows the effect of recession on the products and services offered by the banks involved in Retail Banking.

CHAPTER-1

INTRODUCTION
OF
BANKING INDUSTRY

INTRODUCTION OF BANKING INDUSTRY

Introduction to Banks

Banks have influenced economies and politics for centuries. Historically, the primary purpose of a bank was to provide loans to trading companies. Banks provided funds to allow businesses to purchase inventory and collected those funds back with interest when the goods were sold. For centuries, the banking industry only dealt with businesses, not consumers.

Definition:

A *banker* or *bank* is a financial institution whose primary activity is to act as a payment agent for customers and to borrow and lend money.

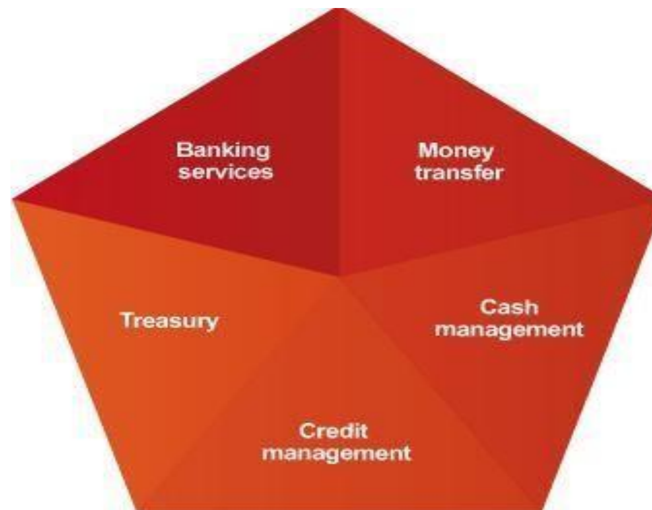
The definition of a bank varies from country to country. Under English common law, a banker is defined as a person who carries on the business of banking, which is specified as:

- Conducting current accounts for his customers
- Paying cheques drawn on him
- Collecting cheques for his customers

Other statutory definitions:

- "*Banking business*" means the business of receiving money on current or deposit account, paying and collecting cheques drawn by or paid in by customers, making of advances to customers.
- "*Banking business*" means the business of either or both of the following:

a) Receiving from the general public money on current, deposit, savings or other similar account repayable on demand or within less than 3 months or with a period of call or notice of less than that period.
b) Paying or collecting cheques drawn by or paid in by customers.



Traditional Banking Activities

- Banks act as payment agents by conducting checking or current accounts for customers, paying cheques drawn by customers on the bank and collecting cheques deposited to customers' current accounts.
- Banks also enable customer payments via other payment methods such as telegraphic transfer, EFTPOS (electronic transfer of funds at point of sales), and ATM.
- Banks provide almost all payment services and a bank account is considered significant by most businesses, individuals and governments. Non-banks that provide payment services such as remittance, companies do not consider them an adequate substitute for having a bank account.
- Banks borrow money by accepting funds deposited on current account, accepting term deposits and by issuing debt securities such as banknotes and bonds.
- Banks lend money by making advances to customers on current account, by making instalment loans and by investing in marketable debt securities and other forms of money lending.
- Banks borrow and lend most funds from households and non-financial businesses, but non-bank lenders provide a significant and in many cases adequate substitute for bank loans and money market funds, cash management trusts and other non-bank financial institutions in many cases provide an adequate substitute to banks for lending savings to.

Economic functions

The economic functions of banks include:

- Bank issues money in the form of banknotes and current accounts subject to payment at the customer's order. These claims on banks can act as money because they are negotiable and repayable on demand and hence valued at par and effectively transferable by mere delivery in the case of banknotes or by drawing a cheque.
- For netting and settlement of payments banks act both as collection agent and paying agents for customers and participate in inter-bank clearing and settlement systems to collect, present, be presented with and pay payment instruments. This enables banks to economize on reserves held for settlement of payments, since inward and outward payments offset each other. It also enables payment flows between geographical areas, reducing the cost of settling payments.
- For credit quality improvement banks lend money to quality commercial and personal borrowers. The improvement comes from diversification of the bank's assets and bank's own capital which provides a buffer to absorb losses without defaulting on its own obligations.
- For maturity transformation banks borrow more on demand debt and short term debt, but provide more long term loans. Bank can do this because they can aggregate issues (accepting deposits and issuing banknotes) and redemptions (withdrawals and redemptions of banknotes), maintain reserves of cash, invest in marketable securities that can be readily converted to cash if needed and raise funds as needed from various sources (wholesale cash markets and securities markets) because they have a high and more well known credit quality than most other borrowers.

Law of Banking

Banking law is based on a contractual analysis of the relationship between the bank and the customer. The definition of bank is mentioned earlier, whereas a customer is any person for whom the bank agrees to conduct an account.

The law implies following rights and obligations:

- The bank account balance is the financial position between the bank and the customer, when the account is in credit, the bank owes the balance to the customer, when the account is overdrawn and the customer owes the balance to the bank.
- The bank can pay the customer's cheques up to the amount standing to the credit of the customer's account plus any agreed overdraft limit.
- The bank may not pay from the customer's account without a mandate from the customer, e.g. a cheque drawn by the customer.
- The bank engages to promptly collect the cheques deposited to the customer's account as the customer's agent and to credit the proceeds to the customer's account.

- The bank has a right to combine the customer's accounts, since each account is just an aspect of the same credit relationship.
- The bank has a lien on cheques deposited to the customer's account, to the extent that the customer is indebted to the bank.
- The bank must not disclose the details of the transactions going through the customer's account unless the customer consents, there is a public duty to disclose, the bank's interests require it, or under compulsion of law.
- The bank must not close a customer's account without reasonable notice to the customer, because cheques are outstanding in the ordinary course of business for several days.

These implied contractual terms may be modified by express agreement between the customer and the bank.

Banking Channels

Banks offer many different channels to access their banking and other services:

- **A branch, banking centre or financial centre** is a retail location where a bank or financial institution offers a wide array of face-to-face service to its customers
- **ATM** is a computerised telecommunications device that provides a financial institution's customers a method of financial transactions in a public space without the need for a human clerk or bank teller. Most banks now have more ATMs than branches, and ATMs are providing a wider range of services to a wider range of users. Most ATMs enable card holders from other banks to get their account balance and withdraw cash, even if the card is issued by a foreign bank.
- **Mail** is a postal system where written documents typically enclosed in envelopes and also small packages containing other matters are delivered to destinations around the world. This can be used to deposit cheques and to send orders to the bank to pay money to third parties. Banks also normally use mail to deliver periodic account statements to customers.
- **Telephone banking** allows its customers to perform transactions over the telephone. This normally includes bill payments for bills from major billers (e.g. for electricity).
- **Online banking** is a term used for performing transactions, payments etc. over the internet through a bank, credit union or building society's secure website.

Types of Banks

Banks' activities can be divided into**:**

- **Retail banks**- dealing directly with individuals and small businesses
- **Business banks**- providing services to mid-market business
- **Corporate banks**- directed at large business entities
- **Private banks**- providing wealth management services to high net worth individuals and families
- **Investment banks**- relating to activities of the financial markets.

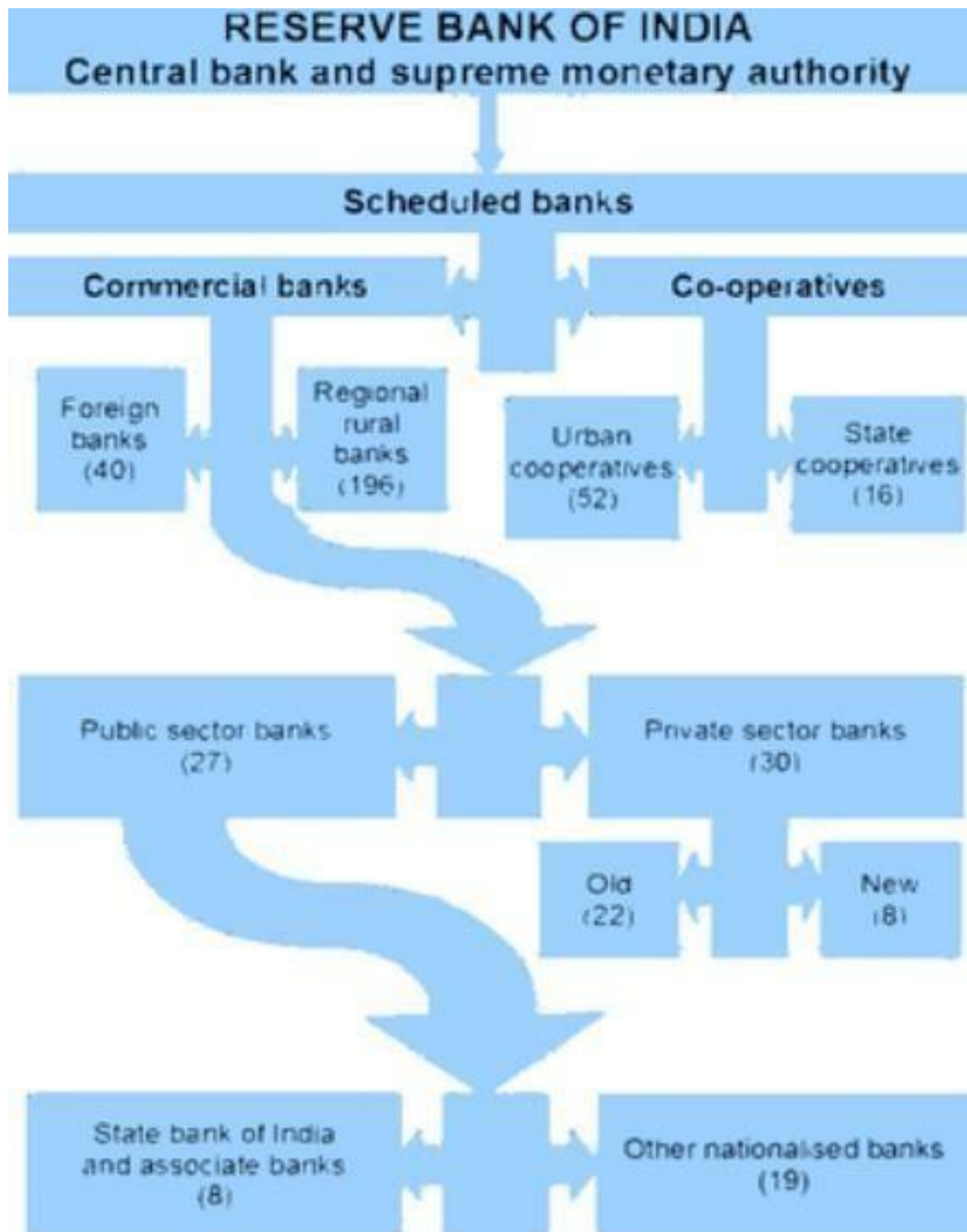
Most banks are profit-making private enterprises. However, some are owned by government or have non-profits motives.

Central banks are normally government owned banks, often charged with quasi-regulatory responsibilities, e.g. supervising commercial banks or controlling the cash interest rate. They generally provide liquidity to the banking system and act as the **lender of last resort** in event of a crisis.

Types of Investment Banks:

- **Investment Banks** "underwrite" (guarantee the sale of) stock and bond issues, trade for their own accounts, make markets, and advise corporations on capital markets activities such as mergers and acquisitions.
- **Merchant Banks** were traditionally banks which engaged in trade finance. The modern definition, however, refers to banks which provide capital to firms in the form of shares rather than loans. Unlike venture capital firms, they tend not to invest in new companies.
- **Universal Banks** more commonly known as financial service companies, are engaged in several of these activities. Large financial institutions are similarly diversified and engage in multiple activities.

Banking in India



Early History

- The first fully Indian owned bank was the Allahabad Bank, established in 1865. However, at the end of late-18th century, there were hardly any banks in India in the modern sense of the term.

- The American Civil War stopped the supply of cotton to Lancashire from the Confederate States. Promoters opened banks to finance trading in Indian cotton. With large exposure to speculative ventures, most of the banks opened in India during that period failed.
- The depositors lost money and lost interest in keeping deposits with banks.
- Foreign banks too started to arrive, particularly in Calcutta, in the 1860s. Calcutta was the most active trading port in India, mainly due to the trade of the British Empire, and so became a banking centre.
- Around the turn of the 20th Century, the Indian economy was passing through a relative period of stability. Indians had established small banks, most of which served particular ethnic and religious communities.
- The presidency banks dominated banking in India. There were also some exchange banks and a number of Indian joint stock banks. All these banks operated in different segments of the economy.
- The exchange banks, mostly owned by Europeans, concentrated on financing foreign trade. Indian joint stock banks were generally under capitalized and lacked the experience and maturity to compete with the presidency and exchange banks.
- By the 1900s, the market expanded with the establishment of banks such as Punjab National Bank, in 1895 in Lahore and Bank of India, in 1906, in Mumbai - both of which were founded under private ownership.
- Punjab National Bank was the first Swadeshi Bank founded by the leaders like Lala Lajpat Rai and Sardar Dyal Singh Majithia. The Swadeshi movement in particular inspired local businessmen and political figures to found banks of and for the Indian community.
- A number of banks established then have survived to the present such as Bank of India, Corporation Bank, Indian Bank, Bank of Baroda, Canara Bank and Central Bank of India.

Banks in India

- Without a sound and effective banking system in India it cannot have a healthy economy. The banking system of India should not only be hassle free but it should be able to meet new challenges posed by the technology and any other external and internal factors.
- For the past three decades India's banking system has several outstanding achievements to its credit.
- The most striking is its extensive reach. It is no longer confined to only metropolitans or cosmopolitans in India. In fact, Indian banking system has reached even to the remote corners of the country. This is one of the main reasons of India's growth process.
- Banking in India originated in the first decade of 18th century. The first banks were The General Bank of India, which started in 1786 and Bank of Hindustan, both of which are now defunct.

- The oldest bank in existence in India is the State Bank of India, which originated as the "The Bank of Bengal" in Calcutta in June 1806. This was one of the three presidency banks, the other two being the Bank of Bombay and the Bank of Madras.
- The presidency banks were established under charters from the British East India Company. They merged in 1925 to form the Imperial Bank of India, which, upon India's independence, became the State Bank of India.
- For many years the Presidency banks acted as quasi-central banks. The Reserve Bank of India formally took on the responsibility of regulating the Indian banking sector from 1935. After India's independence in 1947, the Reserve Bank was nationalized and given broader powers.

From 1786 till today, the journey of Indian Banking System can be segregated into three distinct phases. They are mentioned below:

- Early phase from 1786 to 1969 of Indian Banks
- Nationalisation of Indian Banks and up to 1991 prior to Indian banking sector reforms.
- New phase of Indian Banking System with the advent of Indian Financial & Banking sector Reforms after 1991.

Phase I

- The General Bank of India was set up in the year 1786. Next came Bank of Hindustan and Bengal Bank. The East India Company established Bank of Bengal (1809), Bank of Bombay (1840) and Bank of Madras (1843) as independent units and called it Presidency Banks.
- These three banks were amalgamated in 1920 and Imperial Bank of India was established which started as private shareholders banks, mostly European shareholders.
- During the first phase the growth was very slow and banks also experienced periodic failures between 1913 and 1948. There were approximately 1100 banks, mostly small.
- To streamline the functioning and activities of commercial banks, the Government of India came up with The Banking Companies Act, 1949 which was later changed to Banking Regulation Act 1949 as per amending Act of 1965.
- Reserve Bank of India was vested with extensive powers for the supervision of banking in India as the Central Banking Authority.

First World War (1914-1918);

- The period during the First World War (1914-1918) through the end of the Second World War (1939-1945), and two years thereafter until the independence of India were challenging for Indian banking.

- During those days public has lesser confidence in the banks. As a result deposit mobilisation was slow. Contrary to it the savings bank facility provided by the Postal department was comparatively safer. Moreover, funds were largely given to traders.

At least 94 banks in India failed between 1913 and 1918 as indicated in the following table:

Years	Number of banks that failed	Authorised capital (Rs. Lakhs)	Paid-up Capital (Rs. Lakhs)
1913	12	274	35
1914	42	710	109
1915	11	56	5
1916	13	231	4
1917	9	76	25
1918	7	209	1

Post-independence:

- The partition of India in 1947 adversely impacted the economies of Punjab and West Bengal, paralyzing banking activities for the long time.
- India's independence marked the end of a regime of the Laissez-faire for the Indian banking. The Government of India initiated measures to play an active role in the economic life of the nation and the Industrial Policy Resolution adopted by the government in 1948 envisaged a mixed economy.

This resulted into greater involvement of the state in different segments of the economy including banking and finance. The major steps to regulate banking included: In 1948, the Reserve Bank of India, India's central banking authority, was nationalized, and it became an institution owned by the Government of India.

- In 1949, the Banking Regulation Act was enacted which empowered the Reserve Bank of India (RBI) "to regulate, control, and inspect the banks in India."
- The Banking Regulation Act also provided that no new bank or branch of an existing bank may be opened without a license from the RBI and no two banks could have common directors.

However, despite of these provisions, control and regulations banks in India except the State Bank of India, continued to be owned and operated by private persons. This changed with the nationalisation of major banks in India on 19th July, 1969.

Phase II

- Government took major steps in the Indian Banking Sector Reform after independence.
- By 1960s, the Indian banking industry has become an important tool to facilitate the development of the Indian economy. At the same time, it has emerged as a large employer.
- Indira Gandhi, Prime Minister of India at that time expressed the intention of the Government of India in the annual conference put her thoughts forward for the **nationalization** of the banks**.**
- In 1955, it nationalised Imperial Bank of India with extensive banking facilities on a large scale especially in rural and semi-urban areas. It formed State Bank of India to act as the principal agent of RBI and to handle banking transactions of the Union and State Governments all over the country.
- Seven banks forming subsidiary of State Bank of India was nationalised on 19th July, 1969, major process of nationalisation was carried out when 14 major commercial banks in the country were nationalised.
- Second stage of nationalisation in Indian Banking Sector Reform was carried out in 1980 with seven more banks.
- The stated reason for the nationalization was to give the government more control of credit delivery and the government of India controlled around 91% of the banking business of India.
- In the year 1993, the government merged New Bank of India with Punjab National Bank. It was the first and only merger between nationalized banks and resulted in the reduction of the number of nationalized banks from 20 to 19.
- After this until the 1990s, the nationalized banks grew at a pace of around 4%, closer to the average growth rate of the Indian economy.

The following are the steps taken by the government of India to regulate banking institutions in the country:

- 1949 : Enactment of Banking Regulation Act.

- 1955 : Nationalisation of State Bank of India.
- 1959 : Nationalisation of SBI subsidiaries.
- 1961 : Insurance cover extended to deposits.
- 1969 : Nationalisation of 14 major banks.
- 1971 : Creation of credit guarantee corporation.
- 1975 : Creation of regional rural banks.
- 1980 : Nationalisation of seven banks with deposits over 200 crore. After the nationalisation of banks, the branches of the public sector bank India rose to approximately 800% in deposits and advances took a huge jump by 11,000%.

Phase III

- This phase has introduced many more products and facilities in the banking sector in its reform measures. In 1991, under the chairmanship of Mr. Narasimham, a committee was set up by his name which worked for the liberalisation of banking practices.
- This move, along with the rapid growth in the economy of India, revitalized the banking sector in India, which has seen rapid growth with strong contribution from all the three sectors of banks, namely; government banks, private banks and foreign banks.
- The new policy ushered a modern outlook and tech-savvy methods of working for traditional banks.
- All this led to the retail boom in India. People not just demanded more from their banks but also received more.
- The financial system of India has shown a great deal of resilience. It is sheltered from any crisis triggered by any external macroeconomics shock as other East Asian Countries suffered.
- This is all due to a flexible exchange rate regime, the foreign reserves are high, the capital account is not yet fully convertible and banks and their customers have limited foreign exchange exposure.

Banking in India

Central Bank	Reserve Bank of India

Nationalized Banks	Allahabad Bank • Andhra Bank • Bank of Baroda • Bank of India • Bank of Maharashtra • Canara Bank • Central Bank of India • Corporation Bank • Dena Bank • Indian Bank • Indian Overseas Bank • Oriental Bank of Commerce • Punjab & Sind Bank • Punjab National Bank • Syndicate Bank • Union Bank of India • United Bank of India • UCO Bank • Vijaya Bank • IDBI Bank
State Bank Group	State Bank of India • State Bank of Bikaner & Jaipur • State Bank of Hyderabad • State Bank of Indore • State Bank of Mysore • State Bank of Patiala • State Bank of Saurashtra • State Bank of Travancore
Private Banks	Axis Bank • Bank of Rajasthan • Bharat Overseas Bank • Catholic Syrian Bank • Centurion Bank of Punjab • City Union Bank • Development Credit Bank • Dhanalakshmi Bank • Federal Bank • Ganesh Bank of Kurundwad • HDFC Bank • ICICI Bank • IndusInd Bank • ING Vysya Bank • Jammu & Kashmir Bank • Karnataka Bank Limited • Karur Vysya Bank • Kotak Mahindra Bank • Lakshmi Vilas Bank • Nainital Bank • Ratnakar Bank • SBI Commercial and International Bank • South Indian Bank • Amazing Mercantile Bank • YES Bank
Foreign Banks	ABN AMRO • Barclays Bank • Citibank • HSBC • Standard Chartered • Deutsche Bank
Regional Rural Banks	South Malabar Gramin Bank • North Malabar Gramin Bank • Pragathi Gramin Bank • Shreyas Gramin Bank

CHAPTER-2

INTRODUCTION OF RESERVE BANK OF INDIA

Reserve Bank of India

The financial system deals with people's money and thus it is necessary to generate, maintain and promote the confidence and trust of those people at all the times. This is done by regulating the financial system and the rationale for doing so is:

- To protect investors' interest thorough timely disclosure by the institutions and access to revenue information by the investors.
- To ensure that the financial markets are fair and efficient.
- To ensure that the participants measure up to the rules of the market place.

Thus in order to fulfil the above objectives a central regulatory body was formed named Reserve Bank of India (RBI). RBI was constituted under Reserve Bank of India Act 1934 and began functioning from 1st April 1935. RBI is controlled by the Central Board of Directors, comprising of Governor, four Deputy Governors and fifteen directors nominated by the Union Government.

The main objectives of RBI are as follows:

- To promote growth and maintenance of price stability.

- To maintain monetary stability so that the business and economic life can yield welfare gain of a mixed economy.
- To maintain financial stability and sound financial institutional health so that economic units can conduct their business with confidence.
- To maintain a stable payment system in order to execute financial transactions safely and efficiently.
- To ensure that credit allocation by financial system is conducted as per national economic priorities and social concerns.
- To regulate the money and credit supply in the economy in order to ensure price stability.
- To promote the development of financial markets.
- To ensure orderly conditions in forex market and reduction in exchange rate volatility.

Main Functions of RBI:

Issuing Notes: RBI has the sole authority to issue, circulate, withdraw and exchange the currency notes. It issues the notes in denomination of Rs.2, 5, 10,20, 50,100,500 and 1000. Except Rs. 1 notes and coins, which are issued by the government of India. But are put into circulation by RBI. RBI has 17 Issue Offices and over 4000 currency chests where new and reissuable notes are stored. As a cover for note issue, RBI keeps a minimum value of Gold coins and Bullion and foreign securities as part of total approved assets.

Government's Bankers: RBI acts as a banker to the central and the state government. It provides them banking services of deposits, withdrawal of funds, making payments and receipts, collection and transfer of funds and management of public debt.
Governments deposits are received free of interest and RBI does not receive any remuneration for the routine banking business of the government. It also makes advances to the government to subject to overdraft limits, in order to control fiscal deficit. But it charges commission for managing the public debt and interest on overdraft from the government.

Bankers' Bank: The commercial and state cooperative banks are scheduled banks have to maintain , stipulated reserves in cash and in approved securities as a percentage of the demand and time liabilities deposits. These are commonly known as Cash Reserve Ratio and Statutory Liquidity Ratio. RBI has power to change its bank rates to regulate the cost of bank credit.

It also act as a ' *Lender of the last resort'* for banks by rediscounting bills and by enforcing refinance mechanism for certain kinds of credit subject to certain rules and regulations.

Banks' Supervision- From November 1993 RBI's supervisory functions had been separated from the traditional one. In 1994 Board of Financial Supervision (BSF) was established to oversee the Indian financial system which included not only commercial and state co-operative banks but also All-India Financial Institutions (AIFIs) and Non-Banking Finance Companies. The BSF is chaired by the Governor of RBI; it also has full time vice-chairman and 6 other members.

Following are the supervisory powers of RBI which it exercises over commercial banks:

- To issue licences for setting up new banks and for establishing new branches of the existing ones.
- To prescribe minimum paid-up capital and reserves, cash reserves and other liquid assets requirements.
- To inspect working of the scheduled banks in India and abroad.
- To conduct investigations for complaints, irregularities and frauds pertaining to the banks.
- To control appointments, reappointment and termination of the CEO of private banks. To approve for mergers and acquisitions of two banks.

Development of Financial system- RBI has initiated with several steps for the development of banking and overall financial system of the country. For this specialised financial institutions are build up by RBI:

- Industrial Development Bank of India (IDBI),1964 for industrial finance.
- National Bank for Agriculture and Rural Development (NABARD), 1981for Agriculture credit.
- Export-Import Bank of India (EXIM), 1981 for export-import finance.
- Deposit Insurance and credit Guarantee Corporation of India (DICGC).

Exchange Control: RBI is responsible for maintaining stability of the external value of our national currency in order to regulate the forex market it used Foreign Exchange Regulation Act (FERA), 1947 which later on replaced by Foreign Exchange Management Act (FEMA).It manages forex reserves in the form of gold and foreign securities.

Monetary Policy: RBI controls money supply, credit volume and the cost of bank credit in the economy. RBI controls inflationary and deflationary situations by changing the level of money supply. As we approached towards market oriented financial system

RBI's annual Credit Policy Statements transformed into Monetary and Credit Policy as the link between the two strengthened.

Changes in Monetary Policy framework: Year 1991 have seen significant change in the policy environment. Together with the long term growth in the money supply, now RBI also focuses on the short term liquidity management. For this Liquidity Adjustment Facility (LAF) was initiated in the year 2000, which operates on the line of repo and reverse repo options for the movements of short term interest rates.

Other tools of monetary control are:

- CRR
- SLR
- Bank rates
- Open – market operations.
- Selective credit controls
- Credit rationing/allocation, credit planning, inventory and credit norms.

Basel Norms: II

There is a tremendous change in the banking and financial systems all over the world. After globalisation Banking System in India has attained vital importance. Day by day due to increase in commercial operations there banking complexities are increases as well, in terms of banking transactions, capital requirements, liquidity, credit and various risks associated with them.

Basel Committee

For banks which are active globally, it is imperative to strengthen their capital in accordance with the supervisory standards and guidelines formulated by the Basel Committee. The committee which was constituted by Central Bank Governors of a Group of 10 countries in 1974 under the aegis of the Bank of International Settlements (BIS) has, over the years set out standards for capital measurement.

In the late 1980s, the Basel Committee on Banking Supervision took initiative to develop capital adequacy standards that lead to international convergence of supervisory

regulations of active banks the world over. Its major goal was to strengthen the soundness and stability of the international banking framework. Its objective is to enhance understanding of key supervisory issues and improve the quality of banking supervision worldwide. The Committee's Secretariat is located at the Bank for International Settlements (BIS) in Basel, Switzerland.

This initiative resulted in the Basel Capital Accord of 1988. The Basel Accord comprises a definition of regulatory capital, measures of risk exposure, and rules specifying the level of capital to be maintained in relation to these risks.

The World Trade Organisation (WTO), of which India is a member nation, requires the countries like India to get their banking systems at par with the global standards in terms of financial health, safety and transparency by implementing the Basel II Norms by 2009.

Need For Such Norms

The first accord **Basel Accord I** was established in 1988 and was implemented by 1992. It was the very first attempt to introduce the concept of minimum standards of capital adequacy.

Then the second accord by the name **Basel Accord II** was established in 1999 with a final directive in 2003 for implementation by 2006 as Basel II Norms. Unfortunately, India could not fully implement this but is now gearing up under the guidance from the Reserve Bank of India to implement it from 1 April, 2009.Basel II Norms have been introduced to overcome the drawbacks of Basel I Accord. For Indian Banks, its the need of the hour to get ready and practice the banking business at an equal level of global standards and make the banking system in India more reliable, transparent and safe. These Norms are necessary since India is and will witness increased capital flows from foreign countries and there is increasing cross-border economic & financial transactions.

Features of Basel-II Norms

Basel II Norms are considered as the reformed & refined form of Basel I Accord. The Basel II Norms primarily stress on 3 factors, viz. Capital Adequacy, Supervisory Review and Market discipline. The Basel Committee calls these factors as the **Three Pillars to manage risks.**

Pillar I: Capital Adequacy Requirements

Under the Basel II Norms, banks should maintain a minimum capital adequacy requirement of 8% of risk assets. For India, the RBI has mandated maintaining of 9% minimum capital adequacy requirement. This requirement is popularly called as Capital Adequacy Ratio (CAR) or Capital to Risk Weighted Assets Ratio (CRAR).

Tier 1 Capital- It is regarded as the core measure of a bank's financial strength. It consists of financial capital which is reliable in the terms of liquid, primarily includes Shareholders' equity. Other examples of Tier 1 capital are common stock, preferred stock (irredeemable and non-cumulative) and retained earnings.

The reason for holding capital is that it should provide protection against unexpected losses. These are different from expected losses as provisions, reserves and current year profits are for covering expected losses.

Specifically, Tier 1 Capital is a measure of capital adequacy of a bank and is the ratio of a bank's core equity capital to its total risk-weighted assets. Risk weighted assets is the total of all assets held by the bank which are weighted for credit risk according to a formula determined by the Regulator which is the country's Central Bank. Most Central Banks follow the BIS (Bank of International Settlements) guidelines in setting asset risk weights. Assets like cash and coins usually have zero risk weights, while unsecured loans might have a risk weight of 100%.
It is calculated as**:**
Tier One Capital / Risk Weighted Assets

Tier 2 Capital- It is a measure of a bank's financial strength with regard to the reliable form of financial capital. The forms of banking capital were largely standardised in the Basel I accord, issued by the Basel Committee on Banking Supervision and are left by the Basel II accord.
Tier 1 Capital- It is considered to be more reliable form of capital. There are several classifications of Tier II Capital. In the Basel I accord, these are categorised as undisclosed reserves, revaluation reserves, general provisions, hybrid instruments and subordinated term debt.

Undisclosed Reserves- Undisclosed reserves are not common but are accepted by some regulators where a bank has made a profit but this has not appeared as normal retained profits or in general reserves.

Revaluation Reserves- A revaluation reserve is a reserve created when a company has an asset revalue and an increase in value is brought to account. A current revaluation is very likely to show a large increase in value. The increase would be added to a revaluation reserve.

General Provisions- A general provision is created when a company is aware that a loss may have occurred but is not sure of the exact nature of that loss. General provisions were commonly created to provide for losses that were expected in the future. As these did not represent incurred losses, regulators tended to allow them to be counted as capital.

Hybrid Instruments- Hybrids are instruments that have some characteristics of both debt and shareholders' equity. Provided these are close to equity in nature, in that they are able to take losses on the face value without triggering liquidation of the bank, they may be counted as capital.

Subordinated Term Debt- Subordinated term debt is debt that is not redeemable (it cannot be called upon to be repaid) for a set (usually long) term and ranks lower (it will only be paid out after) ordinary depositors of the bank.

A loan (or security) that ranks below other loans (or securities) with regard to claims on assets or earnings. Also known as "junior security" or "subordinated loan". In the case of default, creditors with subordinated debt wouldn't get paid out until after the senior debt holders were paid in full. Therefore, subordinated debt is more risky than unsubordinated debt.

Both tier 1 and tier 2 capital were first defined in the Basel I capital accord.

Pillar II: Supervisory Review

Banks mostly are endangered with three types of risks- credit, operational & market risks. Basel II Norms under this Pillar wants to ensure that not only banks should have adequate capital to support all the risks but also to encourage these banks to develop and use better risk management techniques for monitoring and managing their risks

The Supervisory Review has four key principles;

- Banks should have a process for assessing their overall capital adequacy in relation to their risk profile and a strategy for monitoring their capital levels.
- Supervisors should review and evaluate bank's internal capital adequacy assessment and strategies, as well as their ability to monitor and ensure their compliance with regulatory capital ratios.

- Supervisors should see that the banks operate above the minimum regulatory capital ratios and have the ability to hold capital in excess of the minimum set standard.
- Supervisors should seek to intervene at an early stage to prevent capital from falling below the minimum level and should take relevant remedial actions, if capital adequacy level is not restored.

Pillar III: Market Discipline

Market discipline imposes banks to conduct their banking business in a safe, sound and effective manner. Mandatory disclosure requirements on capital and risk exposure are required to be fulfilled, so that market participants can assess a bank's capital adequacy. Qualitative disclosures such as risk management objectives and policies, etc. may also be published.

Sub-Prime Crisis

The *Sub-Prime mortgage crisis* is an ongoing economic problem that became more apparent during 2007-2008 and is the situation of contracted liquidity in the global credit markets and banking system. The downturn in the U.S. housing market, risky lending and borrowing practices and excessive individual and corporate debt levels have caused multiple adverse effects on the world economy. The crisis has passed through various stages, exposing weaknesses in the global financial system and regulatory framework.

Sub-Prime lending is the practice of making loans to borrowers who do not qualify for market interest rates owing to various risk factors, such as income level, size of the down payment made, credit history, and employment status.
A number of factors were responsible for the crisis. Some of these include: the inability of homeowners to make their mortgage payments, poor judgment by the borrower or the lender, speculation and overbuilding during the boom period, risky mortgage products, high personal and corporate debt levels, financial innovation that distributed and perhaps concealed default risks, central bank policies, and regulation.

It's Impact on Indian Economy

The sub prime crisis in the US, following the collapse of the housing sector boom, has sent cascading effect to the economies of many countries. During the high demand period for housing loans in the US, when the real estate sector was booming, people

with a bad credit history and a higher chance of defaulting on their payments, were provided loans at higher than normal interest rates (*sub-prime rates*). A decline in economic activity in the US resulted in lower disposable incomes and hence a decline in demand. Simultaneously there was a rise in supply due to repayments and foreclosures arising out of a higher interest rate. This triggered the sub-prime crisis.

Sectors such as stock markets and bank investment funds have been affected worldwide, especially in European and Asian countries. The central banks of many countries on these continents have taken ambiguous action to prevent credit crises that could lead to economic recession. One possible impact of US sub prime crisis on global markets is losses pertaining to securities. It would make credit conditions stringent. Consequently, loss incurred on securities has increased. As a cumulative effect, the financial markets have spiral downward causing the monetary policies to become more loss. With regard to equity markets, it is noticed that equity markets have go down .As a result of the credit constraints, business investment in the India has dropped, unemployment also in future may rise and there are possibilities of a prolonged phase of depression in the consumer prices.

"I THOUGHT WE WERE JUST BUYING A HOUSE!"

In India banks, financial services, real estate infrastructure, information technology are the most impacted sectors.

Indian Financial Services:

- The US sub-prime market crisis, which so far caused losses worth $181 billion to the world's top 45 banks by the end of the year 2008, has started hitting Indian banks also.
- India's largest private sector bank ICICI Bank was the first bank to announce a loss of about Rs. 1056 corers owing to the sub prime crisis of US in the year 2008 results.
- The public sector banks have had a limited position in the structured products and therefore impact is expected to be minimal. But negative sentiments will hit harder.
- Punjab national Bank, Bank of India, State Bank of India, Bank of Baroda were major banks having an exposure to the instruments issued by Lehman and Merrill Lynch.
- However the banking sector in general will have to face tight liquidity conditions apart from further mark-to-market losses. The net non performing assets of entire banking sector are less than 2% and it is well capitalized. The capital adequacy ratio is around 13% as against the statutory requirement of 8 to 9%.

Impact on Major Banks

- **ICICI**- Reported exposure of $80 mm, $12 mm provisions, Expected loss at $ 28 mm.
- **SBI-** Reported exposure at $5 mm, Expects to recover 70%.
- **PNB**- Reported exposure at $5 mm Expected loss at $ 2 mm.
- **BOI-** Reported exposure of $ 11 mm.
- **BOB**- Reported exposure Expected loss of $ 5 mm of $ 10 mm, Expected loss at $ 4mn
- **Edelweiss:** 2.6% stake bought by Lehman**.**
- **Emkay Global-** Lehman Holdings at 4.05%.
- **Axis Bank**- Reported exposure $ 1.5 mm through mark to market forex counter party deal. Impact is negligible.

Reinstating Investor Confidence

The RBI has suggested a series of moves aimed at defending the rupee from further depreciation and easing the tight short-term liquidity situation in the banking system. In its move to meet the liquidity requirements of the economy, RBI has reduced the statutory liquidity ratio. In addition to the normal method of borrowing funds, RBI will also allow banks to acquire additional liquidity up to one percent of their deposits and seek waiver of penal interest.

Indian banks' exposure to the risky derivative instruments is very small because of the RBI's prudent guidelines. Better regulation saved the Indian banks from the crisis that has affected the other markets. Steps taken by the central banks, long term strong fundamentals and recovery in the stocks markets have calmed down nerves at least in the short term.

But the future still remains on shaky grounds. A downward revision in earnings estimate for the corporate sector is expected. A conservative approach with sufficient asset class diversification will insulate investor portfolios.

Future Outlook

Banks- stable and strong

- The banks are expected to continue going strong due to limited impact from exposures.
- The profitability may see a lower growth on account of rising cost of funds and lower credit growth.
- Tight liquidity conditions may see banks suffering on the bond portfolio.
- Need to avoid banks with high NPAs, low CAR and low Current Account and Saving Account.

Financial Services:

- This sector is most impacted on account of global uncertainty.
- The broking firms have been seeing low volumes with investors now less forthcoming to invest in the markets.
- The effect on revenue streams of insurance companies and AMCs would have a limited impact based on their bond portfolios. Need to avoid less diversified businesses for sometime.

The need of the hour is to have a more open economy or be open to trade, attract investments, which would re-kindle innovative concepts and enhance foreign direct investment. The growth has to be such that it is sustainable, only then will the impact of US sub prime crisis on India be negligible.

Asset- Liability Management

Banks are in the business of managing risks. Of these risks liquidity and interest rate risk management are extremely important for any bank. Banks face various challenges in managing these risks. An Asset Liability Management system helps the bank in doing so. They accept deposits of varying maturity from customers and pay loans of different maturities on the other side. Besides this, banks also transfer the risk appetite of

customers as they accept fixed rate deposits and give floating rate loans. Similarly, they accept floating rate deposits and pay fixed rate loans. All these activities result in concentration of liquidity and interest rate risk in a bank's book.

In banking, **Asset Liability Management** (ALM) is the practice of managing risks that arise due to mismatches between the assets and liabilities (debts and assets) of the bank.

Banks face several risks such as the liquidity risk, interest rate risk, credit risk and operational risk. ALM is a strategic management tool to manage interest rate risk and liquidity risk faced by banks, financial service companies and corporations.

Banks manage the risks of asset-liability mismatch by matching the assets and liabilities according to the maturity pattern or the matching the duration, by hedging and by securitization. Modern risk management now takes place from an integrated approach to Enterprise Risk Management that reflects the fact that interest rate risk, credit risk, market risk and liquidity risk are all interrelated. Increasing integrated risk management is done on a full mark to market basis rather than the accounting basis that was at the heart of the first interest rate sensitivity gap and duration calculations.

Ever since the initiation of the process of deregulation of the Indian banking system and gradual freeing of interest rates to market forces and consequent injection of a dose of competition among the banks, introduction of Asset-Liability Management in the public sector banks (PSBs) has been suggested by several experts. But, initiatives in this respect on the part of most bank managements have been absent. This seems to have led the Reserve Bank of India to announce in its monetary and credit policy of October 1997 that it would issue ALM Guidelines to banks. While the guidelines are awaited, an informal check with several PSBs showed that none of these banks have moved decisively to introduce ALM. One reason for this negligence appears to be a wrong notion among bankers that their banks already practice ALM. As per this understanding, ALM is a system of matching cash inflows and outflows and thus of liquidity management. Hence, if a bank meets its cash reserve ratio and statutory liquidity ratio stipulations regularly without undue and frequent resort to purchased funds, it can be said to have a satisfactory system of managing liquidity risks and hence of ALM.

The actual concept of ALM is however much wider and of greater importance to banks' performance. Historically, ALM has evolved from the early practice of managing liquidity on the bank's asset side to a later shift to the liability side, termed as liability management; to a still later realisation of using both assets as well as liabilities sides of the balance sheet to achieve optimum resources management. But that was till the 1970s. Volatility of interest rates in USA and Europe caused the

focus to broaden the issue of interest rate risk.. ALM began to extend beyond the bank treasury to cover the loan and deposit functions.

The induction of credit risk into the issue of determining adequacy of bank capital further enlarged the scope of ALM. In the current decade, earning a proper return of bank equity and hence maximisation of its market value has meant that ALM covers the management of the entire balance sheet of a bank. This implies that the bank managements are now expected to target required profit levels and ensure minimisation of risks to acceptable levels to retain the interest of investors in their banks. This also implies that costing and pricing policies have become of paramount importance in banks.

In the regulated banking environment in India prior to the 1990s, the equation of ALM to liquidity management by bankers could be understood. There was no interest rate risk as the interest rates were regulated and prescribed by the RBI. Spreads between the deposit and lending rates were very wide; these spreads were more or less uniform among the commercial banks and were changed only by RBI. If a bank suffered significant losses in managing its banking assets, the same were absorbed by the comfortably wide spreads. The bank balance sheet was not being managed by banks themselves. It was being managed through prescriptions of the regulatory authority and the government. This situation has now changed.

The banks have been given a large amount of freedom to manage their balance sheets. But the knowledge, new systems and organizational changes that are called for to manage it, particularly the new banking risks are still lagging. The turmoil in domestic and international markets during the last few months and impending changes in the country's financial system are a grim warning to our bank managements to gear up their balance sheet management. It is suggested that the banks should introduce ALM which would focus on liquidity management, interest rate risk management and spread management.

Broadly, there are 3 requirements to implement ALM in these banks, in the stated order:

- Developing a better understanding of ALM concepts
- Introducing an ALM information system
- Setting up ALM decision-making processes (ALM Committee/ALCO)

The above requirements are already met by the new private sector banks. These banks have their balance sheets available at the close of every day. Repeated changes in interest rates by them to manage interest rate risk and their maturity mismatches are based on data provided by their MIS. In contrast, loan and deposit pricing by banks is based partly on intuitions, partly on estimates of internal macro data and partly on their competitors' rates. Hence, banks would first and foremost need to focus on putting in place an ALM which would provide the necessary framework to define measure, monitor, modify and manage interest rate risk.

The ALM process rests on three pillars:

ALM information systems	ALM organisation	ALM process
=> Management Information System => Information availability, accuracy, adequacy and expediency	=> Structure and responsibility => Level of top management involvement	=> Risk parameters => Risk identification => Risk measurement => Risk management => Risk policies and tolerance levels

ALM Information Systems

Information is the key to the ALM process. Considering the large network of branches and the lack of an adequate system to collect information required for ALM which analyses information on the basis of residual maturity and behavioural pattern it will take time for banks in the present state to get the requisite information. The problem of ALM needs to be addressed by following an ABC approach i.e. analysing the behaviour of asset and liability products in the top branches accounting for significant business and then making rational assumptions about the way in which assets and liabilities would behave in other branches.

In respect of foreign exchange, investment portfolio and money market operations in view of the centralised nature of the functions, it would be much easier to collect reliable information. The data and assumptions can then be refined over time as the bank management gain experience of conducting business within an ALM framework. The spread of computerisation will also help banks in accessing data.

ALM Organization

The Board should have overall responsibility for management of risks and should decide the risk management policy of the bank and set limits for liquidity, interest rate, foreign exchange and equity price risks.

The Asset - Liability Committee (ALCO) consisting of the bank's senior management including CEO should be responsible for ensuring adherence to the limits set by the Board as well as for deciding the business strategy of the bank in line with the bank's budget and decided risk management objectives.

The ALM desk consisting of operating staff should be responsible for analysing, monitoring and reporting the risk profiles to the ALCO. The staff should also prepare forecasts showing the effects of various possible changes in market conditions related to the balance sheet and recommend the action needed to adhere to bank's internal limits.

The ALCO is a decision making unit responsible for balance sheet planning from riskreturn perspective including the strategic management of interest rate and liquidity risks. Each bank will have to decide on the role of its ALCO, its responsibility as also the decisions to be taken by it. The business and risk management strategy of the bank should ensure that the bank operates within the limits / parameters set by the Board. The business issues that an ALCO would consider will include product pricing for both deposits and advances, desired maturity profile of the incremental assets and liabilities, etc.

In addition to monitoring the risk levels of the bank, the ALCO should review the results of and progress in implementation of the decisions made in the previous meetings. The ALCO would also articulate the current interest rate view of the bank and base its decisions for future business strategy on this view. In respect of the funding policy, for instance, its responsibility would be to decide on source and mix of liabilities or sale of assets.

Towards this end, it will have to develop a view on future direction of interest rate movements and decide on a funding mix between fixed vs floating rate funds, wholesale vs retail deposits, money market vs capital market funding, domestic vs foreign currency funding, etc. Individual banks will have to decide the frequency for holding their ALCO meetings

Composition of ALCO

The number of members in ALCO would depend on the size of each institution, business mix and organizational complexity. To ensure commitment of the Top Management, the CEO/CMD/ED should head the Committee. The Chiefs of
Investment, Credit, Funds Management / Treasury (forex and domestic), International Banking and Economic Research can be members of the Committee. In addition the Head of the Information Technology Division should also be an invitee for building up of MIS and related computerization. Some banks may even have sub-committees.

Committee of Directors:

Banks should also constitute a professional Managerial and Supervisory Committee consisting of three to four directors which will oversee the implementation of the system and review its functioning periodically. **ALM Process:**

The scope of ALM function can be described as follows:

- Liquidity risk management
- Management of market risks (including Interest Rate Risk)
- Funding and capital planning
- Profit planning and growth projection
- Trading risk management

The primary objective of an Asset Liability Management system is liquidity and interest rate risk management.

Liquidity Risk Management

Liquidity risk is often related to bank's inability to pay to its depositors. Thus, a bank's inability to pay to its depositors is the ultimate expression of liquidity risk. Liquidity risk at initial stages may lead to distress pricing of assets and liabilities. Liquidity Risk Management has become increasingly a challenging task in Indian Banks.

A bank with high degree of liquidity risk may be forced to borrow funds from inter bank market at inflated rates or has to increase its deposit rates. As the bank may not be able to transfer these increased costs to borrowers, ultimately its net interest income shall be affected. Further, as bank's cost of funds goes up, increasingly it looks for risky avenues to increase its earnings. The process may lead to wrong selection of borrowers as well as venturing into risky areas (such as equity financing, giving unsecured loans etc) increasing overall risk profile of the bank. Therefore, liquidity risk has strong correlation with other risks such as interest rate risk and credit risk.

Measurement of Liquidity Risk

Liquidity risk is measured through either Stock Approach or Flow Approach.

Under **Stock Approach** certain standard ratios are computed. Some of the ratios widely used in banks are liquid assets to short-term liabilities, core assets to core liabilities, inter bank borrowings to total assets, overnight borrowings to total assets etc.

However, management of liquidity through ratios suffers from certain drawbacks, as it does not take into account the market liquidity aspect of assets and liabilities. For example, presence of some short-term investments may show the improved liquidity risk of the bank whereas the investment itself may be highly illiquid. The ratios, though good indicator of liquidity may be good for a point of time only, as balance sheet profile constantly changes.

On the other hand the **Flow Approach**, which is the alternative model for measuring and managing liquidity has been accepted by most of the banks.

Under flow approach, cash flows are segregated into different maturity ladders and net funding requirement for a given time horizon is estimated. The net funding requirement over a given time horizon gives a fair idea of liquidity risk faced by an institution.

Generally banks perform an in-depth analysis of their liquidity profile by analyzing:

- The profile of liability holders,
- The extent of purchased fund providers,
- ABC analysis of depositors etc

They also prepare scenario analysis with different degrees of rollovers and different level of asset securitization, asset sale and other realizations to develop the contingency funding requirement. Ultimately a plan is prepared to meet liquidity requirements in the event of crisis and cost thereof to meet the crisis. The Board of directors and top management periodically review these results.

Importance of liquidity risk management has also been highlighted by *Basel Committee* on Banking Supervision in the document stated as “Sound Practices of managing Liquidity in Banking Organizations”. World-wide, banking regulators are mandating banks to conduct scenario analysis of liquidity risk and prepare contingency plans to meet liquidity requirements in unforeseen circumstances.

The major challenges faced by Indian Banks in liquidity management are:

- Maturities of bank deposits are shrinking over last couple of years. This is mainly due to tightening of liquidity of banks for long-term deposits.
- With decline in interest rates, a considerable portion of customers migrated to other savings alternatives like post office deposits, mutual funds, etc. depriving banks of long term resources.
- Falling interest rates and lack of credit growth in past years prompted banks to put major portion of their deposits in long-term government securities which may not remain liquid at all times. Further, government securities are subject to price risk and a bank may not be able to generate adequate liquidity without selling them at loss.

Asset securitization is also likely to emerge as an effective tool used by banks to manage liquidity risk.

Currency Risk

Floating exchange rate arrangement has brought in its wake pronounced volatility adding a new dimension to the risk profile of banks' balance sheets. The increased capital flows across free economies following deregulation have contributed to increase in the volume of transactions. Large cross border flows together with the volatility has rendered the banks' balance sheets vulnerable to exchange rate movements.

Dealing in different currencies brings opportunities and risks as well. If the liabilities in one currency exceed the level of assets in the same currency, then the currency mismatch can add value or erode value depending upon the currency movements. The simplest way to avoid currency risk is to ensure that mismatches, if any, are reduced to zero or near zero. Banks undertake operations in foreign exchange like accepting deposits, making loans and advances and quoting prices for foreign exchange transactions.

Irrespective of the strategies adopted, it may not be possible to eliminate currency mismatches altogether. Managing currency risk is one more dimension of Asset-Liability Management.

Mismatched currency position besides exposing the balance sheet to movements in exchange rate also exposes it to country risk and settlement risk.

Following the introduction of "Guidelines for Internal Control over Foreign Exchange Business" in 1981, maturity mismatches (gaps) are also subject to control. Following the recommendations of expert group on Foreign Exchange Markets in India (Sodhani Committee) the calculation of exchange position has been redefined and banks have been given the discretion to set up overnight limits linked to maintenance of additional Tier I capital to the extent of 5 per cent of open position limit.

Interest Rate Risk

The phased deregulation of interest rates and the operational flexibility given to banks in pricing most of the assets and liabilities have exposed the banking system to Interest Rate Risk. It is the risk where changes in market interest rates might adversely affect a bank's financial condition. Changes in interest rates affect both the current earnings and also the net worth of the bank. The risk from the earnings' perspective can be measured as changes in the Net Interest Income or Net Interest Margin.

In the context of poor MIS, slow pace of computerization in banks and the absence of total deregulation, the traditional Gap analysis is considered as a suitable method to measure the Interest Rate Risk. The Gap or Mismatch risk can be measured by calculating Gaps over different time intervals as at a given date. Gap analysis measures mismatches between rate sensitive liabilities and rate sensitive assets (including off-balance sheet positions). An asset or liability is normally classified as rate sensitive if:

- Within the time interval under consideration, there is a cash flow.
- The interest rate resets/reprices contractually during the interval.
- RBI changes the interest rates in cases where interest rates are administered.
- It is contractually pre-payable or with drawable before the stated maturities.

The Gap Report should be generated by grouping rate sensitive liabilities, assets and off balance sheet positions into time buckets according to residual maturity or next repricing period, whichever is earlier. The difficult task in Gap analysis is determining rate sensitivity. All investments, advances, deposits, borrowings, purchased funds etc. that mature/reprice within a specified time frame are interest rate sensitive. The Gaps may be identified in the following time buckets:

- Upto 1 month
- Over one month and Upto 3 months
- Over 3 months and Upto 6 months
- Over 6 months and Upto 12 months
- Over 1 year and Upto 3 years
- Over 3 years and Upto 5 years
- Over 5 years
- Non-sensitive

The Gap is the difference between Rate Sensitive Assets (RSA) and Rate Sensitive Liabilities (RSL) for each time bucket. The positive Gap indicates that it has more RSAs than RSLs whereas the negative Gap indicates that it has more RSLs. The Gap reports indicate whether the institution is in a position to benefit from rising interest rates by having a positive Gap (RSA > RSL) or whether it is in a position to benefit from declining interest rates by a negative Gap (RSL > RSA). The Gap can, therefore, be used as a measure of interest rate sensitivity.

Each bank should set prudential limits on individual Gaps with the approval of the Board/Management Committee. The prudential limits should have a bearing on the total assets, earning assets or equity. The banks may work out earnings at risk, based on their views on interest rate movements and fix a prudent level with the approval of the Board/Management Committee. RBI will also introduce capital adequacy for market risks in due course.

CHAPTER-3

INTRODUCTION OF RETAIL BANKING

INTRODUCTION OF RETAIL BANKING

Retail Banking Overview

With a jump in the Indian economy from a manufacturing sector to a service sector, banking as a whole is undergoing a change. A larger option for the consumer is getting translated into a larger demand for financial products and customization of services is fast becoming the norm than a competitive advantage. With the Retail banking sector expected to grow at a rate of 30% players are focusing more and more on the Retail and are waking up to the potential of this sector of banking. At the same time, the banking sector as a whole is seeing structural changes in regulatory frameworks and securitization. The faster one adapts to these changing dynamics, the faster is one expected to gain the advantage.

Retail Banking

Retail banking refers to banking in which banks undergo transactions directly with consumers, rather than corporations or other banks. Services offered include: savings and checking account, mortgages, personal loans, debit cards, credit cards, and so forth.

Objectives of Retail Banking

- Provide target customers a full range of financial products and banking services.
- Give the customers a one stop window for all their banking requirements.

Types of Retail Banks

- **Commercial Bank**: After the Great Depression, the U.S. Congress required that banks only engage in banking activities, whereas investment banks were limited to capital market activities. Since the two no longer have to be under separate ownership, some use the term "commercial bank" to refer to a bank or a division of a bank that mostly deals with deposits and loans from corporations or large businesses.
- **Community Banks**: Locally operated financial institutions that empower employees to make local decisions to serve their customers and the partners
- **Community Development Banks:** Regulated banks that provide financial services and credit to under-served markets or populations.

Postal Savings Banks: Savings banks associated with national postal systems.
- **Private Banks**: Manage the assets of high net worth individuals.
- **Offshore Banks**: Banks located in jurisdictions with low taxation and regulation. Many offshore banks are essentially private banks.

- **Savings Bank:** Their original objective was to provide easily accessible savings products to all strata of the population. Nowadays, savings banks have kept their focus on retail banking: payments, savings products, credits and insurances for individuals or small and medium-sized enterprises. Apart from this retail focus, they also differ from commercial banks by their broadly decentralised distribution network, providing local and regional outreach and by their socially responsible approach to business and society.
- **Building Societies and Landesbanks**: Conduct retail banking.
- **Ethical Banks**: Banks that prioritize the transparency of all operations and make only what they consider to be socially-responsible investments.
- **Islamic Banks:** Banks that transact according to Islamic principles.

The Retail Banking environment today is changing fast. The changing customer demographics demands to create a differentiated application based on scalable technology, improved service and banking convenience. Higher penetration of technology and increase in global literacy levels has set up the expectations of the customer higher than never before. Increasing use of modern technology has further enhanced reach and accessibility.

The market today gives all retail bankers a challenge to provide multiple and innovative contemporary services to the customer through a consolidated window as so to ensure that the bank's customer gets "Uniformity and Consistency" of service delivery across time and at every touch point across all channels. The pace of innovation is accelerating and security threat has become prime of all electronic transactions. High cost structure rendering mass-market servicing is prohibitively expensive.

Present day tech-savvy bankers are now more looking at reduction in their operating costs by adopting scalable and secure technology thereby reducing the response time to their customers so as to improve their client base and economies of scale.

The solution lies to market demands and challenges lies in innovation of new offering with minimum dependence on branches; a multi-channel bank and to eliminate the disadvantage of an inadequate branch network. Generation of leads to cross sell and creating additional revenues with utmost customer satisfaction has become focal point worldwide for the success of a bank.

Features of Retail Banking

- On-line, real time processing and cost saving through Multi channel transactions.
- Relationship banking enabled through extensive mining of all customer transactions.
- Rapid time-to-market with new product and service offerings.
- Rapid Customer Acquisition. Multi-currency and multi-language support so as to ensure geographic reach across continents.
- Multi-layer security, monitoring and reporting.
- Seamless integration with advanced delivery systems including teller and branch automated teller machine (ATM), point-of-sale (POS), interactive voice response, corporate and home banking

A customer-centric collection system

Banks and Financial Institutions have consciously become aggressive in retail lending. One of the key reasons for this is to build customer relationship and retain them. While this helps improve the top line, a huge collection / recovery machinery is needed to protect and improve the bottom line.

With continuous changes in the global economy, new technology and increased competition, managing receivables is becoming even more challenging. This has increased the pressure on banks in terms of managing delinquencies and customer attrition. Banks are increasingly feeling the need to review their approach, innovate and bring about new techniques to delinquencies.

For success of any collection / recovery strategy, meticulous follow up and action at the appropriate time are essential. Early warning systems, to prompt a bank engaged in lending take decisions on a change in the strategy is vital in today's highly competitive environment.

Origination (customer acquiring process) and Receivables management are two sides of the same coin. Risk management without an effective receivables management process is incomplete and would often render futile, the bank must take precautions in the origination process. This would force impracticable controls and safety measures, seriously impairing the growth of bank and therefore the top line.

A Good Receivables Management System Support

- Better utilization of money (re-deployment of funds)
- Higher profitability (more owned funds)
- Lower non performing loans
- Better capital adequacy
  Lower borrowing rates
- Higher competitive advantage
- Easier quality customer acquisition
- Higher market share
- Higher confidence to target sub-prime customer segment
- Confidence to launch products with higher risk
- Provide opportunity to increase non interest income (better realization of penalty fees)
- Lowers operational cost

7- Key Steps

As retail banks sees to modularize and standardize their process models they should follow seven steps.

- Group similar process steps within individual products' end to end process. But be sure to cut these groups similarly in terms of scope and task.
- Assess commonality among these groups of process steps. To what extent is the underlying process similar across product, across channels and along the end to end process.
- Drive to standardize business rules for common tasks. Question the relevance of differences. Often differences are the result of arbitrary decisions and have no specific business justification.
- Combine the group into process modules and clearly define the input, output and processing for these modules.
- Assess strategic operational relevance for each module.
- Understand IT, legal and regulatory constraints.
- Designate specified IT tools to support each process module.

Need of Retail Banking

Poor industrial production due to lack of demand has resulted into poor credit off take. Banks cannot rely on big corporate. As there is regular rise in deposits, banks are flushed

with funds. But deployment avenues are not there. Looking at growing NPA's and high cost, banks do not want to take risk by manufacturers in recession. With narrowing investment opportunities and poor credit off take banks turn towards retail banking which present attractive opportunity with lesser risk and reasonable return.

Growing consumerism in India also encourages retail banking. The domain of retail banking market has tremendous growth potential and finance for companies as at present it is largely untapped. And this is a scenario the requirements of customers are growing. In the past people never believed in buying consumer goods on credit. But today the attitude is changing. The demand for consumer products has increased. Today about most of the consumer goods are purchased through finance scheme as against 6 years ago. In retailing of deposits also banks have better scope now. The stock market and the real estate market are not performing to the expectations of the investors. To tap this market, banks should come out with variety of new deposits products. Banks are also going for cross selling of products of other banks and financial institutions. This will boost the fee based income. With the spreads shrinking, banks need to focus on increasing the share of their non-interest income.

Due to recession and industrial slow-down, many of the corporate have either shelved or postponed their development plans. A number of corporate borrowers are side tracking and raising money through commercial paper and the debt market. These are not only cheaper than banks' credit but at times they succeed in raising money at rates below bank rates. To overcome these problems banks have formulated strategies to go for retail banking as major thrust area. Technology today plays an important role in sustaining one's competitive advantage. The internet banking is changing the banking industry and is having the major effect on banking relationship. Researchers emphasize that web technology is more important for retail financial services than for any other industry. Internet banking involves use of internet for delivery of banking products and services. It also helps in enabling integrated sales of other allied products. A successful internet banking solution offers:

- Exceptional rates on savings, CDs and many other money market instruments.
- Credit cards with low rates.
- Easy online applications for all accounts, including personal loans and mortgages.
- 24 hour account access.
- Quality Customer Service with personal attention.

Advantages previously held by large financial institutions have shrunk considerably. The internet has levelled the plane field and afforded open access to customers in the global market place. Internet banking is cost effective delivery channel for financial institutions.

Six Primary Drivers of Retail Banking Include:

- Improved customer access
- Facilitate the offering of more services.
- Increase customer loyalty
- Attract new customers
- Provide services offered by peers
- Reduce customer attrition

These are continuous forces that help retail banking to grow constantly. Also new players in retail banking should mainly focus on the above six key elements.

In today's world technology is changing continuously and future is becoming uncertain. Globalization, technology and emphasis on shareholder value are the three mare important forces that are reshaping the business around the world.

Banking industry itself is undergoing tremendous transformation. The traditional role of taking deposits and making loans is under pressure. Disintermediation of financial services, changing consumer life style, technology and threat from non-traditional sources are redefining the products and services that are rendered by traditional banks.

The challenge for banks is to be proactive in helping customers to manage their finances during this uncertain scenario. Customers are demanding more flexible and conveniently situated channel to be available at times that suits them and not the banks. Greater access to information has increased as, today customers are more aware of products and prices. They are less tolerant towards mistake. Successful banks will have to get it right the first time and all the time.

There are two models emerging in the banking scenario today. One of them is universal banking where banks attempt to provide products and services developed by them to the customers. The second type is that of a super market of financial services where banks not only offer their products but by of others as well.

Technology would help in meeting certain challenges. The advances in the past few years and the advent of internet made a big shift in the delivery of services.

On the retail side, banks have to use technology to the mass customer with improved services and drive down the costs. Data ware housing and mining would enable bank to understand the target customers better. The next challenge that could be overcome by technology is managing increased volumes and lowering down the transaction cost.

Technology would also need to be harness to increase productivity, improved information control and provide alternative means of delivery of services. This would help in achieving transparency which would further enhance banks mass market scope.

In order to remain in competition it is important that banks should turn historical information into knowledge about the consumer behaviour, change its people's skills to adapt a new environment as they will be the ones who generate shareholder value.

Relationship management is the core in banking industry today and customers never had it so good before. Banks have finally come of age and emphasis is meeting the needs of customers of a saving driven economy.
Consolidation within the banking industry with mergers and acquisitions between public and new private sector banks has indicated the beginning of new age in the banking arena. Banks' infrastructure and its workforce play a key role in marketing for its products. Banks these days finance almost everything from homes to cars, consumer

durables, education plans, senior citizens schemes and for children as well etc. Banks also retail mutual funds and insurance hence converting into one stop financial services supermarket.

Services designed for customer convenience like “Bill Desk” offering universal electronic bill presentment and payments service that will allow banks to cater to more & more potential urban customers.

Taking reference from the past couple of years it can be stated that with intensifying competition among various banks, focus should be on providing more efficient services than merely concentrating on the products. The need of the hour is to identify and anticipate customer requirements and develop threshold capabilities for servicing those needs.

Software such as CRM (Customer Relationship Management) enables banks to store relevant customer information in its database which can be utilized at the times of needs. Private and foreign banks as it enable them to know their customers better in an ever changing environment where customers are surrounded with many options to switch over. Banks are trying to prove their worth by enticing customers with a surplus of value added services.

Emerging Changes in Retail Banking

In today’s world technology is changing continuously and predicting the future is becoming increasingly difficult. Globalization, technology and emphasis on Shareholder’s value are the three most important forces that are radically reshaping the business around the world.

The banking industry itself is undergoing tremendous transformation. The traditional role of taking deposits and making loans is under pressure. Disintermediation of financial services, changing consumer lifestyle, technology, and threat from non-traditional sources are redefining the products/services and their delivery as rendered by traditional bank.

The challenge for banks is to be proactive in helping customers to manage their finances during this uncertain financial future. Customers are demanding more flexible and conveniently situated channel to be available at times that suits them and not the bank. Greater access to information has increased completion, as customers today are more aware of products and their prices. They are also less tolerant of mistakes. Successful banks will have to get it right the first time and all the time.
There are two models emerging in the banking scenario today. One of them is universal banking in which banks are attempting to provide products and service to customers developed by them. The second is that of a supermarket of financial services banks not only offer the products developed by them but by other banks also.
Retail investors’ transaction on this service competition from non-traditional sources is becoming increasingly important. Now banking will be competing having financial

muscle, selling skills and production and distribution skills. Technology would help banks meeting certain challenges. The advances in the past few years and the advent of internet call caused a big shift in the delivery of services. On the retail side banks will have to use technology to reach the mass customers, improve services and drive down the costs. Data warehousing and mining would be required to enable banks to understand and target customers better.

The next challenge that technology would help banks in managing increased volumes and lowering of transaction costs. Technology would also need to be harnessed to increase productivity, improve control on information and provide alternative means of delivery of services. In the new schemes of things audio (telephone banking) and video channels (TV, internet) would emerge as main alternative to the branch. Interactive broadcasting holds the promise of immense consumer choice.

Technology brings with it certain issues. The power of technology can make the delivery of financial services borderless where the restraining factor has infected the human element. These new delivery channels have phase out the old ones at pace that customers find it convenient. Nevertheless, banks have to consider the fact that on one hand technology requires heavy investments in hardware and application and on the other it brings more transparency, which in turn put huge pressure on margins.

The winners in the next century would be the ones who turn historical information into “knowledge” about the consumer behaviour, make the best technology win and change people’s skills to adapt to the new environment. They will be the ones who generate Shareholder value.

Relationship management is the name of the game in the banking industry today and the customers never had it so good before. In a saving driven economy like ours banks have finally come off age and emphasis is now on making the customer feel that he is the king.

Consolidations within the banking industry with mergers and acquisitions between public and new private sectors banks have entered in new age of business in the banking arena.

Among merging trends Bancassurance is the new buzz word for the marketing of insurance of insurance products by tapping the retail distribution network of banks. It is felt that banks can play a key role in the marketing of insurance products as they already have the infrastructure and organizational workforce in place.
Banks these days finance almost everything from homes to cars. Customer durables, education, schemes for senior citizens, schemes for children and also retail mutual funds and insurance thereby converting a one stop financial services Supermarket.
Services designed for customers’ convenience like ‘Bill Desk’ offering universal electronic bill presentment and payment services that will allow customers to receive a portion of the urban customers’ loyalties.

However, it has become increasingly evident over the past couple of years. With intensifying competition among various banks that focus must now to shift services rather than mere products. The need of the hour is to identify and anticipate customer requirement and develop capability of servicing those needs.

Software such as CRM (Customer Relationship Management) which enable heaps of relevant customer information to be stored in computers and to be retrieved at the click of a button, and becoming popular among public, private and foreign banks as it enables them to know their customer better in an ever changing environment where loyalties are fickle and competition is fierce. Banks are trying to prove their worth by wooing customers with a plethora of value added services as now the race is to be better than the best.

Products and Services Offered

Most of the banks provide similar kinds and services in Retail Banking. However there are few differences attracted with the products, fees charged, and rate of interest etc. the following are the products and services offered by the banks.

- Saving account
- Current account
- Demat account
- Fixed account
- ATM
- Net banking
- Debit cards
- Credit cards
- Phone banking
- Mobile banking
- Electronic transfer of funds
- Mutual funds
- Door step delivery
- Forex services
- Wealth management services
- Loans:
    - ✓ Home loans
    - ✓ Personal loans
    - ✓ Loans against shares
    - ✓ Vehicle loans (commercial vehicles, cars & two wheelers)

Saving Account

Each bank has its own criteria for opening a saving account. However basic difference lies in average minimum cash balance requirement between public sector and private banks is different.

Following are some key features of saving account:

- Generally a debit cum ATM card is provided with the convenience of acceptance at merchant establishments and cash withdrawal at ATMs.
- Internet banking is offered free of cost in most of the banks.
- One can give standing instructions like transferring to fixed deposit accounts at regular intervals.
- Nomination facility is available.
- Interest is payable half yearly.
- Non-maintenance of the minimum average quarterly balance attracts a fee, which differs from bank to bank.

Current account

Current account is similar to savings account barring few changes. The main difference is that one need to pay interest on the amount of deposits. These are some of the features of current account:

- Make payment by giving standing instructions
- Remit funds from any part of the country to your account
- Overdraft facility
- Nomination facility available
- Low minimum balance required
- Free ATM cum debit card, Net banking.

Fixed Deposit

Fixed deposits generally stand for safety credibility and attractive rates of interest. These deposits have been further packed with the following features:

Traditional

- Interest payable monthly, quarterly, half yearly as per customers' convenience.
- Maturity period ranges from 15 days to 10 years.

Reinvestment

- Interest is compounded quarterly and reinvested with principal amount.
- Maturity period ranges from 6 months to 10 years.

Demat account

An account which shows shares in dematerialization form, which is prerequisites of share trading, is called Demat account. These accounts are opened with two depositories by banks, broking houses and brokers. In India, there are two depositories- National Securities Depositories Limited (NSDL) and Central Depositories Services Limited (CSDL). Under the depositories act, investors can avail of the services of the depositories through Depositories Participants (DP) such as ICICI bank. DP's are like bank branches wherein shares in physical forms need to be deposited for converting the same to electronic form.

ATM services

ATM means automated teller machines, which can be operated by using an ATM card. It helps in withdrawing money 24*7*365 from anywhere. Generally all the account holders are equipped with ATM cards, which is subject to annual fee.

With this card, there is no need to carry cash in the wallet and one need not fear of overspending on their credit card. One can now withdraw cash and make purchases anytime one wishes to.

Net Banking

The internet banking portal of bank enable its retail banking customers to operate their accounts all across in India, removing the restrictions imposed by geography and time. It is the platform that enables the customers to carry out their banking activities from their desktop, aided by the power and convenience of the internet.

Availing the internet banking services, one can do the following normal banking transactions online:

- Self accounts funds transfer across India.
- Third party transfers in the same branch
- New account opening
- Demand Draft requests
- Standing instructions
- New Cheque-book request

Apart from these the other salient value added features available are:

- Railway tickets booking.
- Utility bill payments
- LIC and other insurance premium payments
- Mutual funds investments
- Credit card dues payments

- Deposit taxes
- Setting up SMS alerts from transaction information.

Net banking leads to cost reduction for banks and convenience for customers. The net banking charges fifers from banks to banks. The bank should have strong security system in place to avoid hacking of sensitive information.

Debit and Credit Cards

The bank offers a varied range of cards to suit the customers' requirements. These cards having a wide acceptance, nationally and internationally, coupled with benefits of channels like internet and mobile, which enhances ones experience.

Credit cards give a facility of cash, convenience and range of benefits anywhere in the world. These benefits range from lifetime free cards, insurance benefits, global emergency assistance services, discounts, utility payments, travel discounts and much more.Debit card is a revolutionary form of cash that allows customers to address their bank account around the clock, around the world. The debit card is used for shopping at selected outlets in India and worldwide.

Phone banking endeavour to raise the bar to meet the rising requirements of their customers by providing quality products and services to suit varied banking needs. Phone banking service is yet another, technology and customer centric step in that direction.

Phone banking services enables to access authentic, instantaneous information on account balances and transactions. The service is available totally free of cost round the clock 365 days a year. A telephone and a 4-digit TIN (Telephone Identification Number) is need to access the account. The different services available through phone banking are:

Accounts related services

- Updated balance inquiry
- Balance as ob date
- Last five transactions
- Statement of accounts by fax, e-mail or post.
- Request for cheque-book
- Hot listing of ATMs or debit cards.
- Status of cheque issued or deposited
- Funds in clearing
- Bills payment details

Demat account related services

- Details of the Demat account
- Holding details in ascending or descending orders
- Holding statement by Fax, Mail or E-mail
- Billing details
- Billing details by Fax, mail or e-mail

Product Information

- Deposit rates
- Foreign Exchange Rates.

Mobile Banking

In today's work environment, daily deadlines, appointments and meetings are inevitable. And often, one is hard pressed for time. In such a situation, anytime, anywhere banking comes as a great convenience. By M- banking or mobile banking all the transactions are done in a jiffy through the mobile phone.

The banks put their banking services in their customers' pockets. Mobile banking comes in as a part of banks initiative to offer multiple channels providing convenience to its customers, a versatile multifunctional, free service that is accessible and viewable on the display screen of customers' mobiles.

The service allows a mobile phone user to carry on the transactions using SMS facility. All one needs to do is to type out a short text message on the mobile and send it out to a pre-designated number. The response is sent back as an SMS.

One needs to have an account in the respective bank that offers mobile banking facility. In order to access this service an account holder can apply for mobile banking through the account opening document. The transactions on M-banking can range from balance inquiry to bill payments and account statements.
This facility is available on all the mobile phones irrespective of cellular service provider, the technology works on Push-Pull architecture. The customer drives Pull services and the bank sends out Push services to the customer.

Electronic Fund Transfer

EFT is the new facility provided to the exporters for submitting the license fee through the internet without visiting the bank for the payment. This procedure is being proposed to facilitate payments through electronic means. The facility shall be available only for electronic field applications. This electronic payment facility is applicable for deposit of application fees, in case of all licensing schemes (for which Electronic Filling of application facility is available).

An exporter having valid importer code need to have an internet banking account, ID and password from any of the banks. License fee can be submitted simultaneously while filling the E-Com application without visiting the bank. It will also reduce the time required to make payment as compared to manual mode like DD etc.

Mutual Funds

Mutual funds pool money of several of the investors to purchase a wide variety of securities while pursuing a specific goal. Returns generated are distributed to the investors. The investment is done on the basis of prevailing Net Asset Values of various schemes; however they are subjected to market risk. Banks offer investment in Mutual Funds through Multiple Channels as follows:

- Bank Branches. Bank ATMs.
- Bank Website

Dedicated workforce to serve:

Before being deputed, officers complete a comprehensive training and once deputed, they receive through instructions in financial planning skills and techniques. Throughout their careers officers also attend programs to update their skills.

- All officers in charge of Mutual Funds are certified professionals by AMFI(Association of Mutual Funds in India)
- Many of these officers also hold professional degrees like, MBA, CA, ICWA, CFA, etc.
- Banks keep the investors updated on the latest happenings in the Mutual Fund industry and the various financial markets through regular electronic Updates. They also sent out a monthly magazine to customers.

Door Step Delivery

Door step delivery is a service that transports cash, cheques and drafts, at the customer's convenience to his/her residence or office.

Pick up Facility:

Customer can pick up cash, cheques and drafts from his office and deposit in his account.

Delivery facility:

- The customer can get cash, cheques and drafts and pay orders to his office. The following are the advantages of door-step delivery:
- Security of the customer's hard money with the bank's safety measures during each transaction.
- Save on staff costs.
- Skip the queues to deposit or withdraw cash.

Forex Services

Banks provide Forex services in the following manner:

Spot contracts: spot contract is the simplest and the most common foreign exchange transaction very widely used by the corporate to cover their receivables and payables. It is a commitment by the client to buy or sell one currency against another at a fixed rate of delivery two business days after the business days after the transaction.

Forward contracts: with forward contracts, one can negotiate a rate today to exchange foreign currency on a future date. Forward contract is a contract on a future in a future date a predetermined rate. The rate on the forward exchange rate contract is based on the spot rate and the differential in interest rates between the two markets involved. This type of transaction helps to manage foreign exchange risk because by setting the exchange rate in advance, one can eliminate the uncertainty related to fluctuations in currency until the time one pays for it or receives it.

Forward Rate Agreement: A forward rate agreement is a financial contract between a bank and the customer to exchange interest payments for a "notional principal" amount on settlement date, for a specific period from start date to maturity date. Accordingly on the settlement date, cash payments based on contract and settlement rate are made by the bank and the customers. The settlement rate is the agreed benchmark or hedging the interest rate risk arising of lending of lending or borrowing made at fixed or variable interest rates.

Currency Swaps: A foreign exchange transaction in which a bank agrees to exchange specified amount of one currency for another currency at a fixed price, that is the bank and the customer agree to exchange payment streams or cash flows both in terms of principle and interest. Simply stated, currency swap is an extended forward contract and normally for periods beyond one year.

Utility Payment Services

Through this service, the customer can pay bills of following public utilities:

- Electricity bill
- Telephone bill
- Credit cards
- Mobile bill
- Insurance premiums.

Apart from this, the customer can also train/air tickets by paying nominal.

Wealth Management

Wealth Management means banking services provided primarily to high net worth individuals (HNI). It focuses on performance and valuation rather than a plain emphasis on keeping money safe secure. Wealth includes existing as well as fresh funds and apart from the traditional equity (both listed and private equity), debt and mutual funds, comprises real estate, art jeweller etc. the advantages banks have in providing this

service is that there is certain seamlessness in the entire operation, from marketing and investment decision to the proceeds, including charges being credited or debited to customer's account. Further, the essence of this business is security and confidentiality, which is what good banking essentially, as all about. Wealth management also known as Private banking and offers:

Advisory services: flexible, unbiased investment advice customized to meet client needs.

Transaction support: All transactions, both in the primary and secondary markets through a panel of brokers.

Custodial services: Important from the point of view of removal of settlement hassles and efficient follow-up of all corporate actions.

Loans

The following features are categorized as personal loans:

- Loans for salaried and self employed individuals.
- Loans are available from 12-60 months.
- No security, collateral or guarantors required.
- Loans can be used for any purpose with no questions regarding the end use of the loan.
- All loan repayments are done via. Equated monthly instalments(EMI)

Vehicle loans

Commercial vehicle:
Funding of products include trucks, trippers, light commercial vehicles, pick-ups, 3wheelers etc.

Range of services: funding of new vehicles, refinance on used vehicle, balance transfer on high cost loans and other banking products.

Car loans:

- Tie-ups with all leading automobile manufacturers to ensure the best deals.
- Flexible schemes and quick processing.
- Hassel-free application process on one click.

Housing loans

Most of the banks today provide home loans at very competitive rates. The rate of interest has been increased due to global financial slowdown as compared to past decade.

Loans against Shares and Debentures

Loans against securities enable to obtain loans against the securities that a customer holds. So that one can get instant liquidity without having to sell securities. One can avail loans up to a certain amount against shares/debentures to enable to meet contingencies, personal needs or even for subscribing to rights or new shares. A current account will be opened and the customer can withdraw money as and when he/she requires. Interest will be charged only on the amount withdraw and for the time span utilized. Loans will not be sanctioned for:

- Speculative purposes
- Inter-corporate investments
- Acquiring controlling interest in company/companies.

Rating

Debentures must have been rated AA+ or higher by CRISIL or equivalent rating by any other reputed agency like ICRA, etc. Most of the banks offer loans against:

- Demat Shares
- RBI Relief Bonds
- Mutual Funds Units
- Life insurance policies (Single Premium)

CHAPTER-4

RESEARCH METHODOLOGY

Title of the Study:

"AN ANALYSIS OF RETAIL BANKING IN INDIAN BANKING SECTOR"

Objective:

- To understand the Indian Banking System.
- To understand the retail trends followed by the modern retail Banks.

Scope of study:

- My study will help to understanding the Indian banking system as well as to identify the existing bank "Market reputation"
- My study will provide information about general practices adopted by the various bank in order to carry their retail banking business.

Type of research:

Research design	Descriptive

Sample size 10 commercial banks

Method of selecting sample:

- **Questionnaire:** The data was collected through questionnaire, in which different question were asked.

Limitations of the study:

Every research has its own limitations and the present research work is no exception of his general rule. The inherent limitation of the study are as under- .

- The structural constraint was that the survey was concluded for determining the pre-determined objectives.
- Some persons are not response properly and the sample was chosen based on convenience and availability of persons.
- This study is geographically restricted to Udaipur city only.
- The sample size is small due to the specified reasons.
- Findings are based on sample survey through questionnaires method.
- Hence there is a scope for the respondents to be biased.
- The time period in which the project has to be completed was very less

Questionnaire Analysis:

METHODOLOGY

For the purpose of my study I decided to take 10 major players in the banking industry. These banks are chosen from the urban area of Udaipur and hence all my findings are pertaining to the urban area only.

The banks which I visited include;

Private Banks	Public Banks
ICICI	SBI
AXIS	Bank of Baroda
HSBC	IDBI
HDFC	Indian Overseas Bank
KOTAK MAHINDRA BANK	Vijaya Bank

Through this survey I tried to find out how is the retail activities are conducted and carried over by these banks.

The questionnaire is designed to gain an insight of the general practices adopted by the banks in order to carry on their retail banking business.

Following are the **findings** and the analysis of the survey conducted by me. The questionnaire for the same has been attached in the annexure.

S. No.	Details	No. of Banks	%
I	**Products and services**		
i	Saving account	30	100

II	Customers	No. of Banks	%
i	Less than 20	1	0.3
ii	20 to 40	16	4.8
iii	40 to 60	4	2.4
iv	60 and above	9	2.7

III	Types of customers	Most	Least
i	Individuals	9	2.7
ii	Corporate firms	6	1.8
iii	Co-operative society	6	1.8
iv	Local authorities	6	1.8
v	Illiterates	8	2.4

IV	Target segment	Most	Least
i	Students	12	4
ii	Professionals	5	3
iii	Corporate		
iv	HNIs	9	2.7
v	Senior citizens	4	2.4

V	Channels for communication	Most	Least
i	Personal banking	16	4.8
ii	Internet banking	8	2.4
iii	ATMs	6	1.8

VI	Modes of communication	No. of banks	%
i	Pamphlet/booklet	3	0.9

ii	Telemarketing	5	1.5
iii	Bill statement	7	2.1
iv	Picked up from ATM	8	2.4
v	Newspapers	5	1.5

VII	**Share of retail banking**	**No. of banks**	**%**
i	Less than 15%	6	1.8
ii	15% to 30%	1	0.3
iii	30% to 50%	9	2.7
iv	More than 50%	12	3.6

VIII	**Importance of retail banking**	**No. of banks**	**%**
i	Gives more margin	6	1.8
ii	Growth prospects	9	2.7
iii	Revenue from rural segment	9	2.7
iv	Cross selling	3	0.9
v	Expand customer	3	0.9

X	**Rate of defaults**	**No. of banks**	**%**
i	High	2	20
ii	Moderate	1	10
iii	Low	7	70

XIII.	Products in demand before global slowdown	No. of banks	%
i	Saving account	8	80
ii	Current account	6	60

Chapter-5

FACT AND FINDINGS

FACT AND FINDINGS

Retail Risk Management

Employing Economic Capital allows the institution to compare the size of each risk and its capital costs to the cost of any potential risk mitigation, facilitating better decision making. To reduce the risk in retail banking practices strategy, tactics, and specialization are three reasons why more retail bankers are using economic capital.

Many banking experts fear a wake of rising interest rates and energy prices, inflation fears, and cooling house prices. They believe that the best bankers can hope for is a soft landing for the economy. However, even a soft landing might have a severe effect on retail banking businesses in terms of sharply rising credit losses and sharply falling business volumes. Historically, economic capital has been slow to take hold in retail banking because losses have been perceived as less volatile than in commercial lending.

However, three considerations are now having a major consideration turning for the retail bankers toward using economic capital:

Strategy

Amid expanding retail product lines, banks are realizing that conventional measures of risk and profitability make it difficult to compare the long-run performances of various businesses. For example, a bank can not compare the profitability of a credit card business with that of fee based businesses after taking long term loss volatilities into account.

Tactics

Banks continue to seek a wider spectrum of customers, including non-prime customers, across a range of products. As these markets expand and margins compress due to competitive pressures, it is becoming imperative that banks take into account economic capital costs in their profitability and pricing decisions. Banks are really concerned about the risk segments which are making risk-adjusted profits and the way by which the bank can drive up long-run profitability through risk-adjusted pricing.

Focus

Retail banks that specialize in products or geographical regions have prospered over the last decade, but ratings agencies and regulators are concerned about the effect of concentration risks on capital adequacy in the event of a downturn.

Issues regarding the capital cost of preserving business focus will take on a sharper edge over the next couple of years.

Comparing the long-run performance of retail businesses using traditional measures, such as return on assets or return on equity, can be complicated and misleading. Economic capital attempts to solve this problem by supporting the banks to compare

the (risk-adjusted) profitability of different activities over the whole economic cycle and see more clearly which the most deserving areas of further investment are. Economic capital analysis must be based on estimates of particular risk factors that drive risk in each retail portfolio.

Banks must not be tempted to use simplistic proxies for risk, such as the cost of regulatory capital or generalized capital factors based on information from other banks. These rule-of-thumb approaches fail to measure borrower risk (i.e., probability of default) in an accurate manner, but in retail there are many additional complicating factors.

A kind of gap that typically exists between accurate risk-adjusted return on capital (RAROC) numbers based on economic capital and traditional return-on-equity calculations where risk cost estimates are based on a mix of regulatory capital costs and management judgment.

It is experienced that the gap tends to be widest for business lines such as mortgage lending and direct vehicle lending**,** where economic capital is usually much lower than regulatory capital.

The economic capital number for most retail lines of business tends to be lower than the regulatory capital requirement for that business. If economic capital analyses are to support strategic decisions, banks must take into account a range of risk types—not just credit risk. This is especially important for retail banking because, unlike commercial lending, some retail activities attract virtually no credit risk but do attract other kinds of risk, such as business risk, operating risk. Approaches that focus overly on credit risk ignore the capital costs of these other risks.

LINES of BUSINESS	BUSINESS RISK	FINANCIAL RISK	EVENT RISK
Checking and savings	• Competition • Disintermediation • Operating leverage		• Fraud • Robbery • Employees

Credit cards	• Attrition/Inactivit y • Competition • Strategic regulations		• Consumer litigation • Fraud • Employees
Mortgages	• Competition • Unbundled value chain • Technology costs	Fluctuating real estate markets	• Consumer litigation • System • Model • Compliance risks
Autolending/Leasing	• Competition • Adverse selection	Residual value	• Consumer litigation • System • Model • Compliance risks • Fiduciary risk
Asset management	Expense ratio Net fund flows	Revenue as a % of the assets under management	Fiduciary risk
Brokerage	Competition	Commission and volumes varying with market	Consumer litigation System

The given table offers some examples of the kind of risks that can substantially affect economic capital for various retail business lines. For example, as banks have discovered over the last few years, interest rate risk can be a significant and complex driver of risk in mortgage origination and servicing. A rise in interest rates tends to drive business volumes down (as prepayments fall) while driving up the value of mortgage

servicing rights (as mortgages stick around longer). Interest rate sensitivity in mortgage businesses often account for more economic capital than operational risks, despite the attention paid to the latter risk source over the last few years.

Not all retail businesses incur financial risks, but most are affected to some degree, by the business risks. Business risk results from the volatility of revenues at a particular business and the way this interacts with the business's operating leverage (defined as the balance between the fixed and variable components of a bank's operating cost base). The risk parameters for business risks in retail operations can be estimated by looking at historical bank operating information (e.g., revenue and expense volatilities) and by factoring in expert judgments from business leaders.

This is one of the key emerging areas in retail economic capital analysis, not least because bank executives can manage their business risk profile to some degree through altering bank strategies (e.g., by reducing terms for leasing property or by increasing flexibility in employment and remuneration practices).

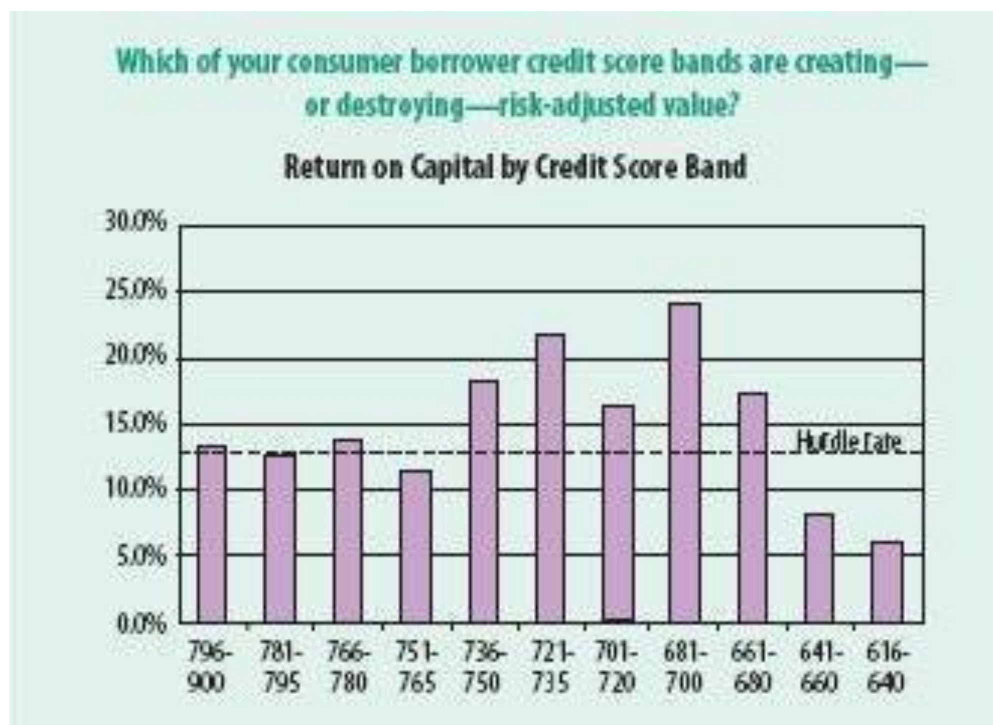
Economic Capital as Retail Risk Radar

When consumer credit quality deteriorates, it often brings a number of risks in retail banking. These range from the miss pricing of credit, to unexpected risks as risks associated with mortgage businesses, lower than expected real estate recoveries and business risk driven by unused capacity.

The time to deal with these risks is before a consumer slowdown turns them into actual losses. But simply making a superficial list of the potential risks that the bank is exposed to across its retail activities is not enough. The size of the risk and its cost in terms of bank capital remain unclear, and so the risk identification process rarely turns into a properly prioritized risk management process.

By contrast, the process of building an economic capital framework compels retail banks to consider their whole spectrum of risk in relation to capital costs. Banks can then compare the size of each risk and its capital costs to the cost of any potential risk improvement to decide whether they prefer to live with an exposure or to manage it in a more active way.

Improving Competitive Tactics



Where economic capital numbers are robust, they can be applied to tactical and competitive decisions. The above figure illustrates how retail banks can use economic capital based analysis to explore the profitability of their portfolios in terms of credit bureau score bands.

In this example, the bank is clearly finding it difficult to make returns above its hurdle rate (dotted line) in the competitive market for customers with good credit scores. The bank is also making low returns from borrowers with low credit scores— probably because it has underestimated the margins that it should be pricing into these offerings.

However, the analysis reveals that the bank is making a very healthy risk-adjusted margin on customers with slightly below-average creditworthiness in the 735-660 range. The bank in this figure might use this analysis to alter its tactics in various ways. For example, it might:

- Compete more fiercely for customers in the 735-660 range.
- Attempt to build a wider relationship with high-credit score customers so that it makes money from these customers overall.
- Make quite subtle shifts in its offerings to low-credit-score customers in terms of reducing limits, reducing maturity, increasing collateral, securing guarantees,

or improving pricing to tilt these relationships back into risk- adjusted profitability.

The great benefit of risk factor- based economic capital analysis is that it tells the bank exactly how much it must alter each risk and return factor to influence a particular credit segment. Banks must accurately measure all the risks associated with a given portfolio, including default risks in terms of relative credit scores.

The positive factor for retail banks is that the data-rich nature of retail credit markets and the wide use of standardized credit scores make it relatively easy for economic capital to estimate borrower probability of default. Indeed, many banks should think of this as a way to overcome the existing limitations:

- Where banks do not have good internal data on borrower default, bureau score bands offer a decent substitute because they are easy to link to default rates using data published by the credit bureaus.
- Where banks do have good internal data, they should consider building custom scoring models that outperform bureau scores in terms of risk prediction. The bank can then use its risk-adjusted profitability analysis to identify and compete for customers.

Retail Concentration Risks Regulators and ratings agencies increasingly ask banks with regional and product concentrations to explain how they assess the effect of these concentrations on their capital adequacy. It is done through economic capital analysis which is designed to relate a bank's whole portfolio of risk to the amount of capital the bank must hold if it is to achieve a particular solvency target.

However, implementing an economic capital model means estimating correlation numbers for each retail risk portfolio; to do this, banks will have to turn to external data sources. This is more problematic for retail than for commercial lending, where researchers can to some degree depend on the analysis of correlations in the movement of equity prices on the public stock exchanges.

Finally, banks with both commercial and retail lending portfolios should take care to apply methodologies that accurately aggregate the capital from different portfolios and risk types. These banks often gain important diversification benefits from their retail portfolios at the enterprise level, so poor aggregation methodologies tend to significantly overestimate the bank's capital requirement.

Chapter-6

ANALYSIS AND INTERPRETATION

ANALYSIS AND INTERPRETATION

Analysis:

I). As per the findings we can state that the traditional services like saving account, current account, fixed deposits are provided by all the banks but demat account is still restricted to 80% only. In the category of loan segment home loan is provided by all the banks. Vehicle and personal loans accounts for 80% and 60% respectively. Whereas loans against shares is offered by 70%. Services like electronic transfer (100%), debit/credit card (90%), phone banking (90%), net banking (90%) and mobile banking (70%) are being offered by a fairly large number of banks, thus, more and more number of banks is adopting the new technology in order to cater to their potential customers. Due to increase in the international transactions 100% banks today are dealing in foreign exchange.

But wealth management and door step delivery is limited up to 50% banks only.

II). As per the findings of the survey 80% of the banks have their daily customer- walk-in of nearly 60 and above. So this can be stated that today also people prefer to carry on their financial transactions by them; they don't prefer to conduct their transactions through new technological means like net or mobile banking. Large banks like ICICI have approximately 500 walk in customers per day. **III).** Category of customers visiting the Banks:

Individuals are the ones who are visiting the banks most for various financial transactions. Corporate firms and co-operative society are also conducting their banking transactions on a fairly basis. It is the illiterate segment who still not turned out to be a regular customer of banks. It might be because of the reason that today also they are engaged with the unorganized lenders (moneylenders). Hence, approachable segment like individuals and corporate the banks should also target to the illiterates mainly belonging to the remote areas; in order to mobilize their income into savings.

IV). Most targeted segment by the banks:

Keeping in view the competitive trends banks are almost trying to cover each and every segment where they could serve their potential customers. The most targeted segments of the banks turned out to be professionals (due to stable income) and senior citizens (pertaining to saving habits because of arising needs). Apart from them banks like ICICI are focusing on NRIs.

V). Channels used by the banks to deliver the products:

According to the banks personal banking is the most in use channel in order to deliver the products by them. Besides this banks have moved towards technological up gradation; as they now widely use sources like internet banking and ATMs, the same can be seen in the above findings too. Telephone remains the least used medium.

VI). In order to penetrate more into market nearly every bank believes in corresponding with the customers about its new offerings. According to 80% banks, newspapers are the most common means in order to communicate about their new products and services with its potential customers and also because through newspapers a wider area can be covered more economically and easily. 60% of the banks are also conducting their activities through booklets/pamphlets. Telemarketing again remains least preferred having a share of 20% only.

VII). According to 40% of banks retail activities constitute more than 50% of their total banking business. As the demand for retail products like loans, credit/debit cards etc. is increasing the share of retail banking in the total banking business is also expanding considerably. 30% banks have retail activity of less than 15% in their total operations, thus mostly banks are either focusing completely on the retail business or they are not conducting it as its major set of activities.

VIII). 80% of the banks believe that retail banking is important to them as it will enlarge their customer base which is significant to achieve better growth prospects which was supported by 60% of the banks. This will help them in terms of revenue generation and to gain a competitive edge over the other peer players. Importance of retail segment in terms of covering more of rural segment is not that much considerable as it is favored by 30% banks only.

IX). Problems faced by banks while carrying out retail activities:

According to the banks the major challenges which they face while carrying out their retail banking business are operational problems and neck competition from the other players in the respective sector. The banks as a result experience a pressure on their margins. Non-performing assets are another issue which the banks can't easily under-estimate.

X). 70% of the banks says that they have seen a low level of NPAs, thus it can be stated that the banks are very careful in their operations and also keep a trackof their customer profile. Only 20% of the banks are facing an increase in their NPA level

XI). Strategy for Risk Management:

As per the banks surveyed in order to mitigate their risks, the banks are very cautious, especially in the present scenario as they look for quality borrowers who are credit-worthy and go by KYC (Know Your Customer) norms. As per our survey it was also

revealed that besides the above measures every bank has its own specific strategy to tone down its risks;
HDFC- They use the *CIBIL account* which is designed by RBI, where they can go through their borrowers' details, come out with the probability of the default rate and take the corrective actions if needed. **HSBC**-They have their own vertical catering for the purpose of risk management.

AXIS-They have their own policy-design primarily focusing on the aspect of risk management.

IDBI- They give importance to operational efficiency in order to keep a control on their risk level.

SBI- They have a continuous follow up in order to keep a track of their activities where they could take preventive measures when they sense any uncertainty.

Bank of Baroda believes in more comprehensive approach for their risk management. They do not rely on their internal database only (like balance-sheet) but they also look out for the market reports and prevailing market trends. **XII).** Reasons for non performing assets:

According to the banks, NPAs are attributable to a number of reasons like lack of operational efficiency, no proper follow up of the guidelines (KYC norms), improper understanding of the products and schemes. As far as customer is concerned in relation with NPAs than the reason varies from person to person; as the customer may fail to repay the instalment together with the principal amount due to his insufficient income, loss faced in the venture for which the loan must have been taken. As per the response of one of the banks, the probability of default by the customer intentionally is limited up to 0.1% only. Market conditions are also responsible for NPAs.

XIII). As per the findings before the global liquidity crisis 80% of the banks have seen a high demand for their saving account and personal loan. Current account, debit/ credit cards, vehicle loan, mutual funds, demat account and loan against shares were there with a moderate demand for 60% to 50% of banks. Demand for forex services was low for all the banks.

XIV). According to the banks after the slowdown where the banking sector experienced a major set-back; demand for all the financial products and services have gone down; these were having a considerable of demand before the slowdown. A fall in the Demat account was witnessed by a majority of the banks. Only 1% banks are having the demand for Demat account now. Only 2% banks are catering their customers with loan against shares, earlier it was 5%. But in case of fixed deposit the demand has not reduced to that extent it has reduced by only 1% whereas saving and current account have reduced to almost half of its earlier demand.

Chapter-7

SWOT ANALYSIS

SWOT ANALYSIS

[Strengths, Weaknesses, opportunities and Threat]

Strengths

- Existing retail banks and building societies have large database of customer information, with which to develop their revised marketing strategies.
- Existing banks and building societies have large networks of Automatic Teller Machines (ATMs) in place, and many millions of cardholders.
- The majority of customers who have personal savings, mortgages and investments with existing banks and building societies will be reluctant to suffer the inconvenience of moving their accounts.
- New entrants to the market can bring with them fresh thinking, and develop new ideas which are not hampered by traditional layers of traditionally minded management.
- Retail banks have regular flow of customers visiting their banks two or three a week, to which they can regularly merchandise new banking services. It is retail banks that control the primary flow of transactions, either in cash or electronic form.
- Retail banks generally enjoy a better image with the public than the public sector banks and insurance companies.
- Retail banking is very large and attractive market. The largest banks and financial organizations have access to massive financial resources.

Weaknesses

- Some of the existing retail banks have yet to fully adopt a user friendly approach to customers.
- Smaller organization will find it hard to keep pace with the technological investment needed to remain in the marketplace.
- While customers want convenience, they being given the hard sell, or being bombarded with sales literature.
- Existing investment in staff and branch networks makes it difficult to introduce changes quickly.
- Union resistance to staff reduction poses a major problem.
- Management immerged in many years of traditional banking practice is slow to adopt to new ideas.
- Many of the larger banks still have enormous investments in outdated or no computer systems which are in urgent need of modernization.
- Some of the voice response systems currently being used are unreliable.

- Instead of speeding connections, they place a barrier between the customer and bank in some cases making it almost impossible to get access to account information.

Opportunities

- Retail banking under the new diverse pattern, is a relatively new market, with many opportunities for innovation and new 'lifestyle' product development. The use of new technology to improve customer interference.
- There are opportunities of home banking via digital television.
- There opportunities for liaison between banks and retail banks to provide shop-based banking services.
- There are opportunities for the development of banking facilities in areas of specialized retailing, such as petrol stations. There will be increased use of non-bank locations for the installation of ATMs and kiosks.
- As new generation of computer-literate customers reach adulthood and their post productive years the demand for convenient banking will increase.
- The scale of people pensions and healthcare a major opportunity, as successive governments has reduced Department of Social Security DSS support.
- Large retail banks wishing to offer independent banking services are likely to apply for the own banking licenses.

Threats

- There are likely to be many new market entrants from the non-financial sector.
- The retail financial services market is in danger of becoming over supplied, bringing the probability of future casualties, mergers and acquisitions.
- There are likely to be increasing competition from large overseas banking corporations.
- Banks burdened by heavy overheads, may experience trouble attempting to maintain competitive pricing against new market entrant bringing specialized product to the market.
- Future customers are unlikely to develop the same degree of loyalty to a bank, as has been the case with their 21st century counter path.
- There will be continued government pressure to provide free or low cost banking services to customers.

CONCLUSION

&

SUGGESTION

CONCLUSION

Limitations of Retail Banking

The bank into retailing will have to face following bottlenecks in its operations

- Huge sales and promotion expenditure
- Managing human resources
- Managing technology
- Pressure on margins
- Continuous follow-up
- Attitude hurdles
- Security problems

Huge Sales and Promotion Expenditure

In order to survive in the world of fierce competition with so many players, each bank has to incur huge amount of funds on sales and promotion. No bank can deny this

expenditure because they need to build their image among the customers, to get business.

Managing Human Resources

Retail banking caters to the need of individual customers. For this purpose qualified and trained staff is needed to be maintained. For training those employees, banks spend a huge amount of money. Sometimes these trained personnel leave the job halfway which increases the expenditure of the bank. Apart from this banks also have to maintain various cells regarding customer grievance, employee grievance, etc.
which again increases the expenditure of the bank.

Managing Technology

Technology plays an important role in retail banking. Today majority of transactions in banks are done through ATMs, Mobile banking, Phone banking, Internet banking. For this purpose it is necessary effective and efficient management of technology. Maintaining technology incurs huge expenditure, which sometimes create problem for the banks to accumulate funds for these purposes.

Pressures on Margin

To retain the existing customer base as well as to expand, the banks are pressurized to keep the minimum prices possible. Thus the banks have huge pressures on their margins.

Continuous Follow-up

In order to earn more profit banks are going for mass banking. But in this race the maintenance of the customer base becomes very difficult. The problems like NPA's and delay in payment of usage changes occur which leads to losses for the banks. Thus the banks have to maintain continuous follow-up programs, which require efficient technology, human resources as well as surplus funds to control expenditure on such programs.

Attitude Hurdles

Earlier the major players in the banking industry were public sector banks. But due to the advent of liberalization and globalization, private and foreign sectors banks have come up which has resulted into a drastic change in the Indian Banking scenario. With these banks the latest technology has also come up. But still a huge chunk of people

does not avail itself with the benefits. People still prefer going to banks and carry out the regular paper work when then same thing can be done very easily through their mobile phones and internet. Thus people from rural areas should be given proper information and should be educated and their attitude needs to be changed, since it is a major hurdle for the growth of the retail banking products.

Security Problems

Retail banking products like net banking, phone and mobile banking and ATMs are solely dependent on technology. If there is any problem in the network or a system as a whole, it would result into huge losses for the banks as well as their customers.
Therefore proper security measures should be in place to secure customers' date and identification codes.

"This study has helped me to know the whole functioning of one of the major pillars of our economy which is Banks. With the Advent of Globalization and Liberalization new ways to improve customer relationship have emerged in front of the banks. These new ideas will help them in acquiring new customers and maintaining the existing customer base. One of the new fast emerging tools with banks to improve up on customer retention and satisfaction is Retail Banking and by adopting this many banks have achieved growth in their business like never before"

SUGGESTION

The banking industry worldwide has been showing steady progress since 2002. Much of the growth in the worldwide banking industry can be attributed to the surge in the retail-banking sector in the Asia Pacific region and the countries of Latin America.

The Banking industry in the economies of Brazil, Russia, India and china has been showing exemplary growth owing to improving economic condition, liberalization, changing consumer demographics and large segment of untapped population. These countries are witnessing steep growth in the uptake of retail loans specially housing, car education, credit cards and other personal loans.

In India total asset size of the retail banking industry grew at a rate of 120% to reach a value of $66 billion in 2005. This growth in retail banking sector has helped in the growth of the overall banking sector. In future the retail banking industry in India is likely to reach a value of $300 billion by 2010.

The future of retail banking would be in favour of rural banking, Bancassurance, financial cards, mobile banking, role of technology in rural banking, pension funds, and the future course of action or strategies for pension fund industry to be taken at macro level.

Marketing issues may be the key focus for the Global players entering in Indian market because of the nature of Indian retail banking market requires new entrant to have to devise marketing programs to establish and enhance brand awareness, which in turn will help the new entrant to show its presence and help to create a niche for them.

India's retail-banking assets size is expected to grow at the rate of 18% a year over the next four years (2006-2010), Retail loan to drive the growth of retail banking in future, Housing loan accounts for a major chunk of retail loan.

Many banks experienced extensive losses in their portfolios as a result of the stock-market decline, especially banks with strong investment banking arms and exposure to equity markets. These banks are now searching for more profitable markets to enter in order to recover losses caused by the stock-market decline. So banks in near future will have to take major steps keeping in mind the uncertainty of the external environment.

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Questionnaire

Q1). What products and services does your bank offer your customers?

Saving a/c	[ ]	Electronic transfer	[ ]
Current a/c	[ ]	Mobile banking	[ ]
Fixed banking	[ ]	Mutual funds	[ ]
Demat a/c	[ ]	Door step delivery	[ ]
ATM	[ ]	Forex services	[ ]
Personal loan	[ ]	Utility payment services	[ ]
Net banking	[ ]	Wealth management	[ ]

Debit/credit card	[ ]	Home loan	[ ]
Vehicle loan	[ ]	Loan against shares	[ ]
Phone banking[ ]			

Q2). Number of walk-in- customers per day?

Less than 20	[ ]	20 – 40	[ ]
40 – 60	[ ]	60 and above	[ ]

Q3). Types of customers visiting your bank rank them according to your preference in terms of banking transactions. **M-** Being most preferred and **L-** Being the least preferred?

Individuals	[ ]	Co-operative society [ ]	
Corporate firms	[ ]	Local authorities	[ ]

Q4). Which segment does your bank target the most for your products? Put **M-** Being most targeted and **L-** Being the least targeted?

Students	[ ]	HNIs	[ ]
Professionals	[ ]	Senior citizen	[ ]
Corporate	[ ]	Others (Specify)	[ ]

Q5). Channels used by your bank to deliver products to your customers. Put **M-** Being most used and **L-** Being the least used?

Personal banking	[ ]	ATMs	[ ]
Internet banking	[ ]	Telephone	[ ]

Q6). How do you communicate about new products and services?

No [ ]

If Yes, through

Pamphlet/ booklet	[ ]	Picked up from ATM	[ ]
Tele-marketing	[ ]	News paper	[ ]
Bill statement [ ]			

Q8). What is the share of retail banking in your total business?

Less than 15%	[ ]	15 to 30%	[ ]
30 to 50	[ ]	30 to 50%	[ ]
More than 50%	[ ]		

Q9). Why retail banking is important for your bank?

Gives more margin	[ ]	Cross selling	[ ]
Growth prospects	[ ]	Expand customer base[ ]	
Revenue from rural		Others (Specify)	

Q10). The problems faced by your bank while carrying out retail activities? **H-** High, **M-** Moderate and **L**- Low.

Pressure on margin	[ ]	Neck & neck competition [ ]	
Operational problems [ ]		NPAs [Others (Specify)]	