The Role of Retail Banking In Indian Economy

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ABSTRACT - Retail banking is when a bank executes transactions directly with consumers, rather than corporations or other banks. Services offered include savings and transactional accounts, mortgages, personal loans, debit cards, and cards. Today, retail banking is being considered as one of the most innovative financial services provided by the various commercial Public Sector Banks (PSBs), private sector and foreign banks. Retail banking has a huge potential considering the growing demand for its products namely, term deposits, consumer durable loans, auto loans, debit card, credit cards, ATM facilities, insurance, online banking, etc. The growing sector of retail lending has contributed significantly to the development of the economy. Like other developed countries, India too, has a developed retail banking sector which accounts for one-fifth of all banks credit. Retail lending across the globe has been a showcase of innovative services in the commercial banking sector. Countries, like China and India, have emerged as potential markets with changing investment opportunities. The higher growth of retail lending in emerging economies can be attributed to the rapid growth of personal wealth, favorable demographic profile, rapid development in information technology, the conducive macroeconomic environment, financial market reforms and small micro-level supply side factors. The retail banking strategies of banks are undergoing a major transformation, as banks are beginning to adopt a mix of strategies like organic growth acquisition and alliance formation. This has resulted in a paradigm shift in the marketing strategies of the banks. PSBs are adopting aggressive strategies, leveraging their branch network to garner a large share of the retail market. This article attempts to highlight the prospects and the future role of retail banking in India. Retail banking is widely recognized as an important factor for the economic development of a country. Retail banking helps the Indian banking industry by providing a wide range of innovative services. Retail loan is estimated to have accounted for nearly one-fifth of all bank credit. Over the past few years housing sector is experiencing a boom in its availability of credit. The retail loan market has decisively got transformed from a seller's market to a buyer's market. The days are gone when getting a retail loan was difficult. All the above statements bring out the speed of development that retail banking is experiencing in India. Retail banking is a very wide term that refers to the dealings of commercial banks with individual customers, both on liabilities and assets side. Mortgages, loans (e.g., personal/housing, auto and educational) on the asset side are the more important products offered by the banks. Related ancillary services include credit cards and depository services.

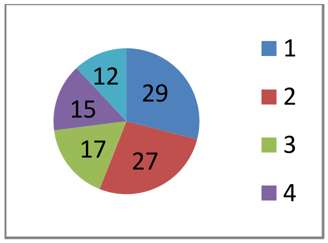
Keywords: Retail Banking, Information Technology, Financial Market Reforms, Public Sector Banks, Retail Banking Sectors, , Commercial Banks, Indian Banking Industry, Economic Development,

Introduction

Retail Banking in which banking institutions execute transactions directly with customers Typical products: savings and transaction accounts; mortgages; personal loans; debit and credit cards, etc Working principle: Law of Large Numbers; probabilistic modeling Critical success factors: Distribution – Branch, channels Branding Unit costs – cost per account, cost per transaction Pricing Risk management **.**The term is generally used to distinguish these banking services from investment banking, commercial banking or wholesale banking. It may also be used to refer to a division of a bank dealing with retail customers and also be termed as personal banking services According to the Report's Customer Experience Index, which surveyed over 18,000 bank customers across 35 markets, 10% of retail banking customers are likely to leave their banks in the next six months while an additional 41% say they are unsure if they will stay or go. To re-build the customer-bank relationship, the Report finds banks can become more customer-centric more personal interactions. Retail banking what's been good for Indian banks hasn't been good enough for the country scorching pace of growth since liberalization: CAGR of around 30% to touch a figure of INR 9700 Billion. Bankable households are growing at a CAGR of 28% (2007-11) what's powering this growth? Economic prosperity and growth rate Young population (70%<35 years) Technology channels: ATM, POS, Web, Mobile Retail loans constitute 7% of our economy versus 35% in other Asian countries Retail assets are at only 25% of total banking assets 41% of India's adult population is un-banked Number of loan accounts: 14% of adult population 73% of farm households have no access to institutional credit Share of money lenders in rural debt has moved from 17% in 1991 to 30% in 2002

Service wise division of retail banking transactions:

Serial NO	Services	Percentage
1	Credit card	29
2	Debit card	27
3	ECS dr	17
4	Neft/Eft	15
5	Necs/Ecs	12



SOURCE: RBI Monthly Report

Retail Banking in the World

North America continues to lead the Customer Experience Index with Canada (81%), and the United States (80%) in the lead. Italy, Saudi Arabia and China reported the largest relative gains in share of customers with positive experience this year. Fees, Mobile Capabilities, Quality of Service or Knowledge of Customers? This is the single most important factor driving customers to switch banks. The World Retail Banking Report provides insights into customer attitudes towards retail banking using a comprehensive Voice of the Customer survey which polled over 18,000 retail banking customers in 35 countries. The survey analyzes customer experiences across 80 banking touch points that span the products banks offer, the importance of different channels for obtaining services and the transactions that occur over the lifecycle of a banking relationship some banks turned to consolidation as a way of cutting expenses in order to survive difficult economic conditions. Often consolidation works as intended, but it also has its limitations. Federal law prohibits any single bank in the United States from holding more than 10 percent of the U.S. customer market. When banks merge, they also make gains in their customer base. Several banks in the United States are approaching the 10-percent mark, so for those banks, further consolidation may not be a way to solve their problems. Global Retail Banking 2020 study, up to 50 percent of branches in today's U.S. bank networks may be declared obsolete -- although not necessarily defunct -- by 2020. Given that branches constitute 75 percent of a bank's total retail distribution costs, according to research from Capgemini, implementing smart, technologically savvy retail strategies will be critical to driving shareholder value.

Trends in Retail Banking

According to the Report's Customer Experience Index, which surveyed over 18,000 bank customers across 35 markets, 10% of retail banking customers is likely to leave their banks in the next six months while an additional 41% say they are unsure if they will stay or go. To re-build the customer-bank relationship, the Report finds banks can become more customer-centric more personal interactions

ATM machines and Internet Banking, many consumers still prefer the personal touch of their neighborhood branch bank. Technology has made it possible to deliver services throughout the branch bank network, providing instant updates to checking accounts and rapid movement of money for stock transfer

Retail banking now encompasses not just branches, but also anywhere that banking services can be conveniently provided to consumers. Whether it means a service kiosk in a train station, a mini-branch in a grocery store, a premium branch in a central business district, or a bank-on-wheels that visits corporate workplaces, proximity to targeted customers ultimately matters more than having a traditional bank façade. Flexibility and agility will provide a competitive advantage for bank

Technology is becoming the centerpiece of retail bank executives will expect their IT departments to identify and implement technology-based solutions to enhance the customer experience. Some banks, are even experimenting with quasi-Internet cafes, offering high-tech lounge environments with relaxing furnishings and Wi-Fi access along with ATMs, self-service kiosks, areas for plug-in consumer devices, tutorials for mobile and Web banking and videoconferencing for service consultations delivered by call center staff. Furthermore, the move to a cash-light society will trigger still more changes in how branches are deployed.

As per the RBI statistical data for year ranging from 1998-2008 the mean personal loan is Rs.12, 463,240 Lakhs against a total bank credit of Rs. 66,899,292 Crores. This average personal loan amount is against a population of 1054 million on other hand housing loans amounts to housing loans Rs. 70, 22,354 Lakhs

The role of Retail Banking in Indian Economy

Retail banking in India is not a new phenomenon. It has always been prevalent in India in various forms. For the last few years it has become synonymous with mainstream banking for many banks. The typical products offered in the Indian retail banking segment are housing loans, consumption loans for purchase of durables, auto loans, credit cards and educational loans. The loans are marketed under attractive brand names to differentiate the products offered by different banks. As the Report on Trend and Progress of India, 2003-04 has shown that the loan values of these retail lending typically range between Rs.20, 000 to Rs.100 lack. The loans are generally for duration of five to seven years with housing loans granted for a longer duration of 15 years. Credit card is another rapidly growing sub-segment of this product group. In recent past retail lending has turned out to be a key profit driver for banks with retail portfolio constituting 21.5 per cent of total outstanding advances as on March 2004. The overall impairment of the retail loan portfolio worked out much less then the Gross NPA ratio for the entire loan portfolio. Within the retail segment, the housing loans had the least gross asset impairment. In fact, retailing make ample business sense in the banking sector. While new generation private sector banks have been able to create a niche in this regard, the public sector banks have not lagged behind. Leveraging their vast branch network and outreach, public sector banks have aggressively forayed to garner a larger slice of the retail pie. By international standards, however, there is still much scope for retail banking in India. After all, retail loans constitute less than seven per cent of GDP in India *vis-à-vis* about 35 per cent for other Asian economies — South Korea (55 per cent), Taiwan (52 per cent), Malaysia (33 per cent) and Thailand (18 per cent). As retail banking in India is still growing from modest base, there is a likelihood that the growth number

Seem to get somewhat exaggerated. One, thus, has to exercise caution is interpreting the growth of retail banking in India **.**The following away the retail Banking Contributing service to development of Indian Economy

Credit Cards: While usage of cards by customers of banks in India has been in vogue since the mid-1980s, it is only since the early 1990s that the market had witnessed a quantum jump. The total number of cards issued by 42 banks and outstanding, increased from 2.69 core as on end December 2003 to 4.33 core as on end December 2004. In view of this ever increasing role of credit cards a Working Group was set up for regulatory mechanism for cards. The terms of reference of the Working Group were fairly broad and the Group was to look into the type of regulatory measures that are to be introduced for plastic cards (credit, debit and smart cards) for encouraging their growth in a safe, secure and efficient manner, as also to take care of the best customer practices and grievances redressed mechanism for the card users. The Reserve Bank has been receiving a number of complaints regarding various undesirable practices by credit card issuing institutions and their agents. The RBI and a set of guidelines would be issued which are going to pave the path of a healthy growth in the development of plastic money in India. The RBI is also considering bringing credit card disputes within the ambit of the Banking Ombudsman scheme. While building a regulatory oversight in this regard we need to ensure that neither does it reduce the efficiency of the system nor does it hamper the credit card usage.

Housing Credit: Housing credit has increased substantially over last few years, but from a very low base. During the period 1993-2004, outstanding housing loans by scheduled commercial banks and housing finance companies grew at a trend rate of 23 per cent. The share of housing loans in total non-food credit of scheduled commercial banks has increased from about 3 per cent in 1992-93 to about 7 per cent in 2003-04. Recent data reveal that non-priority sector housing loans outstanding as on February 18, 2005 were around Rs. 74 thousand core, which is, however, only 8.0 per cent of the gross bank credit. As already pointed out, direct housing loans up to Rs. 15 lack irrespective of the location now qualify as priority sector lending; housing loans are understood to form a large component of such lending.

Support to Indian middle class People: The rise of the Indian middle class is an important contributory factor in this regard. The percentage of middle to high income Indian households is expected to continue rising. The younger population not only wields increasing purchasing power, but as far as acquiring personal debt is concerned, they are perhaps more comfortable than previous generations. Improving consumer purchasing power, coupled with more liberal attitudes toward personal debt, is contributing to India's retail banking segment.

Economic superpower. Retail banking has played a role in a growing economy of India. As the growth story gets unfolded in India, retail banking is going to emerge a major driver. How does the world view us? I have already referred to the BRIC Report talking India as an economic superpower. A. T. Kearney, a global management consulting firm, recently identified India as the 'second most attractive retail destination' of 30 emergent markets.

Increasing purchasing power of middle class people: The rise of the Indian middle class is an important contributory factor in this regard. The percentage of middle to high income Indian households is expected to continue rising. The younger population not only wields increasing purchasing power, but as far as acquiring personal debt is concerned, they are perhaps more comfortable than previous generations. Improving consumer purchasing power, coupled with more liberal attitudes toward personal debt, is contributing to India's retail banking segment.

Financial market reforms: The subject matter of retail banking is of prime importance. In recent years, commercial banks have witnessed development in the form of retail lending, all over the world. The growth in the field of retail lending is primarily because of the speedy advancement in the IT sector, evolving macroeconomic environment, numerous micro level demand and supply side factors and financial market reform. This criterion is based on the market research report on retail banking

Engine of economic growth: Retail banks play a critical role in their home economies, and their activities have implications for the global economy as well. They offer critical credit functions, which largely fuel the engine of economic growth in their economies. When problems hit the retail banking sector the result is often dire economic circumstances for the economy as a whole. When retail banks are failing, little or no credit is available for credit seekers, and economic activity becomes depressed.

Mass-market banking: Retail banks offer a variety of important services to their customers. The retail banking sector is often described as a typical mass-market banking, offering services such as savings and checking accounts and all kinds of personal loans, including auto loans and student loans. Retail banks also offer mortgage services, debit and credit card services and ATM services--all of which have become essential to today's consumers.

Volume driven business. Retail Credit ensures that the business is widely dispersed among a large customer base unlike in the case of corporate lending, where the risk may be concentrated on a selected few plans. Ability of a bank to administer a large portfolio of retail credit products depends upon such factors like; strong credit assessment capability, sound documentation, strong possessing capability, regular constant follow- up, skilled human resource, technological support.

Automation of banking process: The growth in retail banking has been facilitated by growth in banking technology and automation of banking processes to enable extension of reach and rationalization of costs. ATMs have emerged as an alternative banking channels which facilitate low-cost transactions vis-à-vis traditional branches / method of lending. It also has the advantage of reducing the branch traffic and enables banks with small networks to offset the traditional disadvantages by increasing their reach and spread.

Easy and affordable access: Retail loans through a wide range of options / flexibility. Banks even finance cost of registration, stamp duty, society charges and other associated expenditures such as furniture and fixtures in case of housing loans and cost of registration and insurance, etc. in case of auto loans.

Financial Liquidity: Banks Making financing attractive by offering free / concessional / value added services like issue of credit card, insurance, etc.Continuous waiver of processing fees administration fees, prepayment charges, etc. by the Banks. As of now, the cost of retail lending is restricted to the interest costs.

Economic prosperity: The consequent increase in purchasing power has given a fillip to a consumer boom. Note that during the 10 years after 1992, India's economy grew at an average rate of 6.8 percent and continues to grow at the almost the same rate – not many countries in the world match this performance.

Changing consumer demographics: The Size of population indicate vast potential for growth in consumption both qualitatively and quantitatively. India is one of the countries having highest proportion (70%) of the population below 35 years of age (young population). The BRIC report of the Goldman-Sachs, which predicted a bright future for Brazil, Russia, India and China, mentioned Indian demographic advantage as an important positive factor for India.

Technological innovations: Technological factors played a major role. Convenience banking in the form of debit cards, internet and phone-banking, anywhere and anytime banking has attracted many new customers into the banking field. Technological innovations relating to increasing use of credit / debit cards, ATMs, direct debits and phone banking has contributed to the growth of retail banking in India.

Increase the Bank Liquid cash: Treasury income of the banks, which had strengthened the bottom lines of banks for the past few years, has been on the decline during the last two years. In such a scenario, retail business provides a good vehicle of profit maximization. Considering the fact that retail's share in impaired assets is far lower than the overall bank loans and advances, retail loans have put comparatively less provisioning burden on banks apart from diversifying their income streams.

Decline in interest rates: The interest rates were decreased in Indian money market have also contributed to the growth of retail credit by generating the demand for such credit. The interest rates on retail loans have declined from a high of 16-18%in1995-96 to presently in the band of 7.5-9%. Ample liquidity in the banking system and falling global interest rates have also compelled the domestic banks to reduce it

Declining cost of incremental deposits: Banks could afford to quote lower rate of interest, even below PLR as low cost [saving bank] and no cost [current account] deposits contribute more than 1/3rd of their funds [deposits].The declining cost of incremental deposits has enabled the Banks to reduce their interest rates on housing loans as well as other retail segments loans.

Change of Terms of Loans: Offering retail loans for short term, 3 years and long term ranging term ranging from 15/20 years as compared to their earlier 5-7 years only

Challenges of Retail Banking in India

Retention of customers: According to a research by Reichheld and Sasser in the Harvard Business Review, 5 per cent increase in customer retention can increase profitability by 35 per cent in banking business, 50 per cent in insurance and brokerage, and 125 per cent in the consumer credit card market. Thus, banks need to emphasize retaining customers and increasing market share.

Rising indebtedness: India's position, of course, is not comparable to that of the developed world where household debt as a proportion of disposable income is much higher. Such a scenario creates high uncertainty. Expressing concerns about the high growth witnessed in the consumer credit segments the Reserve Bank has, as a temporary measure, put in place risk containment measures and increased the risk weight from 100 per cent to 125 per cent in the case of consumer credit including personal loans and credit cards (Mid-term Review of Annual Policy, 2004-05).

Network management challenges: Difficulty in maintaining and optimizing the performance of retail banking networks. Illustratively, ensuring that all bank products and services are available, at all times, and across the entire organization is essential for today's retails banks to generate revenues and remain competitive. Besides, there are network management challenges, whereby keeping these complex, distributed networks and applications operating properly in support of business objectives becomes essential. Specific challenges include ensuring that account transaction applications run efficiently between the branch offices and data centers.

Money laundering: KYC Issues and money laundering risks in retail banking is yet another important issue. Retail lending is often regarded as a low risk area for money laundering because of the perception of the sums involved. However, competition for clients may also lead to KYC procedures being waived in the bid for new business. Banks must also consider seriously the type of identification documents they will accept and other processes to be completed. The Reserve Bank has issued details guidelines on application of KYC norms in November 2004.

Sub-prime crisis**: A major challenge to retail banking surfaced in late 2008. Retail banks as well as commercial banks had provided sub-prime mortgages to consumers who were not qualified for the size of the loans they received. Although this**

process generated much of the housing boom of the early 21st century, eventually the loans became too cumbersome for borrowers to pay back. This problem led to loan defaults across the United States and led to many bank failures, not only in the United States but around the world. It produced serious deterioration in the global economy and led to the economic and financial crisis that dominated the political landscape in early 2009.

Massive infusion of capital: While retail banks have their share of problems, it is anticipated that with the massive infusion of capital into the banking and financial services sector by the federal government's economic stimulus program, most retail banks will survive, and the smaller retail banks may seek to merge with other banks

Strategy Knowing Your Customer: service should be at the end all in retail banking. Someone has rightly said, “It takes months to find a good customer but only seconds to lose one.” Thus, strategy of Knowing Your Customer (KYC) is important. So the banks are required to adopt innovative strategies to meet customer’s needs and requirements in terms of services/products etc.

Outsourcing activities: The issue of outsourcing has become very important in recent past because various core activities such as hardware and software maintenance, entire ATM set up and operation (including cash, refilling) etc., are being outsourced by Indian banks.

Conclusion

There is a need of constant innovation in retail banking. In bracing for tomorrow, a paradigm shift in bank financing through innovative products and mechanisms involving constant up gradation and revalidation of the banks’ internal systems and processes is called for. Banks now need to use retail as a growth trigger. This requires product development and differentiation, innovation and business process reengineering, micro-planning, marketing, prudent pricing, customization, technological up gradation, home / electronic / mobile banking, cost reduction and cross-selling. While retail banking offers phenomenal opportunities for growth, the challenges are equally daunting. How far the retail banking is able to lead growth of the banking industry in future would depend upon the capacity building of the banks to meet the challenges and make use of the opportunities profitably. However, the kind of technology used and the efficiency of operations would provide the much needed competitive edge for success in retail banking business. Furthermore, in all these customers’ interest is of paramount importance. So, it is vital for banks to improve their customer services and cut off predatory lending strategies, particularly in the area of interest on credit cards. Finally we say that retail banking is one of the most tremendous areas now days to be looked after by the banking industry as it contributes 7% to our GDP and 14% to employment.

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