Chapter 4

RETAIL BANKING IN INDIA - AN OVERVIEW

4.1 Introduction

4.2 Retail Banking

4.3 Retail Finance
4.1 Introduction

One of the spectacular innovations in the commercial banking sector is the retail banking. It refers to banking in which banks undergo transactions directly with consumers rather than with corporates or other banks. Consumer credit is the heart of retail banking. In retail banking the banks provide services to individuals and small business concerns and the dealings are in large volumes and low values. The retail banking portfolio encompasses deposits and assets linked products as well as other financial services offered to individuals for personal consumption. Retail banking is increasingly viewed by banks as an attractive market segment with opportunities for growth and profit. The fastest growing division in the banking sector is the retail sector. Retail banking is a system of providing soft loans to the general public like family loans, house loans, personal loans, loans against property, car loans, auto loans etc. The products are backed by world-class service standards and delivered to the customers through the growing branch network, as well as through alternative delivery channels like ATMs, Phone Banking, Net Banking and Mobile Banking. Today’s retail banking sector is characterised by three basic features; viz:

- Multiple products-deposits, credit cards, insurance, investment and securities
- Multiple channels of distribution- call centre, branch, internet
- Multiple customer groups- consumer, small business and corporate
4.2 Retail Banking

4.2.1 Features of retail banking

Retail banking refers to the dealing of commercial banks with individual consumers, both the liabilities and the asset side of the balance sheet. The important products offered by banks in retail banking are fixed, current/ savings account on liabilities side; and personal loans, house loans, auto loans and educational loans on the asset side. Today’s retail banking sector is characterised by the following features:

- Retail banking aims at doing banking business in large volume of transactions involving low value.
- The retail banking portfolio includes deposits and assets linked products as well as other financial services provided to individuals for personal consumption.
- Retail banking business is an attractive market segment with opportunities for growth and profits.
- It provides an opportunity to banks to diversify their asset portfolio. Since loans are given to a large number of consumers and transactions have very low value, the risk of NPA is reduced because all the consumers do not make default in making loan repayment at a time.
- Retail banking is based on the maxim “do not keep all the eggs in one basket”
Retail banking industry is diverse and competitive. There is a large number of retail banking products that are extremely customer-friendly and are offered by many banks.

Banks adopt multiple channels of distribution of retail banking products. The channels include call centre, branch, internet, mobile phones, ATMs etc.

4.2.2 Advantages of retail banking

Retail banking is mass market banking, where individual consumer’s diverse needs are fulfilled at the local level i.e. by providing multiple products. It has been facilitated by growth of banking technology and automation of banking process. Retail banking has the following advantages.

- Retail deposits are stable and constitute core deposits.
- They are interest insensitive and less bargaining for additional interest.
- Effective customer relationship management with retail customers builds a strong customer base.
- Retail banking increases the subsidiary business of banks.
- Retail banking results in better yield and improved bottom line for banks.
- Retail segment is a good avenue for funds deployment.
- Consumer loans are presumed to be of lower risk and NPA perception.
- Improves lifestyle and fulfils aspirations of people through affordable credit.
- Retail banking provides an opportunity for banks to innovate banking products as per the expectations of various classes of customers.
• Retail banking involves minimum marketing efforts in a demand-driven economy.

• Diversified portfolio due to huge customer base enables banks to reduce their dependence on a few or single borrower.

• Banks can earn good profits by providing non-fund based or fee based services without deploying their funds.

• Credit risk tends to be well diversified as loan amounts are relatively small.

4.2.3 Disadvantages of retail banking

• There can be problems in managing large number of clients, especially if IT systems are not sufficiently robust.

• The cost of maintaining branch networks and handling large number of low-value transactions tend to be relatively high.

• Designing own and new financial products is very costly and time-consuming for the bank.

• Though banks are investing heavily in technology, they are not able to exploit it to the maximum.

• Major disadvantages are monitoring and follow-up of huge volume of loan accounts inducing banks to spend heavily on the human resource department.

• Long term loans like housing loan, due to its long repayment term, can become NPA in the absence of proper follow-up.
4.2.4 Retail banking in India

In the post independence era the evolution and growth of banking sector has gone through innumerable twists and turns. In India banks are nationalised with the main objective of reaching out to the unbanked masses and so retail banking is important in India to provide banking services to unbanked masses.

Retail banking in India is not a new phenomenon. It has always been prevalent in India in various forms ever since banking was first established here. Cooperative banks that have been in existence in India for over a century have always had retail thrust. It is only since the mid-nineties that the term “retail banking” has been used as a means of reinforcing a conscious foray into this particular line of business. 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. These loans are marketed under attractive brand names to differentiate the products offered by different banks.

Unlike wholesale banking, retail banking has high sized business with many banks competing for market share. Retail banks focus mainly on consumer markets. Here the transactions of the banks are directly with consumers and not with corporations or other banks. It refers to the dealing of commercial banks with individual customers, both on liabilities and assets side of the balance sheet.

Although retail banking is, for the most part, mass-market determined, many retail banking products may also extend to small and medium sized business. Nowadays much of retail banking is streamlined electronically via ATMs, or through virtual retail banking known as online banking.
The retail loan portfolio of Indian private sector banks has been growing speedily in the recent past. The entry of new generation banks and foreign banks with innovative technology and technology-driven products has changed the entire scenario. The retail sector which remained unobserved earlier is now the most important area of concern for banks. Banks are offering so many products to the customers and they can choose the one which suits them. As the competition is growing in retail banking, maintaining service quality in banks is becoming essential. The Indian retail banking is expected to grow tremendously because of the changing attitude of customers toward borrowings, low cost of borrowings and optimism regarding economic growth.

4.2.5 Drivers of retail banking in India

The growth in banking technology and automation of the banking process facilitated retail banking. The rapid growth and spread of retail banking is due to the technological development. The nature of products offered in retail banking is also expanded. In a growing economy like India retail banking has vast opportunities and challenges.

The basic reasons for which Indian banks have diversified into retail banking are the following:

1. The retail banking products are customer oriented. Transactions with small value may be cost ineffective in a highly competitive environment. But retail banking eliminates market risk.\(^9\)

2. In India the demand for consumer durables has increased owing to the economic growth and prosperity and the consequent increase in the purchasing power of the people. Major portion of the household sector in
India is middle class people. There is continuous rise in the percentage of middle and the high income households in India. Indian retail banking is facilitated by improved purchasing power of consumers and liberal attitude towards personal debt.

3. India has the highest proportion of the population below 35 years of age (young population). This is a positive factor for the growth of retail banking in India. Changing consumer demographic indicates a vast potential for growth in consumption, both quantitatively and qualitatively.

4. Another important factor which facilitated the growth and development of retail banking is the development of technology. Technological innovations relating to increasing use of credit/debit cards, ATMs, internet and phone banking etc. are attracting many new customers to the banking field.

5. The lower levels of NPA in retail lending and decrease in interest spread in the corporate sector have encouraged the banks to shift towards retail sector. Besides, fall in interest rates, availability of consumer goods at competitive and reasonable prices and income tax benefits, especially in case of housing sector, have also contributed to the growth of retail banking.

Indian banks have adopted the best international practices of accounting and integrated risk management systems after the liberalisation of the economy. Banks have got the opportunity to diversify their risk through the retail loan portfolio. Besides this, the retail advances have lower defaults in repayment compared to the overall bank loans. The comparatively lower provisioning burden on banks on retail loans have compelled them to diversify into retail sector.
There has been dramatic operational transformation in retail banking in the recent years. The factors which compelled banks to rethink their real strategies are increased competition, mergers and acquisitions and new regulatory requirements. The retail banks have adopted latest technology to maximise sales, manage distribution channels and plan operations necessary to acquire, satisfy and retain customers.

4.2.6 Retail banking products

Retail banking includes a comprehensive range of financial products such as deposit products, loan products and payment services. The typical products offered in the Indian retail banking segment are:

4.2.6.1 Retail deposit products

- Savings bank account
- Recurring deposit account
- Current deposit account
- Term deposit account
- Zero balance account for salaried people
- No frill account for common man
- Senior citizen deposit account, etc.

4.2.6.2 Retail loan products

- Home loans to resident Indians for purchase of land and construction of residential house/ purchase of ready built house/ for repairs and renovation of an existing house.
• Home loans to Non-Resident Indians.

• Auto loans for new/used four-wheelers and two-wheelers.

• Consumer loans for purchase of jewels, for meeting domestic consumption etc.

• Education loans for pursuing higher education both in India and abroad.

• Trade related advances to individuals for setting up business, retail trade etc.

• Crop loan to farmers.

4.2.6.3 Retail services

• Safe deposit lockers

• Depository services

• Banc assurance products etc.

4.2.7 Challenges faced by Indian retail banking

A major challenge for retail banks in India is the retention of customers. In this competitive environment the customer retention is very difficult. Profitability of retail banks is highly effected by customer retention. According to a research by Reichheld and Sasser\textsuperscript{11} in the \textit{Harvard Business Review}, 5\% increase in customer retention can increase profitability by 35\% in banking business, 50\% in insurance and brokerage, and 125\% in the consumer credit card market. Thus, banks need to focus on customer retention. They are expected to take utmost care to retain the ongoing trust of the public. Banks are required to adopt innovative strategies to meet customers’ needs and requirements in terms of service and products.\textsuperscript{12} The efficiency of operations would provide the competitive edge for success in retail banking in coming years.
In future rising indebtedness could turn out to be a cause for concern. In developed countries the household debt in proportion to disposable income is much higher. India’s condition is not comparable to that of the developed countries. There will be high uncertainty in such a scenario. There will be huge risk and high uncertainty if there is a disproportion between debt/loan and disposable income. The Reserve Bank has been well aware of this problem. For example, as Revathy has pointed out, 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)\textsuperscript{13}.

Another important issue in retail banking is risks in money laundering and KYC (Know Your Customer) issues. Banks should take utmost care to retain the trust of the public in them. Banks have to consider and verify all the documents seriously which are accepted by them for approving the loans. As the amount of transactions involved is lower, the risk of money laundering is less in retail banking. There is also possibility of waiver of KYC procedures by banks in order to retain customers in this competitive environment.

The core activities in the bank like hardware and software maintenance, ATM setup and operation including cash refilling etc are usually outsourced by banks. So the issue of outsourcing has become very important in recent past in Indian retail banking.

Information technology poses both opportunities and challenges. Many customers prefer the personal touch of their bank even though the bank has ATM and Internet Banking services.
4.2.8 Future of retail banking in India

Retail banking in India has exhibited enormous growth in the recent past and has emerged as one of the major drivers of the overall banking industry. In fact, this growth is attributed to the vast growth of personal wealth, favourable demographic profile, rapid IT development, financial market reforms and micro-level supply side factors coupled with the conducive macro-economic environment.

There are immense opportunities for retail banking in a growing economy like India. One of the important factors contributing to this is the rise of Indian middle class. There will be a continuous rise in the percentage of middle to high-income Indian households. This may lead to substantial growth in the retail sector.

Retail lending is only a part of retail banking. Retail depositors play an important role in retail banking. The retail shopkeepers, the self employed, the pensioners, the home makers, and the employed need to get a place in the bank. The Government of India and the Reserve Bank of India are very particular about Financial Inclusion now-a-days. So the entire banking industry is viewing retail banking as an emerging business opportunity in tune with financial inclusion.

In retail banking credit history information about the households is extremely important. Banks have a traditional resistance to share credit information of their clients to uphold the confidentiality of banker-customer relationship. The credit information is not passed between banks as well as bank sectors. The Credit Information Bureau (India) Limited (CIBIL) was incorporated in 2000 in India. The main aim of CIBIL is to provide credit information to credit granting institutions. They collect and disseminate credit information pertaining to both commercial and
consumer borrowers. The banks must exercise due diligence before declaring a borrower as defaulter.

The banks are using outsourcing as a means for cost reduction and achieving efficiency in operations. To cope with the increasing market orientation, competition and technological innovations, the banks are increasingly using outsourcing. Thus outsourcing has become an important element in retail banking sector.

There is a glorious future for retail banking in India. It helps in the development of individual customers who avail the products or services as well as in the overall development of the society. Retail banking has proved to be an effective tool to improve the bottom lines of banks. Thus there is vast scope for retail banking business in India.

4.3 Retail Finance

Retail finance or retail lending is that segment of retail banking which offers various loan products to the customers. Housing loans, loan for the purchase of durables, auto loans, credit cards and educational loans are the typical products offered in Indian retail finance segment. The loan values of retail lending ranges between Rs. 20,000 to Rs.100 lakhs. The duration of loans is generally five to seven years. Housing loans have a longer duration of 15 to 30 years.

Retail banking results in better yield and improved bottom line for the bank and hence retail segment is a good avenue for funds deployments. It is presumed that consumer loans are of lower risk and NPA perception. Banks can reduce their dependence on a few or single borrower through diversified portfolio of huge customer base. Banks are providing non-fund based or fee-based services and can
earn good profits without deploying their funds. It is possible to improve the lifestyle and fulfill the aspirations of the people through affordable credit in retail lending. Further, through increased production activity, the economic revival of the nation can be achieved. Since the evolution of banking, retail banking has been prevalent in various forms in India.

There are vast changes in the Indian retail finance market during the last few years. Earlier, Indians believed in the concept of saving and then spending and were against the concept of availing credit for purchases. The overzealous lenders, who realised the huge latent potential of the Indian consumers, came up with a variety of customer credit products and they forced them up on consumers. This has changed the psychology of Indian consumers who no longer consider credit as a social stigma. They are willing to fulfill their dreams and aspirations through the credit facilities.

Penetration of retail loan products is very low in India. Home loans in India form only about 6% of our GDP, while the same is about 60% in advanced countries. Of every 1000 Indians, only eight own a car, whereas this number is nearly 500 in developed countries. Combined with rising affluence in the country and increasing disposable incomes, these low levels of penetration indicate that, for retail loan providers in India, the growth story is likely to continue for a long time.

In India retail lending is becoming an important segment of bank credit. The inclusive, comprehensive and pervasive growth of India can be obtained through it. In future the growth of retail banking will be decided by retail lending. The credit off-take by the under banked segments of the society needs to be improved. There is expanding middle class persons in need of varied banking services and India is the
second largest consumer market in the world and consumers in this country are dreaming of purchasing power.

Through the growth of consumer lending at a faster pace and making it available at affordable rates, the aspirations of these consumers can be fulfilled. Personal loans, also called consumer loans, are now-a-days very popular in India because of the spurt in the income levels of middle-income segment and the growth of consumerism. These loans are easy to arrange on the basis of fixed monthly repayment program. Banks are facing tough competition not only amongst themselves but also from NBFC’s.

4.3.1 Characteristics of retail loans

- Retail loans are small size loans.
- With well diversified portfolios the needs of a large number of customers can be met.
- The target customers are generally individuals or small organisations.
- Standard products are offered to customers.
- Centralised operations of retail credit exist in most of the banks.
- Because of decentralisation, banks can make quick credit related decisions.
- These loans are designed to cover varied segments of risks.
- Volume of business is high.
- Number of transactions is large.
Retail exposure of banks include various types of retail credit such as residential mortgages, credit card, automobile and personal loans etc. Retail loans have the following features:

- Types of facilities - Retail loans are the finance facility of a fixed amount extended to meet a one-time requirement of a customer, for a fixed tenure, to be repaid over a period in instalments.

- Secured / Unsecured facilities - Secured loans are always secured by an underlying asset against which funding is extended. Unsecured loans do not have any underlying security and are purely extended based on the creditworthiness of the borrower.

- Interest - On a loan given at a fixed rate, interest is charged throughout the tenure of the loan at that rate which is fixed at the time of granting the loan. In case of floating rate of interest, the rate of the loan varies from time to time according to the movement of interest rate in the market. Loans that are fixed in the initial years and become floating later would be considered as teaser loans.

- Tenure - The tenure depends upon the amount of loan and repayment capacity of the customer.

- Loan to Value ratio - Loan to Value ratio refers to the maximum percentage of the value of the asset that is given as a loan. It varies according to the nature of the asset and also the rate at which the asset is expected to depreciate.
Retail lending is a spectacular innovation in the commercial banking in recent years. Rapid advancement in information technology, financial market reforms, the evolving macroeconomic environment, and several micro level demand and supply side factors have contributed to the growth of retail lending in developing countries. In recent past, retail lending has turned out to be a key profit driver for banks with retail portfolio constituting 18.80% of total outstanding advances as on March 2013. The overall impairment of the retail loan portfolio worked out much less than the gross NPA ratio for the entire loan portfolio.

Retail loans have been a prime driver of credit growth in Indian banking sector. Table 4.1 shows the aggregate advances and retail advances of scheduled commercial banks in India for the period from 2004 to 2013.

Table 4.1

<table>
<thead>
<tr>
<th></th>
<th>Aggregate advances (a)</th>
<th>Retail advances (b)</th>
<th>Percentage of (b) to (a)</th>
</tr>
</thead>
<tbody>
<tr>
<td>As on March 31</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>864271</td>
<td>189041</td>
<td>21.90</td>
</tr>
<tr>
<td>2005</td>
<td>1105725</td>
<td>266611</td>
<td>24.10</td>
</tr>
<tr>
<td>2006</td>
<td>1517497</td>
<td>375739</td>
<td>24.76</td>
</tr>
<tr>
<td>2007</td>
<td>1949567</td>
<td>487860</td>
<td>25.02</td>
</tr>
<tr>
<td>2008</td>
<td>2394565</td>
<td>571048</td>
<td>23.84</td>
</tr>
<tr>
<td>2009</td>
<td>2857525</td>
<td>593816</td>
<td>20.78</td>
</tr>
<tr>
<td>2010</td>
<td>3345619</td>
<td>622752</td>
<td>18.61</td>
</tr>
<tr>
<td>2011</td>
<td>4076867</td>
<td>743972</td>
<td>18.25</td>
</tr>
<tr>
<td>2012</td>
<td>4673435</td>
<td>859912</td>
<td>18.40</td>
</tr>
<tr>
<td>2013</td>
<td>5369681</td>
<td>1009501</td>
<td>18.80</td>
</tr>
</tbody>
</table>

Source: Report on Trends and Progress of banking in India- various issues
The total amount of retail credit of scheduled commercial banks in India shows an increasing trend during this period. But the percentage of retail advances to total advances is decreasing during the period. The main reasons for the reduction in growth rate of retail credit are the rise in interest rate, measures adopted by RBI for inflation control, global financial meltdown etc.

4.3.2 Retail loan portfolio

The retail loan portfolio of scheduled commercial banks in India consists of housing loan, loan for the purchase of consumer durables, credit card, auto loans and other personal loans.

4.3.2.1 Housing loan

Housing loans are those loans provided by commercial banks directly or indirectly for the purpose of purchase, construction, re-construction or repairing of the house property. There are a variety of home loan schemes for each bank. They are home purchase loan, home improvement loan, home construction loan, home extension loan, home conversion loan, land purchase loan, balance transfer loan, bridge loan and home loans for NRIs.

4.3.2.2 Consumer durables loan

These kinds of loans are provided for purchasing consumer durable products like television, music system, washing machine etc. These are the unique kind of loans that are provided by banks to attract more and more people towards them. Banks generally provide a minimum amount of Rs. 5000 and maximum of Rs. 200,000 with a maximum repayment period of five years as consumer durables loan.
4.3.2.3 Credit card

Credit card is a small plastic card that allows its holder to buy goods and services on credit and to pay at fixed intervals through the card issuing agency. Banks issue credit card to selected customers depending on their income, credit worthiness, reputation etc. Credit card receivables constitute a significant portion of retail credit in India.

4.3.2.4 Auto loans

Auto loans/vehicle loans are those loans provided by commercial banks for the purpose of purchase of vehicles. Auto loans may be car and two wheeler loans or commercial vehicles loan.

4.3.2.5 Other personal loans

Personal loans are intended to meet any kind of personal expenses of the borrower such as family functions, medical expenses, travel expenses in India and abroad, marriage expenses of children, buying computers/laptops, festival celebrations etc.

Table 4.2 shows the retail loan portfolio of scheduled commercial banks in India for the period from 2004 to 2013.
### Table 4.2

**Retail loan portfolio of scheduled commercial banks in India**

(Amount in Rs. Crore)

<table>
<thead>
<tr>
<th>Item</th>
<th>As on March 31</th>
</tr>
</thead>
<tbody>
<tr>
<td>Housing loan</td>
<td>89449</td>
</tr>
<tr>
<td></td>
<td>(47.32)%</td>
</tr>
<tr>
<td>Consumer durables loan</td>
<td>6256</td>
</tr>
<tr>
<td></td>
<td>(3.31)%</td>
</tr>
<tr>
<td>Credit card receivables</td>
<td>6167</td>
</tr>
<tr>
<td></td>
<td>(3.26)%</td>
</tr>
<tr>
<td>Auto loan</td>
<td>35043</td>
</tr>
<tr>
<td></td>
<td>(13.14)%</td>
</tr>
<tr>
<td>Other personal loans</td>
<td>87170*</td>
</tr>
<tr>
<td></td>
<td>(46.11)%</td>
</tr>
<tr>
<td>Total retail loan</td>
<td>189042</td>
</tr>
<tr>
<td></td>
<td>(100)%</td>
</tr>
</tbody>
</table>

**Source:** RBI- Report on Trends and Progress of banking in India-various issues.

**Note:** Figures in parentheses represent percentage to total.

* include auto loans and other personal loans

The increase in retail credit during the period was entirely attributed to the housing loan segment, which constituted the single largest portion of total retail loans of Indian banks. As on 31st March 2013, housing loan constituted 47.09% of the total retail advances followed by auto loan (14.37%), credit card receivables (2.65%) and consumer durables loan (0.34%). Other personal loans were 35.84% of total retail loans. During the period the proportion of credit card receivables, consumer durables loan and personal loans to total retail loans decreased. The proportion of housing loan and auto loan was fluctuating during the period. As the
retail sectors are rate-sensitive, credit to these sectors in future would be impacted by the emerging interest rate environment. Figure 4.1 shows the retail loan portfolio of scheduled commercial banks in India as on March 2013.

Figure 4.1
Retail Loan Portfolio of Scheduled Commercial Banks in India as on March 2013.

4.3.3 Retail lending in Kerala

The retail loan portfolio of scheduled commercial banks in Kerala includes housing loan, vehicle loan, consumer durables loan, credit card etc. The table below shows aggregate advances and retail advances of scheduled Commercial banks in Kerala from 2004 to 2012.
<table>
<thead>
<tr>
<th>As on March 31</th>
<th>Aggregate advances(a)</th>
<th>Retail advances(b)</th>
<th>Percentage of (b)to (a)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>32536.54</td>
<td>10579.67</td>
<td>32.52</td>
</tr>
<tr>
<td>2005</td>
<td>39714.71</td>
<td>14217.63</td>
<td>35.79</td>
</tr>
<tr>
<td>2006</td>
<td>51730.13</td>
<td>18348.24</td>
<td>35.47</td>
</tr>
<tr>
<td>2007</td>
<td>61066.58</td>
<td>22646.69</td>
<td>37.09</td>
</tr>
<tr>
<td>2008</td>
<td>72944.62</td>
<td>25882.28</td>
<td>35.48</td>
</tr>
<tr>
<td>2009</td>
<td>81973.33</td>
<td>31272.75</td>
<td>38.15</td>
</tr>
<tr>
<td>2010</td>
<td>98137.84</td>
<td>34596.27</td>
<td>35.25</td>
</tr>
<tr>
<td>2011</td>
<td>126230.35</td>
<td>38930.89</td>
<td>30.84</td>
</tr>
<tr>
<td>2012</td>
<td>151849.08</td>
<td>43479.66</td>
<td>28.63</td>
</tr>
</tbody>
</table>

*Source: Compiled from RBI- Basic Statistical Returns of Scheduled Commercial Banks in India- Various issues.*

The total retail advances of scheduled commercial banks in Kerala have increased during the period. The percentage of retail advances to total advances was increasing up to 2009 and is decreasing from 2010 onwards. This is in tune with the general trend at the national level. The percentage of retail advances to total advances shows a decreasing trend since 2010. A comparison of percentage of retail advances to total advances of scheduled commercial banks in India and Kerala is given in Figure 4.2.
Figure 4.2

Retail Advances as Percentage of Aggregate Advances of Scheduled Commercial Banks in India and Kerala

Table 4.4 shows the retail loan portfolio of scheduled commercial banks in Kerala for the period from 2004 to 2012.
Table 4.4
Retail loan portfolio of scheduled commercial banks in Kerala -2004-2012
(Rs in Crores)

<table>
<thead>
<tr>
<th>Items</th>
<th>As on march 31</th>
</tr>
</thead>
<tbody>
<tr>
<td>Housing loan</td>
<td>5559.10</td>
</tr>
<tr>
<td></td>
<td>(52.55)</td>
</tr>
<tr>
<td>Consumer durable loan</td>
<td>200.43</td>
</tr>
<tr>
<td></td>
<td>(1.89)</td>
</tr>
<tr>
<td>Credit card receivables</td>
<td>2.51</td>
</tr>
<tr>
<td></td>
<td>(0.02)</td>
</tr>
<tr>
<td>Vehicle loan</td>
<td>1130.51</td>
</tr>
<tr>
<td></td>
<td>(10.69)</td>
</tr>
<tr>
<td>Other personal loans</td>
<td>3689.63*</td>
</tr>
<tr>
<td></td>
<td>(34.87)</td>
</tr>
<tr>
<td>Total</td>
<td>10579.67</td>
</tr>
<tr>
<td></td>
<td>(100)</td>
</tr>
</tbody>
</table>

Source: Compiled from RBI-Basic Statistical returns of Scheduled commercial banks in India- various issues

Note- Figures in parentheses represents percentage to total

*- includes credit card receivables
Housing loan constitutes the major share of retail loans in Kerala followed by other personal loans and vehicle loan. The consumer durables loan and credit card receivables are the least in the retail loan portfolio and are less than one percentage of total retail advances in Kerala. This is also similar to the ratio of all India scheduled commercial banks. The retail loan portfolio of scheduled commercial banks in Kerala as on March 2012 is shown in figure 4.3.

![Retail Loan Portfolio of Scheduled Commercial Banks in Kerala as on March 2012](image)

**Figure 4.3**
*Retail Loan Portfolio of Scheduled Commercial Banks in Kerala as on March 2012*

### 4.3.4 Methods of charging interest

Interest is the fee which is paid by the borrower for borrowing money from the lender. Interest on loans can be calculated either on a flat rate or reducing/diminishing rate method. In the case of flat rate method, interest is charged on the full amount of the loan throughout the entire period of the loan. In the case of reducing balance method, interest is calculated only on the outstanding loan balance.
as reduced by the monthly principal payment. The reducing balance method may be monthly reducing or yearly reducing or even daily reducing basis. In yearly reducing system, the principal, for which interest is paid, reduces at the end of the year. Thus, here interest is to be paid on a certain portion of principal which had already been paid back. The principal reduces every month in monthly reducing system. In daily reducing system, the principal reduces from the day the EMI is paid.

4.3.4.1 Fixed rate interest

In fixed rate interest, the rate of interest remains unchanged for the entire duration of the loan. The borrower does not benefit the drop of interest rate in the market. Here, the rate of interest is fixed in advance when the loan is taken. So the borrower knows the exact amount he needs to pay in future. It is beneficial for a person who would like to know his future cash outlays in advance.

4.3.4.2 Floating rate interest

This is the rate of interest that fluctuates according to the market lending rate. Floating interest rate is linked to Prime Lending Rate (PLR). When PLR is revised, the interest rate also stands revised. This means the customer takes the risk of paying more in case the lending rate goes up. Here the interest rate is not determined while borrowing but is depend on some underlying rates. By taking a floating rate loan both the lender and borrower are exposed to a certain degree of risk.

4.3.4.3 Teaser loans

Loans with interest that are fixed in the initial years and become floating later would be considered as teaser loans. Interest rates, that are a mixture of fixed and floating are called teaser rates. In October 2010, RBI had increased the standard
provisioning requirements five times for teaser loan products, as compared to other categories and so it reached to 2% for such loans.

4.3.5 Equated Monthly Instalment (EMI)

EMI is the fixed amount payable monthly throughout the repayment period of a loan by the borrower to the lending institution. It consists of a portion of interest as well as principal. The EMI system is popular with the borrowers as they find it more convenient to pay only a fixed amount per month throughout the loan period. EMI system of loan repayment has the following features.

- Each instalment contains both components of principal repayment and interest charges.
- Interest is calculated on reducing balance method.
- Interest component is higher in the beginning and progressively lower towards the end. That means, the principal component of an EMI is lower during initial periods and higher during later periods.
- The amount of EMI depends on;
  1. The period of compounding i.e., whether the compounding is yearly, half yearly, quarterly or monthly. If the compounding is more frequent, then the amount of EMI would be higher and vice versa.
  2. The rate of interest.
  3. Period of repayment - if the repayment period is more, then EMI would be lower and vice versa.
EMI = \frac{p \times r \times (1+r)^n}{(1+r)^n - 1}

Where p = principal i.e. loan amount

r = rate of interest per month

n = no. of instalments
References


