PRODUCTS AND GROWTH OF INDIAN RETAIL BANKING

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ABSTRACT

Retail Banking in India is imperative for the fact that it contributes for economic growth and provides faster results than many other means. The question on whether retail banking boom has paused is often in the air due to global recession and its impact on Indian economy. Continued raising NPAs in the sector coupled with decreasing net interest margins, necessitating commercial banks shift focus from lending to investment activities. On the other hand, the discussion on the size, growth and direction of retail banking is worth mentioning in the era of modern banking and policy initiatives for financial inclusion. This article describes the importance of retail banking in Indian economy, its features, growth across products and product lines, and concludes with the challenges in lending.

Key words: Indian Retail Banking, Growth in Retail Banking, Retail Banking Products Services, Analysis of Indian Retail Banking.

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RETAIL BANKING

Retail banking may be defined as the cluster of products and services that banks provide to consumers and small businesses through branches, the Internet, and other channels.[1] Retail Banking is part of commercial banking that offers a variety of services to individual customers and small businesses. A clear distinction can be made in the role of a bank with respect to retail banking as an intermediary that canalizes the funds for, and from large number of individual customers.

The term retail banking has come into formal use only after its mention in Basel committee on Banking Supervision (BCBS) in June 2004, which suggested the segment reporting as part of identifying and mitigating credit risk based on the exposure to various sectors. Following the recommendations of BCBS, RBI in April 2007, initiated reporting of retail banking activities by commercial banks. In India, prior to the developments on Basel accord, commercial banks used to report banking activities under two heads, namely, treasury and other banking business. In its Policy announcement, RBI has made that all Scheduled Commercial Banks(SCBs) were advised to divide erstwhile 'other banking segment' into three categories –corporate/wholesale banking, retail banking and other banking operations. It further provided that banks were required to adopt the following business segments for public reporting purposes from March 31, 2008:

Treasury

Corporate/Wholesale Banking

Retail Banking

Other banking business.

RETAIL BANKING PRODUCTS AND SERVICES

A logical and systematic classification of retail banking services are provided by the World Retail Bank Report 2006 that divided them into the following groups, namely, Core day-to-day Banking Services, Savings services, Credit services, Other Products and Services.[2]

A brief outline of the services is provided in the following paragraphs.

[1] Risk, Return, and Industry Structure seminar on The Role of Retail Banking in the U.S. Banking Industry: Paper Presentation by Timothy Clark, Astrid Dick, Beverly Hirtle, Kevin Stiroh, and Robard Williams

[2] World Retail Banking Report 2006 by Capgemini, EFMA and ING

Core Banking services: These include day to day needs of customers such as deposits and withdrawal, transfer of funds, means of payment and exception handling services such as stop payment on lost cheques, errors in bank statements.

Account Management Services: These include receipts and payments at the bank counter, attending the customer needs through branch, internet, ATMs, mobile and phone banking. Recording and updating the customer transaction with the bank. Pass book, general enquiries of the customers on deposits, withdrawals and balance enquiries, payment means, charges etc., ATMs, Internet Banking and phone banking have considerably reduced the work on the branches on such services with the advent of information technology in banking. Issuance of checkbooks was earlier done at the branch but now a days a customer can order for a check book through any of the other modes of banking. Balance enquiry can also be made through any of these channels and for any errors and rectifications thereof, the customers are needed to visit the branch.

Account statement is a common service very often required by most customers. Banks provide a statement in paper for a charge and the customers who uses internet, can download their account statements directly by logging in to their account. Change of address, change in PIN, complaint on Loss of ATM or Debit Cards are also permitted through non-branch banking. A customer can withdraw cash either at the branch or at ATM. Few banks attempted cash withdrawals by phone banking but it does not seem to be successful.

Means of Payment: Banks offer various means of payments in the form of transfer of funds between various accounts of a customer as well as to third parties. These include payment through checks, debit cards, Credit cards, wire transfers, standing orders and direct debit. Checks issued to third parties and self withdrawals can be made through branches. Payment to third parties by check consumes necessary time lag depending upon the distance between the branches and when the transaction involves different banks. Checks are popularly being used as promises to pay at a future date and have been used as a legal binding between the parties in settlements. Lenders often require borrowers to provide post dated checks to make sure of the payments.

Savings services: Savings services include current and fixed deposits, recurring Deposits. Interest rates on savings deposits vary with the tenure. Long term deposits fetch more interest than short term. Banks are making focused attempts to different demographical segments. For example, pensioner deposits are being promoted by banks with higher rates of interest. In order to achieve the objective of financial inclusion, banks are offering accounts to low income groups and are allowing 'no frills' accounts to pensioners and students for collecting their sanctions through banks. Many banks are operating their own mutual funds where as others are merely operating as retailing intermediary of the mutual funds to their customers on commission basis from the parent fund operators.

Credit services : Credit Services of retail banks include overdraft, cash credit, consumer credit, revolving credit (such as credit card), loans and mortgages. Overdraft is a form of informal credit where a current accountholder is allowed to withdraw more sums than the actual balance up to a certain limit. This facility is mostly common among small businesses. Interest is charged on overdrawn sums. With the induction of credit cards, the use of overdraft has considerably reduced as credit cards offer more flexibility.

TRENDS IN RETAIL BANKING

There has been a delay in identification of the segment as a contributor for economic growth despite the fact that it serves the function of demand creation where there is under employment of resources. There has been a declining trend in personal loan segment during 1969-84. The share of personal loans decreased from 4.4 percent to 3.0 percent between 1981 and 1984, and no significant change in education loans during post nationalization era (1969-1991).[3] The evolution of retail banking in India can be traced back to the entry of foreign banks. The conventional banking business by Public sector banks (PSBs% was done on a more generalized approach and there was no demarcation as retail and non-retail activities. Customer and Industry segmentation was adopted within the overall business plan of banks.[4] Retail banking operations were limited and subliminal in Indian Banking Industry prior to liberalization.

Retail Banking in India redefined the growth of banking in the era of liberalization. Foreign Banks operating in India explored and attempted individual consumer needs in the late 1970s and 1980s.[5] Standard Chartered Bank and Grindlays Bank were the pioneers of introducing focused retail loan products in India. Citi Bank is the first company to introduce credit cards in India during early 1980s. Bank of Baroda and Andhra Bank among Indian public sector banks to

[3] Bank Credit in India-Vasireddy Chandrayya-1990-Discovery Publishing House-New Delhi.
[4] Retail Banking-First Edition, IIBF ; Macmillan Publishers2010- p.no13.
[5] Retail Bankingby Dr. J.Sethuraman, Indian Instutute of Banking &Fianance,Mumbai 2010,p.13.

extend retail credit products and other public sector banks namely, State Bank of India, Indian Overseas Bank, Bank of India followed the trend in late 80s. With the advent of new generation private banks in early 1990s, immediately after liberalization, commendable expansion in retail loan segment has been acknowledged.

Privatization, deregulation, de-licensing of branch expansion, advent of information technology in banking sector, initiative of financial inclusion have brought retail banking into limelight. Rising income levels has been the prime cause for growth in retail banking. It is reported that the per capita income was $260 US in the year 1980, rose to US $ 550 in 2003 and it is expected to touch US $ 4,000 by the year 2020.[6]

Other contributing factors include Changes in the socio-economic set up such as nuclear family system propelled the growth of retail banking in India. Indian Retail Banking continues to redefine the credit growth in the country. Retail loans grew at a compounded 30.5% a year from 1999 to 2004. It grew by a whopping 44.4% in 2005-06 to touch Rs3,538 billion. Housing, which constitutes more than 52% of all retail loans, grew at a robust rate of 44.35% during 2005-06.[7]Outstanding Education loan segment is expected to grow at 36.41% until March 2009 from March 2007 onwards to cross Rs. 27000 Crore Mark. Two-wheeler finance industry is projected to forge ahead at a CAGR of 14.21% until 2009-10 from 2005-06. Bankable households in India are estimated to move up at a CAGR of 28.10%. During 2006-07, gross credit extended by Indian commercial banks grew by 34.83% to touch INR19,495 billion. Retail credit constitutes about 25% of the total credit and has grown by 28.0% amounting to INR 4,218.3 billion during 2007-2011.[8] By the end of the year 2010, Retail Banking in India is expected to evince a CAGR of 28% to touch the figure of INR 9 700 Billion.

Table III.2. Number of Bank Branches of Scheduled Commercial Banks

	Rural	Semi-urban	Urban	Metro-politan	Total
Scheduled Commercial Banks	23,776	22,468	17,878	17,118	81,240
	(29.3)	(27.7)	(22.0)	(21.1)	(100)

[6] The changing Paradigms in Indian Banking-KV Kamath-vinimaya April-June 2012. P.18

[7] Research and Markets (http://www.researchandmarkets.com/reports/c80789)

[8] Booming Indian Retail Banking Sector, RNCOS, January 1, 2008

Public Sector Banks	22,188	17,773	14,248	13,257	67,466
	(32.9)	(26.3)	(21.1)	(19.6)	(100)
Private Sector Banks	1581	4687	3569	3615	13,452
	(11.8)	(34.8)	(26.5)	(26.9)	(100)
Foreign Banks	7	8	61	246	322
	(2.2)	(2.5)	(18.9)	(76.4)	(100)

Source: RBI documents[9]

The number of branches in rural, semi-urban, urban and metropolitan centers across the country is evinced from the above table. All Scheduled commercial banks have 81,240 branches of which 23,776 (29.3 percent) are located in rural areas. 22,468 (27.7 percent) in semi-urban areas, 17,878 (22 percent) in urban areas and 17,118 (21.1 percent) in metropolitan cities. More than half of the branch distribution is located in rural and semi-urban areas reflecting the increased usage of banking services in these areas.

A drive for financial inclusion, which is the need of the hour, may raise the number of branches in semi-urban and rural areas in the forthcoming years. A further look on the branch distribution reveals that Public sector banks have 59.2 percent of branches located in semi-urban and rural areas while private sector banks have only 46.6 percent in these areas. Of the public sector banks, SBI and its associate have more coverage in semi-urban and rural areas than others.

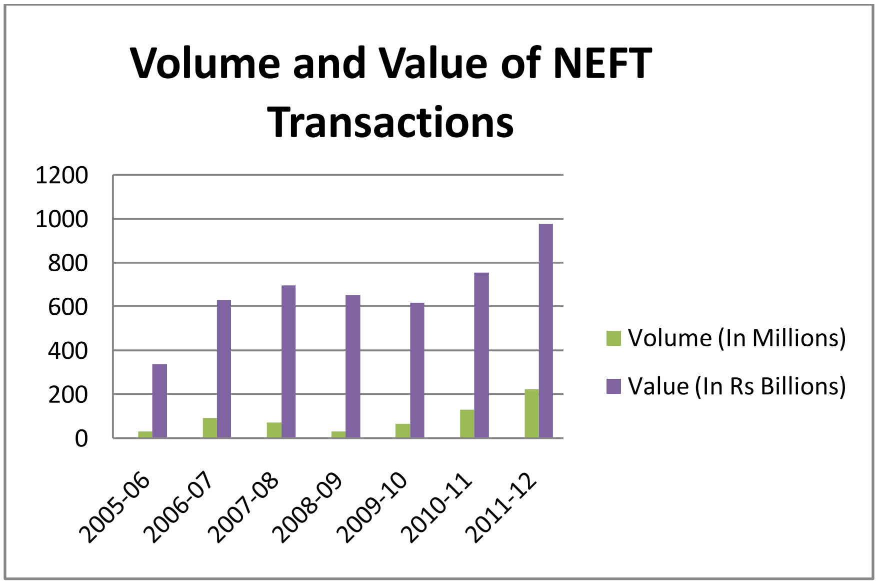
In 1969, there has been one bank office for a population of 64 thousands in the country, which has come down to 13, 400 by the end of March 2011.

Having introduced the in March 2004, Scheduled commercial banks have 95,686 ATMs across the country by the end of March 2012. Of these, 49.7 percent of ATMs are on-site (attached to a bank branch) and 50.3 percent are off-site (Not attached to a bank branch). Compared to public sector banks, private sector banks have nearly double the number of ATMs than their branches showing more interest on retail segment. Following them, the State Bank group has 137.6% of ATMs compared to their branches revealing the tendency towards retail segment.

9 Trends and Progress of Banking, Appendix Table IV.9 : Branches and ATMs of Scheduled Commercial Banks

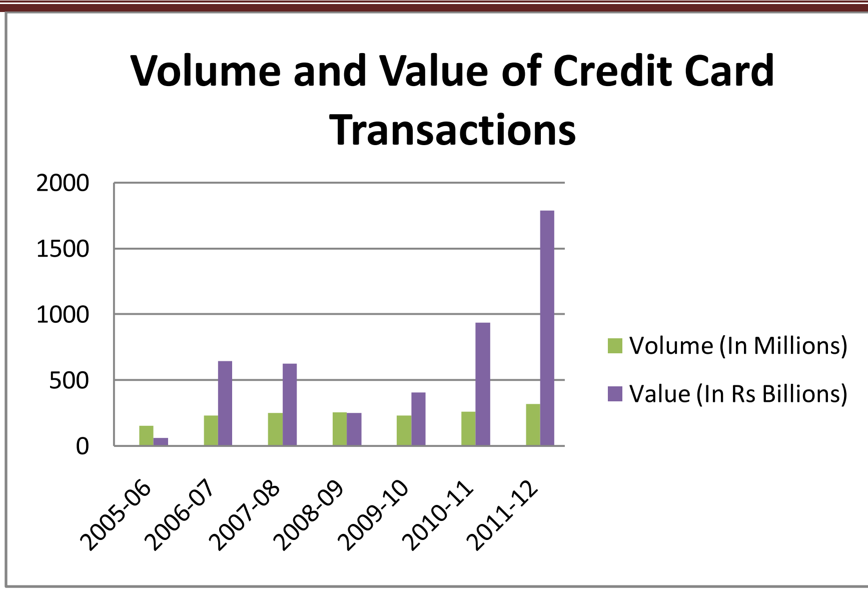
NEFT TRANSACTIONS

Volumes and Value of NEFT Transactions: RBI has introduced National Electronic Fund Transfer (NEFT) from November 2005.



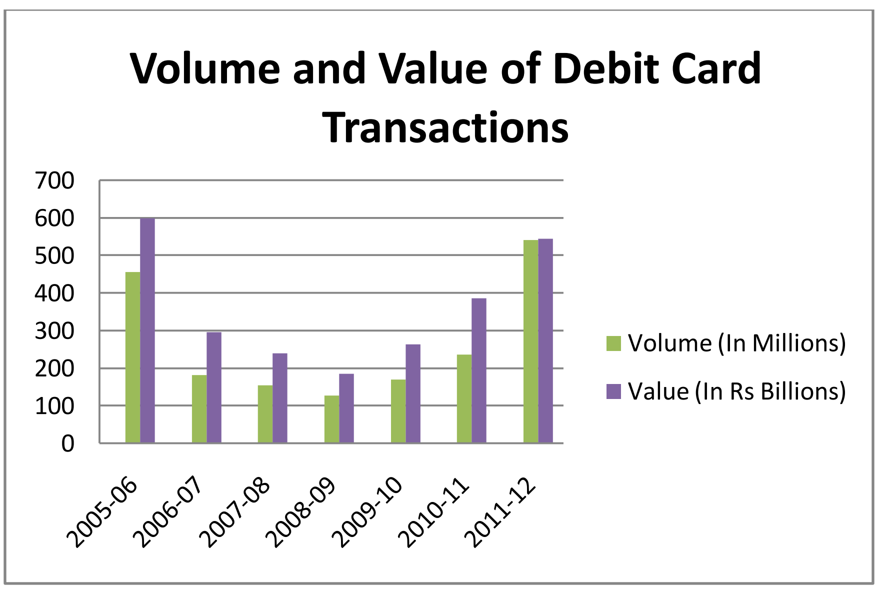
Source: RBI Documents

The NEFT transactions for the period between 2005-06 and 2011-12 have been showing a tremendous increase with an average annual growth rate of 67.4 percent by volume and recorded a compound annual growth rate of 39.5 percent. The value of the NEFT transactions during the period observed have also been drastically increased with an average annual growth rate of 195.7 percent and a compounded growth rate of 75.5 percent. The higher growth rate in volume over values signifies that more and smaller ticket transactions are taking place revealing the demand from retail payments.



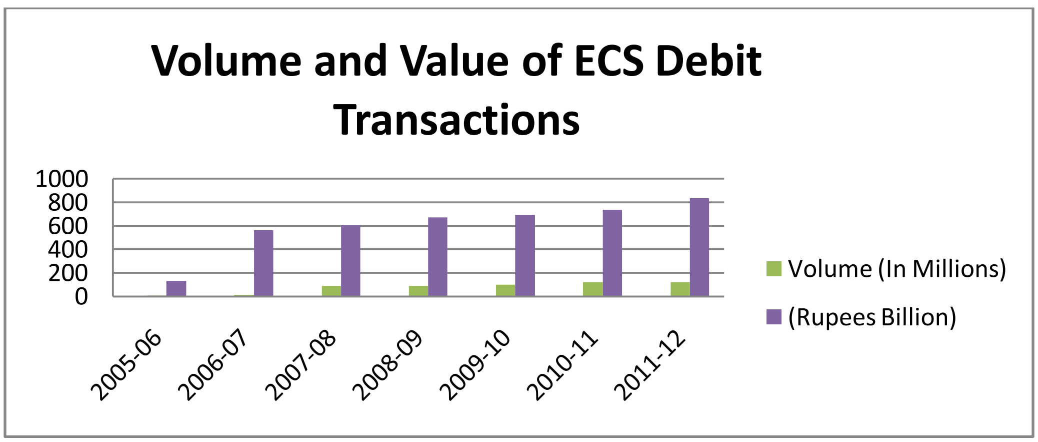
Source: RBI Documents

Credit card usage as a means of payment has also been found to be growing at an average annual rate of 14.2 percent in terms of volume and 22.8 percent in terms of value. The compound annual growth rate in volume was found at 12.9 percent during the period observed. On the other hand, the value of credit card transactions as a means of payment was found to be growing at an average rate of 22.8 percent with a compound annual growth rate of 19.3 percent. Negative growth rates were identified during 2008-09 and 2009-10 with 6.5 percent and 5.4 percent respectively.



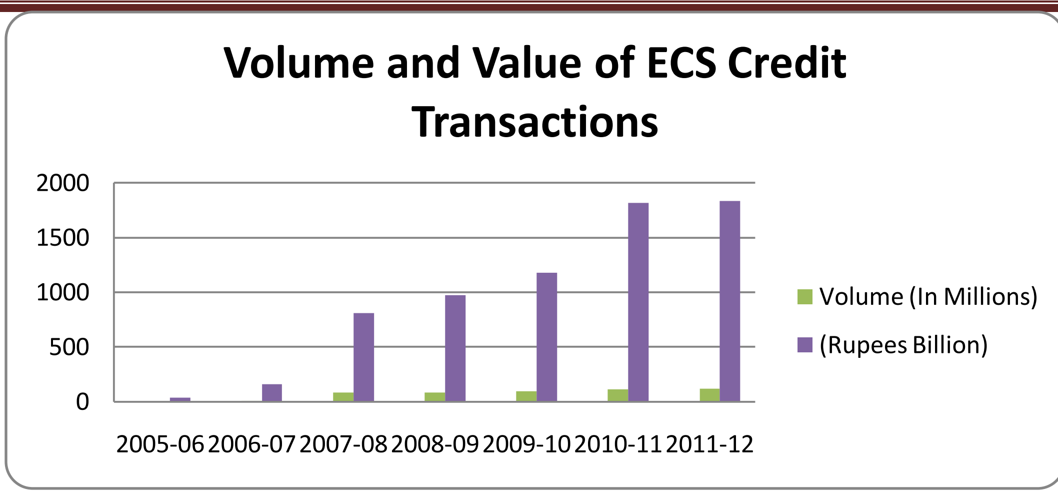
Source: RBI Documents

The volume of Debit Card transactions was found to be growing at an average annual rate of 18 percent 2.9 percent compound annual growth rate. Negative growth rate in was found in volume during 2006-2009 and the volume is rapidly growing for the past three years. On the other hand, the value of debit card transactions were growing at an average rate of 6.3 percent with recorded negative growth during 2006-09. The growth in value of transactions against the volumes reveal that the larger valued transactions were made during 2009-11 and smaller valued transactions were raised during 2011-12. One reason for this is most of the cardholders use debit card as a means of withdrawing cash from ATMs and many of them are less knowledgeable on the use as a means of payment. On the other hand, debit cards provide limited payment facility to cardholders through ATMs and large number of retail outlets are not yet covered by Electronic Funds Transfer services in semi-urban and rural areas.



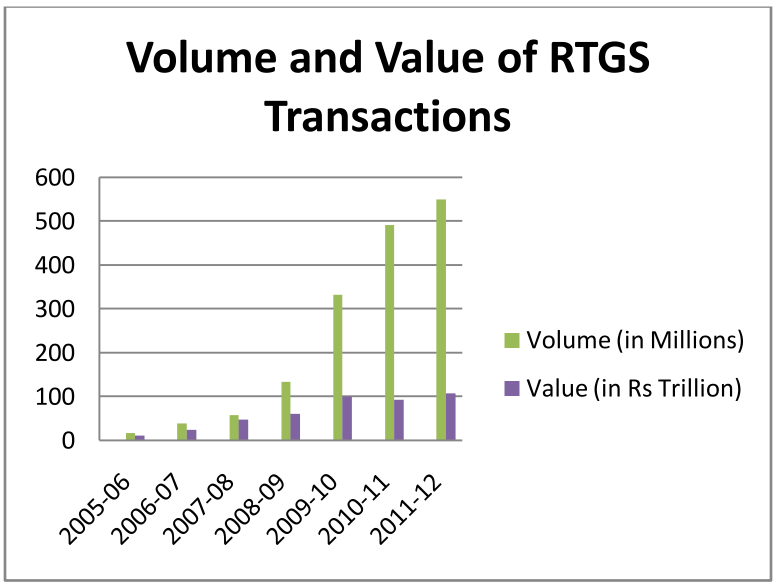
Source: RBI Documents

The ECS debit transactions were found growing at an average annual rate of 45.9 percent in terms of volume and 62.5 percent in terms of value. The growth was high during 2006-07 and there was negative growth during 2009-10 in terms of volume with 6.7 percent decline from the previous year. A higher growth in value than volumes indicate the growth in average size of the transactions.



Source: RBI Documents

ECS Transactions during the period have shown an average annual growth rate of 148.3 percent in terms of volume and 149.4 percent growth in terms of value signifying the use of the service by public and private sector organizations making salary transfers and other payments to various beneficiaries. These transactions have seen a compound annual growth rate of 75.2 percent and and 96.1percent compound annual growth rates. Highest growth rates were found during 2006-2008 and volatile growth rates in rest of the years. It is worth noting that the growth rate in these transactions have considerable fallen during 2011-12.



Source: RBI Documents

In terms of volumes, Real Time Gross Settlement transactions have shown an average growth of 84.52 percent during 2005-06 and 2011-12 and with a CAGR of 77.3 percent. Value of these transactions for the mentioned period recorded an average annual growth rate of 51.7 percent with a compound annual growth rate of 45.3 percent. These figures signify that the RTGs transactions are becoming more retail year by year. The growth in RTGS transaction were found to be slowed down during 2010-12.

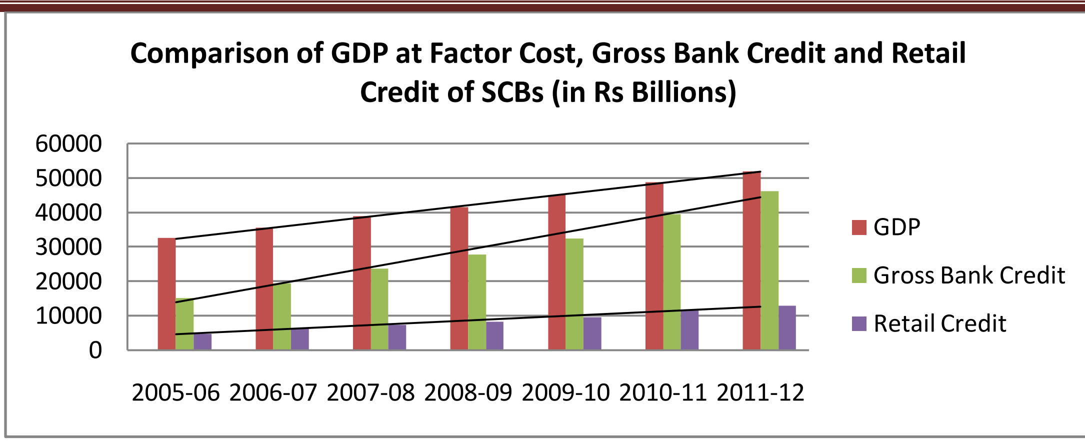
Retail Loans

Table below shows a comparison of Gross Banking Credit of scheduled commercial banks and Retail Banking Credit with the country's GDP at factor cost and at constant prices. During the period between 2005-06 and 2011-12, GDP has grown at an average rate of 8.3 percent per annum, while gross bank credit has grown by 22.9 percent and retail credit of scheduled commercial banks has grown by 22 percent. Gross bank credit stood at 46.3 percent of GDP at the end of March 2006 has recorded a double fold growth to reach 88.6 percent of GDP by the end of March 2011-12.

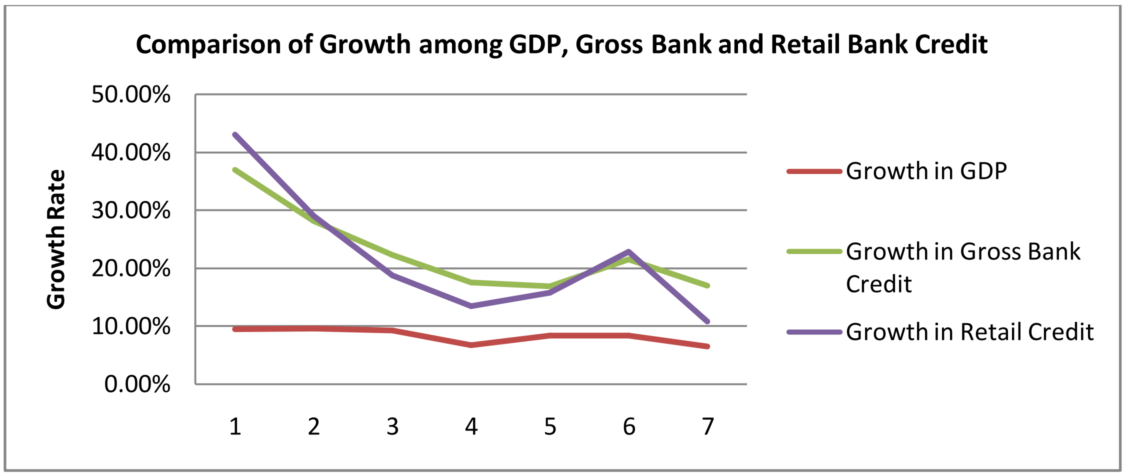
Table III.1 Comparison of Gross Banking Credit and Retail Banking Credit with GDP in Rs Billions

Year	GDP at Factor Cost	Growth	Gross Bank Credit	Percentage of GDP	Growth	Retail Credit	Percentage of GDP	Growth
2005-06	32530.73	9.5%	15070.77	46.3%	37.0%	4702.85	14.5%	43.1%
2006-07	35643.64	9.6%	19311.90	54.2%	28.1%	6068.21	17.0%	29.0%
2007-08	38966.36	9.3%	23619.13	60.6%	22.3%	7210.27	18.5%	18.8%
2008-09	41586.76	6.7%	27755.49	66.7%	17.5%	8186.07	19.7%	13.5%
2009-10	45076.37	8.4%	32447.88	72.0%	16.9%	9479.2	21.0%	15.8%
2010-11	48859.54	8.4%	39420.83	80.7%	21.5%	11638.97	23.8%	22.8%
2011-12	52025.14	6.5%	46118.52	88.6%	17.0%	12892.09	24.8%	10.8%
Average		**8.3%**			**22.9%**			**22.0%**

Source: Calculated from RBI Documents



Source: RBI documents



Retail banking credit has grown from 14.5 percent of GDP to 24.8 percent of GDP during the same period. The correlation coefficients of GDP to Gross Bank Credit and GDP to retail bank credit were found to be 99.6 percent and 99.7 percent, which almost equal the unitary correlation. These figures indicate the role of gross bank credit and retail banking credit in economic development.

Data on Retail loans in comparison with the GDP at factor cost and gross bank credit has provided the following result on analysis.

Comparative Analysis of GDP, Gross Bank Credit and Retail Credit

	Correlation with GDP	Slope with GDP
Gross Bank Credit	0.728506	0.633957
Retail bank Credit	0.750949	2.377961

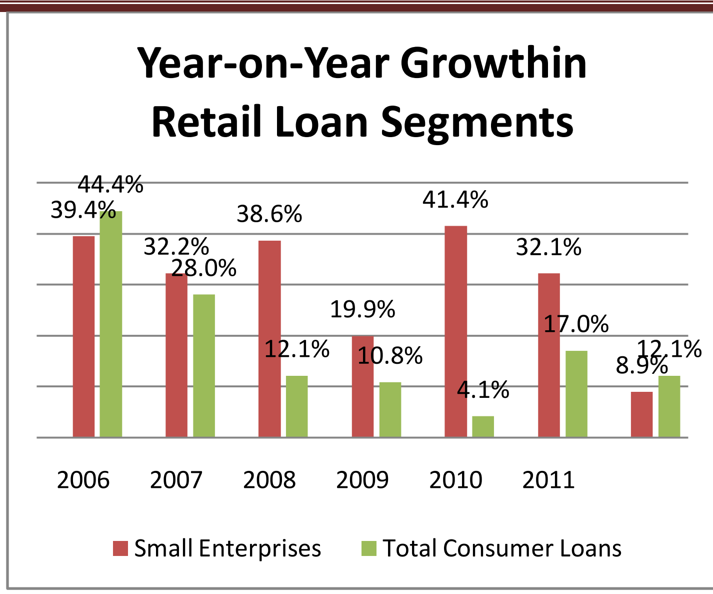
Gross Bank credit has 72.8 percent positive correlation with the GDP while retail bank credit has 75 percent. The Beta coefficient of Gross Bank credit with GDP was found to be 0.63 while retail bank has a slope of 2.38. These two measures indicate that retail banking has stronger affiliation with GDP. The relationship between bank credit and GDP can be views as both cause and effect. An increase in bank credit helps in more employment that in-turn raises the income levels. Increased income levels resulting in increased savings lead to increased bank credit. Growth in retail lending results in higher growth in GDP than credit to other sectors for the simple reason that, it creates demand for goods and services instantly.

An overview at various forms of retail loans provides the following information depicted in table below.

Table III. 7. Growth Rate in Major Retail Segments

	2005	2006	2007	2008	2009	2010	2011	2012	Average Annual Growth
Small Enterprises	-	39.4%	32.2%	38.6%	19.9%	41.4%	32.1%	8.9%	30.4%
Total Consumer Loans	-	44.4%	28.0%	12.1%	10.8%	4.1%	17.0%	12.1%	18.4%
Total	-	43.1%	29.0%	18.8%	13.5%	15.8%	22.8%	10.8%	22.0%

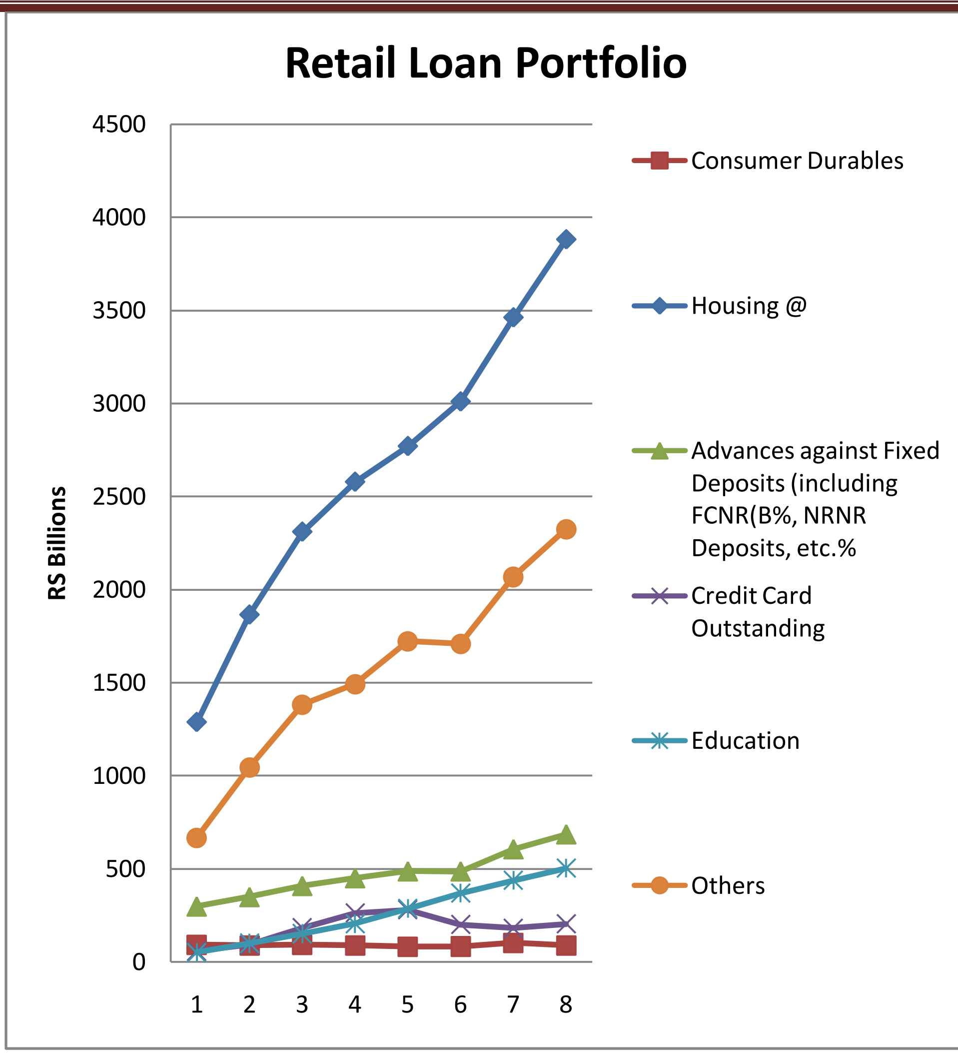
Source: RBI Annual Reports



Source: RBI Documents

Retail loans of scheduled commercial banks are classified under two heads, namely Small enterprises and consumer loans. The data on retail loans for the study period revealed that loans for small enterprises constituted an average of 32 percent of total retail loans, while consumer loans constituted 68 percent. The share of SME loans has been rising from 25.4 percent at the end of 2005-06, reached to 40.4 percent by 2011-12. Consumer lending has shown a decline from 74.6 percent at the end of March 2006 to 59.6 percent by the end of 2011-12.

The study on growth in small enterprises and consumer loan segments reveals that the growth in loans to small enterprises is higher with average annual growth rate of 30 percent while consumer segment has grown at an average rate of 18.4 percent. During the period of study, loans to small enterprises were recorded a highest growth rate of 41.1 percent during 2009-10, followed by a 39.4 percent growth during 2005-06. In the consumer lending front, the highest growth was 44.4 percent during 2005-06 and 28 percent during 2006-07. Both SME and Consumer loans have shown a decline during 2011-12. During 2009-10 , there was a remarkable difference in the growth between SME and consumer loan segments.



Examination into retail loans reveal that housing loans occupied nearly half of the retail loans with an average of 51 percent during the period of study, followed by other loans that include loans for small businesses, personal loans, and gold loans etc. with 29.94 percent. Advances against fixed deposits were found to be 8.92 percent on an average to the total retail loans. Loans for education and credit card outstanding balances at the end of consecutive years have shown that they comprised of 4.93 percent and 3.65 percent respectively during the period of study. Loans for consumer durables occupy the smallest portion of retail loans with 1.68 percent on average of total retail loans.

The share of consumer durables in retail loans were at 3.65 percent at the end of March 2005 has been gradually decreasing and reduced by more than half by the end of March 2012.

The composition of Housing loans in total retail loans was more or less consistent hovering around 50 percent. A declining trend is observed in loans against fixed deposits that were 12.18 percent at the end of March 2005, gradually decreased to 8.31 percent by the end of March 2010 and have slightly increasing from 2011 and reached to 8.91 percent by 2012. Credit card outstanding has been most volatile during the period of study. They recorded 2.35 percent of retail loans at the end of March 2005 rose to 5.2 percent by March 2008 and started declining to reach 2.64 percent by March 2011. There was a marginal increase in their share of total retail loans. Education loans have shown an increasing trend all the years of study from 2.09 percent by end of March 2005 to 6.59 percent by the end of March 2012. Other personal loans include gold loans, loans for small businesses, unspecified personal loans for individuals. They have shown a mixed trend during the period ranging from 27.15 percent (2005) to 30.59 percent (2009).

Table III.9. Analysis of Growth in Consumer Loans

	2006	2007	2008	2009	2010	2011	2012	Average	CAGR
Consumer Durables	-3.30%	4.62%	-4.24%	-6.96%	1.26%	22.56%	-13.39%	0.08%	0%
Housing @	44.82%	23.90%	11.60%	7.43%	8.66%	15.01%	12.11%	17.65%	11%
Advances against Fixed Deposits	16.91%	17.02%	10.21%	8.16%	-0.05%	24.40%	13.17%	12.83%	10%
Credit Card Outstanding	59.32%	99.40%	44.23%	6.09%	-28.04%	-10.17%	12.93%	26.25%	12%
Education	96.46%	51.22%	35.01%	39.19%	28.98%	18.58%	14.82%	40.61%	26%
Other Personal Loans	56.95%	32.37%	7.76%	15.52%	-0.77%	21.10%	12.38%	20.76%	12%

Source: RBI Annual Reports

With an exception to housing and education loans, the growth of retail loans found to have decelerated during the period of study, recording negative growth in certain loans often. Loans for Consumer durables have been negative for the years ended March 2006, 2008, 2009 and 2012, marginal increase in such loans was found in 2010 with 1.26 percent and a growth nearly equivalent to the overall retail loans was found at the end of March 2011 with a year-on-year rise of 22.56 percent. These loans have marginally grown at an average of 0.8 percent during the period of study.

Growth in housing loans has been at a decreasing rate from 2005 to 2009, and has been rising since 2010. Theses loans have recorde a highest growth at the end of March 2006 with 44.82 percent against the total outstanding at the end of March 2005 and a lowest growth was found during 2008-09. Advances against fixed deposits have decreasing growth rates upto 2010, in which year, there was a marginal negative growth rate of 0.05 percent in the loans during 209-10.

Growth in credit card outstanding has been highly volatile ranging from a negative growth rate of 10.17 percent at the end of 2011 to 99.4 percent positive growth at the end of March 2007 as against 59.32 percent at March 2006. Similar but positive trend is oserved with edcuation loans, which rose by a maximum of 96.46 percent during 2005-06 gradually declined to 14.82 percent growth rate in 2011 and a sharp rise in the loans was found at the end of March 2012.

A U curve growth rate is seen across other personal loans that inculde un specified and small business individual loans. This segment grew by 56.95 percent by the end of March 2006 gradually decreased to 15.52 percent by the end of March 2009, registered a marginal negetive growth rate at the end of March, 2010. These loans were 21.1 and 12.38 percent at the end of years March 2011 and 2012 respectively.

Edcuation loans registered a highest compounded annual growth rate (CAGR% of 26 percent during the period, followed by credit card outstanding and other personal laons with 12 percent each, hoasung loans by 11 percent and advaces against fixed deposits with 10 percent. There was no growth in consumer durables during the period of observaion

RBI considers loans to individuals as personal loans including loans for consumer durables, credit card dues, housing, education and auto loans. Loans to small business provided for setting up of small businesses are shown in separate heading and loans for working capital are included in the other personal loans. Two of these- housing and education form part of priority sector lending and personal loans were treated under separate heading until 2004-05.

The above data provides evidence that commercial banks have focused more on housing and personal loans. Of these two segments, housing loans are based on mortgage of the primary asset, thus largely secured as long as the real estate is a booming sector. Personal loans may take secured chunk as some of them are on the personal guarantee of the third party for the borrower. Rest of the personal loans are not collateralized and form part of unsecured loans of commercial banks. Credit card receivables are un-collateralized and are risky loans made on the premises of credit worthiness and financial integrity of the borrowers. Auto loans are made on hypothecation of automobile vehicles on which loan has been made. Despite the costs in recovery on default of the borrowers, such loans are largely secured.

Another important point to note that the growth of housing and retail loan in private sector banks were more during March 2009-10 and 2010-11 than public sector banks(PSBs% and foreign banks. Lower growth rates in retail lending for PSBs and foreign banks can be assigned to conservative approach on retail lending on delinquency cost experience of the banks in the recent past due to global economic slowdown and loss of consumer confidence in the country. As on March 2012, 31 percent of retail loans were unsecured and registered an increase of 24.9 percent during the year.[10]

Leading private sector banks ICICI, HDFC and HSBC are gearing to increase their retail loan portfolios to 50 percent in the forthcoming two years, while State Bank of India is planning to raise its retail loan portfolio to 30 percent.[11] Axis bank has also announced that they wish to increase the share of retail loans in their total advances to 25 percent in the forth-coming two years.[12]One compelling reason for expansion in retail loan segment is that the risk of commercial banks will be spread across different loan products and large number of individuals. The individual exposure of commercial banks is at minimum, as the ticket size of each loan is small. As a strategic measure, commercial banks focus on different retail segments to specialize, obtain economies of scale, and leverage on experience curve for improving their efficiency in operations. On the other hand, Barclays Bank has recently announced that it would like to exit

[10] Financial Stability Report(2011) –RBI documents, June 2011, p.34.
[11] www.Economic Times.com- August 1, 2011.
[12] Financial Express- May 19, 2010.

from the retail loan segment and would like to focus on wealth management services. Such a move from Barclays as it claims that retail loan portfolio had negatively affected the bank's profitability in recent years.

One understanding from the contradictory moves of commercial banks is that the banks with wide spread branch network are being benefited more with retail loans than others. The ambitions of commercial may be constrained with increase in inflation, higher interest rates, and to a little extent, the regulatory norms such as priority sector lending.

Retail loans by commercial banks have so far only reached the urban salaried households and a recent initiative by few banks expanded the market to tier II cities across the country, breaking the barriers of customer information. A further expansion of the securities to rest of the countries including small towns will fuel the economic growth in various fronts as discussed earlier. Commercial banks are now able to leverage robust growth in information technology for expansion of the sector.

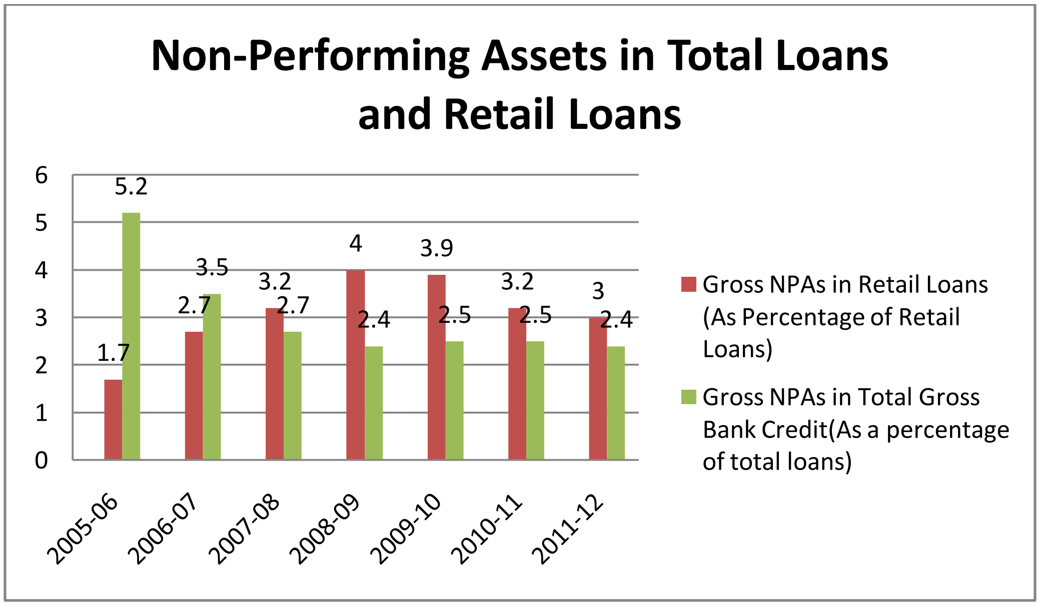
Due to global recession, growth in retail credit is hampered from the financial year 2008-09. Retail credit of all scheduled commercial banks decelerated during 2007-08 to 17.1 per cent from 29.9 per cent in 2006-07 and 40.9 per cent in 2005-06. It also remained lower than the growth in overall credit by the banking sector (23.2 per cent%. As a result, the share of retail credit in total loans and advances declined to 24.5 per cent at end-March 2008 from 25.8 per cent at end-March 2007. Deceleration in the retail portfolio of banks was on account of decline in credit for consumer durables and deceleration in the growth of auto loans, housing loans and other personal loans The outstanding amount under credit card receivables, however, increased by almost 50 per cent during 2007-08 reflecting the increase in the usage of credit cards for various payments.[13]

A recent estimate on retail loans, NPAs are expected at 3 to 4% of total retail loans by the end of the year 2009. According to CRISIL, a leading credit Rating Agency, Indian total loan portfolio is around 5 Lakh crores and that of retail loan portfolio is around 1 Lakh crores. It means Indian banks' retail NPAs are likely to be around 3 to 4 thousand crores by the end of 2009.[14] CRISIL

[13] Trends and Progress in Banking 2008, RBI documents
[14] NPAs Retail Loan portfolio to touch 4% in '09;crisil; The Financial Express 01 August 2008.

also adds that level of NPAs among housing loans, which comprise of nearly 50% total retail loan portfolio, is least because of appreciating land values.

On the other side, gross NPAs have been drastically brought down from 15.7 percent in 1997 to 2.25 percent in March 2011, however the phenomenal growth in retail lending has been contributing the level of NPAs on par with agricultural loans.



The Data on Gross NPAs in retail loans revealed that they were 1.7 percent of total retail loans during at the end of March 2006, have consistently grown to 4 percent by the end of March 2009 and started declining to reach 3 percent by the end of March 2012. Except for the end of March 2006, Retail NPAs have dominated the NPAs of overall credit of commercial banks.

The volume of NPAs in housing loans declined during the year but that of personal loans were marginally increased. Even though the impact of Global economic crisis could not cause much harm to the economy due to strong economic fundamentals, it has necessarily strained the servicing of loans by urban salaried class. Insufficient mechanism to access credit information of the borrower and information asymmetry has been of serious concern for regulator [15]. Hesitation of member banks to share customer information on strategic front is one of the main hurdles for commercial banks. Many banks use their individual approaches in assessing the credit worthiness of the borrowers.

[15] Valedictory remarks by Shri Anand Sinha, Deputy Governor, Reserve Bank of India at the Bancon-2011 at Chennai on November 6, 2011

The banking supervisory has suggested certain norms for curtailing the level of NPAs. One of such measures include changes in risk weights of various retail loans from time to time. For instance the risk weight for housing loan has been increased from 75 percent to a range of 50-125 based on the location and type of borrower. On the other hand, she raised the provision of teaser rates from 0.40 to 2 percent on housing loans. Another important measure suggested by the regulator is to increase Loan to value ratio on housing loans be raised to 80 percent from the previous level of 85percent. In other words, the margin requirement for barrower has been increased by 5 percent.

Securitization offers great space for lending for commercial banks in general and retail lending in particular[16]. Loans made to individuals for various retail purposes are bundled and converted into securities that can be exchanges in capital markets. Some of these take the form of Asset Backed Securities (ABS) and others take the form of Mortgage Backed Securities (MBS). The main objective of introduction of ABS and MBS is to convert illiquid banking assets into liquidity. The very purpose of these securities is to float the illiquid assets into capital markets to minimize the risk of credit. However, the risks of default as per the present features of ABS and MBS issued by Indian banks lie with the originator (bank). These securities have specific tenures. Subprime mortgages increase the risk of both the parties. The success of these securities depends on the asset quality of the loans. However, the method offers wide array of opportunities for commercial banks, the application and implementation of the concept suffers various flaws. In his recent address Mr. Anand Sinha, the Deputy Governor of RBI brought out the potential problems in the process. Some of these include misconception of the purpose of securities as disowning the risks rather than managing the risks, complexity attached to involvement of more intermediaries in the process, rush from the bankers to use them for long term loans rather than short term ones and incorrect estimation of risks and the default correlations of underlying assets. As a measure to curtail such mal-practices, RBI has issued new

[16] Mr. Anand Sinha, Deputy Governor, Reserve Bank of India "*Seeing both the Forest and the Trees- Supervising Systemic Risk*" co-hosted by The Board of Governors of the Federal Reserve System, The International Monetary Fund, and The World Bank at Washington, D.C, June 1-3, 2011

guidelines to include a portion of the securities adopted by the originating bank and retention of the loans for a minimum period by them.

Asset Backed Securities are more popular than mortgage backed securities as they are shorter tenured and the loans are spread across large number of individuals. The market for these securities has not well developed and deterioration of asset quality in recent times have resulted in slower growth than the rate of growth in retail lending. Over and above these, credit default swaps are in place for commercial banks to effectively operate the retail loans at a charge that ensures liquidity for commercial banks.

An examination of securitization volumes and their composition in India reveals that Asset Backed Securities (ABS) are most popular that comprise of unsecured advances of commercial banks. These comprise of personal loans, credit card receivables and auto loans. Their share in total securitization was 71.5 percent during 2005-06, gradually decreased to 24.9 percent by the end of March 2009 and has been rising since 2009-10 to reach 71.2 percent by the end of March 2012. Mortgage Backed Securities (MBS) are secured loans issued by banks on the mortgage of property or real assets such as housing loans and loans against the security of deposits, gold, etc.

MBSs comprised of 20.1 percent of total securitization at the end of March 2006 declined to 0.9 percent by the end of March 2008, has been increasing to reach 21 percent by the end of March 2012.

CDOs or LSOs or SLSDs were volatile in volumes ranging from 6.1 percent to 66.9 percent of total securitization. They gradually rose upto 2008-09 to reach 66.9 percent from 8.4 percent at the end of March 2006. They have shown a declining trend since 2009-10 from 34.2 percent to 6.4 percent at the end of March 2012. Other forms of securitization has small presence with less than 2.5 percent over the years.

SUMMARY

Retail Banking is the set of banking services to individuals and small businesses. Such services include account management, payments, loans and cross selling. The account management services include Current and Savings Accounts offered by banks which allow a customer to deposit and withdraw sums of money into and from their accounts. Payment services of banks include money transfers through cheques, drafts, payments through electronic funds transfer such as debit and credit cards, Real Time Gross Settlement, Electronic Clearing services, Automated Teller Machines and Branch network. Except for branch networks, other channels as a means of payment have been growing at an exponential rate catering the needs of millions of customers.

Retail Banking loans include loans to individuals and small businesses. These are classified as Consumer loans for personal consumption and Small and Medium Enterprises loans (SME). The study revealed that out of the retail loans, SME loans occupied 32 percent and consumer loans occupied 68 percent. The average annual growth in retail loans was found to be 22 percent while the growth rates in SME and Consumer segments were found to be 30.4 and 18.4 percent respectively during the period.

Consumer Loans are divided into different sectors such as loans for consumer durables, Housing Loans, Education loans, automobiles and personal loans etc. the data collected on overall retail loans of Scheduled commercial banks revealed that education loans have been growing at an average annual rate of 26 percent followed by credit card outstanding and personal loans with 12 percent each. Similar but little less growth is seen in loans against fixed deposits and housing. The growth in loans for consumer durables have been declining.

Indian banks have been actively utilizing credit derivatives such as Collateral Debt Obligations, Collateral Liability Obligations, Asset Backed Securities, Mortgage Backed Securities etc to mitigate both the liquidity, interest rate and to some extent the credit risks.

India still has untapped potential for banks in retail space as the retail loans only stood at less than 25%. Despite the progress, banking services are not outreached more than 65% of population. The efforts towards financial inclusion may lead to more expansion in the segment in the near future. Banks offer the ideal platform in terms of strong financial systems being in place having a huge retail presence of 1,55,000 outlets, 75,000 ATMs, 20,000 Correspondents, 3,000 micro finance institutions, 10,000 NGOs with 10 million Self-help Group base.[17] Indian domestic savings are 9.7 percent of GDP in the year 2010-11 and banks account for 29 percent of total financial flow in the country.

[17] Dr. Sanjiv Agarwal(2007) Segment Report by banks by - the Indian Banker, May p.13.

Retail loans by commercial banks have so far only reached the urban salaried households and a recent initiative by few banks expanded the market to tier II cities across the country, breaking the barriers of customer information. A further expansion of the securities to rest of the countries including small towns will fuel the economic growth in various fronts as discussed earlier. Commercial banks are now able to leverage robust growth in information technology for expansion of the sector.

Major challenges in retail banking include:

a. Collecting and updating information on credit worthy potential borrowers
b. Understanding the needs of customer
c. Updating the knowledge on products and services that are in demand among the segments
d. Designing and developing various credit products matching with the income patterns of specific segments
e. Efficient and effective management of assets and liabilities
f. Trade off between risk and return
g. Compliance to the regulatory norms in lending

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