BANKING SHIKSHA

PAPER IV – RETAIL BANKING & WEALTH MANAGEMENT

Module A: Retail Banking

Chapter 2:

Retail Banking: Role within the Bank Operations

Retail Banking is often considered the face of a bank, as it is the primary point of contact for the general public. However, its significance extends far beyond customer interaction; it is a cornerstone of a bank's overall operations and financial health. The role of retail banking can be understood through its contributions to several key areas:

1. Mobilization of Deposits:

- **Foundation of Banking:** The core function of any bank is to accept deposits from the public. Retail banking is the primary engine for this, gathering funds through a wide array of products like Savings Accounts, Current Accounts, and Term Deposits (Fixed and Recurring).
- **Low-Cost Funds (CASA):** A significant achievement for retail banking is the mobilization of funds through Current Account and Savings Account (CASA) deposits. These are low-cost funds for the bank compared to term deposits or borrowings from the market. A higher CASA ratio is a key indicator of a bank's profitability and financial strength.

- **Source for Lending:** These retail deposits form a large and stable pool of funds that the bank can then lend out to its retail and corporate clients, thereby earning interest income.

2. **Contribution to the Bank's Bottom Line (Profitability):**

- **Interest Income:** Retail banking is a major contributor to a bank's interest income through its diverse loan portfolio, which includes home loans, auto loans, personal loans, and credit card advances. The interest earned on these loans is a primary revenue stream.
- **Fee-Based Income (Non-Interest Income):** Beyond interest, retail banking generates substantial fee-based income from a variety of services. This includes:
  - Processing fees for loans.
  - Annual fees and transaction charges on credit and debit cards.
  - Commissions from the sale of third-party products like insurance (bancassurance) and mutual funds.
  - Charges for services like ATM usage, online fund transfers (NEFT, RTGS, IMPS), and cheque book issuance.
- **Profitability through Cross-Selling:** By building strong relationships with a large customer base, retail banking creates numerous opportunities for cross-selling other banking products. For example, a salaried customer with a savings account may also be a good candidate for a personal loan, a credit card, or an investment product.

3. **Risk Diversification:**

- **Spreading the Risk:** Unlike corporate or wholesale banking where a single default from a large borrower can have a significant impact on the bank's financial health, retail banking spreads the credit risk across a vast number of small-ticket loans. The principle of "the law of large numbers" applies here; while some defaults are inevitable, they are generally predictable and manageable within a large portfolio.

- **Stability in Economic Downturns:** The retail loan portfolio often demonstrates greater resilience during economic downturns compared to corporate loans, as individual defaults are less correlated than defaults in a specific industrial sector.

4. Brand and Image Building:

- **Visibility and Reach:** A strong retail presence through a network of branches, ATMs, and digital platforms makes the bank more visible and accessible to the general public. This constant interaction helps in building brand recognition and trust.
- **Customer Loyalty:** Positive experiences with retail banking services can foster long-term customer loyalty. A satisfied customer is more likely to use other services offered by the bank and recommend it to others.

5. Implementation of Monetary Policy:

- Retail banks are at the forefront of implementing the monetary policy directives of the central bank (the Reserve Bank of India). For instance, when the RBI changes the repo rate, retail banks are the primary channel through which these changes are transmitted to the public in the form of revised lending and deposit rates.

Business Models in Retail Banking

Banks adopt different business models for their retail operations based on their strategic objectives, target customer segments, and organizational capabilities. The primary business models are:

1. The Strategic Business Unit (SBU) Approach:

- **Concept:** In this model, retail banking is treated as a distinct Strategic Business Unit within the bank's overall structure. It has its own dedicated management team, resources, and profit and loss (P&L) responsibility.
- **Characteristics:**
  - **Autonomy:** The retail SBU operates with a fair degree of autonomy in terms of product development, marketing strategies, and operational decisions.
  - **Specialization:** It allows for a focused and specialized approach to the retail market.
  - **Accountability:** The head of the retail SBU is directly accountable for the performance and profitability of the unit.
- **Advantages:**
  - Clear focus on the retail segment.
  - Enhanced accountability and performance measurement.
  - Greater flexibility and speed in responding to market changes.
- **Applicability:** This model is commonly adopted by large public sector and private sector banks in India, where retail banking is a significant part of their overall business.

2. The Departmental Approach:

- **Concept:** Under this model, retail banking functions are carried out by various departments within the bank, such as the deposits department, the loans department, and the card department.
- **Characteristics:**
  - **Functional Silos:** Each department operates as a separate functional silo, with its own set of responsibilities.
  - **Lack of a Unified View:** This model often lacks a single, unified view of the retail customer. For example, the loans department may not have easy access to the customer's deposit history.
- **Disadvantages:**
  - Can lead to a fragmented customer experience.
  - Slower decision-making due to the need for inter-departmental coordination.
  - Missed opportunities for cross-selling.
- **Applicability:** This was a more common approach in the past. While some elements may still exist, most modern banks have moved towards a more integrated model to provide a seamless customer experience.

3. The Integrated Approach:

- **Concept:** This model is a hybrid approach that seeks to combine the advantages of the SBU and departmental models. While retail banking may be a distinct SBU, it works in close integration with other verticals of the bank, such as corporate banking, treasury, and wealth management.
- **Characteristics:**

- **Shared Resources:** Certain resources, such as technology infrastructure and risk management functions, may be shared across different business units to achieve economies of scale.
- **Holistic Customer View:** The focus is on creating a single, 360-degree view of the customer across all the bank's products and services.

- **Advantages:**
  - Provides a seamless and unified experience for the customer.
  - Maximizes opportunities for cross-selling and up-selling.
  - Improves operational efficiency by sharing resources.
- **Applicability:** This is the most prevalent and effective model for modern retail banking, as it aligns the bank's structure with the goal of being customer-centric.

4. The Target Market Approach:

- **Concept:** Some banks or financial institutions may choose to focus on specific niche segments within the broader retail market.
- **Characteristics:**
  - **Niche Focus:** The bank develops specialized products and services tailored to the unique needs of its target segment. For example, a bank might focus exclusively on high-net-worth individuals (HNIs), non-resident Indians (NRIs), or specific professional groups like doctors or defense personnel.
- **Advantages:**
  - Allows the bank to build deep expertise and a strong reputation within its chosen niche.
  - Can lead to higher customer loyalty and profitability within the target segment.

- **Applicability:** This model is often adopted by smaller, specialized banks or by wealth management divisions within larger banks.

Summary

I. Role of Retail Banking in Bank Operations

1. Mobilization of Deposits

- Core function: Accepting public deposits via Savings, Current, Fixed, and Recurring Deposit accounts.
- **CASA Deposits** (Current Account, Savings Account): Provide low-cost, stable funds; a higher CASA ratio reflects better financial health.
- Funds mobilized through retail deposits are used for lending, driving interest income.

2. Contribution to Profitability

- **Interest Income**: Generated from home, auto, personal loans, and credit cards.
- **Fee-Based Income**:
  - Loan processing fees
  - Card-related charges
  - Commissions on selling insurance and mutual funds
  - Service charges (ATM, NEFT/RTGS/IMPS, cheque books)
- **Cross-Selling**: Retail banking helps upsell additional products (e.g., loans, cards, investments) to existing customers.

3. Risk Diversification

- Risk is spread across many small-ticket loans, reducing impact from individual defaults.
- Retail portfolio is more resilient during economic downturns compared to corporate loans.

4. Brand and Image Building

- Retail banking is the bank's public face through branches, ATMs, and digital presence.
- Builds customer loyalty and trust through quality service and accessibility.

5. Implementation of Monetary Policy

- Retail banks transmit RBI's monetary policy decisions to the public via changes in lending and deposit rates.

II. Business Models in Retail Banking

1. Strategic Business Unit (SBU) Approach

- Retail banking functions as an independent business unit with its own P&L.
- Features: Autonomy, specialized focus, and accountability.
- Benefits: Faster decisions, clear focus, measurable performance.
- Common in large private and public sector banks.

2. Departmental Approach

- Functions split across departments (loans, deposits, cards).
- Issues: Fragmented customer view, slower decisions, weak cross-selling.

- Less common in modern banking; now largely phased out.

3. Integrated Approach

- Combines benefits of SBU and departmental models.
- Focus on 360-degree customer view; shared infrastructure and coordinated verticals.
- Benefits: Seamless experience, efficient operations, better cross-selling.
- Most widely used model in modern customer-centric banking.

4. Target Market Approach

- Focus on niche segments (e.g., HNIs, NRIs, doctors, defense personnel).
- Customized products and services for the selected group.
- Benefits: Higher loyalty, profitability, and brand reputation.
- Adopted by specialized banks or wealth management divisions.

Important Questions

1. **What is the primary role of retail banking in deposit mobilization?**
   A. Issuing government bonds
   B. Accepting deposits from large corporates
   C. Accepting deposits from the public through various accounts
   D. Managing foreign reserves

2. **CASA stands for:**
   A. Credit Account and Savings Account
   B. Current Account and Service Agreement

C. Current Account and Savings Account
D. Consolidated Assets and Savings Allocation

3. **Why are CASA deposits important to banks?**
   A. They are high-risk investments
   B. They represent long-term borrowings
   C. They provide high-cost funding
   D. They are low-cost funds and improve profitability

4. **Retail banking is a significant contributor to a bank's interest income primarily through:**
   A. Corporate bonds
   B. Government securities
   C. Retail loan portfolio
   D. Interbank lending

5. **Which of the following is NOT a source of fee-based income in retail banking?**
   A. NEFT and RTGS charges
   B. Loan processing fees
   C. ATM service charges
   D. Repo rate interest

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6. **Cross-selling in retail banking refers to:**
   A. Selling the bank's shares to the public
   B. Offering multiple banking products to the same customer
   C. Selling banking services to other banks
   D. Disposing of non-performing assets

7. **What is the key advantage of risk diversification in retail banking?**
   A. It increases loan ticket size
   B. It limits the number of borrowers
   C. It spreads risk across many small loans
   D. It eliminates the need for provisioning

8. **During economic downturns, retail loans are generally more stable than corporate loans because:**
   A. Retail customers receive government bailouts
   B. Defaults are uniformly spread
   C. Individual defaults are less correlated than corporate defaults
   D. Retail borrowers do not default

9. **A visible retail banking presence helps in:**
   A. Minimizing operational costs
   B. Promoting customer confusion
   C. Building brand recognition and customer trust
   D. Increasing the repo rate

10. **Retail banks implement RBI's monetary policy by:**
    A. Printing money
    B. Changing foreign exchange reserves
    C. Modifying their lending and deposit rates
    D. Adjusting export tariffs

11. **In the SBU approach, retail banking functions as:**
    A. A government-regulated entity
    B. An informal customer group
    C. A distinct profit and loss center with dedicated management
    D. A non-performing asset recovery team

12. **Which of the following is not a characteristic of the SBU model?**
    A. High degree of autonomy
    B. Fragmented customer view
    C. Dedicated management team
    D. Specialization in retail services

13. **One key disadvantage of the Departmental Approach is:**
    A. Improved speed in service delivery
    B. Seamless customer experience
    C. Fragmented customer view and missed cross-selling opportunities
    D. High levels of specialization

14. **Which retail banking model combines features of both SBU and Departmental Approaches?**
   A. Centralized Lending Model
   B. Integrated Approach
   C. Wholesale Banking Model
   D. Outsourced Retail Model

15. **What is a key feature of the Integrated Approach?**
   A. It operates only through physical branches
   B. Uses separate systems for each product
   C. Provides a 360-degree view of the customer
   D. Avoids technology to reduce costs

16. **Which of the following best describes the Target Market Approach?**
   A. Retail services for all segments
   B. Focus on large-scale industrial lending
   C. Customized banking for specific customer groups
   D. Exclusive focus on government customers

17. **An example of the Target Market Approach is:**
   A. Offering standard home loans to everyone
   B. Providing customized services to NRIs and doctors
   C. Setting uniform rates for all loans
   D. Operating without profit objectives

18. **Which model is most prevalent among modern, customer-centric banks?**
    A. Departmental
    B. SBU
    C. Integrated
    D. Centralized Treasury

19. **The Strategic Business Unit model is primarily adopted by:**
    A. NBFCs and fintechs
    B. Co-operative societies
    C. Public and private sector banks with large retail operations
    D. Regional Rural Banks only

20. **Which business model is likely to result in slower decision-making due to inter-departmental coordination?**
    A. SBU
    B. Integrated
    C. Target Market
    D. Departmental

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Answer Key

1. C
2. C
3. D
4. C
5. D
6. B
7. C
8. C
9. C
10. C
11. C
12. B
13. C
14. B
15. C
16. C
17. B
18. C
19. C
20. D

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