Introduction
CHAPTER - 1
INTRODUCTION

Financial sector reforms initiated in India since 1991 as a part of the economic reforms has dramatically transformed the operation of banking industry in post reform era. In the ongoing reforms process, whereas deregulation has opened up new opportunities for banks to diversify their business Portfolio into insurance, credit card, investment banking, mortgage financing depositing services, securitization, futures option, online trading etc the liberalized system at the same time has also opened the doors to a sizeable number of international players in the banking industry in India.

In 2001-2002 the various kinds of banking industries functioning in the country comprises of
1. Commercial banks which include Indian scheduled banks and non scheduled banks
2. Regional rural banks
3. Local area bank
4. Co-operative banks

There are 27 public sector banks(nationalized bank 19 SBI and its associates 8 ) 30 private sector banks (old private banks 22 new private bank 8).

Foreign banks in India 40 regional rural bank 195 scheduled co-operative banks 52 scheduled state co-operative banks 16.
The operational flexibility and functional autonomy given to the industry has dramatically changed the business environment of the banking industry. Banks can pursue their planned objectives using sound management strategy subject to compliance of statutory as well as certain prudential regulation.

There is a change in the perception to measure the bank’s overall performance in terms of profitability and productivity status of technological upgradation risk management practices, quality of assets, observing global accounting standards, corporate governance, HRD support system, MIS, knowledge management etc. This is in sharp contrast to the practices followed in the pre-reform era where deposits mobilized and levels of advances were the sole determining factors used for performance evaluation.

In the progress of implementation of financial sector reforms, deregulation in interest rates and growing incidence of disintermediation, have resulted in the market share of the banks. There is a tremendous growth rate of deposits but the opportunity for lending has come down. The corporate have started for getting cheap source of funds from elsewhere through equity issuance and external commercial borrowings. This has reduced the lending opportunities for banks. There is an increased threat of NPAs development of fear psychosis on the part of bank official resulting in low growth in credit disbursement. According to new benchmark standards introduced by the Indian bank’s association (IBA vision 2010) the existing rates of CRR and SLR are reduced. This
will leave ample funds with the banking system thus worsening the situation still further.

Banks have invested more than 40% of total deposit in SLR securities against the stipulated 25% resulting in massive deployment in call-money market and reverse repose.

In this situation banks have got no other go to expand their asset book expect chasing individuals. Retail loans are more attractive to the bankers because of their high yielding income in terms of upfront fees as against corporate loans with no or negligible upfront fees. Secondly, retail lending is safe as the rate of NPA in this type of advances is low compared to corporate loans. Finally, there is a very good opportunity for the banker to cross-sell other retail products like credit cards, insurance products, mutual funds and demat facilities to the depositors.

Retail banking is not new to banks. It is now being viewed as an attractive market segment offering good opportunities for the growth with profits. It has attracted the attention of the banks only in recent times as a solution to some of the above problems discussed. Retail banking and Retail lending are used synonymously, the latter is just one side of the retail banking which is one of the fastest in the world. “It would become the third largest economy in the world by 2050”. Goldman sachs, one of the leading investment banks reports. A.T. Kearney, a global management consulting firm recently identified India as the “Second most attractive” retail destination of 30 emerging markets. The standard of living of the people has been increasing even though at a much lesser
pace when compared to Western countries or the countries of South East Asia. Because of a good agriculture output, the surplus income left in the hands of the people after satisfying their basic needs has given rise to the desire of investing in various banking products. The middle class population has grown in the last decade to 20 crores. Because of the time and resource constraints services offered under one roof. The advancement in information technology has helped the banks to satisfy the customers needs, quickly, accurately and without any fault.

Retail advances are on a rising trajectory. The retail advances have grown by 74.5% while non-food advances have grown by 52.19% during 2000-2003. During the corresponding period, housing loans have grown by 95.95%. During the period 2000-2003 the Compounded Annual Growth Rate (CAGR) registered by the retail assets has been at over 25%. According to CRIS-INFAC estimates even if the compounded growth were to increase to 40% for the next five years the risk profile of the retail portfolio would remain stable as long as the debt servicing obligation for any year is less than or equal to the households discretionary income generated in that year.

Essential Prerequisites for Retail Credit

Ability of any bank to administer a large portfolio of retail credit products depend on such factors, as the following which also determine the successful delivery of retail credit. (Manoj 2003)
1. Strong credit assessment capability

   It requires a good infrastructure. If the credit assessment is qualitative, then there is a reduced need to follow-up in the future.

2. Sound Documentation

   A robust system for the credit documentation is a necessary prerequisite for the healthy growth of retail credit portfolio as in the case of credit assessment which in turn will reduce the need to follow-up at a future point of time.

3. Strong processing capability

   Since large volumes of transactions are involved, excellent infrastructure for the processing of day-to-day transactions, maintenance of backups, etc. is required.

4. Regular and constant follow-up

   It should start from the customer enquiry and last till the loan is repaid in full.

5. Skilled Human Resources

   This is an essential prerequisite as only highly skilled and
Experienced manpower can withstand the rigor of administering a diverse and complex retail credit portfolio.

6. Technological support

It is needed to provide instantaneous service to the customers at large, faster processing, maintaining database etc

7. Strategic cost management

This would help in enhancing the profitability from retail banking operations through

Tie-up arrangement with other players in volume chain

Strategic sharing of resources by different players (viz ATM facilities)

Creation of in-house facilities for undertaking certain special assignment to minimize transaction

8. Market research and market intelligence

It is for taking up lead ship in the retail market segment. This will help to create and maintain a huge and updated customer data-base so as to
enable developing a customized range of products and services suited to various customer groups.

9. Enterprise CRM

It helps to survive and prosper in retail credit market of cut-throat competition. It is a cyclical closed loop business process, which seeks to identify, maintain, and enlarge the “best” customer of an organization. It helps to drive its business growth and profitability through creation of lifetime value and long standing relationships with such customers.

10. More delivery channels/customer touch points

It is to ensure maximum customer convenience. Thus internet banking, tele-banking, any time any where banking, ATMs, electronic data capture point of sales etc have become necessary pre-requisites for success in retail credit. The promise of lower transaction costs increases sales productivity.

11. Product innovation

According to Peter Drucker innovation that is not in tune with the strategic realities will not work, confusing novelty with innovation (should avoided) test of innovation is that it creates value; novelty creates only amusement. Banks, therefore, need to innovate products suiting the needs and requirements of different types of customers.
12. Business process reengineering

   It simplified processes and aligning them around delivery of customer service impinging on reducing customer touch points are its essence. Work flow and document management should be integrated part of process change. The documentation issues have to remain simple both in terms of documents to be submitted by the customer at the time of loan application and those to be executed upon sanction.

13. Rural orientation

   Action is yet to be taken on the retail front in rural India. It offers vast market to the players which remain untapped.

14. Cross-selling of products and services

   Cross selling in this new-age marketing weapon of selling a gamut of products to existing customers is being increasingly used by private banks to boost retail business (Muthukumar 2004). While the extent of successful cross-selling is high for personal loans (50%) it is comparatively low for home loans (10-20%) and car loans (10.10%)
Challenges in retail banking

Due to cut-throat competition in the retail market and attendant risk-factors linked thereof, bankers need to overcome the following constraints and should come out with suitable business strategies.

Absence of a clear cut and comprehensive corporate policy covering strengths and limitation in regard to retail banking i.e. SWOT analysis.

Lack of awareness amongst bankers, particularly the frontline officers that retail banking centers around ‘service’ and business is only a by-product.

Failure to assess properly the ever increasing customers’ expectations

Improper identification and assessment of retail segments

Even though a wide-range of products and services are offered, bank’s core competence in handling products and services is ignored

Inability to innovate and respond to the changing needs of customers in terms of new products and services.

Sub-optimal utilization of the available technology to cope with expanding horizons of retail business.
Lack of marketing thrust and dependence on ‘walk in business’

Underutilization of existing data-base and inability to “cross-sell” across banks.

Poor service quality and lack of proper understanding of customer relationship management.

**Future perspective**

Retail banking segment of the banking industry is continuously undergoing innovations and process reengineering adjustments and alignment. Given the size advantages, diverse customer-base and scope for future expansion, there is a need for evolving a systems approach to retail banking. Integrated financial automation should be the key to retail banking. Whereas the existing customer repository of demographic and financial product-lines and services should be facilitated for future expansion of retail operations including cross-selling of products and services across banks. In this integration process, customer service, customer relationship and customer retention should be some of the high priority areas for future expansion of retail banking segment in India.

Financial intermediaries play a key-role by tapping savings from surplus saving sector and canalizing such savings for the purpose of investment in deficit spending sector. They act as a conduit pipe in transmitting savings from the sector where it is surplus to the sector where there is deficit. Among the financial intermediaries Commercial Banks occupy a strategic position on account of the fact that they are the largest.
repositories of community savings and help to meet the diverse requirement of borrowers by way of loans. In the past, commercial banks had pursued several policies under the impetus of social banking that contributed towards the welfare of the people and society.

The economy of any country consists of numerous entities which are vital for the smooth functioning of the economy. Each of these entities has a role to play and any disturbance or hindrance in their proper functioning would cripple economy. It is recognized that the main entities of economy are the household sector and the corporate sector comprising of private sector and public sector and of course, the government.

Members of these sectors borrow funds at different periods of time. Household sector comprises of individuals who borrow to purchase houses, automobiles etc. Businesses borrow for capital expenditures and government frequently borrows for public expenditures and for many other purposes as well.

Banks are the oldest form of financial intermediaries in India. They play a key role in canalizing the savings of the household sector to Organized and unorganized sectors. The Reserve Bank of India is the Central Bank acting as monetary authority of the country and serve as the banker to the government as well as the banker’s bank. Commercial banks perform the activities of accepting deposits and other normal banking activities together with ancillary activities.
Banking institutions are segregated into various categories on the basis of their incorporation and their business. Various kinds of banking institutions functioning in the country comprise of (i) commercial banks which include Indian Scheduled Banks, Foreign Scheduled Banks and Non-scheduled Banks (ii) Regional Rural Banks (iii) Local Area Banks and (iv) Co-operative Banks. At present there are 27 public sector banks. (Nationalized banks (19), SBI and its associates (8) 30 private sector banks (Old private banks 22, New private banks 8) Foreign Banks in India 40 Regional Rural Banks 195. Scheduled Co-operative banks are 68 of which scheduled urban Co-operative banks are (52) scheduled state co-operative banks (16).

Banking operations are basically divided into two segments: One is the corporate banking or wholesale banking which serves the financial needs of the corporate houses, companies and the other is Retail Banking. It is a form of mass banking where financial needs of the individuals like professionals, salaried persons, self-employed, housewives, students etc. are met.

The new millennium has brought in new sunshine for Indian retail credit segment. Banking industry has been experiencing a sea change with regard to retail lending. There has been an explosion of retail credit by banks. This is mainly due to the circumstantial need of the banks to expand business volumes and enter an area that was not encouraged before. Previously, banks were reluctant to consider retail credit applications for three dominant reasons.
**Retail credit was more risky while volume wise it did not have enough potential to contribute to banks’ bottom line.**

**Large number of low value accounts involved higher administration overheads.**

**The main retail credit wing-home loans with longer repayment period has the effect of creating Asset – Liability mismatch under the bank’s Asset – Liability Management (ALM) system since**

**Lend able resources of the banks are essentially of short maturity.**

But things have changed for the better. Retail credit is now the centre of gravity in Indian banking. Most of the banks have now formulated variety of retail credit schemes beginning with home loans to even gas kit loan for car owners. Some banks have as much as 26 such schemes. The websites of banks are full of retail credit schemes as points of attractions.

As per the latest available report (2006), loans to individuals to buy vehicles, houses and various kinds of consumer durables occupy around 40 - 45% of annual growth of credit in other sectors such as commercial and institution priority sector credit etc.

This phenomenal growth has arisen in banking more out of business compulsion and not by choice because:

**Commercial and Institutional credit over the last three years has not picked up in the same pace as in the past. Industrial credit as a proportion to net bank credit has come down from 50.3% in March 2000 to 42.9% in march 2002.**

The windows of External
• Commercial Borrowing by large corporate have opened up opportunities to them for cheaper sources of credit. It is imperative for banks to increase their share in service sector.
• Computerization in banks has made it convenient for banks to handle large volume but low value retail credit accounts smoothly.
• Rate of interest (together with processing charges etc) in retail credit accounts is found to be more remunerative as against average C & I advance rate of interest of say 8 – 8.5%. Retail credit average rate of interest is at least 1 – 1.5% higher.
• Not much seriousness is now being shown in correcting Asset – Liability mismatches. Since it is taken for granted that savings bank deposits and time deposits would continue to be the perennial resource base of the banks – apparent mismatch may not have any material bearing in managing banking business.
• Bankers have expressed an opinion that delinquency rate in retail credit is generally lower than that of C & I credit / other credit.

HOUSING FINANCE – A PRIORITY SECTOR

Certain types of credit extended by commercial banks for housing are now reckoned as priority sectors. These include both direct and indirect housing finance. The types of direct finance which have been brought under the ambit of priority sector include (1) loans up to Rs.5 lakhs in rural and semi-urban areas and (2) up to Rs.10 lakhs in urban and metropolitan areas for construction of houses granted to individuals. Besides loans up to Rs.50,000 for repairs to damaged houses by
individuals are also treated as priority sector. The type of indirect housing finance which has been made part of priority sector lending includes assistance given to any governmental agency or institution for construction of houses or for slum clearance and rehabilitation of slum dwellers subject to a ceiling of Rs.5 lakhs per housing unit. Assistance given to non governmental agencies approved by the NHB for the purpose of refinance, for construction of houses or for slum clearance and rehabilitation of slum dwellers subject to a ceiling of loan component of Rs.5 lakhs per housing unit is included in the scheme. Further more, subscription to bonds issued by NHB and Housing and Urban Development Corporation (HUDCO) exclusively for financing of housing, irrespective of the loan size per dwelling unit would also be considered as loans to priority sector.

**SCOPE OF THE STUDY**

The study is conducted in Retail Banking covering loan products such as Home loans, Car loans, Educational loans and personal loans which are widely popular in India. Home loan is the main driver in Retail Banking since housing finance satisfies the basic necessity of life namely, housing for society and also profitable for the banker. It has a low rate of non-performing loans. The concessions given in the various budgets for interest on loan up to Rs.1,50,000/- and repayment of principal up to Rs.1,00,000 (along with other savings of the individuals) are the main catalytic agent for going in for housing loan. The major developments during the period were the aggressive role played by the commercial banks in the industry and the dramatic fall in the interest rates across all maturities. Banks despite being a late entrant have overtaken the HFCs in
the home loan markets. The share of banks in total home loan disbursements has risen from 43.6% in the year 2000-01 to 65.5% in 2002-03.

The study is confined to Tiruchirappalli District. The researcher has selected the district as the district has more number of industries like Barath Heavy Electricals Limited, Railway workshop at Ponmalai, Heavy Alloy Penetrator Project and more ancillary units in and around Trichy. The population consist of more proportion of working people which gives ample scope for the bankers to distribute the home loans. The Indian Overseas Bank is the lead bank of the district. State Bank of India has the major share in the housing loan market in the district. So, the two banks are selected for the analysis. The study covers a period of 5 years from 2000 – 2001 to 2004-2005.

**OBJECTIVES OF THE STUDY**

Objectives of the study are listed as under

(i) To review the home loan market in Tiruchirappalli.

(ii) To review the role of banks in housing development

(iii) To analyze the profile of the borrowers on the basis of economic and demographic factors

(iv) To suggest measures to promote the Retail loan market with special reference to home loan.

(v) To compare the loan portfolio of banks with Housing Finance Company (i.e.) LICHF.
METHODOLOGY

Sources of Data

The secondary data used and referred in this study are the reports on the banking trends published by RBI, IBA Bulletin, reports of the press (i.e.) Business Today, Business world, Economic Times and Business Line Moreover. Special reports published by ICFAI University in different magazines and Journals are referred to.

Primary data are also collected through questionnaire from the borrowers to understand their profile.

Sampling Design

Primary data has been obtained from a total of 200 borrowers 100 from LICHF and 100 from banks. Out of total questionnaire circulated ninety seven are collected from LICHF and eighty five are collected from banks. The rest are rejected due to inconsistent information.

Hypotheses

The following hypotheses are framed in this study.

(i) The higher level of income has resulted in increasing inclination to borrow.

(ii) Concessions provided to interest on borrowed capital and repayments of principal in various budgets are the main driving forces for the growth of housing finance.

Statistical tools applied in this study are:

(i) Chi-square tests

(ii) ANOVA
Limitations of the study

The main limitations of this study are:

(a) Primary data have been collected from the miniscule percentage of the population which represents only partially the Indian Scenario.

(b) The study is done by interview method with the bankers. Bankers expressed their inability to part with the commercial and competitive data in quantitative terms. They are of the opinion that the divulging of information may be prejudicial to the growth and profitability of a particular branch.

CHAPTER SCHEME

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6. Role of RBI in monitoring the market
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Reference

1 RBI report on Trend and progress of banking in India 2000-01.
2 Hand book on housing statistics