ROLE WITHIN THE RETAIL BANKING

JAIIB RBWM

RETAIL BANKING: ROLE WITHIN THE BANK OPERATIONS

- Banks follow different approaches for their retail banking activities. The role and importance of retail banking across banks differ and different models are adopted by banks.
- The models and processes depend upon the importance attached to the retail banking space in their overall corporate business strategies and the business projection over the years for retail banking.
- The models adopted by banks vary among the public sector, private sector and foreign banks.

The main approaches are as follows:

a. Strategic Business Unit (SBU) Approach,
b. Departmental Approach,
c. Integrated Approach (part of the overall business plan).

- Public Sector Banks in India generally have adopted the Departmental Approach as their retail banking business model. The model is uniformly adopted by all the banks immaterial of their balance sheet size or geography.
- In a research study on the models followed by about 10 banks comprising of public, private and foreign banks, the SBU approach is adopted by one of the top five public sector banks based in Mumbai and their business model is in alignment with private sector banks and foreign banks.

- In old generation private sector banks, the approach is more conservative. The business model for retail banking is built as a part of the overall business plan and not done as a separate departmental activity, leave alone SBU.

- In new generation private sector banks, the business model is very clear. They had set up Strategic Business Units (SBU) to have clear focus and business objectives.

- In foreign banks also, SBU is the business model followed with defined business focus. The demarcation as a SBU is more a Management by Objectives (MBO) process wherein the business model is dealt as a modular strategy for achieving targeted profits.

BUSINESS MODELS

- Banks generally structure their retail banking models mainly on a positioning platform and to be the best/top three among the peer group players or across players.

- Strategies are based on the positioning objectives and vary from bank to bank depending on the importance attached to the business model.

- Foreign banks generally do not go by positioning objectives but purely on business objectives. They go by customer, business and profit targets.

APPLICABILITY OF RETAIL BANKING CONCEPTS

Retail Banking as a concept has a number of elements which individually and collectively contribute to the success of the segment. It spans across implementation models, business process structure, product and process models etc.

Applicability of the different retail banking concepts that shape the success of the space are explained below:

Implementation Models

- Banks adopt different models for implementing their retail banking initiatives.
- The most common strategies are end to end outsourcing, predominant outsourcing, partial outsourcing and in house sourcing.
- The implementation model depends on the product range, process requirements, technology preparedness, delivery capabilities including human resources and regulatory prescriptions.
- Most of the PSBs use only in house resources for retail banking. Only for some activities like ATM/ Credit Cards/Debit Cards, the issue part is outsourced due to lack of in - house facilities.
- In case of old private sector banks also, the activities are carried out through in house resources only.
- In case of new generation private sector banks, the model is a balanced mix of outsourcing and in house, though a little skewed towards outsourcing. In some banks, asset side is outsourced whereas liability side is not outsourced, though centrally processed.

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- In foreign banks, the implementation model is mostly outsourced based on the business model.

Business Process Structure in Retail Banking

Boston Consulting Group had conducted a study on the retail banking processes (Transforming Retail Banking Processes) and introduced four broadly defined process models implemented across banks. These models were defined based on the technology and customer interface capabilities of the banks studied.

The four broad classifications are:

a) Horizontally Organised Model
b) Vertically Organised Model
c) Predominantly Vertically Organised Model
d) Predominantly Horizontally Organised Model

- The horizontal or vertical model depends on the level of customer information available in a single platform in the data base side for offering multiple products/services across assets, liabilities and other services.
- Horizontally organised model is a modular structure using different process models for different products offering end to end solutions product wise.
- Vertically organised model provides functionality across products with customer data base orientation and centralised customer data base is used across products.
- Predominantly horizontally organised model is mostly product oriented with common customer information for some products. In predominantly vertically organised model, common information, available for most of the products.

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- In most of the PSBs, horizontally organised model is the standard norm.
- New private sector banks generally follow a vertically organised model.
- This shows mostly products are sold based on standalone customer information and common customer information is not available for all products.
- In foreign banks, it is mostly predominantly vertically organised model which implies that retail banking initiatives are attempted with common customer information across products.

Business Approach (Domain Specific) in Retail Banking

The business strategies with regard to the domains targeted are approached in different ways by different banks. The most common approaches are as follows:

Segmented Approach

- where branches are classified based on the business potential with regard to retail space and business targeted in these segments of branches only with focused marketing strategies.
- These branches will be positioned as resource centre branches and will form part of the overall segmentation plan of the bank. Branches are classified as Resource Centres, Profit Centres, Priority Centres and General Centres to have a clear business focus.
- This concept is an effective business model for PSBs with large network and useful for focused strategies and already getting implemented in some public sector banks.

Geography based approach

where retail models are built based on geographies.

Classification based approach

- where strategies are designed based on the type of branch viz., Rural, Semi Urban, Urban and Metro. This strategy helps in better product structuring for specific types of branches.
- Most of the PSBs have not developed any specific business model on the above lines and generally adopt a holistic model based on the corporate objectives for retail.
- In some banks, segmented approach is being built in the corporate model but not a standalone segmented approach.
- In old private banks also, the overall corporate objective for retail is the basis for the model and segmentation is built in that model only to a limited extent.
- **In new generation private sector banks**, a mix of segmented model and **classification-based model** is adopted to capture the retail potential in a structured way in segments where it matters.
- In foreign banks, the model not restricted to any of the above but is based on the retail plan of the banks.

Product Models in Retail Banking

- Product portfolio structuring play an important role in the retail banking strategies of banks and extend across liability, asset, other service and third-party products.
- Though essentially retail assets and liability products constitute the basic structure of retail banking, the trend has changed in the recent years and marketing of third-party products has emerged as one of the important constituents of retail banking initiatives of banks.

The product models of banks

(a) Liability Products

- Liability products are offered to retail banking customers basically under three spaces - Savings Accounts, Current Accounts and Term Deposit Accounts. Product differentiation among these accounts is best achieved by adding different value propositions.
- Attempts are made by banks to expand the scope of generic products from a plain vanilla account to a value enriched account.
- Functionality of products is now perceived to include changed needs. Built in ATM/Debit Cards/Credit Cards/Multi City Cheques have become generic features. Internet Banking, Telephone Banking, Mobile Banking have become essential value play.
- Monies in accounts are not allowed to sit idle and undertake active traveling by means of sweep facilities from savings accounts to fixed deposit accounts above a certain specified level.
- This increases the earning potential of the deposit balances in Savings Accounts. In case of Current Deposits also most of the above features are built in.
- All banks offer term deposit products with provision for monthly, quarterly or cumulative interest payment options

(b) Retail Asset Products

- Retail asset financing is a major component of retail banking model of banks.
- Product, price, process and delivery innovations are receiving constant attention in the retail asset side.

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- Cross selling and product bundling opportunities are always structured and implemented around retail asset products.
- The focus is so high that in some banks retail assets constitute as high as 40 to 45 percent of the total asset base. The main advantage is the stability of the asset base because of the large customer base.
- Other important reasons are the better spreads in income, risk diversification and scope for capturing additional revenue streams from other avenues.
- The standard retail asset products offered by banks are Housing Loans, Consumer Durable Loans, Car Loans, Credit Cards and Personal Loans.
- Retail Loans are also structured by some banks to target specific professional segments like doctors, architects and advocates etc., to finance their professional requirements.

(c) Other Products/Services

- Other products and services broadly cover the beyond product facilities tagged to the products and services.
- These enhance the service experiences of the customers by providing process and delivery efficiencies by additional service tools to the basic products.
- One set of these products are Credit Cards, Debit Cards, ATM Cards, Telephone Banking, Mobile Banking, Internet Banking, Depository Service.
- Distribution of third-party products like life and non-life policies, mutual funds, retail sale of gold coins, bill payment services, payment gateway for rail, air ticket bookings, wealth management services, portfolio management services and private banking are some of the other services offered by banks.

- These services are offered with twin objectives of customer multiple need satisfaction and also to augment fee-based income.
- Old private sector banks offer standard services, they do not offer Credit Cards, Telephone Banking, Mobile Banking, Broking Services, Gold Coins etc., but some banks offer Depository Services, Mutual Fund Distribution, Life and Non-Life policies. Wealth Management, Portfolio Management and Private Banking are not attempted by them.

New generation private banks and foreign banks offer the complete bouquet of all the above products/services.

Product Development in Retail Banking

- Product Development is attempted by banks in different ways. In house product development independently developing the products based on research and on the market, dynamics is one way.
- In the process, hybrid cross pollination incorporating the best features in the products available in the market along with additional value engineering form part of the product development.
- Another way of product development is based purely on market conditions and customer segments without any background research and also "follow the leader approach' by developing on the same lines as the leader.
- The other most common model is simply following the instructions of the Top Management without any background research or analysis.
- The basis for these product developments, as said earlier, is either on the segmentation approach or geography-based approach or classification-based approach or approach based on specific customer segments.

- In the development process, geography is not given importance but type of branch and centre and business potential are given due importance.
- In private sector banks, both old and new, product development is done in house independently, incorporating the market dynamics, segmentation, classification, customer segments, market dynamics and the product positioning adopted by other players.
- The **product development starts** from conducting a market survey about the need levels and gap among the target group, identifying the needs, developing the product, pilot testing to a sample universe, getting feedback, fine tuning the product based on feedback and then the final roll out of the product across targeted segments.
- In PSBs, market survey is done only through in house resources and not outsourced.
- In some banks, no market survey is done and products developed are launched based on industry practices and need are expressed by customers and without any pilot run and feedback.

Process Models for Products and Services

Processing of products and services in retail banking is basically approached from three dimensions viz.,

I. The entire processing is done through in house resources,
II. Some products processed in house and for some products outsourcing is done for process and
III. The third approach is outsourcing of entire process subject to prescribing process standards.

- In PSBs and **old private banks** the entire process for products and services are done through in house resources but in some banks, process part of some products are outsourced. But generally, no outsourcing is done for the process part.

- In **new generation private sector banks**, outsourcing is attempted partially for some process areas.
- In **foreign banks**, the entire process is outsourced and normally happens through a dedicated back office covering the entire gamut of retail banking services.

Centralised Retail Assets Processing Centres

Banks adopt different process models for retail asset products.
The common form of process models is **Centralised Retail Assets Processing Centres** where all the retail loans sourced at the branches and marketing team are processed at a single point and assets are financed through that centre or processing alone done at the centre and financing done at the branches.
Another model is centralized processing for some asset products (say Housing Loans) and regional processing centres or stand-alone processing at branches for other products.
The third model is no centralized processing but only regional processing hubs to cater to specific cluster or geography of branches and process on or more loans.

- It will exist along with the stand alone processing at the branch level. Some banks follow the stand-alone branch level processing and delivery of retail assets without resorting to any centralized model or regional hubs.
- The ultimate aim is to build absolute process efficiencies.
- Public sector banks are also implementing the centralized processing model for all assets in a phased way. Some banks have centralized/regional processing hubs for some products and stand-

alone model for other products and in most of the banks, no centralized model is followed but process happen only through either regional hubs or branches or a blend of both.

- In private sector banks, in case of old banks the model is mainly stand alone and in new banks, a blended model comprising of centralized processing for some products and regional hubs for some other products are followed for effectively controlling the lead time for processing. In foreign banks, centralised processing is the norm for retail asset processing.
- In centralised processing all the above activities are carried out in a single point.
- In regional processing hubs, the same activities are carried out geography wise.
- In some banks, some activities like issue of cheque books, cards, PIN mailers are centralised or done at regional hubs while opening of accounts will be on a stand-alone basis.
- Some banks follow the conventional model of stand-alone processing at the branch level.
- Process models differ for products which require single stage process and multi stage process.

For example,

opening a fixed deposit and issuing receipt involves only a single stage process. Likewise, giving car loan is a single stage process. But in case of housing loans or Savings/Current Accounts, multi stage processing is involved. In this scenario, the process model should be stand alone or centralised depending on the product for better process/delivery efficiencies. Banks adopt different models in this area.

Process time

Process time is a major differentiator in the efficacy of retail banking operations. Process Time is business sensitive and customer sensitive. It is an important component of business promises with regard to product delivery. It reflects the confidence and process efficiencies of the bank, The quicker the process time, more the delivery exigency and customer recognition Banks are implementing process time prescriptions for different retail asset products.

Pricing of Products and Services

- Banks develop models for pricing of products and services based on certain fundamental parameters.
- Market dynamics, risk perception, return expectations, tenor/duration, resources position, asset liability management positions and customer profile are some of the variables which are factored into the pricing model by banks.
- The balancing of these various variables dynamically with changing market dynamics is the key function for good pricing model
- In PSBs, though pricing is market driven and competitive, in almost all the banks, pricing is mainly driven on the basis of the asset liability management practices of the banks. Regulatory advices form part of the price structuring.
- some banks have started implementing aggressive pricing strategies in Housing Loan segment to not only capture fresh accounts but also focus on migration from other banks. They follow a structured **step-up pricing model** with an initial low and attractive price and switch over to market related pricing after 3 years.
- The pricing will be slightly aggressive than PSBs in order to capture business in the competitive environment in case of old private sector banks.

- In new private banks and foreign banks, though the pricing fundamentals almost remain the same, the pricing of products are always aggressive and ahead of the market to set a price race in the market for demand driven products like term deposits, credit cards, car loans, housing loans etc.

Price structuring for products and services

Stand-alone pricing

- Price structuring for products and services is attempted by banks in many ways.
- Stand-alone pricing for different products and services is the basic structure.
- While the general structuring is basically an outcome of the pricing models, fine tuning always happens due to different factors. Quantum and volumes are two important determinants.
- Price Preferences/Price rebates based on the above also form part of the structuring.
- Special quotes for high value deposits and concessional rates of interest are examples of this structuring.
- In addition to stand alone pricing structure, most of the PSBs have **price concessions** as well as rebates as a part of the pricing structure. But the same is applied depending on the volumes, quantum and of course relationship.
- Offering rebates on completing the repayment schedule is also attempted by some banks.
- In case of other products and services, some banks are structuring additional models indirectly as a part of the pricing structure. In addition to or in lieu of price rebates/discounts, alternate pricing propositions for other services are offered as additional facilities.

For example, free remittance facilities, issue of drafts, waiver of service charges, processing charges are offered as concealed price structures and offered as tag on for quantum and volume business. Almost all banks follow the above structure both as a pricing initiative as well as cross selling initiative.

Technology Models in Retail Banking

- The technology platform for retail banking plays a major role in the retail banking initiatives of banks.
- In today's scenario, technology is the backbone of the process and delivery efficiencies of banks. The technology models basically adopted by banks are in House Models, Outsourced Models, Partially in House and Partially Outsourced Models.
- Each model will have advantages and disadvantages and the overall business will be the decider of the effectiveness of the model.
- Most of the PSBs have primarily in house models with partial outsourcing also.
- Almost all old private banks follow outsourced model for technology basically because of the scale to migrate to Core Banking Model.
- In case of new private banks, the model is predominantly outsourced with partial in-house model. In foreign banks, outsourced model is mostly adopted.

Technology and Retail Banking are inseparables

- Technology is the enabler for building and translating a customer data base into retail banking business. Banks adopt different technology platforms in line with the global trends. The levels of technology implementation in PSBs started from stand-alone Automated Ledger

- Automated Ledger Posting Machines (ALPs) in the early days of computerisation to total branch automation and regional net worked hubs.
- PSB banks have reengineered their technology initiatives and started implementing core banking solutions networking the customers and accounts in a single platform.
- Some banks have almost completed the core banking solutions process while in other banks the level of implementation is at various stages.
- The level of implementation of core banking will directly increase the chances of availability of customer data base across products and will increase the scope for cross selling and up selling.
- Core banking gives clues about the level to which the data base is horizontally or vertically organized. Horizontal or vertical organized refers to whether data is available product wise on a stand-alone basis or data is available customer wise on an integrated basis.

DISTINCTION BETWEEN RETAIL AND CORPORATE/WHOLESALE BANKING

Retail Banking and Corporate or Wholesale Banking differ in their basic approach to banking. The major differences between the two segments are discussed as follows:

I. Retail Banking targets at the individual segment while corporate banking deals mainly with corporate clients.
II. Retail Banking is a mass market banking model whereas wholesale/corporate banking look at a relatively smaller segment of business/corporate client base as compared to retail segment.
III. Retail Banking is a B2C approach (Business to Customer) whereas corporate banking is a B2B approach (Business to Business).
IV. The ticket size of loans in retail banking is low whereas the ticket size is high in corporate loans.
V. Risk is widespread in retail banking as customer base is huge Whereas in Corporate Banking, the risk is more as the ticket size is big though customer base is relatively small.
VI. Returns are more in retail banking as the spreads are more for different asset classes in retail. But in corporate banking, the returns will be low as corporates bargain for lower rates due to higher loan amounts.
VII. Monitoring and recovery in retail assets are more laborious because of the larger customer base as compared to corporate banking.
VIII. In the liability side also, the cost of deposits is relatively less and mostly gone along with the card rates as the ticket size in retail deposits is small. In corporate banking, as the ticket sizes of deposits will be large, the cost of deposits will be high due to pressure from the corporates for higher rates and competitive.
IX. The impact of NPA will be more pronounced in corporate banking than retail banking as the ticket sizes in corporate loans are higher than retail loans.