



# CAIIB

## RETAIL BANKING

# Module-A





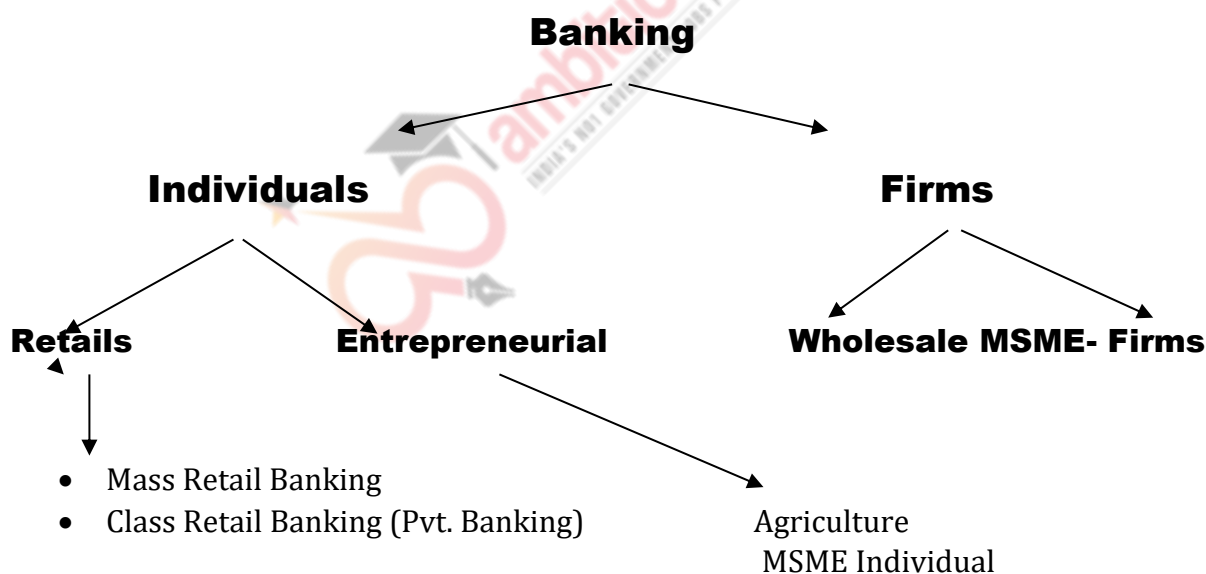
# CAIIB – Retail Banking

## Module A- Retail Banking

### Index

No. of Unit	Topics Name
Unit 1	<b>Retail Banking Introduction</b>
Unit 2	<b>Retail Banking: Role within the Bank Operations</b>
Unit 3	<b>Application of Retail Banking Concept and Distinction between Retail and Corporate/Wholesale Banking</b>

### Unit 1: Retail Banking Introduction



### Retail Banking

- "Retail Banking is a banking service that is geared primarily toward individual consumers. Retail banking is usually made available by commercial banks, as well as smaller community banks. Unlike wholesale banking, retail banking focuses strictly on consumer markets. Retail banking entities provide a



wide range of personal banking services, including offering savings and checking accounts, bill paying services, as well as debit and credit cards.

- Through retail banking, consumers may also obtain mortgages and personal loans. Although retail banking is, for the most part, mass-market driven, many retail banking products may also extend to small and medium sized businesses. Today much of retail banking is streamlined electronically via Automated Teller Machines (ATMs), or through virtual retail banking known as online banking."

## Characteristics of Retail Banking

The definitions of retail banking as discussed above bring out the following characteristics:

- Banking facilities targeted at individual customers.
- Focused towards mass market segment covering a large population of individuals.
- Offer different liability, asset and a plethora of service products to the individual customers.
- The delivery model of retail banking is both physical and virtual i.e. services are extended through branches and also through technology driven electronic off site delivery channels like ATMs, Internet Banking and Mobile Banking.
- Extended to small and medium size businesses.

## Advantages of Retail Banking

- Client base will be large and therefore risk is spread across the customer base.
- Customer Loyalty will be strong and customers tend not to change from one bank to another very often.
- Attractive interest spreads since spreads are wide, since customers are too fragmented to bargain effectively; Credit risk tends to be well diversified, as loan amounts are relatively small.
- There is less volatility in demand and credit cycle than from large corporates.
- Large numbers of clients can facilitate marketing, mass selling and the ability to categorize/select clients using scoring systems/data mining.

## Constraints in Retail Banking

Though retail banking as a segment has a number of embedded advantages, the segment suffers from constraints also. **A few of the constraints are listed below:**

- Problems in managing large numbers of clients, especially if IT systems are not sufficiently robust.
- Rapid evolution of products can lead to IT complications
- The costs of maintaining branch networks and handling large numbers of low-value transactions tend to be relatively high. (For this reason banks are encouraging clients to use cheaper distribution channels, such as ATMs, the telephone or internet for these transactions and reserve the branches for higher added value transactions).



- Higher delinquencies especially in unsecured retail loans and credit card receivables.

### **Prerequisite for Success of Retail Banking**

*There are various factors that can subscribe to the success of retail banking in India:*

- Presence of an efficient delivery mechanism
- Product appropriateness
- Pricing
- Scoring models for assessing the credit worthiness
- Consumer protection environment

### **Challenges for Retail Banking**

- Consumer Protection & Pricing
- Inadequacy of MIS
- Understanding of KYC/AML issues
- Managing Risk
- Effects of disruptive new technologies
- Continuing growth

### **Reason for the Growth of the Retail Banking Segment**

- Rise of the young Indian Professionals
- Growth as an Economic Superpower
- Increasing purchasing power of middle class people
- Financial market reforms
- Engine of economic growth
- Mass Market banking
- Volume driven business
- Automation of banking process
- Easy and affordable access
- Financial liquidity
- Economic prosperity
- Changing consumer demographics
- Technology innovations
- Increase the Bank Liquid cash
- Decline in interest rates
- Declining cost of incremental deposit
- Changes of terms of loans

## **Unit 2: Retail Banking: Role within the Bank Operations**



The business models for retail banking show interesting revelations across types of banks. The models adopted by banks vary among the public sector, private sector and foreign banks. **The main approaches are as follows:**

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

### Business Model

- Banks generally structure their retail banking models mainly on a positioning platform and to be the best/top three among the peer group players or across players. Strategies are based on the positioning objectives and vary from bank to bank depending on the importance attached to the business model.
- Among the public sector banks, some banks aim for a place among the top three retail players across banks including peer group banks while some other public sector aim for a space in the top three among the peer group. But the strategy adopted by these banks was a part of the overall strategy based on the business mix, projections and corporate objectives of the bank.

## Unit 3: Application of Retail Banking Concept and Distinction between Retail and Corporate/Wholesale Banking

### Business Process Structure in Retail Banking

- **Horizontally organized model** is a modular structure using different process models for different products offering end to end solutions product wise.
- **Vertically organized model** provides functionality across products with customer data base orientation and centralised customer data base is used across products.
- **Predominantly horizontally organized model** is mostly product oriented with common customer information for some products.
- **In predominantly vertically organized model**, common information is available for most of the products.

### Business Approach (Domain Specific) in Retail Banking

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

- **Segmented Approach** - where branches are classified based on the business potential with regard to retail space and business targeted in these segments of branches only with focused marketing strategies. These branches will be positioned as resource centre branches and will form part of the overall



segmentation game plan of the bank. Branches are classified as Resource Centres, Profit Centres, Priority Centres and General Centres to have a clear business focus. This concept is an effective business model for PSBs with large network and useful for focused strategies and already getting implemented in some public sector banks.

- **Geography based approach** - where retail models are built based on geographies.
- **Classification based approach** - where strategies are designed based on the type of branch viz., Rural. Semi Urban. Urban and Metro. This strategy helps in better product structuring for specific types of branches.

## Product Models in Retail Banking

### Liability Products

Liability products are offered to retail banking customers basically under three spaces - **Savings Accounts, Current Accounts and Term Deposit Accounts**. Product differentiation among these accounts is best achieved by adding different value propositions.

- Retail deposit are stable and constitute core deposits.
- They are interest insensitive and less bargaining for additional interest.
- They constitute low cost funds for the banks.
- Effective customer relationship management with the retail customers build a strong customer base.

### Retail Asset Products

**Retail asset financing is a major component of retail banking model of banks.** In fact retail loans are the backbone of the revenue streams of banks. In any customer expansion strategy, retail loan is packed as the main attraction uniformly by all banks.

- Retail banking results in better yield/improved bottom line for a bank.
- Retail segment is good revenue for funds deployment.
- Consumer loans are presumed to be of lower risk and NPA perception.
- Helps economic revival of nation through increased production activity.
- Improves lifestyles and fulfils aspirations of the people through affordable credit.
- Retail banking involves minimum marketing efforts in a demand-driven economy.

### Other Products/Services

- **Other products and services broadly cover the beyond product facilities tagged to the products and services.** These enhance the service experiences of the customers by providing process and delivery efficiencies by additional service tools to the basic products.
- One set of these products are Credit Cards, Debit Cards. ATM Cards, Telephone Banking. Mobile Banking, Internet Banking. Depository Service and Broking Services. Distribution of third party products like life and non life policies,



mutual funds, retail sale of gold coins, bill payment services, multi city cheques, payment gateway for rail, air ticket.

### Process Models for Products and Services

- **Processing of products and services in retail banking is basically approached from three dimensions** viz., the entire processing is done through in house resources, some products processed in house and for some products outsourcing is done for process and the third approach is outsourcing of entire process subject to prescribing process standards.
- In PSBs and old private banks the entire process for products and services are done through in house resources but in some banks, process part of some products are outsourced. But generally no outsourcing is done for the process part. In new generation private sector banks, outsourcing is attempted partially for some process areas. In foreign banks, the entire process is outsourced and normally happens through a dedicated back office covering the entire gamut of retail banking services.

### Pricing of Products and Services

- **Banks develop models for pricing of products and services based on certain fundamental parameters.** Market dynamics, risk perception, return expectations, tenor/duration, resources position, asset liability management positions and customer profile are some of the variables which are factored into the pricing model by banks. The balancing of these various variables dynamically with changing market dynamics is the key function for good pricing model.
- In addition, regulatory advices (both overt and covert) also influence the pricing models. The fundamental concept of costing in pricing has now gelled with the asset liability management practices of banks.

### Technology Models in Retail Banking

- **The technology platform for retail banking plays a major role in the retail banking initiatives of banks.** In today's scenario, technology is the backbone of the process and delivery efficiencies of banks. The technology models basically adopted by banks are In House Models, Outsourced Models, Partially In House and Partially Outsourced Models.
- Each model will have advantages and disadvantages and the overall business will be the decider of the effectiveness of the model.

### **Distinction between Retail and Corporate/Wholesale Banking**

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



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







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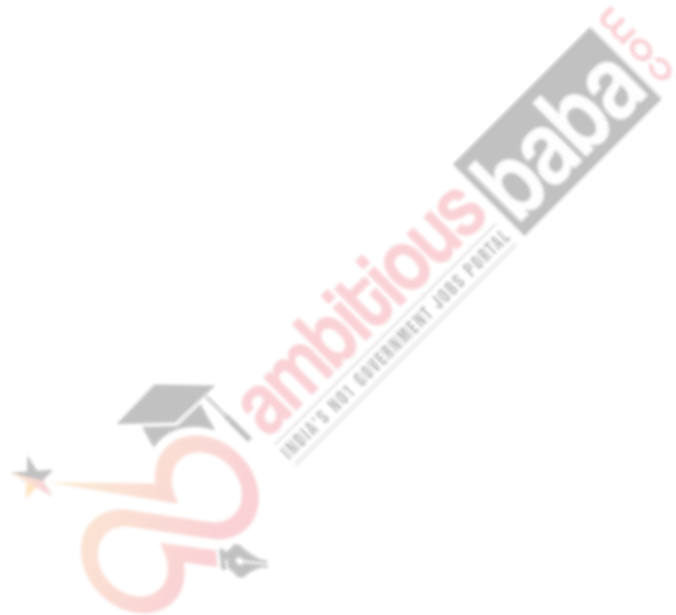
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