FINANCIAL MARKETS

PGDF-103

BLOCK 1:

INTRODUCTION TO FINANCIAL MARKETS, MONEY MARKET AND CAPITAL MARKET

Dr. Babasaheb Ambedkar Open University
Ahmedabad

FINANCIAL MARKETS

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ROLE OF SELF INSTRUCTIONAL MATERIAL IN DISTANCE LEARNING

The need to plan effective instruction is imperative for a successful distance teaching repertoire. This is due to the fact that the instructional designer, the tutor, the author (s) and the student are often separated by distance and may never meet in person. This is an increasingly common scenario in distance education instruction. As much as possible, teaching by distance should stimulate the student's intellectual involvement and contain all the necessary learning instructional activities that are capable of guiding the student through the course objectives. Therefore, the course / self-instructional material are completely equipped with everything that the syllabus prescribes.

To ensure effective instruction, a number of instructional design ideas are used and these help students to acquire knowledge, intellectual skills, motor skills and necessary attitudinal changes. In this respect, students' assessment and course evaluation are incorporated in the text.

The nature of instructional activities used in distance education self-instructional materials depends on the domain of learning that they reinforce in the text, that is, the cognitive, psychomotor and affective. These are further interpreted in the acquisition of knowledge, intellectual skills and motor skills. Students may be encouraged to gain, apply and communicate (orally or in writing) the knowledge acquired. Intellectual-skills objectives may be met by designing instructions that make use of students' prior knowledge and experiences in the discourse as the foundation on which newly acquired knowledge is built.

The provision of exercises in the form of assignments, projects and tutorial feedback is necessary. Instructional activities that teach motor skills need to be graphically demonstrated and the correct practices provided during tutorials. Instructional activities for inculcating change in attitude and behavior should create interest and demonstrate need and benefits gained by adopting the required change. Information on the adoption and procedures for practice of new attitudes may then be introduced.

Teaching and learning at a distance eliminates interactive communication cues, such as pauses, intonation and gestures, associated with the face-to-face method of teaching. This is particularly so with the exclusive use of print media. Instructional activities built into the instructional repertoire provide this missing interaction between the student and the teacher. Therefore, the use of instructional activities to affect better distance teaching is not optional, but mandatory.

Our team of successful writers and authors has tried to reduce this.

Divide and to bring this Self Instructional Material as the best teaching and communication tool. Instructional activities are varied in order to assess the different facets of the domains of learning.

Distance education teaching repertoire involves extensive use of self-instructional materials, be they print or otherwise. These materials are designed to achieve certain pre-determined learning outcomes, namely goals and objectives that are contained in an instructional plan. Since the teaching process is affected over a distance, there is need to ensure that students actively participate in their learning by performing specific tasks that help them to understand the relevant concepts. Therefore, a set of exercises is built into the teaching repertoire in order to link what students and tutors do in the framework of the course outline. These could be in the form of students' assignments, a research project or a science practical exercise. Examples of instructional activities in distance education are too numerous to list. Instructional activities, when used in this context, help to motivate students, guide and measure students' performance (continuous assessment)

PREFACE

We have put in lots of hard work to make this book as user-friendly as possible, but we have not sacrificed quality. Experts were involved in preparing the materials. However, concepts are explained in easy language for you. We have included many tables and examples for easy understanding.

We sincerely hope this book will help you in every way you expect.

All the best for your studies from our team!

FINANCIAL MARKETS

Contents

BLOCK 2: FINANCIAL SERVICE, CONSUMER BEHAVIOUR AND BANKING PRODUCTS

BLOCK 3: DISTRIBUTION, PRICING, RETAINING CUSTOMERS AND CONSULTANCY SERVICES

UNIT 1 DISTRIBUTION, PRICING AND PROMOTIONS STRATEGY FOR BANKING SERVICES

Introduction, Banking Services and Issues in Delivery, Channels of Distribution for Banks, Types of Branches, Electronic Methods of Distributing Financial Services, Pricing of Banking Products/Services, Pricing Objectives, Pricing Methods, Pricing Reviews and Committees, Price Setting in Practice, Promotion of Banking Products/Services, Guidelines on Advertising by Public Sector Banks, Sales Promotion, Internal Communication, Marketing Information Systems (MIS)

UNIT 2 ATTRACTING AND RETAINING CUSTOMERS IN BANKING SERVICES

Introduction, Defining Customer Value and Satisfaction, Factors Influencing Consumer Behaviour in Banking, Relationship Marketing and Attracting Customers, Customer Relationships Management, Retaining Customers Through Quality, Service and Values , Delivering Customer Value and Satisfaction, Image as a Managed Perception, Fulfilling Promises : Internal and Interactive Marketing, Customer Service and Customer Care, Bank Marketing : Future Challenges

UNIT 3 ADVISORY AND CONSULTANCY SERVICES

Introduction, Portfolio Management, Credit Rating, Takeovers and Mergers, Trustee Services, Depository Services, The Marketing Approach for Merchant Banking Services

BLOCK 4: MARKETING OF PENSION FUNDS AND GLOBALIZATION

UNIT 1 MARKETING OF PENSION FUNDS

Introduction, Emerging Dimensions Relating to Investment Services, Pension Funds: A General Overview, Why Pension Plan?, Types of Pension Plan, Pension Fund Risk, Funds Management, Pension Fund Investment: General Guidelines, Pension Funds and Capital Markets, Pension Funds: Some Related Statistics

UNIT 2 GLOBALISATION AND ITS IMPACT ON FINANCIAL SERVICES MARKETS

Introduction, Globalisation of Financial Markets and its Impact on Local Markets, Globalisation of Markets: The Main Drivers, Globalisation of Markets: The Road Ahead, Some Asian Trends, Globalisation and Consumer Orientation, The Emerging Imperatives for Financial Services

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FINANCIAL MARKETS

BLOCK 1: INTRODUCTION TO FINANCIAL MARKETS, MONEY MARKET AND CAPITAL MARKET

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Block Introduction

The study of financial market plays a significant role in the study of any management program. Considering the need and importance of this subject for the management students this subject has been introduced into this curriculum.

In this block the readers would be briefed about the financial markets, money market and capital market. The functions and responsibilities of each of this market would be explained in very detail. Not only has this role do they play in the proper running of an economy been discussed here in very detail.

After going through this block the readers would get sufficient idea about the Financial Market, Money Market and Capital Market.

Block Objective

After learning this block, you will be able to understand:

- The concept and functions of financial markets
- The nature and importance of money market
- The nature and types of capital market
- Distinguish between capital market and money market
- The nature and functions of a stock exchange
- The advantages of stock exchanges from the points of view of companies, investors and society as a whole
- The limitations of stock exchanges
- The concept of speculation and distinguish it from investment
- Outline the stock exchanges in India
- The nature of regulation of stock exchanges in India and the role of SEBI

Block Structure

UNIT 1: FINANCIAL MARKETS: AN INTRODUCTION

Unit Structure

1.0 Learning Objectives

After learning this unit, you will be able to understand:

- The concept and functions of financial markets
- The nature and importance of money market

1.1 Introduction

You are fully aware that business units have to raise short-term as well as long-term funds to meet their working and fixed capital requirements from time to time. This necessitates not only the ready availability of such funds but also a transmission mechanism with the help of which the providers of funds (investors/ lenders) can interact with the borrowers/users (business units) and transfer the funds to them as and when required. This aspect is taken care of by the financial markets which provide a place where or a system through which, the transfer of funds by investors/lenders to the business units is adequately facilitated

1.2 Meaning

We know that, money always flows from surplus sector to deficit sector. That means persons having excess of money lend it to those who need money to fulfil their requirement.

Similarly, in business sectors the surplus money flows from the investors or lenders to the businessmen for the purpose of production or sale of goods and services. So, we find two different groups, one who invest money or lend money and the others, who borrow or use the money.

Now you think, how these two groups meet and transact with each other. The financial markets act as a link between these two different groups. It facilitates this function by acting as an intermediary between the borrowers and lenders of money. So, financial market may be defined as 'a transmission mechanism between investors (or lenders) and the borrowers (or users) through which transfer of funds is facilitated'. It consists of individual investors, financial institutions and other intermediaries who are linked by a formal trading rules and communication network for trading the various financial assets and credit instruments.

Let us now see the main functions of financial market-

(a) It provides facilities for interaction between the investors and the borrowers.

(b) It provides pricing information resulting from the interaction between buyers and sellers in the market when they trade the financial assets.

(c) It provides security to dealings in financial assets.

(d) It ensures liquidity by providing a mechanism for an investor to sell the financial assets.

(e) It ensures low cost of transactions and information.

Check your progress 1

1. __________market provides facilities for interaction between the investors and the borrowers.
   a. Financial
   b. Capital
2. __________may be defined as 'a transmission mechanism between investors (or lenders) and the borrowers (or users) through which transfer of funds is facilitated'.
   a. Capital market
   b. financial market

1.3 Nature and Role of Financial System

The financial system plays the key role in the economy by stimulating economic growth, influencing economic performance of the actors, affecting economic welfare. This is achieved by financial infrastructure, in which entities with funds allocate those funds to those who have potentially more productive ways to invest those funds. A financial system makes it possible a more efficient transfer of funds. As one party of the transaction may possess superior information than the other party, it can lead to the information a symmetry problem and inefficient allocation of financial resources. By overcoming the information a symmetry problem the financial system facilitates balance between those with funds to invest and those needing funds.

According to the structural approach, the financial system of an economy consists of three main components:

1) Financial markets;
2) Financial intermediaries (institutions);
3) Financial regulators.

Each of the components plays a specific role in the economy.

According to the functional approach, financial markets facilitate the flow of funds in order to finance investments by corporations, governments and individuals. Financial institutions are the key players in the financial markets as they perform the function of intermediation and thus determine the flow of funds.

The financial regulators perform the role of monitoring and regulating the participants in the financial system.

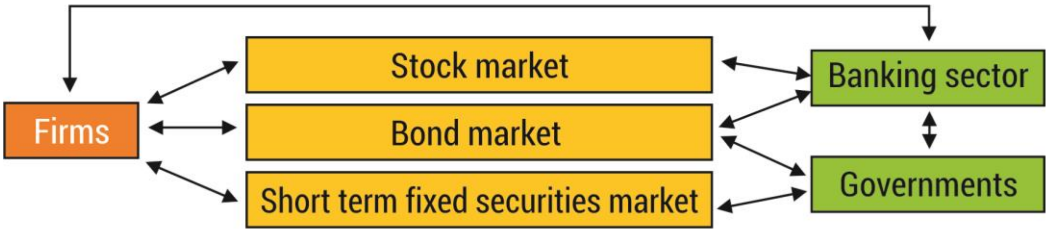

Fig 1.1 The structure of financial system

Financial markets studies, based on capital market theory, focus on the financial system, the structure of interest rates, and the pricing of financial assets. An asset is any resource that is expected to provide future benefits, and thus possesses economic value. Assets are divided into two categories: tangible assets with physical properties and intangible assets. An intangible asset represents a legal claim to some future economic benefits. The value of an intangible asset bears no relation to the form, physical or otherwise, in which the claims are recorded. Financial assets, often called financial instruments, are intangible assets, which are expected to provide future benefits in the form of a claim to future cash. Some financial instruments are called securities and generally include stocks and bonds.

Any transaction related to financial instrument includes at least two parties:

1) The party that has agreed to make future cash payments and is called the issuer;

2) The party that owns the financial instrument, and therefore the right to receive the payments made by the issuer, is called the investor.

Financial assets provide the following key economic functions.

- They allow the transfer of funds from those entities, who have surplus funds to invest to those who need funds to invest in tangible assets;
- They redistribute the unavoidable risk related to cash generation among deficit and surplus economic units.

The claims held by the final wealth holders generally differ from the liabilities issued by those entities who demand those funds. They role is performed by the specific entities operating in financial systems, called financial intermediaries. The latter ones transform the final liabilities into different financial assets preferred by the public.

Check your progress 2

1. The____________system plays the key role in the economy by stimulating economic growth.
   a. Financial
   b. Market
2. A financial system makes it possible a more efficient transfer of__________.
   a. Capital
   b. funds

1.4 Financial Markets as Components of Financial System

A financial market is a market where financial instruments are exchanged or traded. Financial markets provide the following three major economic functions:

1) Price discovery
2) Liquidity
3) Reduction of transaction costs

1) Price discovery function means that transactions between buyers and sellers of financial instruments in a financial market determine the price of the traded asset. At the same time the required return from the investment of funds is determined by the participants in a financial market. The motivation for those seeking funds (deficit units) depends on the required return that investors demand. It is these functions of financial markets that signal how the funds available from those who want to lend or invest funds will be allocated among those needing funds and raise those funds by issuing financial instruments.

2) Liquidity function provides an opportunity for investors to sell a financial instrument, since it is referred to as a measure of the ability to sell an asset at its fair market value at any time. Without liquidity, an investor would be forced to hold a financial instrument until conditions arise to sell it or the issuer is contractually obligated to pay it off. Debt instrument is liquidated when it matures, and equity instrument is until the company is either voluntarily or involuntarily liquidated. All financial markets provide some

form of liquidity. However, different financial markets are characterized by the degree of liquidity.

3) The function of reduction of transaction costs is performed, when financial market participants are charged and/or bear the costs of trading a financial instrument. In market economies the economic rationale for the existence of institutions and instruments is related to transaction costs, thus the surviving institutions and instruments are those that have the lowest transaction costs.

The key attributes determining transaction costs are

- Asset specificity,
- Uncertainty,
- Frequency of occurrence.

Asset specificity is related to the way transaction is organized and executed. It is lower when an asset can be easily put to alternative use, can be deployed for different tasks without significant costs.

Transactions are also related to uncertainty, which has (1) external sources (when events change beyond control of the contracting parties), and (2) depends on opportunistic behaviour of the contracting parties. If changes in external events are readily verifiable, then it is possible to make adaptations to original contracts, taking into account problems caused by external uncertainty. In this case there is a possibility to control transaction costs. However, when circumstances are not easily observable, opportunism creates incentives for contracting parties to review the initial contract and creates moral hazard problems. The higher the uncertainty, the more opportunistic behaviour may be observed, and the higher transaction costs may be born. Frequency of occurrence plays an important role in determining if a transaction should take place within the market or within the firm. A one-time transaction may reduce costs when it is executed in the market. Conversely, frequent transactions require detailed contracting and should take place within a firm in order to reduce the costs. When assets are specific, transactions are frequent, and there are significant uncertainties intra-firm transactions may be the least costly. And, vice versa, if assets are non-specific, transactions are infrequent, and there are no significant uncertainties least costly may be market transactions.

The mentioned attributes of transactions and the underlying incentive problems are related to behavioural assumptions about the transacting parties. The economists Coase (1932,1960, 1988), Williamson (1975, 1985), Akerlof (1971) and others) have contributed to transactions costs economics by analyzing behaviour of the human beings, assumed generally self-serving and rational in their conduct, and also behaving opportunistically.

Opportunistic behaviour was understood as involving actions with incomplete and distorted information that may intentionally mislead the other party. This type of behaviour requires efforts of ex ante screening of transaction parties, and ex post safeguards as well as mutual restraint among the parties, which leads to specific transaction costs.

Check your progress 3

1. _________function means that transactions between buyers and sellers of financial instruments in a financial market determine the price of the traded asset.
   a. Price discovery
   b. Cost discovery
2. ___________function provides an opportunity for investors to sell a financial instrument.
   a. Market
   b. Liquidity

1.5 Financial System and Economic Growth

The term financial system is a set of inter-related activities/services working together to achieve some predetermined purpose or goal. It includes different markets, the institutions, instruments, services and mechanisms which influence the generation of savings, investment capital formation and growth.

Van Horne defined the financial system as the purpose of financial markets to allocate savings efficiently in an economy to ultimate users either for investment in real assets or for consumption. Christy has opined that the objective of the financial system is to "supply funds to various sectors and activities of the economy in ways that promote the fullest possible utilization of resources without the destabilizing consequence of price level changes or unnecessary interference with individual desires."

According to Robinson, the primary function of the system is "to provide a link between savings and investment for the creation of new wealth and to permit portfolio adjustment in the composition of the existing wealth."

From the above definitions, it may be said that the primary function of the financial system is the mobilisation of savings, their distribution for industrial investment and stimulating capital formation to accelerate the process of economic growth.

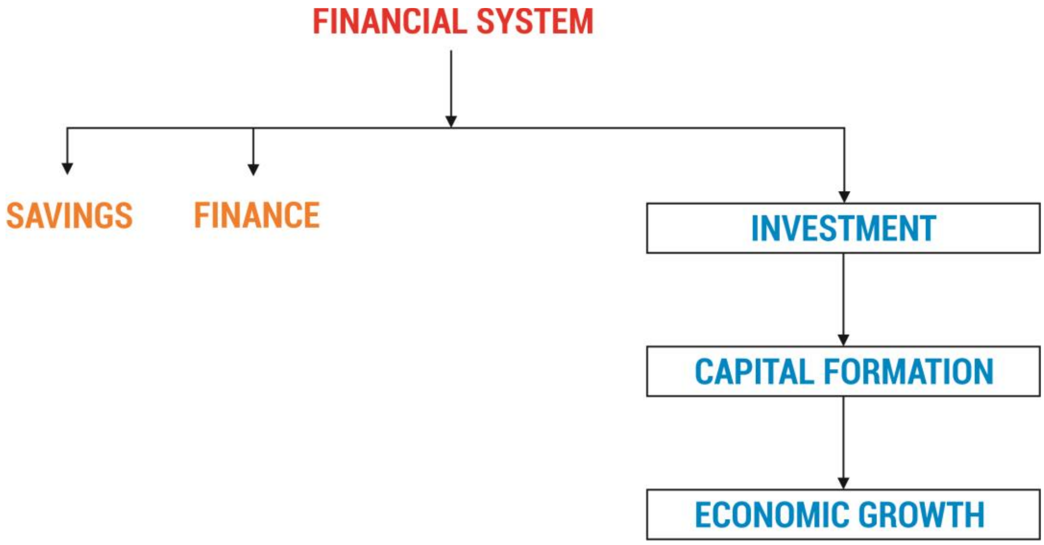

Fig 1.2 The Concept of the Financial System

The process of savings, finance and investment involves financial institutions, markets, instruments and services. Above all, supervision control and regulation are equally significant. Thus, financial management is an integral part of the financial system. On the basis of the empirical evidence, Goldsmith said that "... a case for the hypothesis that the separation of the functions of savings and investment which is made possible by the introduction of financial instruments as well as enlargement of the range of financial assets which follows from the creation of financial institutions increase the efficiency of investments and raise the ratio of capital formation to national production and financial activities and through these two channels increase the rate of growth."

The inter-relationship between varied segments of the economy is illustrated below:-

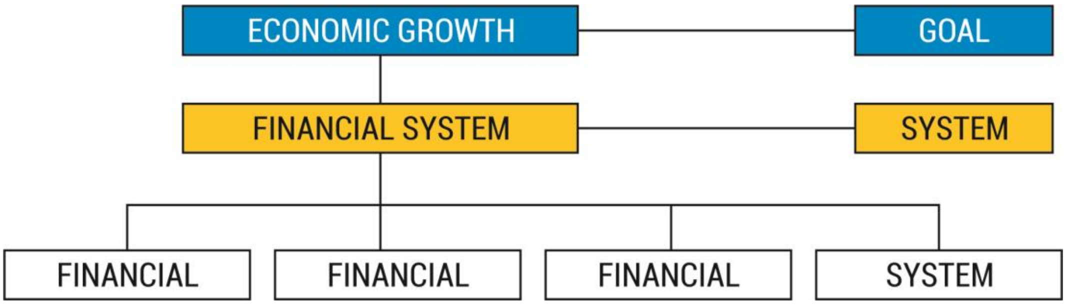

Fig 1.3 Inter-relationship in the Financial System

Check your progress 4

1. __________defined the financial system as the purpose of financial markets to allocate savings efficiently in an economy to ultimate users either for investment in real assets or for consumption.

   a. Van Horne

   b. Robinson

2. According to __________ the primary function of the system is "to provide a link between savings and investment for the creation of new wealth and to permit portfolio adjustment in the composition of the existing wealth."

   a. Van Horne

   b. Robinson

1.6 Financial System Designs

A financial system provides services that are essential in a modern economy. The use of a stable, widely accepted medium of exchange reduces the costs of transactions. It facilitates trade and, therefore, specialization in production. Financial assets with attractive yield, liquidity and risk characteristics encourage saving in financial form. By evaluating alternative investments and monitoring the activities of borrowers, financial intermediaries increase the efficiency of resource use. Access to a variety of financial instruments enables an economic agent to pool, price and exchange risks in the markets. Trade, the efficient use of resources, saving and risk taking are the cornerstones of a growing economy. In fact, the country could make this feasible with the active support of the financial system. The financial system has been identified as the most catalyzing agent for growth of the economy, making it one of the key inputs of development.

1.6.1 Bank-Based and Market Based

In countries such as Japan, France and Germany, where banks provide around 20% of the corporate financing, it is known that banks are making significant effort to develop a relationship banking culture, with long-term loans and preferential interest rates for clients with a 'good history'. These economies can be called Bank-Based Economies.

There are also countries where the borrowing-lending activities take place through organized markets, such as London Stock Exchange, in the UK, or New York Stock Exchange in USA. These are known as Market-Based Economies. Although banks are present in these countries, they are highly competitive, the relationship with lenders and borrowers is purely limited to the transactions of granting loans or taking deposits and loans are usually granted on short-term.

Check your progress 5

1. The use of a stable, widely accepted medium of exchange reduces the costs of __________.
   a. Transactions.
   b. Money
2. The financial system has been identified as the most catalyzing agent for growth of the __________.
   a. Money
   b. economy

1.7 Let Us Sum Up

This unit was of great help in making us understand the basic concepts of financial markets.

In this unit we have learnt in very detail about the meaning, nature and role of financial system. In this unit we have learnt in very detail about financial market as components of financial system. The financial system and economic growth were even discussed here in very detail. Apart from this in this unit we even covered the financial system designs. Overall the whole of the unit covered the financial market in very detail and after going through this unit the readers would have got a sufficient idea about the financial system and the various aspects connected with it.

1.8 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b)

Check your progress 2

Answers: (1-a), (2-b)

Check your progress 3

Answers: (1-a), (2-b)

Check your progress 4

Answers: (1-a), (2-b)

Check your progress 5

Answers: (1-a), (2-b)

1.9 Glossary

1. **Financial Market -** It is a market in which people trade financial securities, commodities, and other fungible items of value at low transaction costs and at prices that reflect supply and demand.

1.10 Assignment

What are the functions of a financial system?

1.11 Activities

What is the difference between 'saving' and a 'financial surplus'?

1.12 Case Study

Discuss financial system and economic growth

1.13 Further Readings

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UNIT 2: MONEY MARKET

Unit Structure

2.0 Learning Objectives

After learning this unit, you will be able to understand:

- The Characteristics and Functions of Money Market .
- Role of the Reserve Bank in the Money Market.

- Intermediates in the money market.
- Development of money market in India.
- Money Market Instruments.

2.1 Introduction

The money market is a market for short-term funds, which deals in financial assets whose period of maturity is up to one year. It should be noted that money market does not deal in cash or money as such but simply provides a market for credit instruments such as bills of exchange, promissory notes, commercial paper, treasury bills, etc. These financial instruments are close substitute of money. These instruments help the business units, other organisations and the Government to borrow the funds to meet their short-term requirement.

Money market does not imply to any specific market place. Rather it refers to the whole networks of financial institutions dealing in short-term funds, which provides an outlet to lenders and a source of supply for such funds to borrowers. Most of the money market transactions are taken place on telephone, fax or Internet. The Indian money market consists of Reserve Bank of India, Commercial banks, Co-operative banks, and other specialised financial institutions. The Reserve Bank of India is the leader of the money market in India.

Some Non-Banking Financial Companies (NBFCs) and financial institutions like LIC, GIC, UTI, etc. also operate in the Indian money market.

2.2 Meaning

The purpose of money markets is facilitate the transfer of short-term funds from agents with excess funds (corporations, financial institutions, individuals, government) to those market participants who lack funds for short-term needs.

They play central role in the country's financial system, by influencing it through the country's monetary authority.

For financial institutions and to some extent to other non-financial company's money markets allow for executing such functions as:

- Fund raising
- Cash management

- Risk management
- Speculation or position financing
- Signaling
- Providing access to information on prices.

Money markets are wholesale markets with very large amounts of transactions, e.g. with transactions from 500 million Euro to 1 billion Euro or even larger ones. This is the most active financial market in terms of volumes of trading.

From the start of emergence the traditional money markets performed the role of monetary policy. In order to influence the supply side, governments have employed methods of direct regulation and control of the savings and investment behaviour of individuals and companies. However due to fast technological advances, internationalization and liberalization of financial markets, possibilities to carry out policy objectives through such measures have diminished. Current policy through market oriented measures is aimed primarily at demand side. Thus money markets serve the interface between execution of monetary policy and the national economies.

Another role of domestic money markets is to serve public policy objectives, i.e. financing public sector deficits and managing the accumulated government deficits. Government public debt policy is an important determinant of the money markets operations, since government debt typically forms a key part of the country's money markets (as well as debt markets). The scope and measures of monetary policy are also linked to the government's budget and fiscal policies. Thus the country's money market shifts are dependent upon the goals of national public policy and tools used to reach these goals.

Changes in the role and structure of money markets were also influenced by financial deregulation, which evolved as a result of recognition that excessive controls are not compatible with efficient resource allocation, with solid and balanced growth of economies. Money markets went through passive adaptation as well as through active influence from the side of governments and monetary authorities.

Finally, money markets were influenced by such international dimensions as increasing capital mobility, changing exchange rate arrangements, diminishing monetary policy autonomy. The shifts in European domestic money markets were made by the European integration process, emergence and development of European monetary union.

Check your progress 1

1. Changes in the role and structure of money markets were also influenced by financial ___________.

   a. regulation

   b. deregulation.

2. Role of __________money markets is to serve public policy objectives.

   a. International

   b. domestic

2.3 Characteristics and Functions of Money Market

The money market is a market for financial assets that are close substitutes for money. It is a market for overnight short-term funds and instruments having a maturity period of one or less than one year. It is not a place (like the Stock market), but an activity conducted by telephone. The money market constitutes a very important segment of the Indian financial system.

Characteristics of Money Market

1. It is not a single market but a collection of markets for several instruments.
2. It is wholesale market of short term debt instruments.
3. Its principal feature is honour where the creditworthiness of the participants is important.
4. The main players are: Reserve bank of India (RBI), Discount and Finance House of India (DFHI), mutual funds, banks, corporate investor, non-banking finance companies (NBFCs), state governments, provident funds and primary dealers. Securities Trading Corporation of India (STCI), public sector undertaking (PSUs), non-resident Indians and overseas corporate bodies.
5. It is a need based market wherein the demand and supply of money shape the market.

Functions of Money Market

A well-developed money market is essential for a modern economy. Though, historically, money market has developed as a result of industrial and commercial progress, it also has important role to play in the process of industrialization and economic development of a country. Importance of a developed money market and its various functions are discussed below:

1. Financing Trade:

Money Market plays crucial role in financing both internal as well as international trade. Commercial finance is made available to the traders through bills of exchange, which are discounted by the bill market. The acceptance houses and discount markets help in financing foreign trade.

2. Financing Industry:

Money market contributes to the growth of industries in two ways:

(a) Money market helps the industries in securing short-term loans to meet their working capital requirements through the system of finance bills, commercial papers, etc.

(b) Industries generally need long-term loans, which are provided in the capital market. However, capital market depends upon the nature of and the conditions in the money market. The short-term interest rates of the money market influence the long-term interest rates of the capital market. Thus, money market indirectly helps the industries through its link with and influence on long-term capital market.

3. Profitable Investment:

Money market enables the commercial banks to use their excess reserves in profitable investment. The main objective of the commercial banks is to earn income from its reserves as well as maintain liquidity to meet the uncertain cash demand of the depositors. In the money market, the excess reserves of the commercial banks are invested in near-money assets (e.g. short-term bills of exchange) which are highly liquid and can be easily converted into cash. Thus, the commercial banks earn profits without losing liquidity.

4. Self-Sufficiency of Commercial Bank:

Developed money market helps the commercial banks to become self-sufficient. In the situation of emergency, when the commercial banks have scarcity of funds, they need not approach the central bank and borrow at a higher interest rate. On the other hand, they can meet their requirements by recalling their old short-run loans from the money market.

5. Help to Central Bank:

Though the central bank can function and influence the banking system in the absence of a money market, the existence of a developed money market smoothens the functioning and increases the efficiency of the central bank.

Money market helps the central bank in two ways:

(a) The short-run interest rates of the money market serves as an indicator of the monetary and banking conditions in the country and, in this way, guide the central bank to adopt an appropriate banking policy,

(b) The sensitive and integrated money market helps the central bank to secure quick and widespread influence on the sub-markets, and thus achieve effective implementation of its policy.

Check your progress 2

1. Industries generally need ____________term loans, which are provided in the capital market.
   a. long-
   b. Short-
2. __________market enables the commercial banks to use their excess reserves in profitable investment.
   a. Capital
   b. Money

2.4 Role of the Reserve Bank in the Money Market

The Reserve Bank of India (RBI) has always been playing the major role in regulating and controlling the India money market. The intervention of RBI is varied - curbing crisis situations by reducing the cash reserve ratio (CRR) or infusing more money in the economy.

Having talked about financial sector and the on-going reform process in the sector, let us now turn our attention to what exact role RBI is playing for the financial sector in general and the financial reform process in particular. As all of you know, RBI is the central bank of the country. Central banks are very old institutions. The Bank of England was set up way back in 1694, the Bank of France is more than 200 years old and the Federal Reserve Bank was set up in 1913. As aptly stated by our Governor, Dr. Bimal Jalan, although RBI, set up in 1935, may appear a 'toddler or at most a young adult', it is one of the oldest central banks among the developing world. Traditionally, central banks have performed roles of currency authority, banker to the Government and banks, lender of last resort, supervisor of banks and exchange control (now it would be more appropriate to call it exchange management) authority. Generally, central banks in developed economies have price or financial stability as their prime objective. The RBI has the twin objectives of maintaining price stability and promoting growth. The objectives are the following:

- Provision of adequate liquidity to meet credit growth and support investment demand in the economy while continuing a vigil on movements in the price level. In line with the above to continue the present stance on interest rates including preference for soft interest rates.
- To impart greater flexibility to the interest rate structure in the medium-term. In developing economies, however, the growth objective assumes greater importance. Recent experience has shown that during recessionary or deflationary conditions achievement of higher growth becomes the dominant objective of central banks, both in developing and developed economies.

Let us now look at the evolution of RBI and its changing role and strategy over time. RBI was set up to regulate the issue of currency and keep reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage (RBI Act, 1934). Within these overall objectives, RBI performs a wide range of promotional functions, which are designed to support the country's efforts to accelerate the pace of economic development with social justice. In keeping with the overall logic of reforms that market based allocation rather than directed allocation of resources led to greater efficiency, the functions of the RBI have undergone a strategic shift under the current reforms. The strategy shifted from controlling institutions and markets to facilitation of efficient functioning of markets and strengthening of the supporting institutional infrastructure. The pre-emptions in the form of CRR and SLR have been progressively reduced. The scope of priority sector has been expanded. The interest rate has been deregulated both on deposits and advances. Allowing DFIs and banks to lend in the short as well as the long end of the market has reduced segmentation of credit market. From conservation of foreign exchange through control of transactions, the focus has shifted to facilitation of foreign exchange transactions. Intervention in the foreign exchange market has shifted from fixing of exchange rate to merely curbing speculative volatility.

Stability issues came to the fore especially after the crises in South East Asian countries in late 1990s. The RBI progressively strengthened prudential regulation relating to capital adequacy, income recognition, asset classification, provisioning, disclosures and transparency. Sequencing of reforms among various segments of the financial sector (banks, DFIs, co-operative banks, NBFCs, money market, debt market and forex market) was determined by the importance of each segment, extent of regulatory powers enjoyed by the RBI and the evolving situation. Furthermore, institutional strengthening was undertaken to ensure the progressive development and integration of the securities, money and forex markets. The RBI has made significant improvements in the quality of performance of regulatory and supervisory functions. Our standards are comparable to the best in the world. Attention is being paid to several contemporary issues such as, relative roles of onsite and off-site supervision, functional versus institutional regulation, relative stress on internal management, market discipline and regulatory prescriptions, consolidated approach to supervision, etc. Several legislative initiatives have also been taken up with Government, covering procedural law, debt recovery systems, Credit Information Bureau, Deposit Insurance, etc. Progress in these is critical for effectiveness of RBI in the regulatory sphere. A recent important legislative development, which will improve the momentum of recovery of dues, is the enactment of Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SRFAESI) Act. Under this Act RBI has been entrusted with the role of stipulating suitable norms for registration of securitisation or reconstruction companies, prescribing prudential norms, recommending proper and transparent accounting and disclosure standards and framing appropriate guidelines for the conduct of asset reconstruction and securitisation.

Check your progress 3

1. The____________has always been playing the major role in regulating and controlling the India money market.

   a. Reserve Bank of India

   b. State bank of India

2. ____________performs a wide range of promotional functions,

   a. SBI

   b. RBI

2.5 Intermediates in the Money Market

Money market participants include mainly credit institutions and other financial intermediaries, governments, as well as individuals (households). Ultimate lenders in the money markets are households and companies with a financial surplus which they want to lend, while ultimate borrowers are companies and government with a financial deficit which need to borrow. Ultimate lenders and borrowers usually do not participate directly in the markets. As a rule they deal through an intermediary, who performs functions of broker, dealer or investment banker.

Important role is played by government, which issue money market securities and use the proceeds to finance state budget deficits. The government debt is often refinanced by issuing new securities to pay off old debt, which matures. Thus it manages to finance long term needs through money market securities with short-term maturities.

Central bank employs money markets to execute monetary policy. Through monetary intervention means and by fixing the terms at which banks are provided with money, central banks ensure economy's supply with liquidity.

Credit institutions (i.e. banks) account for the largest share of the money market. They issue money market securities to finance loans to households and corporations, thus supporting household purchases and investments of corporations. Besides, these institutions rely on the money market for the management of their short-term liquidity positions and for the fulfilment of their minimum reserve requirements.

Other important market participants are other financial intermediaries, such as money market funds, investment funds other than money-market funds, insurance companies and pension funds. Large non-financial corporations issue money market securities and use the proceeds to support their current operations or to expand their activities through investments.

In general issuance of money market securities allow market participants to increase their expenditures and finance economic growth.

Money market securities are purchased mainly by corporations, financial intermediaries and government that have funds available for a short-term period. Individuals (or households) play a limited role in the market by investing indirectly through money market funds. Apart from transactions with the central bank, money-market participants trade with each other to take positions dependent upon their short-term interest rate expectations, to finance their securities trading portfolios (bonds, shares, etc.), to hedge their longer-term positions with short-term contracts, and to reduce individual liquidity imbalances.

Check your progress 4

1. Important role is played by government, which issue money market securities and use the proceeds to finance state budget __________.
   a. Deficits
   b. surplus
2. Central bank employs __________markets to execute monetary policy.
   a. Capital
   b. money
3. Credit institutions account for the largest share of the__________market.
   a. Money
   b. capital

2.6 Development of Money Market in India

While the need for long term financing is met by the capital or financial markets, money market is a mechanism which deals with lending and borrowing of short term funds. Post reforms age in India has witnessed marvellous increase of the Indian money markets. Banks and other financial institutions have been able to meet the high opportunity of short term financial support of important sectors like the industry, services and agriculture. It performs under the regulation and control of the Reserve Bank of India (RBI). The Indian money markets have also exhibit the required maturity and flexibility over the past two decades. Decision of the government to permit the private sector banks to operate has provided much needed healthy competition in the money markets resulting in fair amount of improvement in their performance.

Till 1935, when the RBI was set up the Indian money market remained highly disintegrated, unorganized, narrow, shallow and therefore, very backward. The planned economic development that commenced in the year 1951 market is an important beginning in the annals of the Indian money market. The nationalization of banks in 1969, setting up of various committees such as the Sukhmoy Chakraborty Committee (1982), the Vaghul working group (1986), the setting up of discount and finance house of India ltd. (1988), the securities trading corporation of India (1994) and the commencement of liberalization and globalization process in 1991 gave a further fillip for the integrated and efficient development of India money market.

Check your progress 5

1. Till 1935, when the__________was set up the Indian money market remained highly disintegrated, unorganized, narrow, shallow and therefore, very backward.
   a. RBI
   b. banks
2. Banks and other financial institutions have been able to meet the high opportunity of __________term financial support of important sectors like the industry, services and agriculture.
   a. Long
   b. short

2.7 Money Market Instruments

Money Market is the part of financial market where instruments with high liquidity and very short-term maturities are traded. It's the place where large financial institutions, dealers and government participate and meet out their short-term cash needs. They usually borrow and lend money with the help of instruments or securities to generate liquidity. Due to highly liquid nature of securities and their short-term maturities, money market is treated as safe place.

2.7.1 Treasury Bills

A treasury bill is a promissory note issued by the RBI to meet the short-term requirement of funds. Treasury bills are highly liquid instruments that mean, at any time the holder of treasury bills can transfer of or get it discounted from RBI. These bills are normally issued at a price less than their face value; and redeemed at face value. So the difference between the issue price and the face value of the Treasury bill represents the interest on the investment. These bills are secured instruments and are issued for a period of not exceeding 364 days. Banks, Financial institutions and corporations normally play major role in the Treasury bill market.

2.7.2 Commercial Papers

Commercial paper (CP) is a popular instrument for financing working capital requirements of companies. The CP is an unsecured instrument issued in the form of promissory note. This instrument was introduced in 1990 to enable the corporate borrowers to raise short-term funds. It can be issued for period ranging from 15 days to one year. Commercial papers are transferable by endorsement and delivery. The highly reputed companies (Blue Chip companies) are the major player of commercial paper market.

The aim of its issuance is to provide liquidity or finance company's investments, e.g. in inventory and accounts receivable.

The major issuers of commercial papers are financial institutions, such as finance companies, bank holding companies and insurance companies. Financial companies tend to use CPs as a regular source of finance. Non-financial companies tend to issue CPs on an irregular basis to meet special financing needs. Thus commercial paper is a form of short-term borrowing. Its initial maturity is usually between seven and forty-five days. In US, the advantage of issuing CPs with maturities less than nine months is that they do not have to register with the Securities Exchange Commission (SEC) as a public offering. This reduces the costs of registration with SEC and avoids delays related to the registration process. CPs can be sold directly by the issuer, or may be sold to dealers who charge a placement fee (e.g. 1/8 percent). Since issues of CPs are heterogeneous in terms of issuers, amounts, maturity dates, there is no active secondary market for commercial papers. However, dealers may repurchase CPs for a fee.

2.7.3 Certificate of Deposit

Certificates of Deposit (CDs) are short-term instruments issued by Commercial Banks and Special Financial Institutions (SFIs), which are freely transferable from one party to another. The maturity period of CDs ranges from 91 days to one year. These can be issued to individuals, co-operatives and companies.

Certificate of deposit (CD) states that a deposit has been made with a bank for a fixed period of time, at the end of which it will be repaid with interest.

Thus it is, in effect, a receipt for a time deposit and explains why CDs appear in definitions of the money supply such as M4. It is not the certificate as such that is included, but the underlying deposit, which is a time deposit like other time deposits. An institution is said to 'issue' a CD when it accepts a deposit and to 'hold' a CD when it itself makes a deposit or buys a certificate in the secondary market. From an institution's point of view, therefore, issued CDs are liabilities; held CDs are assets.

The advantage to the depositor is that the certificate can be tradable. Thus though the deposit is made for a fixed period, he depositor can use funds earlier by selling the certificate to a third party at a price which will reflect the period to maturity and the current level of interest rates.

The advantage to the bank is that it has the use of a deposit for a fixed period but, because of the flexibility given to the lender, at a slightly lower price than it would have to pay for a normal time deposit.

The minimum denomination can be 100 000USD, although the issue can be as large as 1million USD. The maturities of CDs usually range from two weeks to one year. Non-financial corporations usually purchase negotiable CDs. Though negotiable CD denominations are typically too large for individual investors, they are sometimes purchased by money market funds that have pooled individual investors' funds. Thus money market funds allow individuals to be indirect investors in negotiable CDs. This way the negotiable CD market can be more active. There is also a secondary market for these securities, however its liquidity is very low.

2.7.4 Commercial Bills

Normally the traders buy goods from the wholesalers or manufactures on credit. The sellers get payment after the end of the credit period. But if any seller does not want to wait or in immediate need of money, he/she can draw a bill of exchange in favour of the buyer. When buyer accepts the bill it becomes a negotiable instrument and is termed as bill of exchange or trade bill. This trade bill can now be discounted with a bank before its maturity. On maturity the bank gets the payment from the drawer i.e., the buyer of goods. When trade bills are accepted by Commercial Banks it is known as Commercial Bills. So trade bill is an instrument, which enables the drawer of the bill to get funds for short period to meet the working capital needs.

Check your progress 6

1. ____________ Market is the part of financial market where instruments with high liquidity and very short-term maturities are traded.

   a. Money

   b. capital

2. A __________is a promissory note issued by the RBI to meet the short-term requirement of funds.

   a. commercial paper

   b. treasury bill

3. ___________is a popular instrument for financing working capital requirements of companies.

   a. Commercial paper

   b. treasury bill

2.8 Collateralized Browsing and Lending Obligation

"Collateralized Borrowing and Lending Obligation (CBLO)", as the name implies is a fully collateralized and secured instrument for borrowing / lending money. CBLO as a product is conceived and developed by CCIL for the facilitating deployment in a collateralized environment. As a product, CBLO aims to benefit those entities who have been phased out of Call/ Notice money market and / or those entities on restrictions have been placed on the borrowing / lending in call / notice money market. CBLO Dealing system is hosted and maintained by Clear corp Dealing Systems (India) Ltd, a fully owned subsidiary of CCIL. CCIL becomes Central Counterparty to all CBLO trades and guarantees settlement of

CBLO trades. CBLO is an RBI approved money market instrument which can be issued for a maximum tenor of one year. CBLO is a discounted instrument traded on Yield Time priority. CBLO instrument that are generally made available for trading are those with maturity of next seven business days and three month end dates. The balances are maintained in electronic book entry. The access to CBLO Dealing system for NDS Members is made available through INFINET and for non NDS Members through Internet. The Funds settlement of members in CBLO segment is achieved in the books of RBI for members who maintain an RBI Current Account and are allowed to operate that current account for settlement of their secondary market transactions. In respect of other members, CBLO Funds settlement is achieved in the books of Settlement Bank.

Check your progress 7

1. __________as a product is conceived and developed by CCIL for the facilitating deployment in a collateralized environment.
   a. CBLO
   b. ILO
2. CBLO is a _________approved money market instrument which can be issued for a maximum tenor of one year.
   a. Government
   b. RBI

2.9 Call Money Market and Term Money Market

The call money market deals in short term finance repayable on demand, with a maturity period varying from one day to 14 days. S.K. Muranjan commented that call loans in India are provided to the bill market, rendered between banks, and given for the purpose of dealing in the billion market and stock exchanges. Commercial banks, both Indian and foreign, co-operative banks, Discount and Finance House of India Ltd.(DFHI), Securities trading corporation of India (STCI) participate as both lenders and borrowers and Life Insurance Corporation of India (LIC), Unit Trust of India(UTI), National Bank for Agriculture and Rural Development (NABARD)can participate only as lenders. The interest rate paid on call money loans, known as the call rate, is highly volatile. It is the most sensitive section of the money market and the changes in the demand for and supply of call loans are promptly reflected in call rates. There are now two call rates in India: the Inter-bank call rate' and the lending rate of DFHI. The ceilings on the call rate and inter-bank term money rate were dropped, with effect from May 1, 1989. The Indian call money market has been transformed into a pure inter-bank market during 2006–07. The major call money markets are in Mumbai, Kolkata, Delhi, Chennai and Ahmedabad.

The money market is a market for short-term financial assets that are close substitutes of money. The most important feature of a money market instrument is that it is liquid and can be turned over quickly at low cost and provides an opportunity for balancing the short-term surplus funds of lenders and the requirements of borrowers. By convention, the term "Money Market" refers to the market for short-term requirement and deployment of funds. Money market instruments are those instruments, which have a maturity period of less than one year. The most active part of the money market is the market for overnight call and term money between banks and institutions and repo transactions.

Call Money / Repo are very short-term Money Market products. There is a wide range of participants (banks, primary dealers, financial institutions, mutual funds, trusts, provident funds, etc.) dealing in money market instruments. Money Market Instruments and the participants of money market are regulated by RBI and SEBI.As a primary dealer SBI DFHI is an active player in this market and widely deals in Short Term Money Market Instruments.

The below mentioned instruments are normally termed as money market instruments:

- Call/ Notice/ Term Money
- Repo/ Reverse Repo
- Inter Corporate Deposits
- Commercial Paper
- Certificate of Deposit
- T-bills
- Inter Bank Participation Certificate

Check your progress 8

1. The___________money market deals in short term finance repayable on demand, with a maturity period varying from one day to 14 days.
   a. Call
   b. black
2. The ____________market is a market for short-term financial assets that are close substitutes of money.
   a. Capital
   b. money

2.10 Let Us Sum Up

The whole of this unit focussed on the Money market of India. Here the readers have been briefed about what exactly is a money market. They have been explained in very detail the various functions and characteristics of money market. These whole units aim to provide sufficient information on money market and thus also cover the role of RBI in the money market of India. This unit focussed on development of money market in India. Various money market instruments have even been discussed here in very detail. The whole of this unit has been explained here in very detail and interesting manner to make it interesting for the students.

After going through this unit the readers would get enough idea about the money market.

2.11 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b)

Check your progress 2

Answers: (1-a), (2-b)

Check your progress 3

Answers: (1-a), (2-b)

Check your progress 4

Answers: (1-a), (2-b), (3-a)

Check your progress 5

Answers: (1-a), (2-b)

Check your progress 6

Answers: (1-a), (2-b), (3-a)

Check your progress 7

Answers: (1-a), (2-b)

Check your progress 8

Answers: (1-a), (2-b)

2.12 Glossary

1. **CP -** It is a popular instrument for financing working capital requirements of companies.

2.13 Assignment

Give four examples of credit instruments of the money market.

2.14 Activities

1. Discuss the function of money market.
2. Discuss money market and its characteristics.

2.15 Case Study

1. Discuss the role played by RBI in money market.
2. Discuss the role of intermediaries in money market

2.16 Further Readings

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UNIT 3: CAPITAL MARKET

Unit Structure

3.0 Learning Objectives

After learning this unit, you will be able to understand:

- Functions and Types of Capital Market
- Reforms in the capital Market
- Intermediaries
- Issue Mechanisms
- Types of Primary Issues
- Public Rights and Private Placement
- ADRs, GDRs, and ECBs.

3.1 Introduction

Capital Market may be defined as a market dealing in medium and long-term funds. It is an institutional arrangement for borrowing medium and long-term funds and which provides facilities for marketing and trading of securities. So it constitutes all long-term borrowings from banks and financial institutions, borrowings from foreign markets and raising of capital by issue various securities such as shares debentures, bonds, etc. In the present chapter let us discuss about the market for trading of securities. The market where securities are traded known as Securities market. It consists of two different segments namely primary and secondary market. The primary market deals with new or fresh issue of securities and is, therefore, also known as new issue market; whereas the secondary market provides a place for purchase and sale of existing securities and is often termed as stock market or stock exchange.

3.2 Meaning

The capital market is the sector of the financial market where long-term financial instruments issued by corporations and governments trade. Here "long-term" refers to a financial instrument with an original maturity greater than one year and perpetual securities (those with no maturity). There are two types of capital market securities: those that represent shares of ownership interest, also called equity, issued by corporations, and those that represent indebtedness, or debt issued by corporations and by the state and local governments.

The Capital market is a market for financial investments that are direct or indirect claims to capital. It is wider than the Securities Market and embraces all forms of lending and borrowing, whether or not evidenced by the creation of a negotiable financial instrument. The Capital Market comprises the complex of institutions and mechanisms through which intermediate term funds and long-term funds are pooled and made available to business, government and individuals. The Capital Market also encompasses the process by which securities already outstanding are transferred.

Check your progress 1

1. The __________market is the sector of the financial market where long-term financial instruments issued by corporations and governments trade.

   a. capital

   b. money

2. The Capital market is a market for __________investments that are direct or indirect claims to capital.

   a. long term

   b. financial

3.3 Functions and Types of Capital Market

Functions of Capital market

Like the money market capital market is also very important. It plays a significant role in the national economy. A developed, dynamic and vibrant capital market can immensely contribute for speedy economic growth and development.

Let us get acquainted with the important functions and role of the capital market.

1. **Mobilization of Savings:** Capital market is an important source for mobilizing idle savings from the economy. It mobilizes funds from people for further investments in the productive channels of an economy. In that sense it activates the ideal monetary resources and puts them in proper investments.

2. **Capital Formation:** Capital market helps in capital formation. Capital formation is net addition to the existing stock of capital in the economy. Through mobilization of ideal resources it generates savings; the mobilized savings are made available to various segments such as agriculture, industry, etc. This helps in increasing capital formation.

3. **Provision of Investment Avenue:** Thus it provides an investment avenue for people who wish to invest resources for a long period of time. It provides suitable interest rate returns also to investors. Instruments such as bonds, equities, units of mutual funds, insurance policies, etc. definitely provides diverse investment avenue for the public.

4. **Speed up Economic Growth and Development:** Capital market enhances production and productivity in the national economy. As it makes funds available for long period of time, the financial requirements of business houses are met by the capital market. It helps in research and development. This helps in, increasing production and productivity in economy by generation of employment and development of infrastructure.

5. **Proper Regulation of Funds:** Capital markets not only helps in fund mobilization, but it also helps in proper allocation of these resources. It can have regulation over the resources so that it can direct funds in a qualitative manner.

6. **Service Provision:** As an important financial set up capital market provides various types of services. It includes long term and medium term loans to industry, underwriting services, consultancy services, export finance, etc. These services help the manufacturing sector in a large spectrum.

7. **Continuous Availability of Funds:** Capital market is place where the investment avenue is continuously available for long term investment. This is a liquid market as it makes fund available on continues basis. Both buyers and seller can easily buy and sell securities as they are continuously available. Basically capital market transactions are related to the stock exchanges. Thus marketability in the capital market becomes easy.

Types of Capital Market

There are two types of capital market

1. Primary market

The primary market is that part of the capital markets that deals with the issuance of new securities. Companies, governments or public sector institutions can obtain funding through the sale of a new stock or bond issue. This is typically done through a syndicate of securities dealers. The process of selling new issues to investors is called underwriting. In the case of a new stock issue, this sale is an initial public offering (IPO). Dealers earn a commission that is built into the price of the security offering, though it can be found in the prospectus.

Features of primary markets are:

This is the market for new long term equity capital. The primary market is the market where the securities are sold for the first time. Therefore it is also called the new issue market (NIM).

In a primary issue, the securities are issued by the company directly to investors. The company receives the money and issues new security certificates to the investors. Primary issues are used by companies for the purpose of setting up new business or for expanding or modernizing the existing business. The primary market performs the crucial function of facilitating capital formation in the economy. The new issue market does not include certain other sources of new long term external finance, such as loans from financial institutions. Borrowers in the new issue market may be raising capital for converting private capital into public capital; this is known as “going public.”

2. Secondary market

The secondary market, also known as the aftermarket, is the financial market where previously issued securities and financial instruments such as stock, bonds, options, and futures are bought and sold. The term “secondary market” is also used to refer to the market for any used goods or assets, or an alternative use for an existing product or asset where the customer base is the second market (for example, corn has been traditionally used primarily for food production and feedstock, but a second- or third- market has developed for use in ethanol production). Another commonly referred to usage of secondary market term is to refer to loans which are sold by a mortgage bank to investors such as Fannie Mae and Freddie Mac.

With primary issuances of securities or financial instruments, or the primary market, investors purchase these securities directly from issuers such as corporations issuing shares in an IPO or private placement, or directly from the federal government in the case of treasuries. After the initial issuance, investors can purchase from other investors in the secondary market.

The secondary market for a variety of assets can vary from loans to stocks, from fragmented to centralized, and from illiquid to very liquid. The major stock exchanges are the most visible example of liquid secondary markets – in this case, for stocks of publicly traded companies. Exchanges such as the New York Stock Exchange, Nasdaq and the American Stock Exchange provide a centralized, liquid secondary market for the investors who own stocks that trade on those exchanges. Most bonds and structured products trade "over the counter," or by phoning the bond desk of one's broker-dealer. Loans sometimes trade online using a Loan Exchange

Check your progress 2

1. _________market is an important source for mobilizing idle savings from the economy.

   a. Capital

   b. money

2. Capital market raises resources for __________ periods of time.

   a. Shorter

   b. longer

3. The __________market is that part of the capital markets that deals with the issuance of new securities.

   a. Primary

   b. secondary

4. In a ________issue, the securities are issued by the company directly to investors.

   a. Secondary

   b. primary

3.4 Reforms in the Capital Market

The major reforms undertaken in capital market of India includes:-

1. **Establishment of SEBI:** The Securities and Exchange Board of India (SEBI) was established in 1988. It got a legal status in 1992. SEBI was primarily set up to regulate the activities of the merchant banks, to control the operations of mutual funds, to work as a promoter of the stock exchange activities and to act as a regulatory authority of new issue activities of companies. The SEBI was set up with the fundamental objective, "to protect the interest of investors in securities market and for matters connected therewith or incidental thereto."

   The main functions of SEBI are:-

   a) To regulate the business of the stock market and other securities market.

   b) To promote and regulate the self-regulatory organizations.

   c) To prohibit fraudulent and unfair trade practices in securities market.

   d) To promote awareness among investors and training of intermediaries about safety of market.

   e) To prohibit insider trading in securities market.

   f) To regulate huge acquisition of shares and takeover of companies.

2. **Establishment of Creditors Rating Agencies:** Three creditors rating agencies viz. The Credit Rating Information Services of India Limited (CRISIL - 1988), the Investment Information and Credit Rating Agency of India Limited (ICRA - 1991) and Credit Analysis and Research Limited (CARE) were set up in order to assess the financial health of different financial institutions and agencies related to the stock market activities. It is a guide for the investors also in evaluating the risk of their investments.

3. **Increasing of Merchant Banking Activities:** Many Indian and foreign commercial banks have set up their merchant banking divisions in the last few years. These divisions provide financial services such as underwriting facilities, issue organising, consultancy services, etc. It has proved as a helping hand to factors related to the capital market.

4. **Candid Performance of Indian Economy:** In the last few years, Indian economy is growing at a good speed. It has attracted a huge inflow of Foreign Institutional Investments (FII). The massive entry of FIIs in the

Indian capital market has given good appreciation for the Indian investors in recent times. Similarly many new companies are emerging on the horizon of the Indian capital market to raise capital for their expansions.

5. **Rising Electronic Transactions:** Due to technological development in the last few years. The physical transaction with more paper work is reduced. Now paperless transactions are increasing at a rapid rate. It saves money, time and energy of investors. Thus it has made investing safer and hassle free encouraging more people to join the capital market.

6. **Growing Mutual Fund Industry:** The growing of mutual funds in India has certainly helped the capital market to grow. Public sector banks, foreign banks, financial institutions and joint mutual funds between the Indian and foreign firms have launched many new funds. A big diversification in terms of schemes, maturity, etc. has taken place in mutual funds in India. It has given a wide choice for the common investors to enter the capital market.

7. **Growing Stock Exchanges:** The numbers of various Stock Exchanges in India are increasing. Initially the BSE was the main exchange, but now after the setting up of the NSE and the OTCEI, stock exchanges have spread across the country. Recently a new Inter-connected Stock Exchange of India has joined the existing stock exchanges.

8. **Investor's Protection:** Under the purview of the SEBI the Central Government of India has set up the Investors Education and Protection Fund (IEPF) in 2001. It works in educating and guiding investors. It tries to protect the interest of the small investors from frauds and malpractices in the capital market.

9. **Growth of Derivative Transactions:** Since June 2000, the NSE has introduced the derivatives trading in the equities. In November 2001 it also introduced the future and options transactions. These innovative products have given variety for the investment leading to the expansion of the capital market.

10. **Insurance Sector Reforms:** Indian insurance sector has also witnessed massive reforms in last few years. The Insurance Regulatory and Development Authority (IRDA) were set up in 2000. It paved the entry of the private insurance firms in India. As many insurance companies invest their money in the capital market, it has expanded.

11. **Commodity Trading:** Along with the trading of ordinary securities, the trading in commodities is also recently encouraged. The Multi Commodity

Exchange (MCX) is set up. The volume of such transactions is growing at a splendid rate.

Apart from these reforms the setting up of Clearing Corporation of India Limited (CCIL), Venture Funds, etc. have resulted into the tremendous growth of Indian capital market.

Check your progress 3

1. The Securities and Exchange Board of India (SEBI) was established in __________.
   a. 1988
   b. 1978
2. To regulate the business of the stock market and other securities market is the function of ________.
   a. RBI
   b. SEBI
3. Under the purview of the SEBI the _______has set up the Investors Education and Protection Fund (IEPF) in 2001.
   a. Central Government of India
   b. RBI

3.5 Intermediaries

Capital markets intermediaries are licensed and regulated under the Securities and Futures Act. They may provide the whole range of capital markets services as specified in the 2nd schedule of the Securities and Futures Act with the appropriate Capital Markets Services licence. Currently, these services or regulated activities include dealing in securities; trading in futures contracts; leveraged foreign exchange trading; advising on corporate finance; fund management; real estate investment trust management; securities financing; providing custodial services for securities; and providing credit rating services.

Individuals who are employed by the capital markets intermediaries to carry out such regulated activities are required to be representatives under the Securities and Futures Act

Firm or person (such as a broker or consultant) who acts as a mediator on a link between parties to a business deal, investment decision, negotiation, etc. In money markets, for example, banks act as intermediaries between depositors seeking interest income and borrowers seeking debt capital. Intermediaries usually specialize in specific areas, and serve as a conduit for market and other types of information is also called a middleman or intermediation.

1. Intermediaries are service providers in the market, including stock brokers, sub-brokers, financiers, merchant bankers, underwriters, depository participants, registrar and transfer agents, FIIs/ sub accounts, mutual Funds, venture capital funds, portfolio managers, custodians, etc.

2. A stockbroker is a regulated professional individual, usually associated with a brokerage form firm or broker-dealer, who buys and sells stocks and other securities for both retail and institutional clients, through a stock exchange or over the counter, in return for a fee or commission. Stockbrokers are known by numerous professional designations, depending on the license they hold, the type of securities they sell, or the services they provide.

3. is a person OR a business entity who makes their money from investments, typically involving large sums of money and usually involving private equity and venture capital, leveraged buyouts, corporate finance, investment banking and/or large scale asset management. A financier makes money through this process when his or her investment is paid back with interest, from part of the company's equity awarded to them as specified by the business deal, or a financier can generate income through commission, performance, and management fees

4. A merchant bank is a financial institution that provides capital to companies in the form of share ownership instead of loans. A merchant bank also provides advisory on corporate matters to the firms they lend to. Both commercial banks and investment banks may engage in merchant banking activities. Historically, merchant banks' original purpose was to facilitate and/or finance production and trade of commodities, hence the name "merchant". Few banks today restrict their activities to such a narrow scope.

5. A company or other entity that administers the public issuance and distribution of securities from a corporation or other issuing body. An underwriter works closely with the issuing body to determine the offering price of the securities, buys them from the issuer and sells them to investors via the underwriter's distribution network EX- MB and syndicate members.

6. Depository system introduced in India in the year 1996. In India, a Depository Participant (DP) is described as an agent of the depository. They are the intermediaries between the depository and the investors. The relationship between the DPs and the depository is governed by an agreement made between the two under the Depositories Act. Service provided Dematerialization, Re-materialization, Transfers of securities, settlement of trades. In India- NSDL & CDSL are the two entities.

7. Registrar is the trusts or institutions that register and maintain detailed records of the transactions of investors for the convenience of mutual fund houses. Registrar or transfer agents are the trusts or institutions that register and maintain detailed records of the transactions of investors for the convenience of mutual fund houses.

8. A mutual fund is a type of professionally managed collective investment scheme that pools money from many investors to purchase securities. While there is no legal definition of the term "mutual fund", it is most commonly applied only to those collective investment vehicles that are regulated and sold to the general public. They are sometimes referred to as "investment companies" or "registered investment companies. Most mutual funds are "open-ended," meaning investors can buy or sell shares of the fund at any time

9. Venture capital (VC) is financial capital provided to early-stage, high-potential, high risk, growth start-up companies. The venture capital fund makes money by owning equity in the companies it invests in. The typical venture capital investment occurs after the seed funding round as the first round of institutional capital to fund growth (also referred to as Series A round) in the interest of generating a return through an eventual realization event, such as an IPO or trade sale of the company. Venture capital is a subset of private equity. Therefore, all venture capital is private equity, but not all private equity is venture

10. A portfolio manager is either a person who makes investment decisions using money other people have placed under his or her control or a person who manages a financial institution's asset and liability (loan and deposit) portfolios. On the investments side, they work with a team of analysts and researchers, and are ultimately responsible for establishing an investment strategy, Portfolio managers are presented with investment ideas from internal buy-side analysts and sell-side analysts from investment banks. It is their job to sift through the relevant information and use their judgment to

buy and sell securities. Throughout each day, they read reports, talk to company managers and monitor industry and economic trends looking for the right company and time to invest the portfolio's capital.

11. A financial professional who has expertise in evaluating the creditworthiness of individuals and businesses. Credit analysts determine the likelihood that a borrower will be able to meet financial obligations and pay back a loan, often by reviewing the borrower's financial history and determining whether market conditions will be conducive to repayment.

Check your progress 4

1. ___________markets intermediaries are licensed and regulated under the Securities and Futures Act.

   a. Capital

   b. money

2. ___________is/are service providers in the market.

   a. RBI

   b. Intermediaries

3. A ___________is a regulated professional individual, usually associated with a brokerage form firm.

   a. Stockbroker

   b. banks

3.6 Issue Mechanisms

As we all know that capital market (securities markets) is the market for securities, where companies and the government can raise long-term funds. The capital market includes the stock market and the bond market. Financial regulators, oversee the capital markets in their respective countries to ensure that investors are protected against fraud. The capital markets consist of the primary market, where new issues are distributed to investors, and the secondary market, where existing securities are traded.

Primary markets

The primary market is that part of the capital markets that deals with the issuance of new securities. Companies, governments or public sector institutions can obtain funding through the sale of a new stock or bond issue. This is typically done through a syndicate of securities dealers. The process of selling new issues to investors is called underwriting. In the case of a new stock issue, this sale is an initial public offering (IPO). Dealers earn a commission that is built into the price of the security offering, though it can be found in the prospectus.

Secondary markets

The secondary market is the financial market for trading of securities that have already been issued in an initial private or public offering. Alternatively, secondary market can refer to the market for any kind of used goods. The market that exists in a new security just after the new issue is often referred to as the aftermarket. Once a newly issued stock is listed on a stock exchange, investors and speculators can easily trade on the exchange, as market makers provide bids and offers in the new stock.

In the secondary market, securities are sold by and transferred from one investor or speculator to another. It is therefore important that the secondary market be highly liquid and transparent. Before electronic means of communications, the only way to create this liquidity was for investors and speculators to meet at a fixed place regularly. This is how stock exchanges originated.

Check your progress 5

1. The __________markets consist of the primary market, where new issues are distributed to investors.

   a. capital

   b. secondary

2. The _________market is a place where existing securities are traded.

   a. primary

   b. secondary

3. The _______market is that part of the capital markets that deals with the issuance of new securities.

   a. primary

   b. secondary

3.7 Types of Primary Issues

Primarily, issues can be classified as a Public, Rights or Preferential issues (also known as private placements). While public and rights issues involve a detailed procedure, private placements or preferential issues are relatively simpler. The classification of issues is illustrated below:

Initial Public Offering (IPO) is when an unlisted company makes either a fresh issue of securities or an offer for sale of its existing securities or both for the first time to the public. This paves way for listing and trading of the issuer's securities.

A follow on public offering (Further Issue) is when an already listed company makes either a fresh issue of securities to the public or an offer for sale to the public, through an offer document.

Rights Issue is when a listed company which proposes to issue fresh securities to its existing shareholders as on a record date. The rights are normally offered in a particular ratio to the number of securities held prior to the issue. This route is best suited for companies who would like to raise capital without diluting stake of its existing shareholders.

A Preferential issue is an issue of shares or of convertible securities by listed companies to a select group of persons under Section 81 of the Companies Act, 1956 which is neither a rights issue nor a public issue. This is a faster way for a company to raise equity capital. The issuer company has to comply with the Companies Act and the requirements contained in the Chapter pertaining to preferential allotment in SEBI guidelines which inter-alia include pricing, disclosures in notice, etc.

Check your progress 6

1. __________is when an unlisted company makes either a fresh issue of securities or an offer.

   a. IPO

   b. BPO

2. ___________is when a listed company which proposes to issue fresh securities to its existing shareholders as on a record date.

   a. IPO

   b. Rights Issue

3. A ________issue is an issue of shares or of convertible securities by listed companies to a select group of persons under Section 81 of the Companies Act, 1956 which is neither a rights issue nor a public issue.

   a. Preferential

   b. Equity

3.8 Public Rights and Private Placement

A rights issue involves selling securities in the primary by issuing rights to the existing shareholders, When a company issues additional equity capital, it has to be offered in the first instance to the existing shareholders on a pro rata basis. This is required under Section 81 of the Companies act, 1956. The shareholders however may be a special resolution forfeit this right, partially or fully to enable a company to issue additional capital the public.

Procedure for rights issue: A company making rights issue sends a letter of offer along with a composite application form consisting of four forms (A, B, C and D) to the shareholders. Form A is meant for the acceptance of the rights and application of additional shares. This form also shows the number of rights shares the shareholders is entitled to. It also has a column through which a request for additional shares may be made. Form B is to be used if the shareholder wants to renounce the rights in-favour of someone else. Form C is meant for application by the renounces in whose favour the rights have been renounced by the original allotted, through Form B. Form D is to be used to make a request for split forms. The composite application form must be mailed to the company within a specific period which is usually 30 days.

Private Placement or Preferential allotment: In private placement, funds are raised in the primary market by issuing securities privately to some investors without resorting to underwriting. The investors in this case may be financial institutions, commercial banks, other company's shareholders of promoting companies, and friends and associates of the promoters.

The merits of private placement are: (1) the process of raising funds is fairly simple. The elaborate procedure required in the case of a public issue is more or less by passed. (2) The issues cost is minimal. (3) In the case of a debenture issue, negotiated directly between the issuing company and the few investors, there may be greater flexibility with respect to terms and conditions. The disadvantageous of private placement are: (1) The Quantum of funds that can be raised may be rather limited, (2) The cost of capital of funds raised by way of private placements may be somewhat higher.

Private Placement of Debentures: Private placement of debentures has become very popular in recent years. The principal buyers of such debentures have been mutual funds, insurance companies, financial institutions, Army Group Insurance, Navy Group Insurance, Air Group and so on.

Check your progress 7

1. A ________involves selling securities in the primary by issuing rights to the existing shareholders.
   a. rights issue
   b. bonus issue
2. In__________, funds are raised in the primary market by issuing securities privately to some investors without resorting to underwriting.
   a. Public issue
   b. private placement

3.9 Resource Mobilization from International Capital Markets

Funds can be raised in the primary market from the domestic market as well as from international markets. After the reforms were initiated in 1991, one of the major policy changes was allowing Indian companies to raise resources by way of equity issues in the international markets. Earlier, only debt was allowed to be raised from international markets. In the early 1990s foreign exchange reserves had depleted and the country's rating had been downgraded. This resulted in a foreign exchange crunch and the government was unable to meet the import requirement of Indian companies. Hence allowing companies to tap the equity and bond market In Europe seemed a more sensible option. This permission encourages Indian companies to become global.

India companies have raised resources from international capital markets through Global depository receipts (GDRs) / American Depository Receipts (ADRs), Foreign Currency Convertible Bonds (PCCBs) and External Commercial Borrowings (ECBs). The last are used as a residual source after exhausting external equity as a main source of finance for large value projects.

3.9.1 ADRs

ADRs are negotiable instruments denominated in dollars, and issued by the US Depository Bank. A non-US company that seeks to list in the US, deposits its shares with a bank and receives receipts which enable the company to issue American Depository Shares (ADSs). These ADS's serve as stock certificates and are used interchangeably with ADRs which represent ownership of deposited shares. There is no legal or technical difference between an ADR and a GDR. As they are listed on the New York Stock Exchange (NYSE) and NASDAQ (National Association of Securities Dealers Automated Association), ADR issued offer access to the US institutional and retail markets while GDR issues offer access only to the US institutional market. GDR listing requires comprehensive disclosures and greater transparency as compared to GDR listing.

3.9.2 GDRs

GDRs essentially equity instruments issued abroad by authorized overseas corporate bodies against the shares/bonds of Indian companies held with nominated domestic custodian banks. The issue of GDR creates equity shares of the issuing company which are kept with a designated bank. GDRs are freely transferable outside India and divided in respect of the share represented by the GDR is paid in Indian rupees only. They are listed and traded on a foreign stock exchange. Trading takes place between professional market makers on an OTC (over the counter) basis. A GDR may represent one or more shares of the issuing company. The shares correspond to other GDR in a fixed ratio. A holder of a GDR can, at any time, convert it into the number of shares that it represents. Till conversion, the GDRs do not carry any voting rights and once conversion takes place the underlying shares are listed and traded on the domestic exchange. Most of the Indian companies have their GDR issues listed on the Luxembourg Stock Exchange and the London Stock Exchange. Indian GDRs are primarily sold to institutional investors and the major demand is in the UK, US, Hong Kong, Singapore, France and Switzerland. Rule 144 A of the Securities and Exchange Commissions (SEC) of the US permits companies from outside the US to offer their GDRs to qualified institutional buyers.

GDRs can be converted into ADRs by surrendering the existing GDRs and depositing the underlying equity shares with the ADR depository in exchange for ADRs. The company has to comply with the Securities and Exchange Commission requirements to materialize this exchange offer process. However, the company does not get any funds by this conversion. The trend is towards the conversion of GDRs into ADRs as ADRs are more liquid and cover a wider market. Besides these, many European investors have been disappointed by poor performance of Indian GDRs in traditional industries and are unwilling to provide more capital.

3.9.3 ECBs

An external commercial borrowing (ECB) is an instrument used in India to facilitate the access to foreign money by Indian corporations and PSUs (public sector undertakings). ECBs include commercial bank loans, buyers' credit and suppliers’ credit, securitised instruments such as floating rate notes and fixed rate bonds, etc. credit from official export credit agencies and commercial borrowings from the private sector window of multilateral financial Institutions such as International Finance Corporation (Washington), ADB, AFIC, CDC, etc. ECBs cannot be used for investment in stock market or speculation in real estate. The DEA (Department of Economic Affairs), Ministry of Finance, Government of India along with Reserve Bank of India, monitors and regulates ECB guidelines and policies. For infrastructure and green-field projects, funding up to 50%

(through ECB) is allowed. In telecom sector too, up to 50% funding through ECBs is allowed. Recently Government of India allowed borrowings in Chinese currency Yuan. Corporate sectors can mobilize USD 750 million via automatic route, whereas service sectors and NGO's for microfinance can mobilize USD 200 million and 10 million respectively.

Borrowers can use 25 per cent of the ECB to repay rupee debt and the remaining 75 per cent should be used for new projects. A borrower cannot refinance its entire existing rupee loan through ECB. The money raised through ECB is cheaper given near-zero interest rates in the US and Europe, Indian companies can repay part of their existing expensive loans from that.

Check your progress 8

1. Funds can be raised in the ___________market from the domestic market as well as from international markets.
   a. Primary
   b. secondary
2. _____________are negotiable instruments denominated in dollars, and issued by the US Depository Bank.
   a. GDR
   b. ADRs
3. ______________essentially equity instruments issued abroad by authorized overseas corporate bodies against the shares/bonds of Indian companies held with nominated domestic custodian banks
   a. GDRs
   b. ADRs
4. A ____________is an instrument used in India to facilitate the access to foreign money by Indian corporations and PSUs.
   a. GDRs
   b. ECB

3.10 Primary Market

The Primary Market consists of arrangements, which facilitate the procurement of long-term funds by companies by making fresh issue of shares and debentures. You know that companies make fresh issue of shares and/or debentures at their formation stage and, if necessary, subsequently for the expansion of business. It is usually done through private placement to friends, relatives and financial institutions or by making public issue. In any Business case, the companies have to follow a well-established legal procedure and involve a number of intermediaries such as underwriters, brokers, etc. who form an integral part of the primary market. You must have learnt about many initial public offers (IPOs) made recently by a number of public sector undertakings such as ONGC, GAIL, NTPC and the private sector companies like Tata Consultancy Services (TCS), Biocon, Jet-Airways and so on.

3.10.1 Scenario in India

In the Financial Year 2008, India saw the greatest year in Indian capital Market raised when the Total Capital raised went Northwards of US$ 9 Billion.

- India has seen a tremendous growth of its Capital Markets with close to 500 Initial Public Offerings (IPO) second only US. While India Ranked IV with respect to the amount of Capital raised contributing to 3.7% of global IPO share.
- At the end of F.Y 12,the P/E ratio of BSE Sensex and S & P CNX NIFTY were 17.8 and 18.7 respectively as compared to 21.2 and 22.1 respectively as at the end of F.Y11 1st Development in Primary Market
- The Overall growth of GDP at factor Cost at contrast Prices, as per Advanced Estimates, is estimated at 6.9 percent in F.Y12 as compared to the revised growth of 8.4% during F.Y11
- Industrial Growth measured by Index of Industrial Production reached 2.9% during F.Y12 as compare to 8.2% in F.Y11 2nd Development in Primary Market •Among the 17 listed companies that were approved for ordinary share issue, 16 have completed their Initial Public Offering(IPO) and among them 12 have already been listed in the Secondary Market too.
- In order to create efficient Capital Market QFI’s been allowed to directly invest in the Indian Equity Market in Jan 2012.

- It is mandatory for Companies to issue IPO of 100 and above in electronic form through Nation Wide Broker Network of Stock Exchanges. 3rd Development in Primary Market Resources mobilized in primary market 0 50 100 150 200 250 300 350 400 450 FY08 FY09 FY10 FY11 FY12 IPOs FPOs Bond/NCD Right Issues Source: SEBI Source: BSE

Check your progress 9

1. The___________Market consists of arrangements, which facilitate the procurement of long-term funds by companies by making fresh issue of shares and debentures.
   a. Primary
   b. Secondary
2. India has seen a tremendous growth of its __________Markets with close to 500 Initial Public Offerings(IPO)Second only US
   a. Primary
   b. Capital

3.11 Debt Market: Private Corporate

Debt market refers to the financial market where investors buy and sell debt securities, mostly in the form of bonds. Entire debt segment is generally consists of 2/3 of primary market and 4/5 of secondary market. The Indian debt market is today one of the largest in Asia and includes securities issued by the Government (Central & State Governments), public sector undertakings, other government bodies, financial institutions, banks and corporates.

Debt Market Can Be Broadly Classified in To:-

1) Govt. securities market)
2) Corporate debt market. The government debt market is the market for bonds and securities issued by the central govt., state govt. and the semi govt. authorities which includes local govt. authorities like city corporations, metropolitan authorities public sector corporations and other govt. agencies such as IDBI, IFCI, SFCs. In broader terms Corporate bonds are fixed income securities issued by corporates i.e. entities other than Government.

Corporate debt market can be classified into:-

- Primary market
- Secondary market

Primary market for corporate debt:-The corporate sector can raise debt funds either through prospectus or private placement. It is a market wherein debt securities of corporate i.e., debentures, bonds, commercial papers, certificate of deposits, etc. of private & public sectors are issued for the first time.

Secondary market for corporate debt:-It is a market where the corporate debt securities of both private sector & public sector undertakings are traded. These securities are traded on Wholesale Debt Segment (WDM) segment of NSE, OTCEI &BSE.

Corporate bonds can be issued in two ways:-Public issue in public issue, corporations issue bonds to the market as a whole. Institutions as well as retail investors can participate in this issue. The cost of borrowing is little high in case of public issue. Private placement in private placement corporate, generally park the bond issuance with few institutions. In India, more than 90% of the corporate bonds are issued through private placement. It is an easiest and cheapest way of borrowing corporate bonds.

Structure of corporate debt market in India The primary market for corporate debt is mainly dominated by private placements (93 per cent of total issuance in 2011-12) as corporates prefer this route to public issues because of operational ease, i.e., minimum disclosures, low cost, tailor made structures and speed of raising funds. Banks/FIs (42.3 per cent of total issuances) followed by finance companies (26.4 per cent) were the major issuer's in2011-12. India lacks a long-term debt market for pure project finance. Corporate bonds issued in India usually carry a rating of AAA indicating lack of interest in bonds of lower rated borrowers in the debt market. Institutional participants, such as, banks, primary dealers, mutual funds, insurance companies, pension funds, corporates, etc. are the major players in this market.

According to SEBI, the total trading volume in the secondary corporate bond market has increased from Rs.961 bn in FY2008 to Rs.2,207 bn in FY2010CAGR of over 50% over the last two years.• SeFY2008 16,547 967FY2009 21,651 1,487Fy2010 20,933 2,20711/28/2012

Check your progress 10

1. __________market refers to the financial market where investors buy and sell debt securities, mostly in the form of bonds.
   a. Debt
   b. share
2. The ___________sector can raise debt funds either through prospectus or private placement.
   a. Government
   b. corporate

3.12 Role of SEBI in the Capital Market

Repealing of CCI Act: SEBI guidelines were issued after the repeal of the CCI Act where by the CCI guidelines became out of date. New guidelines by SEBI were issued starting from the month of June 1992. Some CCI guidelines were still retained, as in the case of those for premium fixation.

Guidelines for new issues made by new companies: They have to be issued at par. Free pricing is permitted only if the new company is promoted by the existing company with not less than 50% of equity.

Guidelines for new issues made by private limited companies: New issues made by Private Limited Companies and Closely held companies could be made by free pricing, for listing purposes if such companies have had three years of track record of consistent profitability out of last 5 years. Not less than 20% of equity is to be offered to the public, in such cases.

Guidelines for new issues made by existing listed companies: Public issues by existing listed companies can be made through free pricing, if they are further issues and if they are disclosed in the prospectus. The NAV and the market price have to be considered for the last 3 years. The companies with foreign holding wishing to enhance the limit up to 51% will have to get the prices approved in the general body meeting by a special resolution under Sec. 81 (A) of the Companies Act, and subject to RBI approval.

Listing of shares on the OTC: If the new issues are made through OTC, normal guidelines will apply if the sponsor is not taking any share. If the shares are taken by the sponsor, subsequent offer to the public may be made at such a price as the sponsor may deem fit. The promoters should retain 25% quota with a lock in period of 5 years, the sponsor should act as market maker for a period of at least 3 years and also find another market maker for compulsory market making. This condition was relaxed recently to encourage OTC Listing.

Underwriting issues: Underwriting is optional if the issue is made to the public and should not include reserved or preferential quota or employees' quota. If the subscription is not up to 90% of the total issue from the public including contribution of underwriters, the public should be refunded of their subscription within 120 days from the date of opening the issue. The compulsory underwriting provision was also waived for smaller issues.

Composite issues: Issues to the public by existing company can be priced differently as compared to the rights issued to shareholders.

FCD & PCD: The issues of Fully Convertible Debentures (FCDs) with a conversion period of more than 36 months will not be permissible unless conversion is optional. In case FCDs are convertible after 18 months, credit rating is compulsory; credit rating is now made compulsory for all issues made to public, other than equity. In case, the non-convertible portion of the Partially Convertible Debentures is to be rolled over, non-maturing debenture holders should have option to withdraw from the scheme.

New Financial Instruments: The terms and conditions of the new instrument such as Deep Discount Bonds, debentures with warrants and secured premium notes etc. Should be disclosed clearly so that the investor can assess the risk and return scenario of the instrument.

Reservation in issues: The unreserved portion offered to public should not be less than the minimum required for listing purposes. Preferential allotment can be made to promoters, companies and shareholders of those companies, NRIs, employees and associate companies of the same group. The allotment shall be subject to a lock in period of three years, if it is made on firm basis, outside public issue.

Deployment of issue proceeds: Where the total proceeds exceed Rs.250 crores, the company will voluntarily disclose the arrangements made to utilize proceeds. When the total issue proceeds exceed Rs.500 crores, there is need for making compulsory disclosure and for the financial institutions to monitor the deployment of funds, to the stock exchanges.

Minimum interval between two issues: 12 months should elapse between the public or rights issue and bonus issue. The promoters should bring in their share of the capital before the public issue.

Employee's stock option scheme: The reservation for employees should not be more than 10% at present and this quota is non-transferable for 3 years and subject to a maximum allotment of 200 shares per employee, and the lock in was removed later.

The Lock in period for Promoters' quota is 5 years and the lock in period for preferential allotment for associates and friends is 3 years.

Bonus shares: Bonus issues are to be made out of free reserves, the share premium collected in cash, Development Rebate Reserves and Investment Allowance Reserve. Contingent liabilities disclosed in the audited accounts should be deducted from net profit for calculation of residual reserves. Residual reserves after the bonus issues should be at least 40% of the increased paid-up capital. 30% of the average profits before tax for the previous 3 years should yield a rate of dividend of 10% on the expanded capital base. Reserves out of revaluation should not be used for bonus payment. Bonus issue cannot be made in lieu of dividends, and if there are partly paid up shares; no bonus issue is permitted. Expanded paid-up capital after bonus issue should not exceed authorized share capital. When a company has PCD or FCD, pending conversion, no bonus issue can be made unless this right is kept open to the holders of FCD and PCD falling due for conversion within 12 months.

Debenture issues: All debentures, which have a life of more than 18 months, should have a DRR created by company out of profits. DRR should be created only for non-convertible portion of the debentures. Contribution to DRR should commence from the date of commercial production and when there are profits after tax, interest and depreciation. The DRR will be considered as a part of the general reserves for payment of the bonus issues. DRR should be created and maintained at 50% of the amount of the debentures before repayment starts. The company should have already redeemed some liability. DRR and the creation of Debentures Trust are necessary only if the debentures have a maturity period exceeding 18 months. The Lead Institution for each issue should monitor the use of debenture funds either from the working capital or from the project finance.

The SEBI now insists on prior licensing of debenture Trustees; Trust deed should be ready within 6 months from the date of allotment. Recent amendment: By a recent amendment to Listing Agreement, the Companies have been asked to provide unabridged Balance Sheet to Shareholders. The companies have to give the disposition of the funds raised in public issues and compare the actual with targets every six months, when they present balance sheet to investors.

Check your progress 11

1. __________guidelines were issued after the repeal of the CCI Act.
   a. SEBI
   b. RBI
2. Underwriting is ___________if the issue is made to the public and should not include reserved or preferential quota or employees' quota
   a. Compulsory
   b. optional

3.13 Let Us Sum Up

Here in this unit the main area of focus was capital market. Every effort has been made in order to make this topic interesting for the readers.

In this unit apart from discussing the meaning and functions of capital market the functions and types of capital market have been discussed. The various reforms that took place in capital market have even been discussed here. The issue mechanism has been discussed here in very detail. The capital market and scenario in India has also been discussed here in very detail.

After going through this unit the readers would sufficiently gain about the capital market.

3.14 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b)

Check your progress 2

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 3

Answers: (1-a), (2-b), (3-a)

Check your progress 4

Answers: (1-a), (2-b), (3-a)

Check your progress 5

Answers: (1-a), (2-b), (3-a)

Check your progress 6

Answers: (1-a), (2-b), (3-a)

Check your progress 7

Answers: (1-a), (2-b)

Check your progress 8

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 9

Answers: (1-a), (2-b)

Check your progress 10

Answers: (1-a), (2-b)

Check your progress 11

Answers: (1-a), (2-b)

3.15 Glossary

CCI guidelines: Guidelines issued by competition commission of India.

3.16 Assignment

What is capital market? How does it differ from money market?

3.17 Activities

Discuss the various reforms in capital market.

3.18 Case Study

Discuss the various intermediaries in capital market

3.19 Further Readings

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UNIT 4: SECONDARY CAPITAL MARKET

Unit Structure

4.0 Learning Objectives

After learning this unit, you will be able to understand:

- Functions of Secondary Market.
- Post Reforms Stock Market Scenario.
- Organization Management and Membership of Stock Exchange.
- Listing of Securities.
- Trading Arrangements.
- Stock Market Index.
- Stock Exchanges in India.

4.1 Introduction

The secondary market known as stock market or stock exchange plays an equally important role in mobilising long-term funds by providing the necessary liquidity to holdings in shares and debentures. It provides a place where these securities can be encashed without any difficulty and delay. It is an organised market where shares and debentures are traded regularly with high degree of transparency and security. In fact, an active secondary market facilitates the growth of primary market as the investors in the primary market are assured of a continuous market for liquidity of their holdings. The major players in the primary market are merchant bankers, mutual funds, financial institutions, and the individual investors; and in the secondary market you have all these and the stockbrokers who are members of the stock exchange who facilitate the trading.

4.2 Functions of Secondary Market

Some of the Important Functions of Stock Exchange/Secondary Market are listed below:

1. Economic Barometer:

A stock exchange is a reliable barometer to measure the economic condition of a country. Every major change in country and economy is reflected in the prices of shares. The rise or fall in the share prices indicates the boom or recession cycle of the economy. Stock exchange is also known as a pulse of economy or economic mirror which reflects the economic conditions of a country.

2. Pricing of Securities:

The stock market helps to value the securities on the basis of demand and supply factors. The securities of profitable and growth oriented companies are valued higher as there is more demand for such securities. The valuation of securities is useful for investors, government and creditors. The investors can know the value of their investment, the creditors can value the creditworthiness and government can impose taxes on value of securities.

3. Safety of Transactions:

In stock market only the listed securities are traded and stock exchange authorities include the companies names in the trade list only after verifying the soundness of company. The companies which are listed they also have to operate within the strict rules and regulations. This ensures safety of dealing through stock exchange.

4. Contributes to Economic Growth:

In stock exchange securities of various companies are bought and sold. This process of disinvestment and reinvestment helps to invest in most productive investment proposal and this leads to capital formation and economic growth.

5. Spreading of Equity Cult:

Stock exchange encourages people to invest in ownership securities by regulating new issues, better trading practices and by educating public about investment.

6. Providing Scope for Speculation:

To ensure liquidity and demand of supply of securities the stock exchange permits healthy speculation of securities.

7. Liquidity:

The main function of stock market is to provide ready market for sale and purchase of securities. The presence of stock exchange market gives assurance to investors that their investment can be converted into cash whenever they want. The investors can invest in long term investment projects without any hesitation, as because of stock exchange they can convert long term investment into short term and medium term.

8. Better Allocation of Capital:

The shares of profit making companies are quoted at higher prices and are actively traded so such companies can easily raise fresh capital from stock market. The general public hesitates to invest in securities of loss making companies. So stock exchange facilitates allocation of investor's fund to profitable channels.

9. Promotes the Habits of Savings and Investment:

The stock market offers attractive opportunities of investment in various securities. These attractive opportunities encourage people to save more and invest in securities of corporate sector rather than investing in unproductive assets such as gold, silver, etc.

Check your progress 1

1. A __________exchange is a reliable barometer to measure the economic condition of a country.

   a. Stock

   b. money

2. The ___________helps to value the securities on the basis of demand and supply factors.

   a. banks

   b. stock market

3. The main function of ___________is to provide ready market for sale and purchase of securities.

   a. stock market

   b. banks

4.3 Post Reforms Stock Market Scenario

After the initiation in 1991 the Indian secondary market now has a three tier form.

1) Regional stock exchanges

2) National Stock Exchange (NSE)

3) Over the Counter Exchange of India (OTCEI)

The NSE was set up in 1994. It was the first modern stock exchange to bring in new technology, new trading practices, new institutions, and new products. The OTCEI was set up in 1992 as a stock exchange providing small and medium sized companies the means to generate capital.

In all, there are, at present 23 stock exchanges in India – 19 regional stock exchanges, BSE, NSE, OTCEI and the Inter connected Stock Exchange of India (ISE). The ISE is a stock exchange of stock exchanges. The 19 regional stock exchanges are located at Ahmedabad, Bangalore, Bhubaneswar, Kolkata. Cochin, Coimbatore, Delhi, Guwahati, Hyderabad, Indore, Jaipur, Kanpur, Ludhiana, Chennai, Mangalore, Pune, Patna, Rajkot and Vadodara. They operate under the rules, by laws and regulations approved by the government and SEBI.

Check your progress 2

1. The NSE was set up in __________.
   a. 1984
   b. 1994
2. In all, there are, at present__________stock exchanges in India.
   a. 17
   b. 23

4.4 Organization, Management and Membership of Stock Exchange

National Stock Exchange of India (NSEI) commenced operations in Whole-sale Debt Market (WDM) in June 1994 and trading in equities has been started in the Capital Market Segment (CM) in November 1994. A large number of members are successfully trading from their respective offices through NSEI's Very Small Aperture Terminal (VSAT) based satellite network. The exchange has opened membership to 13 cities including Mumbai and operations from other cities are expected to commence shortly.

As a national exchange it has set fairly stringent criteria for membership in terms of net worth, education and experience, to ensure that trading members are well capitalised and can provide other professional services to investors.

The main participant in WDM regiment (Government Securities, Treasury Bills, PSU Bonds, CDs, CPs and Corporate debentures) are banks, financial institutions and large corporate, RBI has recently directed banks to use only the NSEI for all transactions in debt securities done earlier through brokers to ensure transparency and facilitate regulations. This has raised the volumes of NSEI's debt trade substantially.

Check your progress 3

1. National Stock Exchange of India (NSEI) commenced operations in Whole-sale Debt Market (WDM) in June ____________.
   a. 1994
   b. 1984

4.5 Listing of Securities

Listing means admission of securities to dealings on a recognized stock exchange. The securities may be of any public limited company, Central or State Government, quasi-governmental and other financial institutions/corporations, municipalities, etc.

The objectives of listing are mainly to:

- provide liquidity to securities
- mobilize savings for economic development
- protect interest of investors by ensuring full disclosures

A company, desirous of listing its securities on the Exchange, shall be required to file an application, in the prescribed form, with the Exchange before issue of Prospectus by the company, where the securities are issued by way of a prospectus or before issue of 'Offer for Sale', where the securities are issued by way of an offer for sale.

Delisting of securities means permanent removal of securities of a listed company from the stock exchange where it was registered. As a result of this, the company would no longer be traded at that stock exchange.+

Companies Act, 1956.

As per S. 73 of the companies Act, 1956, a company seeking listing of its securities on a stock exchange is required to submit a Letter of application to all the stock exchanges where it proposes to have its securities listed before filing the prospectus with the registrar of companies.

SEBI Guidelines.

a. A company is required to complete the allotment of securities offered to the public within 30 days of the date of closure of the subscription list and approach the designated stock exchange for approval of the basis of allotment.

b. Issuer company to complete the formalities for trading at all the stock exchanges where the securities are to be listed within 7 working days of finalization of the basis of allotment.

c. Companies making public/rights issues are required to deposit 1 % of the issue amount with the designated stock exchange before the issue price.

Stock Exchange guidelines.

In addition to all these rules, regulation and compliance every stock exchange have a set of guidelines of its own for the companies to be listed on them. For example they may provide for the minimum issue size and market capitalization of the company

A company has to enter into a listing agreement before being given permission to be listed on the exchange. Under this agreement the company undertakes amongst other things, to provide facilities for prompt transfer, registration, sub-division and consolidation of securities: to give proper notice of closure of transfer books and record dates, to forward 6 copies of unabridged Annual reports, balance sheets and profit & loss accounts, to file shareholding patters and financial results on quarterly basis and to intimate promptly to the exchange the happenings which are likely to materially affect the financial performance of the company and its stock price and to comply with the conditions of Corporate governance.

The companies are also required to pay to the exchange some listing fee as prescribed by the exchange every financial year.

A company not complying with these requirements are may face some disciplinary action, including suspension/ delisting of their securities.

In case the exchange does not give permission to the company for listing of securities, the company cannot proceed with the allotment of shares. However the company may file an appeal before SEBI under S. 22 of SCRA, 1956.

A company delisted by a stock exchange and seeking relisting at the same exchange is required to make a fresh public offer and comply with the extant guidelines of the exchange.

Delisting

As stated above delisting of securities means removal of the securities of a listed company from the stock exchange. It may happen either when the company does not comply with the guidelines of the stock exchange, or that the company has not witnessed trading for years, or that it voluntary wants to get delisted or in case of merger or acquisition of a company with/by some other company. So, broadly it can be classified under two head:

1. Compulsory delisting.
2. Voluntary delisting.

Compulsory delisting refers to permanent removal of securities of a listed company from a stock exchange as a penalizing measure at the behest of the stock exchange for not making submissions/comply with various requirements set out in the Listing agreement within the time frames prescribed. In voluntary delisting, a listed company decides on its own to permanently remove its securities from a stock exchange. This happens mainly due to merger or amalgamation of one company with the other or due to the non-performance of the shares on the particular exchange in the market.

Check your progress 4

1. _______means admission of securities to dealings on a recognized stock exchange.
   a. Listing
   b. Delisting
2. ________of securities mean permanent removal of securities of a listed company from the stock exchange where it was registered.
   a. Listing
   b. Delisting
3. Compulsory delisting refers to ________removal of securities of a listed company from a stock exchange as a penalizing measure at the behest of the stock exchange
   a. Permanent
   b. temporarily

4.6 Trading Arrangements

During the second half of the 1990's, trade liberalization and the pursuit of global free trade underwent a metamorphosis. The political momentum shifted away from what was seen by some nations as the painstakingly slow process of multilateral tariff negotiations to smaller regional and bilateral arrangements - the Regional Trade Agreement.

RTAs are not a new means of trade liberalization; historically, whenever multilateral trade negotiations broke down, bilateral and multilateral free trade agreements filled the void. Such strategic trade arrangements have enabled many states to move towards freer trade at their own pace, and for their own benefits.

Check your progress 5

1. ______ are not a new means of trade liberalization.
   a. RTA
   b. TRA

4.7 Stock Market Index

A stock index or stock market index is a measurement of the value of a section of the stock market. It is computed from the prices of selected stocks (typically a weighted average). It is a tool used by investors and financial managers to describe the market, and to compare the return on specific investments. An index is a mathematical construct, so it may not be invested in directly. But many mutual funds and exchange-traded funds attempt to "track" an index, and those funds that do not may be judged against those that do.

Some indices, such as the S&P 500, have multiple versions. These versions can differ based on how the index components are weighted and on how dividends are accounted for. For example, there are three versions of the S&P 500 index: price return, which only considers the price of the components, total return, which accounts for dividend reinvestment, and net total return, which accounts for dividend reinvestment after the deduction of a withholding tax. As another example, the Wilshire 4500 and Wilshire 5000 indices have five versions each: full capitalization total return, full capitalization price, float-adjusted total return, float-adjusted price, and equal weight. The difference between the full capitalization, float-adjusted, and equal weight versions is in how index components are weighted.

Check your progress 6

1. A _______ is a measurement of the value of a section of the stock market.
   a. stock index
   b. Stock

2. An____________is a mathematical construct, so it may not be invested in directly.

   a. share

   b. index

4.8 Stock Exchanges in India

The first organised stock exchange in India was started in Mumbai known as Bombay Stock Exchange (BSE). It was followed by Ahmedabad Stock Exchange in 1894 and Kolkata Stock Exchange in 1908. The number of stock exchanges in India went up to 7by 1939 and it increased to 21 by 1945 on account of heavy speculation activity during Second World War. A number of unorganised stock exchanges also functioned in the country without any formal set-up and were known as kerb market. The Security Contracts (Regulation) Act was passed in 1956 for recognition and regulation of Stock Exchanges in India. At present we have 23 stock exchanges in the country. Of these, the most prominent stock exchange that came up is National Stock Exchange (NSE). It is also based in Mumbai and was promoted by the leading financial institutions in India. It was incorporated in 1992 and commenced operations in 1994. This stock exchange has a corporate structure, fully automated screen-based trading and nation-wide coverage.

Another stock exchange that needs special mention is Over The Counter Exchange of India (OTCEI). It was also promoted by the financial institutions like UTI, ICICI, IDBI, IFCI, LIC etc. in September 1992 specially to cater to small and medium sized companies with equity capital of more than Rs.30 lakh and less than Rs.25 crore. It helps entrepreneurs in raising finances for their new projects in a cost effective manner. It provides for nationwide online ring less trading with 20 plus representative offices in all major cities of the country. On this stock exchange, securities of those companies can be traded which are exclusively listed on OTCEI only. In addition, certain shares and debentures listed with other stock exchanges in India and the units of UTI and other mutual funds are also allowed to be traded on OTCEI as permitted securities. It has been noticed that, of late, the turnover at this stock exchange has considerably reduced and steps have been afoot to revitalise it. In fact, as of now, BSE and NSE are the two Stock Exchanges, which enjoy nation-wide coverage and handle most of the business in securities in the country.

Check your progress 7

1. The first organized stock exchange in India was started in Mumbai known as ____________.
   a. BSE
   b. NSE
2. The Security Contracts (Regulation) Act was passed in___________for recognition and regulation of Stock Exchanges in India.
   a. 1985
   b. 1956

4.9 Let Us Sum Up

This unit intends to explain the secondary capital market to its readers in very detail.

In this unit the functions of secondary market has been discussed in very detail. The post reform stock market scenario has been discussed here in very detail. Membership and management of stock exchange was also discussed here in very detail. Listing of securities and trading arrangements have been discussed here in very detail. Apart from this stock market index was also explained here in detail. A detailed note of account has been made on stock exchanges of India.

This unit is going to be of great help for the readers in understanding the secondary capital market in very detail.

4.10 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b), (3-a)

heck your progress 2

Answers: (1-a), (2-b)

Check your progress 3

Answers: (1-a)

Check your progress 4

Answers: (1-a), (2-b), (3-a)

Check your progress 5

Answers: (1-a)

Check your progress 6

Answers: (1-a), (2-b)

Check your progress 7

Answers: (1-a), (2-b)

4.11 Glossary

1. **Secondary market -** is the financial market in which previously issued financial instruments such as stock, bonds, options, and futures are bought and sold.

4.12 Assignment

Explain secondary market and its functions.

4.13 Activities

Write a note on post reform stock market scenario.

4.14 Case Study

What do you understand by stock market index.

4.15 Further Readings

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Block Summary

This block intends to explain financial market, capital market and money market.

In this block we have learnt that Financial market is the market that facilitates transfer of funds between investors/lenders and borrowers/ users. It deals in financial instruments like bills of exchange, shares, debentures, bonds, etc. It provides security to dealings in financial assets, liquidity to financial assets for investors and ensures low cost of transitions and information.

Financial Markets can be classified as (1) Money market and (2) Capital market. Money market refer to the network of financial institutions dealing in short term funds through instruments like bills of exchanges, promissory notes, commercial paper, treasury bills, etc. Here we learnt that Capital Market is an institutional arrangement for borrowing medium and long-term funds and which provides facilities for marketing and trading of securities. So it constitutes all long-term borrowings from banks and financial institutions, borrowings from foreign markets and raising of capital by issue various securities such as shares debentures, bonds, etc. The securities market has two different segments namely primary and secondary market. The primary market consists of arrangements for procurement of long-term funds by companies by fresh issue of shares and debentures. The secondary market or stock exchange provides a ready market for existing long term securities. Stock exchange is the secondary market, which provides a place for regular sale and purchase of different types of securities like shares, debentures, bonds & government securities. It is an organised market where all transactions are regulated by the rules and laws of the concerned stock exchanges.

The functions of stock exchanges are to provide ready and continuous market for securities, information about prices and sales, safety to dealings and investment, helps mobilisation of savings and capital formation. It acts as a barometer of economic and business conditions and helps in better allocation of funds. Stock exchanges provide many benefits to companies, investors and the society as a whole. But they also suffer from limitations like exclusive speculation and fluctuation in prices due to rumours and unpredictable events.

This block is certainly going to be of great help in making the readers in understanding the basic concept of financial market in India.

Block Assignment

Short Answer Questions

Write a short note on:-

1. Listing of securities.
2. ADR, GDR.
3. Financial market.
4. Capital market.
5. Primary market and secondary market.

Long Answer Questions

1. Discuss the development of money market in India.
2. Discuss the various money market instruments.
3. Explain the various types of issues in capital market.
4. Discuss the various types of capital market.
5. Define stock exchange and explain its functions.
6. Explain the importance of stock exchanges from the points of view of companies and investors.
7. Explain the role played by SEBI in protecting investors' interests and controlling the business at stock exchange.
8. Write a note on stock exchanges in India.

Enrolment No. [ ]

1. How many hours did you need for studying the units?

Unit No	**1**	**2**	**3**	**4**
Nos of Hrs				

2. Please give your reactions to the following items based on your reading of the block:

Items	Excellent	Very Good	Good	Poor	Give specific example if any
Presentation Quality	☐	☐	☐	☐	________
Language and Style	☐	☐	☐	☐	________
Illustration used (Diagram, tables etc)	☐	☐	☐	☐	________
Conceptual Clarity	☐	☐	☐	☐	________
Check your progress Quest	☐	☐	☐	☐	________
Feed back to CYP Question	☐	☐	☐	☐	________

3. Any Other Comments

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Education is something which ought to be brought within the reach of every one.

- Dr. B. R. Ambedkar

Dr. Babasaheb Ambedkar Open University
'Jyotirmay Parisar', Opp. Shri Balaji Temple, Sarkhej-Gandhinagar Highway, Chharodi,
Ahmedabad-382 481.

FINANCIAL MARKETS

PGDF-103

BLOCK 2:

FINANCIAL SERVICE, CONSUMER BEHAVIOUR AND BANKING PRODUCTS

Dr. Babasaheb Ambedkar Open University
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FINANCIAL MARKETS

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ROLE OF SELF INSTRUCTIONAL MATERIAL IN DISTANCE LEARNING

The need to plan effective instruction is imperative for a successful distance teaching repertoire. This is due to the fact that the instructional designer, the tutor, the author (s) and the student are often separated by distance and may never meet in person. This is an increasingly common scenario in distance education instruction. As much as possible, teaching by distance should stimulate the student's intellectual involvement and contain all the necessary learning instructional activities that are capable of guiding the student through the course objectives. Therefore, the course / self-instructional material are completely equipped with everything that the syllabus prescribes.

To ensure effective instruction, a number of instructional design ideas are used and these help students to acquire knowledge, intellectual skills, motor skills and necessary attitudinal changes. In this respect, students' assessment and course evaluation are incorporated in the text.

The nature of instructional activities used in distance education self-instructional materials depends on the domain of learning that they reinforce in the text, that is, the cognitive, psychomotor and affective. These are further interpreted in the acquisition of knowledge, intellectual skills and motor skills. Students may be encouraged to gain, apply and communicate (orally or in writing) the knowledge acquired. Intellectual-skills objectives may be met by designing instructions that make use of students' prior knowledge and experiences in the discourse as the foundation on which newly acquired knowledge is built.

The provision of exercises in the form of assignments, projects and tutorial feedback is necessary. Instructional activities that teach motor skills need to be graphically demonstrated and the correct practices provided during tutorials. Instructional activities for inculcating change in attitude and behavior should create interest and demonstrate need and benefits gained by adopting the required change. Information on the adoption and procedures for practice of new attitudes may then be introduced.

Teaching and learning at a distance eliminates interactive communication cues, such as pauses, intonation and gestures, associated with the face-to-face method of teaching. This is particularly so with the exclusive use of print media. Instructional activities built into the instructional repertoire provide this missing interaction between the student and the teacher. Therefore, the use of instructional activities to affect better distance teaching is not optional, but mandatory.

Our team of successful writers and authors has tried to reduce this.

Divide and to bring this Self Instructional Material as the best teaching and communication tool. Instructional activities are varied in order to assess the different facets of the domains of learning.

Distance education teaching repertoire involves extensive use of self-instructional materials, be they print or otherwise. These materials are designed to achieve certain pre-determined learning outcomes, namely goals and objectives that are contained in an instructional plan. Since the teaching process is affected over a distance, there is need to ensure that students actively participate in their learning by performing specific tasks that help them to understand the relevant concepts. Therefore, a set of exercises is built into the teaching repertoire in order to link what students and tutors do in the framework of the course outline. These could be in the form of students' assignments, a research project or a science practical exercise. Examples of instructional activities in distance education are too numerous to list. Instructional activities, when used in this context, help to motivate students, guide and measure students' performance (continuous assessment)

PREFACE

We have put in lots of hard work to make this book as user-friendly as possible, but we have not sacrificed quality. Experts were involved in preparing the materials. However, concepts are explained in easy language for you. We have included many tables and examples for easy understanding.

We sincerely hope this book will help you in every way you expect.

All the best for your studies from our team!

FINANCIAL MARKETS

Contents

BLOCK 2: FINANCIAL SERVICE, CONSUMER BEHAVIOUR AND BANKING PRODUCTS

UNIT 1 FINANCIAL SERVICES: AN INTRODUCTION

Introduction, Meaning and Concept, Characteristics of Financial Services, Evolution of Financial Services in India, Significance of Financial Services, Types of Financial Services, Impact of Technology, Challenges before the Financial Services Sector

UNIT 2 MARKETING OF FINANCIAL SERVICES: A CONCEPTUAL FRAMEWORK

Introduction, Marketing and the Financial Services, Marketing as a Functional Area of Management, Financial Services and the Different Marketing Orientations, Difference between Services and Products Physical Goods, Characteristics of Service, Marketing Mix for Financial Services, Marketing Strategy and Financial Services

UNIT 3 CONSUMER BEHAVIOUR FOR FINANCIAL SERVICES

Introduction, The Complexity of Consumer Buying Decisions, Individual Influences on Consumer Behaviour, Needs and Motives, Individual Perception, Learning and Habit Development, Family Influences on Buying Behaviour, Behavioural Models for Analyzing Buyers, Consumer Behaviour Some Learning Points for Financial Service

UNIT 4 BANKING PRODUCTS AND SERVICES

Introduction, Nature of Product, Products and Services in Banking, Elements of Product Mix, Product Life Cycle and Product Strategies, Using Product Life Cycle lo Manage Marketing of Banking Products, New Product Development, Branding in Bank Marketing, Process and Product Development Cycle for Banking Services, Product Development

BLOCK 3: DISTRIBUTION, PRICING, RETAINING CUSTOMERS AND CONSULTANCY SERVICES

UNIT 1 DISTRIBUTION, PRICING AND PROMOTIONS STRATEGY FOR BANKING SERVICES

Introduction, Banking Services and Issues in Delivery, Channels of Distribution for Banks, Types of Branches, Electronic Methods of Distributing Financial Services, Pricing of Banking Products/Services, Pricing Objectives, Pricing Methods, Pricing Reviews and Committees, Price Setting in Practice, Promotion of Banking Products/Services, Guidelines on Advertising by Public Sector Banks, Sales Promotion, Internal Communication, Marketing Information Systems (MIS)

UNIT 2 ATTRACTING AND RETAINING CUSTOMERS IN BANKING SERVICES

Introduction, Defining Customer Value and Satisfaction, Factors Influencing Consumer Behaviour in Banking, Relationship Marketing and Attracting Customers, Customer Relationships Management, Retaining Customers Through Quality, Service and Values , Delivering Customer Value and Satisfaction, Image as a Managed Perception, Fulfilling Promises : Internal and Interactive Marketing, Customer Service and Customer Care, Bank Marketing : Future Challenges

UNIT 3 ADVISORY AND CONSULTANCY SERVICES

Introduction, Portfolio Management, Credit Rating, Takeovers and Mergers, Trustee Services, Depository Services, The Marketing Approach for Merchant Banking Services

BLOCK 4: MARKETING OF PENSION FUNDS AND GLOBALIZATION

UNIT 1 MARKETING OF PENSION FUNDS

Introduction, Emerging Dimensions Relating to Investment Services, Pension Funds: A General Overview, Why Pension Plan?, Types of Pension Plan, Pension Fund Risk, Funds Management, Pension Fund Investment: General Guidelines, Pension Funds and Capital Markets, Pension Funds: Some Related Statistics

UNIT 2 GLOBALISATION AND ITS IMPACT ON FINANCIAL SERVICES MARKETS

Introduction, Globalisation of Financial Markets and its Impact on Local Markets, Globalisation of Markets: The Main Drivers, Globalisation of Markets: The Road Ahead, Some Asian Trends, Globalisation and Consumer Orientation, The Emerging Imperatives for Financial Services

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PGDF-103

FINANCIAL MARKETS

BLOCK 2: FINANCIAL SERVICE, CONSUMER BEHAVIOUR AND BANKING PRODUCTS

BLOCK 2: FINANCIAL SERVICE, CONSUMER BEHAVIOUR AND BANKING PRODUCTS

Block Introduction

As we are progressing the area of production has been increasing, gone are the days when only products which are tangible in nature used to be produced. Now a day the production of services is immensely rising and because of this the importance of this subject can never be underestimated.

In this block we will be discussing about the financial services and the conceptual framework of marketing of financial services. In this unit we will be discussing in very detail about the meaning and importance of financial services. We will be discussing the various types of financial services.The challenges before the financial services sector, the concept of service product mix. The marketing of financial services shall also be discussed here in detail. In this block we will be discussing in very detail about the consumer behaviour for financial services. The study of this topic is very important for the analysts of finance sector. In the fourth unit we will be discussing in very detail about the products of banking industry. Here we shall be discussing the various products of banking industry in very detail.

After going through this unit the students will be confident enough about the basics of financial services the marketing of this sector.

Block Objective

After learning this block, you will be able to understand:

- The importance of financial services
- The types of financial services
- The concept of service product mix in financial service sector

Block Structure

UNIT 1: FINANCIAL SERVICES: AN INTRODUCTION

Unit Structure

1.0 Learning Objectives

After learning this unit, you will be able to understand:

- Explain the concept and meaning of financial services.
- Discuss the significance of financial services.
- Describe the various types of financial services.
- Explain the impact of technology on the financial services sector.
- Enumerate the challenges before the financial services sector.

1.1 Introduction

The financial system is a very complex system dealing with a vast variety of financial activities. The financial system consists of Financial Institutions, Financial Markets and Financial Instruments and the Financial Services, The first component of the Financial System, i.e. the Financial Markets, has been discussed in the first unit.

Financial Markets and Financial Institutions facilitate the functioning of the Financial System through Financial Instruments. The financial markets play a very significant role as far as the transfer of funds (financial assets) from surplus units to deficit units is concerned. This transfer of funds from lenders to borrowers is facilitated by banks and non-banking institutions, as well as various other agencies participating in the market.

In unit 2, we have already studied about the major participants in the Money Market and the Capital Market. Financial Services, the fourth component of the financial system around which this particular course revolves, is a very popular area for study these days. It is rather, highly diverse functional area requiring a great degree of competence and knowledge in a wide range of relevant disciplines. However, in this unit we will be briefly discussing about the various aspects of the financial services and also the challenges this sector is posed with.

1.2 Meaning and Concept

The Financial Services Sector per se has become known in the past 25-30 years, although the concept of financial services has been in existence since times immemorial. However, there is no straight forward definition for the term Financial Services, but if we look at the meaning of the term ‘financial services’ as it is applied in UK, it could be understood to be including banking, insurance, stock broking and investment services as well as a wide range of other business and professional services. In other words, what we can say is that financial services are services that ensure the smooth flow of financial activities in the economy.

Financial services are an important component of the financial system. They cater to the needs of financial institutions, financial markets and financial instruments which are geared to serve individual and institutional investors. Financial institutions and financial markets facilitate functioning of the financial system through financial instruments. In order to fulfill the tasks assigned, they require a number of services of financial nature and hence financial services are regarded as the fourth element of the financial system. Thus, functioning of the financial system depends to a great deal on the range of financial services extended by the providers, and their efficiency and effectiveness.

Financial services include the services offered by both Asset Management Companies and the Liability Management Companies. The asset management companies are viz. leasing companies, mutual funds, merchant bankers and issue/ portfolio managers. Bill discounting houses and acceptance houses come under the liability management companies. Technological innovation and globalization has brought about a key change in the financial services sector, i.e. the convergence occurring within the sector. Similar services are now being offered by different players.

Financial services not only help to raise the required funds but also ensure their efficient deployment. They assist in deciding the financing mix and extend their services up to the stage of servicing of lenders. In order to ensure an efficient management of funds, services such as bill discounting, factoring of debtors, parking of short-term funds in the money market, e-commerce and securitisation of debts are provided by financial services firms. This sector provides services such as banking, insurance, credit rating, lease financing, factoring, venture capital, mutual funds, merchant banking, stock lending, depository services, housing finance, etc. These services are provided by various institutions like stock exchanges, specialised and general financial institutions, and non-banking finance companies, subsidiaries of financial institutions, banks and insurance companies.

Financial services sector is regulated by the Securities and Exchange Board of India (SEBI), Reserve Bank of Indiaand the Department of Banking and Insurance, Government of India, through a plethora of legislations

Check your progress 1

1. Financial services not only help to raise the required funds but also ensure their efficient ______________.
   a. Deployment
   b. Growth
2. Financial services sector is regulated by the _____________.
   a. RBI
   b. SEBI

3. Financial institutions and financial markets facilitate functioning of the financial system through financial____________.
   a. Instruments
   b. Institutions

1.3 Characteristics of Financial Services

Financial services are quite distinct in nature from the other services. The services provided by the financial institutions have some typical characteristics that make these products quite distinct from the products turned out by the industrial enterprises. Some of the basic characteristics of financial services are as discussed:

1. **Customer-Specific:** Financial services are usually customer focussed. The firms providing these services, study the needs of their customers in detail before deciding their financial strategy, giving due regard to costs, liquidity and maturity considerations. Financial services firms continuously remain in touch with their customers, so that they can design products which can cater to the specific needs of their customers. The providers of financial services constantly carry out market surveys, so they can offer new products much ahead of need and impending legislation. Newer technologies are being used to introduce innovative, customer friendly products and services which clearly indicate that the concentration of the providers of financial services is on generating firm/customer specific services.

2. **Intangibility:** In a highly competitive global environment brand image is very crucial. Unless the financial institutions providing financial products and services have good image, enjoying the confidence of their clients, they may not be successful. Thus institutions have to focus on the quality and innovativeness of their services to build up their credibility.

3. **Concomitant:** Production of financial services and supply of these services have to be concomitant. Both these functions i.e. production of new and innovative financial services and supplying of these services are to be performed simultaneously.

4. **Tendency to Perish:** Unlike any other service, financial services do tend to perish and hence cannot be stored. They have to be supplied as required by the customers. Hence financial institutions have to ensure a proper synchronization of demand and supply.

5. **People based services:** Marketing of financial services has to be people intensive and hence it's subjected to variability of performance or quality of service. The personnel in financial services organisation need to be selected on the basis of their suitability and trained properly, so that they can perform their activities efficiently and effectively.

6. **Market Dynamics:** The market dynamics depends to a great extent, on socioeconomic changes such as disposable income, standard of living and educational changes related to the various classes of customers. Therefore financial services have to be constantly redefined and refined taking into consideration the market dynamics. The institutions providing financial services, while evolving new services could be proactive in visualising in advance what the market wants, or being reactive to the needs and wants of their customers

Check your progress 2

1. Financial services are usually _____________focused.
   a. Customer
   b. Service provider
2. Production of financial services and supply of these services have to be _____________.
   a. unrelated
   b. Concomitant

1.4 Evolution of Financial Services in India

The financial services industry in India is in the process of attaining full bloom. To reach the present position, it has passed through a number of stages as mentioned below:

The Stage of Infancy:

This existed between 1960 and 1980 and covered in its gamut merchant banking insurance and leasing services.

Merchant Banking Services were unknown until the early 1960s. The policy makers and researchers had lack of clarity about the term "merchant bankers".

Someone defined them as institutions which were acting; neither as merchants nor as bankers. However the term was used as an umbrella function, providing a wide range of services, starting from project appraisal to arranging funds from bankers. The merchant bankers are expected to identify projects, prepare feasibility reports, develop detailed project reports, and in doing so conduct marketing, managerial, financial, and technical analyses. Having done this, they are approached to garner project finance, and in order to do this resolve the problem's of capital structuring. They are asked to act as abridge between the capital market and the fund-seeking institutions. They underwrite the issues and become subject to developments in case such issues are not fully subscribed. They assist the enterprises in getting listed on the stock exchanges. They offer legal advice on registration of companies and removing legal tangles. They provide advice and help in mergers and acquisitions. They give technical advice on leveraged - buyouts and takeovers. Recently they have added the syndication activity in their portfolio, wherein they form a syndicate or become a part of it to raise project finance. They arrange working capital loans and manage the risk element present in the form of general risk which is covered by the insurance policies of the General Insurance Company.

Investment companies such as the Unit Trust of India, the life insurance business initiated by the Life Insurance Corporation of India, and the general insurance business, also made their mark in the first stage of financial services. During this period, the Life Insurance Corporation of India has grown as a public monopoly. Prior to its setting up, the private sector was operating the life insurance business.The general insurance business was nationalised in the early 1970s. A holding company was set up with four subsidiaries to handle the general insurance business in the public sector. Suggestions were given very frequently to privatise the insurance business, as in no way could the insurance business be considered as a national monopoly.

Leasing made its mark in the closing years of the 1970s. Initially such companies were engaged in equipment lease financing. Later, they undertook leasing operations of different kinds, including financial, operating and wet leasing. During this period the number of leasing firms has shot up to a high of 400. The reorganisation of such firms due to their non-viability later led to a contraction in their numbers.

Modern Financial Services:

Financial services have entered the second rung during the later part of the 1980s. Over the counter services, share transfers, pledging of shares, mutual funds, factoring, discounting, venture capital, and credit rating, constitute some of the modern financial services. In the West, these services emerged on the scene about 100 years back. The mutual fund business is the major provider of funds to industry anywhere in the developed countries. The mutual funds there have been innovative in terms of schemes.They have been giving stable rate of return. Their asset and liability management is transparent. The small investor is secure in their hands. Their business policies are such that they create value for their investors.Investorsare not victimised by shifts in valuation policies, and efforts are made to harmonise the net asset valuation. The mutual funds have their own code of conduct.

Credit rating is another important financial service which made its mark in India in the mid-1980s. Credit rating boosts investor' confidence in capital market operations and prevents fly -by-night companies from making forays in the capital market. There was one credit rating company initially and we have ended up with eight finally. In terms of spread of the credit rating function, initially only debt instruments issues were covered. However later, instruments such as commercial papers and fixed deposits were brought under the purview of credit rating. Incidentally, there is a sovereign credit rating assigned by credit rating firms for the country. The Discount and Finance House of India Limited and a number of factoring institutions, such as State Bank of India Factors and Canbank Factors Ltd. Venture capital funds made their appearance in the late 1980s, Most of these firms have been operating in the public sector.

The Third Flush

The third flush in financial services includes the setting up of new institutions, and paving the way innovating new instruments and also their flotation.

The setting up of depositories has brought the India financial services industry in line with the global financial services industry. It has promoted the concept of paperless trading and resulted into dematerialisation of shares and bonds. The stock-lending scheme approved by the Central Government in 1997-98 budget and the setting up of a separate corporation to deal with the trading of the "Gilts" are innovative measures. The steps initiated to popularise book building in order to help both the investorsand fund users. The online trading interface by the Bombay Stock Exchange, the Delhi Stock Exchange, and computerisation of the National Stock Exchange, is acting as the fulcrum for the development of financial services arid is another major advancement in the field of financial services. This has given a fillip to paperless trading, save the investors from the onslaught of jobbers and brokers, and reduces tax evasion. The guidelines from the Securities and Exchange Board of India in relation to the capital adequacy ratio for the merchant bankers and their categorisation into different groups are a major advancement.

This will ensure investor protection and create a differentiation in the market place. The creation of the Securities and Exchange Board of India itself can be hailed as a path-breaking development in terms of regulation, growth, and development of financial services. The ongoing efforts to revamp the Companies Act, Income-Tax Act, etc. would also lead to the deliverance of effective financial services. The guidelines about permitting foreign financial institutions to operate in the Indian capital market will do a two-way good to the country In terms of enabling the foreign investors to plug into the Indian capital market, and the Indian investors and financial institutions to study the modus operandi of such firms.

Public enterprise disinvestments are sure to prop up the state-of-art in the realm of financial services. It would provide a fillip to the presence of foreign financial firms in India, as well as result into creating pressure on the Indian financial firms to master the disinvestment business. The financial services firms would have to gain expertise in valuation, financial and legal restructuring, and taking the public sector firms to the commercial and capital markets.

During this period financial services firms scouted for funds abroad to finance the Indian corporate sector. They have approached the European capital markets, the most prominent of which belong to the UK and Luxembourg. These portfolio investments have flowed to India through the GDR route. It requires an understanding of raising funds abroad and also working together with world level financial services institutions, such as Lehman Brothers, Arthur Anderson, and Goldman Sachs, to mention a few.

With the passage of the Insurance Regulatory and Development Authority (IRDA) Act, 1999, the Insurance Regulatory and Development Authority was set up with statutory powers to function as the regulator for the insurance sector in India. This act has opened the doors for private players including foreign equity participation up to a prescribed limit of paid up capital. It has come out with regulations on various aspects of insurance business such as licensing of agents, solvency margin for insurers, accounting norms, investment norms and registration of Indian Insurance Companies. RBI allowed banks to enter into the insurance business by issuing a notification specifying insurance as a permissible form of business under section 6(1) (o) of the Banking Regulation Act, 1949. Thus providing banks another avenue for generating fee based income.

New Financial Instruments:

The new financial instruments are both being talked about and are also being used. The critical factors governing the chemistry of the issuance of the new financial instruments relate to maturity, risk, and interest rate. Based on these, in Germany some 400 financial instruments have been innovated. In India, both the market players, such as mutual funds, banks, brokers, stock markets, and the regulators, including the Finance Ministry, the Reserve Bank of Indiaand the regulators, and the Securities and Exchange Board of India, have to make more efforts to create new funds and new instruments. One may like to mention in this case the very non cordial welcome given to securitisation.

The housing finance companies, automobile manufacturers, and development and commercial banks can use this method greatly to their advantage. However, only a few companies have devoted their mind to the application of this method. Both the market players and the regulators have for very long been engaged in the idea of setting up the derivatives market in India. When the Indian economy is trying to become global in nature, the fluctuations in the rate of foreign exchange would be a routine matter, and hence there would be a need for currency, interest, and commodity-based derivatives. Derivatives have now become increasingly important in the field of finance.Futures and options are now traded on many exchanges. Derivative instruments such as Forward Contracts, Swaps and many others are regularly traded both in the exchanges and in the over the counter market.

Check your progress 3

1. Merchant Banking Services were unknown until the early ___________.
   a. 1960s
   b. 1950s
2. Financial services have entered the second rung during the later part of the____________.
   a. 1960s
   b. 1980s

3. Credit rating is another important financial service which made its mark in India in the mid-___________.

    a. 1980s

    b. 1970s

1.5 Significance of Financial Services

The financial services sector plays a very crucial and significant role in a country's economy.

Growth and Development:

The financial sector now represents a significant proportion of the total economic activity in most economies. In most developed economies, the financial services sector has grown rapidly over the post-war period. In India, this sector has come up gradually after independence. However, after the liberalisation process initiated by the government, this sector saw a considerable growth.

When one examines the structure of most economies over the last few decades, the most striking feature is the growth of the services sector as compared to the manufacturing sector. This is well reflected in the employment statistics for the respective countries. Employment is just one of the measures of significance of each group of activities within the economy as a whole.

In UK, at the beginning of 1970's the employment in services sector was 53% against 36% in the manufacturing sector, but towards the beginning of 1990's it has risen to 73% whereas the employment in the manufacturing sector has gone down to 20%. Banking/Insurance/Finance, in the UK at the beginning of 1970's represented around 11% of total employment within the services sector which has raised to over 17% by the 1990's.

In Indiaat the beginning of the 1970's the employment in services sector was 6% against 9.4% in the manufacturing sector, but towards the beginning of the 1990's the employment in the services sector has risen to 7.3% whereas in the manufacturing sector it was only 10%. Banking/ Insurance in Indiaat the beginning of 1970's represented 0.3% of the employment within services sector which has raised to 0.6% by the 1990's.

It may be true that technology had a stronger effect on the manufacturing sector than on the services sector during the earlier days. But it's equally true that the market for manufactured goods has tended towards saturation in the post-industrial economies whereas services have experienced acceleration in demand for their products as income and wealth grew. Another reason for this change, in developed economies like UK could be due to shifting of the manufacturing of more standard goods from high wage economies towards developing economies with lower labour cost. In developing economies like India, however there is an increase in both the sectors, but it's quite evident that the rate of growth is more in the services sector. Thus, the rate of growth of the size of the financial services sector as a proportion of the overall economy is significant.

Role of Financial Intermediation

The financial services sector is made up of financial institutions such as banks, insurance companies, trusts, loan companies, credit unions, securities dealers and exchanges, etc. which act as financial intermediaries. Financial institutions carry out the process of financial intermediations by acting as a channel through which the financial surpluses of some groups in society (e.g. households) are collected and then distributed to other groups in society (e.g. firms) which has a deficit.

It is well known that banks perform the role of taking in deposits from customersand lending it to other customers. Similarly, the insurance companies, particularly those involved in long-term life assurance business, collect premiums from policy holders and invest these surpluses in industrial/commercial activity viathe stock market.

The growing size of the financial activity relative to the overall economic activity in a closely integrated world has implied that disruptions in the financial markets in any economy can engender contagion which can spread rapidly and have adverse economic ramifications. So the financial intermediations role played by the financial services sector is crucially important in mobilizing savings for investment purposes.

Unique Features:

Financial services are unique in themselvesbut they do share many of the features of the products of other services. Financial services are intangible and perishable in nature. The institution providing these services may succeed only if they have a good image and confidence of the clients, and at the same time ensuring that demand and supply go hand-in-hand. The focus of these institutions has to be continuously on the quality and innovativeness of their services in order to gain the trust of their client's thereby building their credibility.

The products of the financial services sector are usually long-term in nature and hence there is a great deal of uncertainty in the mind of the customer as to whether, he had made a right choice. Owing to the nature of these products, the consumer needs to seek external advice. However, much of this advice comes from the institution itself, mostly through their agents. They usually provide advice on product suitability, quality and price either directly or viaan agent/broker that is paid commission by the sellers of the services.

The functions of producing and supplying financial services have to be performed simultaneously for which there has to be a perfect understanding between the financial services firmsand their clients. Even the marketing of these services, needs to have, not only people-orientation, but also process-orientation. Financial services are usually customer-oriented. Financial services institutions study the needs of the customers in detail to suggest financial strategies which give due regard to costs, liquidity and maturity considerations. The providers of financial services remain in constant touch with the market offering new products much ahead of need impending legislation. Financial services have to be constantly redefined and refined on the basis of socio-economic changes such as disposable income, standard of living and educational changes related to the various classes of customers. Financial services institutions while evolving new services could be proactive in visualising in advance what the markets want, or reactive to the needs and wants of customers.

Creation of Credit:

The financial services sector particularly the banking sector is very important to the operation of the economy and to the conduct of the government economic policy. The major liability of banks is the customer's deposit, which is a significant element of the country's money supply. It is through their lending activities, that banks are able to create new bank deposits and hence the country's money supply.

Let us understand what this means with the help of a simple example. The assumption that we are making here is that cash advances are always repaid in the banking system as fresh deposits. Suppose Mr. X, who is a customer of abank, deposits Rs. 1000 with the bank. The bank in turn lends Rs. 500 by way of cash advance to customer Y. The customer Y spends this cash, i.e. Rs. 500, with customer Z, who in turn deposits it with the banking system. Further, suppose that the bank lends you Rs. 1000 by making a loan, and crediting your current account. You, in turn, write a cheque on your account in favour of IGNOU, who deposits the cheque in its account. However, the net effect of lending is that there is no change on the overall banking system balance sheet, but the banking system now owes IGNOU Rs. 1000 rather than you. From this example, it could be seen that the banking system has thus increased its deposits and hence the money supply to 25% of its initial deposit.

This process of deposit creation continues indefinitely, but in practice, the bank needs to retain a reasonable percentage of its deposits in cash or liquid assets. We may not go into these details here, but the point that needs to be emphasized upon is that the banks through their lending activities are able to create new bank deposits and hence increase the country’s money supply

Check your progress 4

1. Banks perform the role of taking in deposits from customersand lending it to other____________.
   a. customers
   b. banks
2. Financial services are ____________and perishable in nature.
   a. Tangible
   b.Intangible
3. Financial services are usually ____________.
   a. customer-oriented
   b. government oriented
4. The _____________sector is very important to the operation of the economy and to the conduct of the government economic policy.
   a. Insurance
   b. banking

1.6 Types of Financial Services

Although there is no such scheme of classification of financial services which may satisfy everyone or which is able to cover all the subtleties of this industry. However, in order to understand the functioning of the financial services industry in abetter perspective we have tried to organize our discussion of the financial services industry by classifying the financial services under three broad categories, i.e. Fee Based Services, Fund Based Services and Insurance Services.

Fee Based Services:

Fee based financial services are those services wherein financial institutions operate in specialised fields to earn a substantial income by way of fees, dividend, commission, discount and brokerage on operations. The major fee based financial services are as follow:

a) Issue Management

b) Corporate Advisory Services

c) Credit Rating

d) Mutual Funds

e) Asset Securitisation

a) Issue Management

Issue management refers to management of securities offerings of the corporate sector to public and existing shareholders on right basis. In simple words Issue Management refers to managing issues of corporate securities like equity shares, preference shares and debentures or bonds. Issue Managers in capital market parlance are know as Merchant Bankers or Lead Managers, although the term Merchant Banking covers a wide range of services such as project counselling, portfolio management, investment counselling, mergers and acquisitions, etc. Issue Management constitutes perhaps the most important and sizeable function within it, so Much so, that very often the terms Merchant Banking and Issue Management are almost used synonymously.

Issue management involves marketing of capital issues, of existing companies including rights issues and dilution of shares by letter of offer, and merchant bankers give advice on decisions concerning size and timing of the public issue in the light of the market conditions. They also provide assistance to the corporate units on the designing of a sound structure acceptable to the financial institutions and determining the quantum and terms of the public issues of different forms of securities. Merchant Bankers also advise the issuing company whether to go for a fresh issue, additional issue, bonus issue, right issue or a combination of these. The various aspects of issue management are dealt.

b) Corporate Advisory Services

Corporate Advisory Services are needed to ensure that a corporate enterprise runs efficiently at its maximum potential through effective management of financial and other resources. The services which come in the ambit of corporate advisory services, for abusiness enterprise, include services such as providing guidance in areas of diversification based on the Government's economic and licensing policies, appraising product lines and analyzing their growth and profitability, consultancy for rehabilitation of sick industrial units, advice on capital structuring and restructuring, etc. These services are usually provided by merchant bankers.

Corporate advisory services constitute an important component of the portfolio of the activities of merchant bankers. It covers any matter worth the benefit for a corporate unit involving financial aspects, governmental regulations, policy changes and business environmental reshuffles, etc. Thus, the scope of the corporate advisory services is very vast ranging from managerial economics, investment and financial management to corporate laws and the related legal aspects. We have discussed at length most of the corporate advisory services.

c) Credit Rating

The origin of this service lies in the financial crisis of the US in 1837. The first mercantile credit rating agency was set up in New York in 1841 to rate the ability of the merchants to pay financial obligations. In India, credit rating came in much later. The first credit rating agency viz. the Credit Rating and Information Services of India Ltd. (CRISIL) was set up in 1987, followed by ICRA in 1994.

The term 'Credit Rating' comprises of two words 'credit' and 'rating'. Credit is trust in a person's ability and intention to pay or reputation of solvency and honesty. Rating means estimating worth or value of, or to assign value to classifying a person's position with reference to a particular subject matter. Rating is usually expressed in alphabetical symbols. Thus, Credit Rating can be defined as an expression of an opinion through symbols about credit quality of the issue of securities or company with reference to a particular instrument.

In India, the scope of credit rating is limited to debt instruments, i.e. debentures, bonds, fixed deposits, commercial paper, etc. However, in developed countries equity shares are also rated. Credit rating is thus an important device in the hands of investors to analyse the instruments floated by issuers. To know more about the typology of credit rating, the credit rating process.

d) Mutual Funds

Mutual fund is a trust that pools the savings of a number of investors who share a common goal. Thus, it offers a common man an opportunity to invest in adiversified, professionally managed basket of securities at a relatively low cost. In other words, mutual funds invest the money collected from the investors, with the help of professional managers, in capital market instruments, such as shares, debenture and other securities.

Mutual fund is usually a long-term investment with a certain level of risk. Of course, the open-ended feature of mutual funds ensures that you get money whenever you want at a short notice, i.e. the scheme on behalf of the unit holders invests in securities, collects the interest payments and dividends from these securities and sells them when you need money. At the time of initial public issue investors can invest in close-ended funds, but afterwards they can either buy or sell the units of the scheme on the stock exchanges where they are listed. In some schemes there is an option of selling back the units to the mutual fund through periodic repurchase at NAV related prices.

As per SEBI Regulations at least one of the two exit routes is to be provided to the investor. The tax-saving Equity Linked Saving Schemes (ELSS) and pension schemes give added benefit of tax rebate.

e) Asset Securitisation

Asset Securitisation is a process whereby loans and other receivables are packaged, underwritten and sold in the form of asset-backed securities. The assets which can be securitised include receivables from the government, trade related receivables, credit card receivables, automobile loans, real estate loans, housing loans etc. Securitisation can be defined as the process which takes place when a lending institution’s assets are removed in one way or the other from the balance sheet of that lending institution and are funded instead by investors who purchase a negotiable instrument evidencing this indebtedness without recourse or with limited recourse to the original lender.

Under Asset Securitisation a financial institution pools and packages individual loans and receivables, creates securities against them, gets them rated and sells them to the investors at large through public offerings or private placements (Trustee). The asset cash flow is remitted to the trustee who in turn pays scheduled interest and principal payment to the investors. Thus, “Securitisation is a synthetic technique of converting assets into securities, securities into liquidity, liquidity into assets and assets into securities on an ongoing basis" thereby providing flexibility of yield, pricing pattern, size risks and marketability of instruments used to the advantage of both borrowers and lenders/investors.

Fund Based Services:

In fund-based services the firm raises funds through equity, debt, and deposits and invests these funds in securities or lends to those who are in need of capital. We will be discussing here some of these fund-based services such as:

a) Leasing and Hire Purchase

b) Housing Finance

c) Credit Cards

d) Venture Capital

e) Factoring

f) Forfaiting

g) Bill Discounting

a) Leasing and Hire Purchase

The growth of leasing industry cans be traced to the formation of First Leasing Company of India in 1973 by Mr. Farouk Irani and remained the only company in the country till 1980. By 1981, a few more companies, i.e. 20th Century Finance Corporation, Shetty Investment and Finance, Jaybharat Credit and Investment, Sundaram Finance, etc. joined the leasing game. During the late 1982, numerous financial institutions and commercial banks started joining in. Since then the industry leapt into prominence and today we find it as a flourishing business.

Leasing refers to a contract under which the owner of an asset allows another person or party to use the assets in return for some rent. The owner of the asset is referred to as the 'lessor' and the person using the asset in return for a payment is referred to as the 'lessee'. However, the lessee is responsible for the maintenance of the asset. In leasing the cost of capital is usually recovered from multiple serial rentals and the final sale of the asset. All financial leases virtually fall under one of the four types of lease financing viz. capital lease, operating lease, sale and lease back and leveraged lease.

According to the International Finance Corporation (IFC) hire purchase is a hybrid instrument that provides an alternative to bank financing for purchasing an asset. A hire purchase involves, in essence, the purchase of an asset on the understanding that the purchaser (called the hirer) will pay in equal periodic instalments spread over a length of time. This service is usually used for financing consumer durables. Now-a-days it is more popular with automobile financing business. Leasing and hire purchase have emerged as a supplementary source of intermediate to long-term finance. These services are provided mainly by non-banking financial companies, financial institutions and other organisations.

b) Housing Finance

Housing is one of the basic needs of the society. It is closely linked with the process of overall socio-economic development of a country. This sector remained neglected for quite some time. It was only in the Seventh and Eighth Five-Year Plans that it was paid heed to. However, today it is a growing industry with the banking sector evincing keen interest, which in turn could have been fuelled by the lack of preferable alternative avenues for investment.

Presently, funds required per dwelling shelter are so high that the individual's saving is not adequate to meet the expenditure of house building. As a result, there is a great demand for external housing finance. To take advantage of this situation, the lending institutions are competing with each other for a market share by offering very attractive terms to the customers in the form of lower rate of interest, liberal collateral requirements, longer payment period etc. These institutions have also introduced the floating rate products besides the fixed rate ones, with the option made available to the borrower for conversion against a nominal payment. The other tactics of market acquisition are speedier processing and disbursement; efficient advisory services, waiver or reductions in associated up front fees etc. We have also discussed therein the housing finance schemes offered by various housing finance institutions.

c) Credit Cards

Credit cards generally known as plastic money, is widely used by consumers all around the world. The convenience and safety factors add value to these cards. The changes in the consumer behaviour led to the growth of credit cards. It is a document that can be used for purchase of all kinds of goods and services in the world. Credit card identifies its owner as one who is entitled to purchase things without cash, purchase services without money and be eligible to get credit from a number of establishments.

The card issuer issues credit cards depending on the credibility of the customers. The card issuer also enters into a tie-up with merchant establishments which are engaged in various fields of business activities. The issuer for its convenience and for proper scrutiny sets up a credit limit for its card holders and a floor limit for its merchant establishments The credit card offers the individual an opportunity to buy rail/air tickets, makes purchases from shops and stay at hotels when they need.

Credit card is a card which enables an individual to purchase certain products/ services without paying immediately. He needs to only present the credit card at the cash counter and has to sign some forms. In short he can make purchase against credit card without making immediate cash payment. Therefore credit cards can be considered as a good substitute for cash and cheques. In order to know the details of this financial service, you may go through the unit on credit cards.

d) Venture Capital

The concept of Venture Capital was introduced in Indiaby the all India Financial Institutions with the inauguration of Risk Capital Foundation (RCF) sponsored by the Industrial Finance Corporation of India (IFCI) to supplement promoters' equity, with a view to encouraging technologistsand professionals to promote new industries. Venture capital implies long-term investment generally in high risk industrial projects with high reward possibilities. This investment may be at any stage of implementation of the project between start-up and commencement of commercial production. Thus, Venture Capital is defined as the organised financing of relatively new enterprises to achieve substantial capital gains. A high level of risk is implied by the term 'venture capital' and is implicit in this type of investment.

e) Factoring

Factoring service caters to the requirements of the Indian Industries in the changed business environment.Its origin can be traced back to the fifteenth century. England and France used the services of specialised agents for exporting goods to their colonies. These agents later came to be known as factoring organisations.

Factoring is an arrangement between the financial institution or banks (factor) and the business concern (the supplier) which provides goods or services to its customers on credit, wherein the factor buys out clients (suppliers) book debts.

There is always a difficulty of foreign languages, customs and laws, fear of distance, ocean barriers etc. which inhibit entrepreneurs from venturing into export business, consequently affecting the country's export. Factoring is a service that relieves the exporters from the fear of credit losses enabling them to offer open account terms to overseas customers. The factor takes over the administration of client's sales ledger, follow-up with debtors and evaluation of credit risks. The fee charged for these services by the factor are usually a percentage of the value of the receivables factored.

In 1990, RBI issued guidelines for factoring services providing it a statutory framework. Banks are permitted to invest in factoring companies to a certain limit but they cannot act as promoters of such companies. Investment of abank in the shares of factoring companies including its factoring subsidiary cannot exceed in the aggregate 10% of the paid-up capital and reserve of the bank.

f) Forfeiting

Forfeiting is a financial tool for exporters, enabling them to convert their 'credit sales' to 'cash sales' by discounting their receivables with an agency called forfaitor. Forfeiting denotes the purchase of trade bills or promissory notes by abank or financial institution without recourse to seller. For exporters it is a 'Risk Management' tool as well because by selling the export receivables to the forfeiter the exporter is relieved of the inherent political and commercial risks involved in international trade. Thus, all risks and collection problems are fully the purchaser's (forfeiter's) responsibility that pays cash to seller after discounting the notes or bills. It is backed by bank guarantee. In India, the Export Import Bank of India (EXIM Bank) facilitates this service with an overseas forfeiter agency for which they charge a commission.

g) Bill Discounting

Bill Discounting, just as factoring and forfeiting, is short-term trade finance, also known as acceptance credit where one party accepts the liability of trade towards third party. Bill discounting is used as a medium of financing the current trade and is not used for financing capital purposes. Trade bills are negotiable money market instruments and these are bought by the intermediaries at a discount before their maturity. Discount houses act as intermediary's between the central bank and the banking system, providing liquidity and ensuring efficient operations of money market. Discount houses play an important role throughout the universe in the whole system of banking.

Insurance Services:

Insurance, as we all know, is the most preferable method of handling risks and hence is also called as 'risk cover'. Risk is nothing but an uncertainty of occurrence of a loss viz. loss of lives, accidents causing permanent disability, loss of houses due to floods etc.

Insurance is a contract between two parties – the insurer (the insurance company) and the insured (the person or entity seeking the cover) – wherein the insurer agrees to pay the insured for financial losses out of any unforeseen events in return for a regular payment of “premium”. In insurance the actual loss is substituted by average loss by spreading the losses of unfortunate few over the entire group. This is a financial service wherein the insured is re-established to his or her approximate financial position prior to the occurrence of loss. Thus, insurance provides a unique sense of security that no other form of investment provides.

Insurance is an attractive investment option as well. These products yield more compared to regular investment options, and this is besides the added incentives offered by insurers. It serves as an excellent tax saving mechanism too. An individual is entitled to a rebate of 20% on the annual premium payable on his/her life and life of his/her children or adult children as per section 88 of the Income Tax Act 1961. In order to nationalise the life assurance business in India, the government had set up the Life Insurance Corporation of India in 1956. Since then it remained the monopoly of the public sector, until 2001 when private players were allowed to operate in this sector. However, before opening up this sector for the private players, an autonomous insurance regulator was set up in 2000. The ‘Insurance Regulatory and Development Authority’ has extensive powers to oversee the insurance business and regulate it in a manner so as to safeguard the interest of the insured. Block V of this course is completely devoted to this sector wherein life insurance, non-life insurance and the broking services are given in detail

Check your progress 5

1. ___________refers to management of securities offerings of the corporate sector to public and existing shareholders on right basis.
    a. Issue management
    b. Foreign management
2. ___________in capital market parlance is known as Merchant Bankers.
    a. Bank managers
    b. Issue Managers

3. Issue management involves marketing of _____________issues.

    a. Capital

    b. Investment

4. The origin of this service lies in the financial crisis of the US in ___________.

    a. 1857

    b. 1837

1.7 Impact of Technology

The financial services industry both nationally and internationally is one of the most dynamic and rapidly growing sectors of the economy. It is critically significant to health of the global economy as well as that of individual businesses and consumers. The overall percentage of employment in the financial services has increased. These developments are cited as a part of the 'information revolution'. Some of the effects of the information technology on the financial services sector are given below.

From the Service Providers Point of View-

Cost Saving: Information technology has contributed to the containment of the cost associated with the management of information and the execution of transactions. A single transaction costs around Rs.50 if conducted through abranch, but if done through ATM this cost comes to about Rs.15. The same transaction if conducted electronically through the internet, costs only Rs.4 Thus we can see that the cost incurred by the financial services firms can be reduced to a great extent by the efficient use of technology, thereby enhancing its profitability. These cost savings can be passed on to the customers to gain a competitive advantage.

One of the major costs of the financial services firms is the labour-cost. The computerisation of bank-branches has increased the efficiency of the functioning of the banks. The networking technology has helped the banks to introduce the single window system. It means that a single person is able to handle the work which was earlier being done by a number of persons. In other words technology has reduced the labour requirements of financial services firms, drastically reducing the cost incurred by these firms on labour.

Product Development: In the financial services sector technological developments have been of great aid in enhancing the existing services, creating new services and also bringing about product differentiation. The traditional service of cash payment has been enhanced by providing an alternative i.e. the debit cards enabling the current account bank customer to make his payments for goods and services without using cheque thereby removing the limitation on transaction size. In UK the development of on-line and touch-screen share-dealing services have simplified the procedures for buying and selling shares.

If observed closely we find that most of the services provided by the financial services sector are not new services but rather they are the new ways of offering traditional services. For example, Internet banking can just be thought of as an alternative way of providing traditional account-based services to retail bank customers. Similarly, the Automated Teller Machines (ATMs) which most of you must be familiar with is simply an alternative way of obtaining cash or making payment. However, the use of computer, telecommunication and information technology and the drifting from conventional bank branch network is what makes these products new.

ATMs are now being used by banks for dispensing railway tickets, movie tickets etc. More value added services could be provided through ATMs thus reducing the fixed and operating costs. Information technology has thus contributed to product differentiation to a great extent, in the financial services sector.

Marketing Tool: Marketing of financial services is to be people-intensive and therefore subject to variability of performance or quality of service. The database technology enables the financial institution, especially banks to access the data collected in connection with one of its services to identify the potential customers for its other services.

Most of the commercial banks, private banks, foreign banks, financial institutions etc who are members of the Indian Financial Network (INFINET) a wide area satellite based network using VSAT technology, have a wider geographical coverage, enabling these banks in tapping new markets and also for providing value added services to the existing customers. Web gives the service providers an ability to serve tens of thousands of customers each day.

Delivery channel: Computers were devised with a focus mainly on advantage of time and place, to the customers. With continuing advantages of wirelers technology flexibility in delivery channel device, is being offered by banks. The successful adoption of the wireless technology has helped banks to provide anytime, anywhere andany device banking. For Ex the international network, SWIFT is being utilized for the speedy transfer of funds across international destinations.

Decision-making Aid: Technology is an aid in the hands of decision makers and not a replacement for managers. Artificial intelligence systems such as the Expert systems are being used for making decisions of a repetitive nature. Since this system uses a common set of decision rules, the decision-making is more consistent across the organisation, unlike human decision makers. The experience and expertise of the managers cannot be replaced by the artificial intelligence systems but definitely it can be used as a supplement to enhance the quality of their decisions.

Globalisation: The information technology revolution has brought about a fundamental transformation, and, no other sector has been affected by advances in technology as much as banking and finance. It has become the most important factor for dealing with the intensifying competition and the rapid proliferation of financial innovations.The surge in globalisation of finance has also gained momentum with the technological advancements which have effectively overcome the national borders.

Widespread use of internet banking has widened frontiers of global banking, and it is now possible to market financial products and services on a global basis.

From Customers Point of View

Accessibility: The computer as well as developments in the information and communication technology has provided an easy access to information. The web helps the customers to access much better and completes information about various products and services being provided by different financial institutions.

The customers find it easy to compare the services and rates of similar kind of services offered by different institutions and then take a decision accordingly. For Ex. the information about the different cards and the services as well as charges that go along with it, offered by various banks can now be easily accessed.

Convenience: The customersare no longer required to go to the banks for withdrawal of cash or to procure any information related to his/her account. The Automated Teller Machines (ATMs) can be used by the customer to withdraw cash anytime, anywhere across the country. It is also possible for them to get funds at home by using internet. It has now become convenient for customers to carry on trading online through their depository participants. Call Centres opened by financial institutions have enhanced the convenience of customers, wherein they can get assistance, as well as information, quickly and accurately.

Speedier Settlement of Transactions: The communication and information technology has no doubt increased the speed with which the transactions can now be made. It's now possible to settle bill payments electronically. The depositories do facilitate quick settlement of securities electronically. An internet enabled inward remittance facility for NRIs is also available. NRIs can send money anytime up to a specific limit to the recipient's account, where it's deposited in rupees at the prevailing rate of exchange through the RTGS (Real Time Gross Settlement). This service not only saves time but is also cheaper.

Check your progress 6

1. The _____________services industry both nationally and internationally is one of the most dynamic and rapidly growing sectors of the economy.

   a. Financial

   b. Insurance

2. The overall percentage of _____________in the financial services have increased.

   a. growth

   b. Employment

3. ______________has contributed to the containment of the cost associated with the management of information and the execution of transactions.

   a. Information technology

   b. Technology

4. One of the major costs of the financial services firms is the ___________.

   a. money-cost

   b. labour-cost

1.8 Challenges before the Financial Services Sector

The financial sector now operates in a more competitive environment than before and intermediates relatively large volume of international financial flows.

Technology has thrown new challenges in the financial services sector and new issues have started cropping up which are going to pose certain problems in the near future.

- In an increasingly competitive environment between banks/insurance companies and the banks, insurance companies and other players of the financial system, it is necessary for these institutions to equip themselves with the right organisational structure. These firms need to properly revamp their organisational structure so that they are able to bear the stress and strains of growth, as well as face the challenge arising from the rapidly changing scenario. The structure should be a judicious blending of the needs for greater delegation of power, decentralisation of control and constant monitoring of performance. Designing of an appropriate organisational structure is abig challenge.
- The employees of the financial services sector (particularly those employed in the public sector banks and insurance companies) need to be trained in operating computers. It’s also necessary that they should be made to appreciate the efficient use of computer in accounting transactions andalso for delivering better services to their customers. Its not only computers, training and development of the staff on the changing systems (internet, electronic commerce) and procedures as well as developing the appropriate mindsets have become absolute imperatives for the financial sector. With the liberalisation of the economy and emergence of new private participants, the acquisition and development of new and improved skills has become a pre requisite for their survival and growth. Thus, the need to train and retrain staff on a continuous basis given the fast paced changes in the IT sector is a major challenge confronting the financial services sector.
- As most of you must be aware that India is one of the signatories of Financial Services Agreement (FSA) of 1997 which gives the Indian financial sector including banks an opportunity to expand their business on a quid pro quo basis. Globalisation of finance has already gained momentum with the technological advancements breaking national borders in the financial services sector. In future globalisation would spread further on account of the likely opening up of the financial services sector under WTO.

As expected, a greater number of international players would be entering the Indian financial system the challenge before the financial institutions is to go global by searching new markets, customers and profits.

- Financial institutions will have to face competition not only at the international level but also at the domestic level and will have to compete with foreign participants operating in India. Most of the Indian firms lack in size, even India's largest bank, SBI is not even a 10th in size of the 9th largest bank Sumitomo Mitsui which has assets of $950 billion against SBI's assets of $91 billion. Size is increasingly becoming important for global participants as it is crucial to improved efficiency. Effective and efficient Intra-firm/Inter-firm consolidation (restructuring) is a major challenge before most of these institutions.
- India's largest financial institution ICICI has already moved a step ahead towards universal banking with its reverse merger with ICICI bank.
- With blurred distinction between the banking and non-banking financial intermediaries, the firm providing financial services need to come up with new products with better services in order to retain its old customers and attract new ones. However with the help of communication and networking technologies the utilization of the existing facilities could be improved to provide enhanced customer convenience and satisfaction. The major challenge before the financial institutions in India thus relates to the need to introduce innovative, customer friendly products and services for which newer technologies have to be brought in multiple areas to reduce the overall transaction costs.
- It's a challenge, especially before the banks, to adopt efficient and effective communication networks to build up integrated delivery channels both vertical and horizontal by installing an enabling and compatible multi channel platform which could support and seamlessly integrate both existing and future delivery channels.
- Providing the customers a single `sign on', a unique ATM PIN, for carrying out transactions across delivery channels is also a challenge in itself.
- Globalisation and technological developments have placed new stresses on the infrastructure of financial services organisations. It has also increased their exposure to operational risks such as system failure, electronic frauds and damaged reputation. They may have to develop a decision support system on the current MIS for the better analysis of the dataand risk

management on real time basis, in addition to other functions such as credit decisions, foreign exchange management, treasury operations etc.

- Security is another major concern of on-line customersand it is the biggest risk to the financial service providers in terms of brand image. The need to comply with international standards including those of certification such as BS7799 or ISO 17799 to meet its information security requirements and ITIL (IT infrastructure Library) in the areas of service management is a emerging challenge before the financial services sector.

The implementation of IT has been confined only to the metros or big urban customers its now time that the benefits of IT should be made available to the rural population as well. Here there will be a need to provide for multi-lingual facilities, which is a migration away from the existing English-only paradigm. Adequate Infrastructural facilities are must, if these benefits have to accrue. Thus, in the fast track Internet world the financial services providers will need to invest heavily in customer relationship management system and brand identify. They may also have to adopt frameworks of best practices for implementing IT Governance using internationally accepted standards

Check your progress 7

1. The _____________services industry both nationally and internationally is one of the most dynamic and rapidly growing sectors of the economy.

   a. Financial

   b. Banking

2. The overall percentage of employment in the ___________services has increased.

   a. Banking

   b. Financial

3. ____________has contributed to the containment of the cost associated with the management of information and the execution of transactions.

   a. Information technology

   b. Banking technology

4. The ____________do facilitate quick settlement of securities electronically.

   a. Financial Institutions

   b. Depositories

1.9 Let Us Sum Up

In this unit we have studied about the meaning and concept of financial services in detail.

In this unit we have covered the meaning of financial services in very detail. We discussed the characterstics of financial services. The importance of financial services has even been discussed here in very detail. Later we even discussed the various types of financial services. The impact of technology in on financial services were discussed in detail where we studied how the new improved technology is helping us in providing better services.Not only this in the later portions we even discussed the various challanges before financial services sector.

This unit was sufficient enough for the readers to understand the basic concepts behind the financial services.

1.10 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b), (3-a)

Check your progress 2

Answers: (1-a), (2-b)

Check your progress 3

Answers: (1-a), (2-b), (3-a)

Check your progress 4

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 5

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 6

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 7

Answers: (1-a), (2-b), (3-a), (4-b)

1.11 Glossary

1. **SEBI -** Stock Exchange board of India.
2. **MIS** - Management information system.

1.12 Assignment

Discuss the meaning and concept of financial services.

1.13 Activities

Discuss the various types of Financial Services

1.14 Case Study

What are the Challenges before the Financial Services Sector of India?

1.15 Further Readings

1. Brean Andeston, 1995 "Financial Services", Macmillan Press Ltd., London.
2. Kimball Dietrich, 1996 "Financial Services and Financial Institutions Prentice - Hall, Inc. New Jersey.

UNIT 2: MARKETING OF FINANCIAL SERVICE'S: A CONCEPTUAL FRAMEWORK

Unit Structure

2.0 Learning Objectives

After learning this unit, you will be able to understand:

- Discuss the Concept of marketing as applicable to financial services marketing.
- Describe the concept of service product mix.
- Discuss various orientations as applied to marketing of financial services.

- Differentiate between products and services on the basis of service characteristics.
- Explain the implication of service characteristics for marketing of financial services.

2.1 Introduction

The first barter exchange can be looked upon as a reflection of the realisation that exchange added value for both the parties to the transaction. This indeed marked the dawn of marketing. The recognition of value addition ultimately led to the development of task specialisation, by far the first real step forward in economic development. The last century has seen 'marketing' develop from a mere practice, into a major academic discipline.

Marketing is both a concept and practice; an approach to exchange relationships, which provides the driving force for formulation of strategies every type of organisation.

Marketing in the true sense of the word, is relatively new to the financial sector. Until recently, marketing in most financial sector organisations was largely synonymous with advertising and public relations and it was not until the 1970s that marketing department was formed on any scale. (Newman 1984). Even then, the role of marketing tended to be more tactical. Strategic marketing as seen as a relatively low status activity with senior management being dominated by executives with abackground in finance (Hooley and Mann, 1988). In the last decade marketing has developed as a more integrated function within financial service organisations largely as a result of rapid changes in the operating environment. Nevertheless, Morgan and Piercy (1990) suggest that marketing remains relatively young management function in\ the financial service sector.

2.2 Marketing and the Financial Services

Marketing is the process of determining consumer demand for a product or service, motivating its sale and distribution it into ultimate consumption at a profit (Brech 1953).

Marketing is not only much broader than selling; it is not a specialised activity at all. It encompasses the entire business.it is the whole business seen from the view point of its final result, that is from the customer's point of view.

Concern and responsibility for marketing must therefore permeate of areas of the enterprise (Ducker).

Marketing is the set of human activities directed at facilitating and consummating exchanges (Kotler 1972).

Marketing is concerned with the creation and maintenance of mutually satisfying exchange relationships (Baker 1976).

The purpose of abusiness is to create and keep a customer (Levitt 1983).

Marketing is the business function that identifies current unfilled needs and wants, defines and measures their magnitude, determines which target markets the organisation can best serve and decides on appropriate products, services and programmes to serve these markets. Thus, marketing serves as a link between ik society's heeds and its pattern of industrial response (Kotler 1988).

To focus on one financial service, i.e. banking, let us look at the definitions as applied in the sector. The definition of bank marketing, as referred to by the NIBM, Pune is as follows:

Bank marketing is the aggregate of functions, directed at providing services to satisfy customers' financial (and other related) needs and wants, more effectively and efficiently than the competitor, keeping in view the organisational objectives of the bank.

This definition highlights the fallowing points:

1. Banks provide services with all the service characteristics discussed later in this, unit being associated with them.
2. The aim is to satisfy customers' needs and wants.
3. The needs and wants are mostly financial in, nature and some incidental to or related to the main functions.
4. The competitive element, efficiency and, effectiveness are major factors in the process, of designing and delivering these services.
5. Organisational objectives are still the driving force.

This could be seen as an extension of the Marketing concept', so modified as to suit the nature of the banking activity.

The aggregate of functions mentioned in the definition, is the sum total of an integrated effort to discover, create, arouse and satisfy customer needs. Each individual opting in the bank is a marketing person who contributes to the total satisfaction of customers.

Bank marketing deals with providing. Services to satisfy customers' financial needs and wants. Banks have to discover/ascertain/anticipate the financial needs of the customers and offer the services which can satisfy those needs. Banks may be required to satisfy the customers' other related needs and want of he customers. Marketing helps in achieving the organisational objectives of the bank, this means that marketing is equally applicable to achieve commercial and social objectives of the banks. Indian banks have dual organisational objectives:

i) Commercial objective to make profit and

ii) Social objective which is a developmental role particularly in the rural areas.

Service areaapproach adopted by the Indian Bank is a marketing approach whereby a specific target market is assigned to each bank branch for need based banking activity in tune with the social objectives.

The marketing concept points to the following essentials which contribute towards bank's success:

a) The bank cannot exist without the customers.

b) The purpose of the bank is to create, win and keep a customer. The customer is and should be the central focus of everything the bank does.

c) It is also a way of organising the bank. The starting point for organisational design should be the customer and the bank should ensure that the services are performed and delivered in the most effective way. Service facilitates also should be designed for customers convenience.

d) Ultimate aim of abank is to deliver total satisfaction to the customer.

e) Customer satisfaction is affected by the performance of all the personnel of the bank.

Marketing is an organisational philosophy. The philosophy demands the satisfaction of customers' (consumer's) needs as the prerequisite for the existence and survival of the bank. Marketing for service industry like banks is philosophy to be understood by the whole organisation from the chief executive to the person working concept at the counter. The first and most important step in applying the marketing concept is to have a wholehearted commitment to customer orientation by all the employees. Marketing is an attitude of mind. The central focus of all the activities of abank is customer.

A traditional marketing department (and officers with marketing designations) usually cannot be responsible for the total marketing function of a service organisation like banks. Else, it is argued that personnel working in other departments like operations and back of the counters may tend to ignore their customer-related responsibilities and totally concentrate on just handling operation and other duties mechanically.

Marketing is much more than just advertising and promotion;' it is abasic part of total business operation. What is required for the bank is the market orientation and customer consciousness among all the personnel of the bank

Check your progress 1

1. ____________ is the process of determining consumer demand for a product or service.

   a. Marketing

   b. Market

2. Marketing is the set of____________activities directed at facilitating and consummating exchanges.

   a. financial

   b. Human

3. ________________marketing deals with providing .services to satisfy customers' financial needs and wants.

   a. Bank

   b. Insurance

4. Marketing is an _____________philosophy.

   a. Organizational

   b. Psychological

5. A ____________marketing department usually cannot be responsible for the total marketing function of a service organisation like banks.

   a. Traditional

   b. modern

2.3 Marketing as a Functional Area of Management

Marketing is complex phenomenon that combines both the philosophy of business and its practice. That is, marketing consists of two inter-related phenomena:

1) A basic concept andat focuses on customers

2) A set of management techniques

Many organisations have a marketing department made up of both marketing generalists e.g. the marketing manager and specialists e.g. the sales manager or marketing research manager. Such marketing department will be based in a physical location within the organisation in the same way as, say personnel or purchasing. The people involved with the day-to-day running of the marketing department will have at their disposal a range (management techniques often referred to as the marketing spectrum or mix. These techniques cover such areas as sales and sales management, advertising and promotion, pricing, packaging, product development, marketing research, planning, distribution, and after-sales-service. Many of the specialisations with the marketing, offer, separate career opportunities and are often undertaken by specialists with the marketing, manager responsible for co-ordinating all the separate but inter-related activities

Looked at from this point of view, marketing is indeed a functional area of management which is usually within the firm and which uses a number of highly developed technique in order to achieve specific objectives. As a function, an important part of marketing's role is to identify correctly, both the current and future needs and wants of specifically defined target markets. This information is then acted upon by the whole organisation it bringing into existence, the products and or services necessary to satisfy customer requirements. It is the marketing function that forms the interface with the firm's existing and potential customers. Marketing provides entrepreneurship by identifying customer requirements, and through marketing, the rest of the firm is able to mobilise resources to capitalise on them.

In fact, the process of marketing management is not different from any other functional area of management in that is essentially comprises of four key tasks: Analysis, Planning, Implementation and Control.

Analysis

The starting point of marketing management decisions is analysis. Customers, competition, trends and changes in the environment and internal strengths and weaknesses must each be fully understood by the marketer before effective marketing plans can be established. Analysis, in turn, requires information using systematic marketing research and marketing information systems.

Planning

The second task of the manager is the planning process. The marketing manager must plan both long-term marketing directions for the organisation (strategic planning), including e.g. the selection of targets and the marketing programmes and tactics that will be used to support these strategic plans.

Implementation

Fourth strategic and tactical plans must, of course, be acted upon, if they are to have any effect. The implementation tasks of marketing management involve such staffing, allocating tasks and responsibilities, budgeting and securing any other resources needed to translate plans into action.

Control

The fourth and sometimes neglected task of the manager is measuring and valuating progress against objectives and target established in plans. Control of marketing plans car be problematical with difficulties associated with both measuring marketing performance and pinpointing cause and effect. For example, market share; a frequently used measure of marketing performance and hence abasis for marketing control, need very careful analysis and interpretation if it is to provide a useful basis for controlling the effectiveness of marketing the strategies 'and plans. Both qualitative and quantity the techniques of control should be used by the marketing manager and including budgetary control, control of marketing mix effectiveness in turn, forms part of analysis function discussed earlier, thereby completing the essentially circular nature of these four inter related tasks.

Although it can be seen that marketing has a very important functional role within the Organisation, the practice of marketing should not be restricted to the marketing, department. A marketing-oriented business has implications for the way people throughout the organisation respond to the initiatives that are forthcoming from marketing.

Check your progress 2

1. ______________is complex phenomenon that combines both the philosophy of business and its practice.
   a. Marketing
   b. Organisation
2. The starting point of marketing management decisions is ___________.
   a. Thinking
   b. Analysis
3. The second task of the manager is the ____________process.
   a. Planning
   b. decision
4. The fourth and sometimes neglected task of the manager is ____________against objectives and target established in plans.
   a. measuring and valuating progress
   b. Analysis process

2.4 Financial Services and the Different Marketing Orientations

There are five competing orientations under which organisations conduct their marketing activity.

The product concept is one of the oldest concepts guiding sellers.

The production concept holds that consumers will favour those products that are widely available and low in cost. Managers of production-oriented organisations concentrate on achieving high production efficiency and wide distribution coverage.

The assumption holds in at lease two types of situations:

1) The first is where the demand of a product exceeds supply, as in may third world countries. Here consumersare more interested in obtaining the product than in its fine points.

2) The second situation is where the products' cost is high and has to be brought down through increased productivity to expand the market.

In the 19th century and early of the 20th century the fundamental role of business was seen as production. Manufacturers were in suppliers' market and were faced with a virtually insatiable demand for goods and services. Firms concentrated on production and productive efficiency in order to bring down costs. Firms tended to manufacture and offer products that they were good at producing with customers' requirements and satisfactions of secondary importance. This production mentality was a workable philosophy as long as a sellers' market existed.

The Product Concept/Orientation

Often sellersare guided by the product concept.

- The product concept holds that consumers will favour those products that offer the most quality, performance or innovative features. Managers in these product oriented organisations focus their energy on making superior products and improving them over time.

These managers assume that buyers admire well-made products and can appraise product quality and performance. Marketing management may become a victim of 'better mouse trap' fallacy, believing that abetter mousetrap will lead people to beat a path to its door. At a place where there are no mice, the product would hardly sell!

Many firms have, in their own opinions, produced excellent products, but not necessarily of the type customers want to buy. Manufacturers who focus their attention on existing products and pay little or not attention to the changing needs and wants of the marketplace suffer from what as often termed 'marketing myopia'. This is very short sighted viewpoint where firms are so busy concentrating on their products that they fail to take customers' requirements into account.

Even today, firms can be found who pay little regards to the needs and wants of their customers and still have the product concept as the guiding philosophy of their businesses. Such firms take the attitude that they produce excellent products and that people will want to buy them.

The Selling Concept/Orientation

The selling concept (or sales concept) is another common approach many firms take to the market.

- The selling concept holds that consumers, if left alone, will ordinarily not bay enough of the organisation's products. The organisation must therefore undertake an aggressive selling and promotion effort.

Philip Kotler defines this selling concept as:-

A management orientation which assumes that consumers will either not buy or not buy enough of the organisation's products unless the organisation makes a substantial effort to stimulate their interest in its products.

From the above definition, the implicitly premises of the selling concept are as follows:

1) Consumers can always be induced to buy more through various 'sales techniques'.
2) Consumers tend to resist purchasing and it is the salesperson's job to overcome this. The firm's key talk then is 40 organise an effective sales force.

Peter Drucker, one of the leading management theorists, puts it this way:

There will always, one can assume, be need for some selling. But the aim of marketing is to make selling superfluous. The aim of marketing is to know and understand the customer so well that the product or service fits him and sells itself; ideally, marketing should result in a customer who is ready to buy. All that should be needed than is to make the product or service available.

Marketing based on hard selling carries high risks. It assumes that customers who are coaxed into buying the product will like it and if they don't, they won't bad-mouth it to friends or complain to consumer organisations. And they will possible forgot their disappointments and buy it again. One study showed that dissatisfied customers may bad-mouth the product to ten or more acquaintances; bad news travels fast. In case of banking it applies thus,

During the times of famous scams in stock market, a foreign bank was in serious trouble as the: probable losses would have threatened its viability to be in the business. Many small scheduled banks had put their funds by way of deposits in that bank. The news items revealed names of such banks and in some cases they were just rumours. It however, had serious implications on those small banks due to such rumours which spread very fast in their command areaand frightened depositors queued up their branches to withdraw their deposits which gave a severe jolt below the belt to such banks as a result of the rumours. They had to do a lot of PR and clarifying work to bring back their deposits.

The Marketing Concept/Orientation

The marketing concept is abusiness philosophy that challenges the previous concepts. Its central tenets crystallised in the mid 1950s.

The marketing concept holds that the key to achieving organisational goals consists in determining the needs and wants of target markets and delivering the desired satisfaction more effectively and efficiently than competitors.

The marketing concept rests on four main pillars, namely.

1) Target market
2) Customer needs
3) Integrated marketing
4) Profitability

These are shown in the figure below, where they are contrasted with a selling orientation.The selling concept takes an inside-out perspective. It starts with the factory, focuses on the company's existing products, and calls for heavy selling and promoting to produce profitable sales. The marketing concept takes an outside-in perspective. It starts with a Well-defined market, focuses on customer need, and integrates all the activities that will affect Customers and produces profits by creating customer satisfaction.

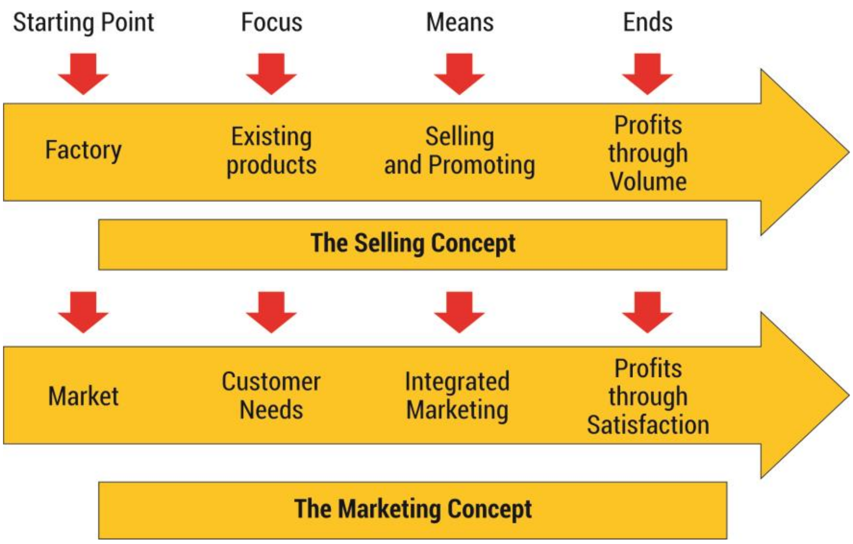

Fig 2.1 Sellingand Marketing Concepts-Contrasted

Peter R Dickson in his book 'Marketing Management' asserts that in the context of crowding of marketplace by competing companies catering to the same target markets, a company to survive, will need to adopt the 'strategic marketing concept' which he define thus:

The strategic marketing concept is defined as:

The corporate mission is to seek a sustainable competitive advantage over competitorsby meeting consumer needs.

The Societal Marketing Concept

In recent years, some have questioned whether the marketing concept is an appropriate philosophy in an age of environmental deterioration, resource shortages, explosive population growth, world hunger and poverty and neglected social services are companies that do an excellent job of satisfying individual consumer wants necessarily acting in the best long run interests of consumers and society?

The marketing concept side-steps the potential conflicts between consumer wants, consumer interestsand long-run social welfare.

For example, the detergent industry caters to the passion for whiter clothes by offering a product that pollutes rivers and streams, kills fish and injures recreational opportunities.

These situations call for a new concept that enlarges the marketing concept. This new concept may be termed the societal marketing concept.

- The societal marketing concept holds that the organisation's task is to determine the needs, wants and interests of target markets and to deliver the desired satisfactions more effectively and efficiently than competitors in a way that preserves or enhances the consumer's and the society's well-being as depicted in figure below:

Fig 2.2 Social Marketing Concept

The societal marketing concept calls upon marketers to balance three considerations in setting their marketing policies, namely 1) company 2) consumer want satisfaction, and 3) the public interest.

Originally, company's based their marketing decisions on maximising short-term company profit. Then they began to recognise the long-run importance of satisfying consumer wants and this introduced the marketing concept. Now they are beginning to factor in society's interests in their decision making.

Check your progress 3

1. There are ____________competing orientations under which organisations conduct their marketing activity.
   a. Five
   b. Six
2. The ______________concept holds that consumers will favour those products that are widely available and low in cost.
   a. product
   b. Production
3. Often sellers are guided by the _____________concept.
   a. Product
   b. Customer
4. Consumers can always be induced to buy ___________through various 'sales techniques.
   a. goods
   b. More
5. Marketing based on hard selling carries _____________risks.
   a. High
   b. low

2.5 Difference between Services and Product Physical Goods

Services now account for more than 70% of employ men and GNP of most industrialised countries. Many industrial corporations also owe their revenue and profitability to the peripheral services they add on to their products. The marketing literature, however, has unit1 recently concentrated almost entirely on physical products. Obviously this is because that is where marketing as a separate function developed earliest, and where it has been most intensively applied, particularly in the field of fast-moving consumer goods. As both academics and practitioners have turned their attention to all increasingly important services markets, the question has been debated, through different actually are services.

When we examine them, we can see that there is not such a clear-cut line between services and products as might be thought. Many products in fact include large elements of service in their delivery. Looked at from the buyer's point of view, services may also form a vital part of the total bundle of benefits which is sought, particularly in industrial markets. Likewise, many services include a large contribution from hardware: hotels, airlines, fast food outlets are all classed as services but the physical elements in the offering are a very large part of what customer’s buy. What is different is that as buyers we do not receive ownership of the physical elements of a service, but merely rent them for a period.

Levitt has suggested that "there are not such things as service industries. There are only industries whose service components are greater or less than those of other industries. Everybody is in service". Levitt was emphasising that with almost every tangible core product, an intangible service component is associated.

Goods-Service Continuum In 1977, Ms. G. Lynn Shostack, the Vice President of Citibank, suggested that marketing 'entities' are combinations of intangible and tangible elements which are distinct and discrete. If these absolute tangible and intangible elements are taken to the two ends of a continuum, as show 11 below, we can observe that all goods and services occupy different positions in the continuum. There is a range which varies from an absolute tangible well like salt to an absolute intangible service like education.

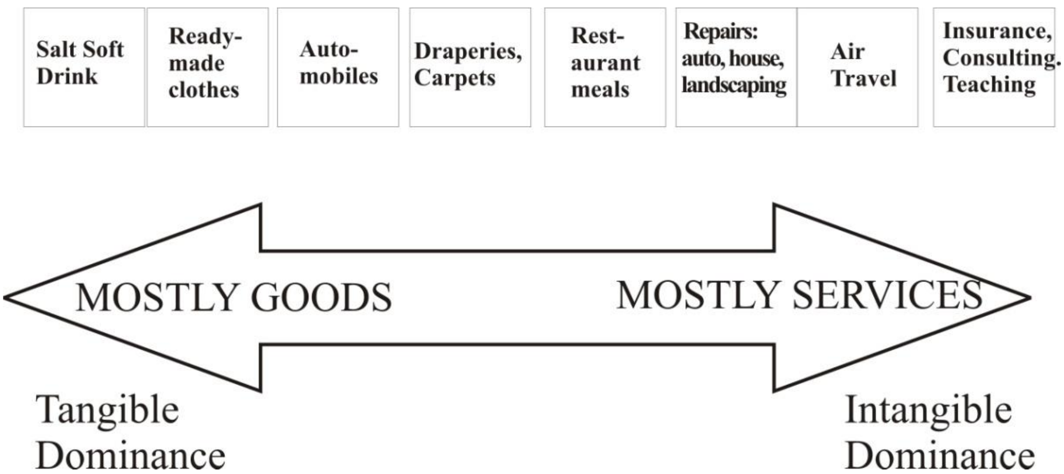

Fig 2.3 Search Goods and Experience Goods

Another approach of distinction as proposed by Theqdore Levitt, classifies goods into and two categories viz. Search goods and experienced goods. Search goods are generally those goods which are packaged goods that the customer can see, evaluate and try prior to the purchase, like a pen or toothpaste like holiday, travel etc. Some call search goods as tangible goods and the other as intangibles. There is a range between the 2 absolute extremes and there could be products falling in this range.

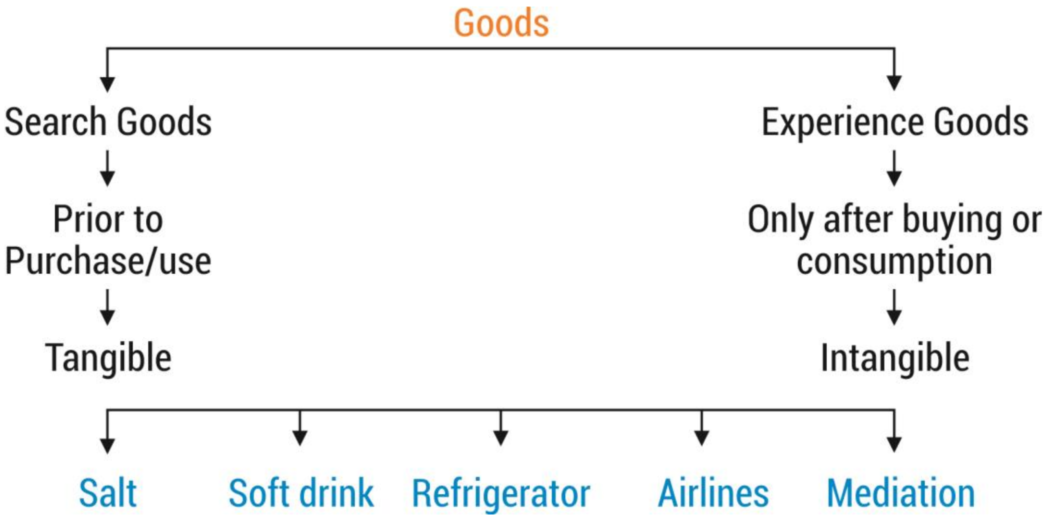

Fig 2.4 Kotlers classification of goods

Philip Kotler's classification is a further improvement in that he suggests five category under which a company' offer to the market place can be distinguished.

1) **A pure tangible good:** No services accompany the product e.g. toothpaste, soap and salt etc.

2) **A Tangible good with accompanying services:** A tangible good accompanied by one or more services to enhance its consumer appeal. Levitt observes that the more, technologically sophisticated the generic product, (e.g. cars, computers) the moredependent are its sales on the quality and availability of its accompanying customer services. (E.g. display rooms, delivery repairs and maintenance, operator training, warranty fulfilment).

3) **A Hybrid:** Equal parts of goods and services: e.g. restaurants

4) **Amajor service with accompanying minor goods and services - Airline:** transportation service, accompanied by food, drinks, ticket stub, airline magazine the service requires a capital intensive good an aeroplane for its realisation, but the primary item is a service.

5) **A pure service:** Baby sitting, banking hair-dressing, gardener, telecommunication, health club, psychotherapy, etc.

Check your progress 4

1. ____________now account for more than 70% of employ men and GNP of most industrialised countries.

   a. Services

   b. products

2. Another approach of distinction as proposed by____________, classifies goods into and two categories viz. Search goods and experienced goods.

   a. Philip Kotler

   b. Theqdore Levitt

3. There is a range between the 2 absolute extremes and there could be ____________falling in this range.

   a. Products

   b. services

2.6 Characteristics of Services

Having looked at the differences between products and services, you may now be ready to describe the essential characteristics of services and understand how these differences affect the financial services.

There is general agreement in the literature that the main characteristics of services are intangibility; inseparability, heterogeneity, perish ability.

Intangibility

Intangibility is relevant only to the pure service element; the hotel bed and the hamburger are very tangible, the problem of intangibility is that it is difficult to communicate and display exactly what the product is. It is often not possible to taste, feel, see hear or small services z before they are purchased. Opinions and attitudes may be sought before hand, a repeat purchase may rely upon previous experience, the customer may be given something tangible to represent the service, but ultimately the purchase of a service is the purchase of something intangible.

Inseparability

This refers to the fact the production and consumption of the service are inextricably intertwined, the implications of this are that the consumer is involved in production. Further, in many cases other consumersare also involved at the same time, as in most retailing situations. This may be a positive aspect of the benefits delivered (in a theatre or club), or it may be potential negative aspect (waiting in queues at the post office). Whether the buyer is physically present or not, the product comes into existence' only when it is bought; it cannot be mass produced in advance (although the physical components may be, to some extent.). Goods are usually purchased, sold and consumed whereas services are usually sold and then produced and consumed. .

Heterogeneity

Heterogeneity or variability is a result of the fact that services are usually delivered by human beings, whose performance is necessarily variable; quality control is extremely difficult. It is often difficult to achieve standardisation of output of certain services. The standard of a service in terms of its conformity to what may be prescribed by the seller may depend on who provides the service or where it is provided. Even though standard systems may be used to handle a flight reservation, book in a car for service, each 'unit' of service may different from other 'units'. Franchise operation attempt to ensure standards of conformity but ultimately, with services it is difficult to ensure the same level of quality of output as it may be with goods. From the customer's point of view too, it is often difficult to judge quality in advance of purchase.

Perishability

This means that the service cannot be stockpiled. If a sent is unfilled when the plane leaves or the play starts, it cannot be kept and sold next day or next week; that revenue is lost for ever. In some cases, such as insurance or banking, it could be argued that potential stocks remain, in the sense that the service is there to be sold every day as long as the underwriting or loan capacity exists. Most services however, are clearly time dependent, in a way that physical product is not. Important marketing decisions in service organisations relate to what service levels will be provided and how to respond in times of low and excessive usage, for example through differential pricing or special promotions.

These characteristics certainly do not apply in equal measure to all services. Some services are highly intangible (e.g. education); others are highly tangible (e.g. fast food restaurant); some may be highly variable (e.g. dental treatment);

some highly standardised (e.g. automatic car wash). The notion of continuum of tangibility, inseparability, heterogeneity and Perishability is helpful in understanding and applying these characteristics.

The origin idea of a single continuum of tangibility for understanding the differences between goods and services has been extended recently to suggest that all four characteristics of services can be described and related in this way. (Payne, 1993)

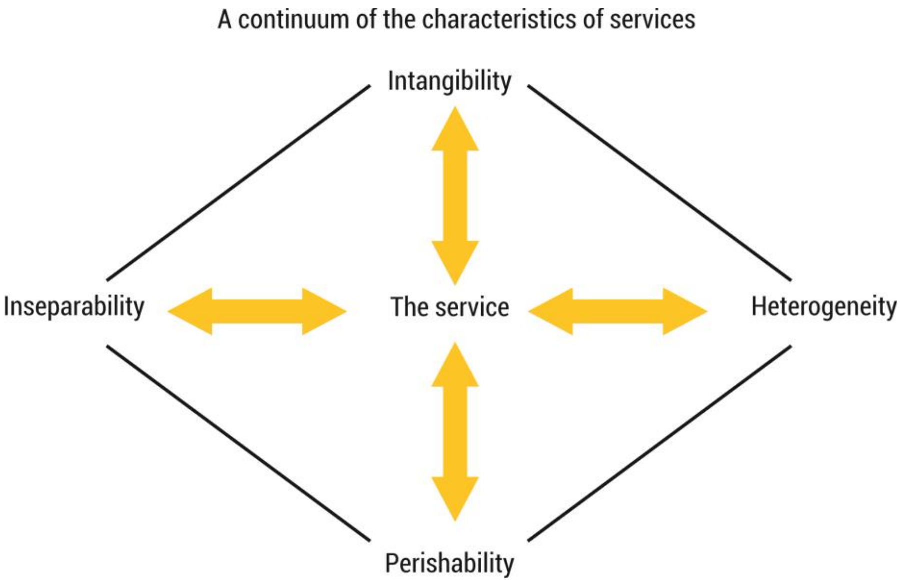

Fig 2.5 A Continuum of the Characteristics of services

Thus, while 1egal service is less tangible, varied and can be performed away from the customer, a fast food service is highly tangible, generally standardised and usually performed near the customer. Different service organisations offering similar services can + place differing emphasis on each of these characteristics to obtain competitive leverage and advantage in the market place. Thus, one management consultant could offer a highly bespoke service and undertake all assignment personally; another could subcontract work to associates, thus potentially increasing the scale of business but possible losing the benefit of a highly individual approach.

These different characteristics have positive and negative implications. The challenge for marketers is to develop strategies and tactics that emphasise the positive effects of these characteristics of finds ways of overcoming them where the consequences are unhelpful. Christian Gronroos (1990) presents the difference between physical goods and services as follows:

Sr. no.	Physical Goods	Services
1	Tangible	Intangible
2	Homogeneous	Heterogeneous
3	Production and distribution separated from consumption	Production, distribution and consumption are simultaneous process
4	A thing	An activity or process
5	Core value produced in factory	Core value produced in buyer seller interactions
6	customers do not participate in the production process	Customers participate in the production
7	Can be kept in stock	Cannot be kept in stock
8	Transfer of ownership	No transfer of ownership

Definition of Service

Discussions on the nature of services lead us to a normally accepted definition of services as follows:

- A service is any act of performance that one party can offer to another that is essentially intangible and does not result in the ownership of anything. Its production may or may not be tied to a physical product.

Gronroos proposed a working definition in 1990. According to him:

A service is an activity or series of activities of more or less intangible nature that normally, not necessarily, take place in interactions between the customer and service employees and/or physical resources or goods and/or systems of the service provider which are provided as solution to customer problems.

This highlights the following important features:

1) Services are by and large 'activities' or they are a series of' activities rather than things.

2) As a result the services 'we intangible.

3) They take place in the interaction between the customer and the service provider which means that the service; are produced and consumed simultaneously.

Customer has a role to play in the production process as the services are provided in response to the problems of customers as solution.

In banking context, the bank has to be continuously aware about the changing demands and expectations of the customers. At times they have to tailor such products/schemes thinking about the customer's probable expectations with changing market scenario e.g. telebanking or e-banking have been thought of much in advance than customer himself asking for such products as the banks have networked ATMs and computerised services like Demat which a customer giving for computers would easily opt to have this benefit. Thus, banks not only have to keep the present needs and wants of customers but also have to innovate to create wants for the customers to extend services/technology to meet his requirements.

Some of the characteristics discussed above have interesting implications for marketing of financial services.

In general, services must be produced and consumed simultaneously. As a consequence, services are perishable and must be produced on demand and 'cannot be inventoried.

The presence of inseparability tends to imply the consumers themselves play a significant role in the production of services. In fact, some experts view customersas quasi or partial employees (Bowen and Schneider, 1988). For a service to be provided typically requires either the physical presence of the consumer or some contact with the consumer to provide the information required for the service to be performed. The consumer making a loan application does not have to be in the physical presence of a loan assessor,but must supply that assessor with information to evaluate the application.

The quality of the service product is typically highly dependent on personal interactions and as a consequence, the potential for variability (heterogeneity) is high. To a large extent, the qualities of inseparability and heterogeneity arise because of the intangible nature of services.The characteristics of services as an act rather than as an object lead to an emphasis on the individuals providing the service and their interactions with the organisation's customers.

In addition to these service characteristics, financial services display an additional feature which affects the marketing process. This is the issue of fiduciary responsibility which refers to the implicate responsibility which financial service organisations have in relation to the establishes that although any business has a responsibility to its customers in terms of quality, reliability and safety of the products it supplies, this responsibility is perhaps much greater in case of financial service organisation. This may perhaps be due to the fact the consumers of such services often find the precise details of the service difficult to comprehend and therefore place their trust in the organisation they deal with. Equally important is the fact that the 'raw materials' used to produce many financial products are consumers' deposits; thus in producing and selling a loan product, the bank has a responsibility to the individuals whose deposits have made that land possible. Christain Ennew etal, in their book 'Cases in marketing financial services' advocates that "any organisation involved in the provision of financial services should retain an awareness of the magnitude of the impact which their marketing and selling activities can have on the lifestyle of an individual or the property of a company".

The implications of intangibility, inseparability and heterogeneity are manifested at both strategic and tactical levels in services marketing. Thomas (1977) stresses the importance of a clear understanding of the nature of the business and the establishment of a distinctive basis on which to compete. The latter is particularly significant given the difficulties of competing on the basis of offering a service with distinctive attributes or features. Ellnew et a1 state 'the ease of copying and the lack of patent protection mean that competition is more commonly based on service levels rather than service attributes and this in turn will tend to increase the emphasis on efficiency and cost effectiveness in service provisions'.

As marketing moves towards tactical issues, it also moves closer to and must be more tailored to, the distinguishing features of specific products and markets. In the context of marketing mix, this suggests that in the case of services, the composition of that mix, and the management of its elements can be quite distinctive.

The essence of marketing strategy is to provide the organisation with a sustainable competitive advantage in the markets in which it operates. This requires that the organisation both understands consumer needs and identifies how those consumers can be grouped into different market segments. By identifying these 'segments and selecting target markets, the organisation can determine where and against whom it intends to compete

Having determined where to compete and whom to compete, the firm will have effectively determined its product/market scope. However, it must also establish an appropriate position for its products in the target markets. The whole purpose of positioning products in markets is to establish a competitive edge for the products. For example, American Express Cards may be seen as positioned as a high prestige charge card, with level of service and price reflecting the prestige of the card holder.

In selecting l a position, the marketing strategy is essentially defining the image which the organisation wishes to create for its product.

Once a position has been selected, that position will guide the formulation of the marketing mix Product attributes, pricing decisions, methods of distribution and communication should all seek to reflect the chosen position

In effect, the marketing mix represents the tactics employed to implement a chosen strategy. The decisions made in respect of marketing mix need to be operationalised and the outcomes monitored to check that the actual outcomes match what was intended. Should the outcome deviate from expectation, corrective action in the form of modification of marketing mix,-or even the overall strategy may be warranted.

The process of deregulation and environmental change is continuing with further liberalisation of financial markets. This presents the financial services sector with a number of new opportunities and threats. As the environment facing suppliers of financial services has become increasingly competitive and uncertain, the importance of marketing in guiding the business development has increased.

Deregulation has removed the traditional restrictions on the types of product which particular institutions could supply and has created the opportunity for expansion into new markets. It has also presented the threat of an increase in the number and variety of competitors in a specific market. In this scenario, tactical marketing alone is no longer appropriate; no financial services organisation can afford simply to continue supplying the same products to the same markets without some consideration of their possible reactions to the changing opportunities and threats now confronting them. The essence of the strategic stance not required, is that the firms should adopt an operative approach to their markets and focus attention on developing a match between organisational strengths and environmental opportunities. This will enable the organisation to identify and satisfy existing customer requirements and anticipates and be prepared for future developments.

The operation of n differentiation strategy depends on effective market segmentation and targeting. The success of any differentiation strategy is dependent on the development of an integrated and coherent marketing mix. This requires the development of an appropriate product which is then priced, promoted and distributed in such a way as to produce an offered service which needs the needs of the target customers more effectively than competing products. Marketing mix is not just a series of tactical responses to changing market condition; it is a core component of any marketing strategy.

Check your progress 5

1. The main characteristics of __________are intangibility; inseparability, heterogeneity, perishability.

   a. services

   b. goods

2. __________is relevant only to the pure service element.

   a. tangibility

   b. Intangibility

3. Legal service is __________tangible, varied and can be performed away from the customer.

   a. Less

   b. More

4. A ____________is any act of performance that one party can offer to another that is essentially intangible and does not result in the ownership of anything.

   a. service

   b. Product

2.7 Marketing Mix for Financial Services

Marketing mix is one of the key concepts in the modern marketing theory. In practice the, marketing mix is considered to be the core of marketing. Neil Borden, while quoting from an article of Jame Culiton, wrote that a marketer is viewed as a 'decider', or an ‘artist’ or a 'mixer of ingredients' who plans various means of competition. "He may follow a recipe prepared by others, or prepare his own as he, goes along, or adopt a recipe to the ingredients immediately available, or experiment with or invent ingredients no one else has tried". If a marketer was a 'mixer of ingredients', what he designed was a marketing mix.

Borden further wrote that 'it was logical to proceed from a realisation of the existence of a variety of marketing mixes to the development of a concept that would comprehend not only this variety, but also the market forces that cause managements to produce a variety of mixes' (to fight competition). Subsequently, Borden's concept of marketing mix was given due recognition in the marketing theory.

- Marketing mix is the set of marketing tools that the firm uses to pursue its marketing objectives in the target market.

There are literally dozens of marketing mix tools. Mc Carthy popularised a four factor classification of these tools called the four Ps: Product, Price, Place (i.e. Distribution) and Promotion.

The particular marketing variables under each P are shown in the figure below:

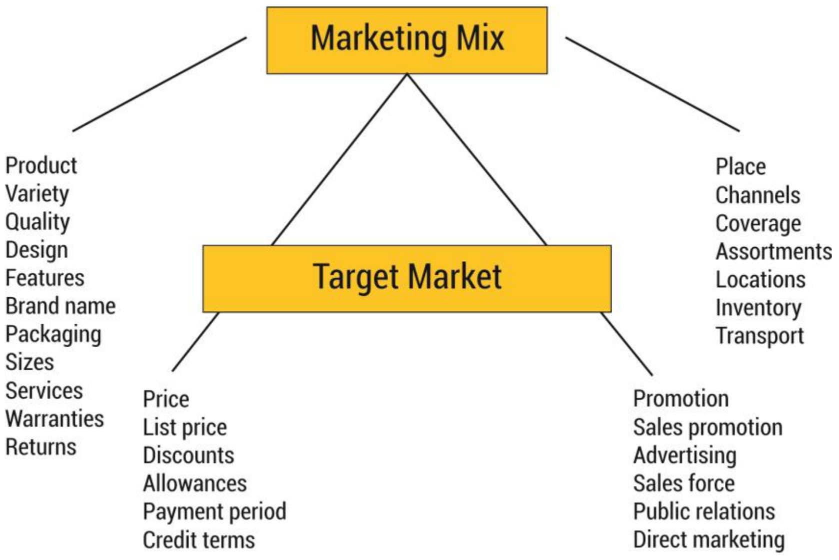

Fig 2.6 marketing mix

A marketing mix is selected from a great number of possibilities. Marketing mix decisions must be made for both the distribution channels and the final consumers. The following diagrammatic representation of a company's marketing mix strategy, by Kotler, points to the interplay of various factors and players in the market, which can affect the results of the marketing efforts.

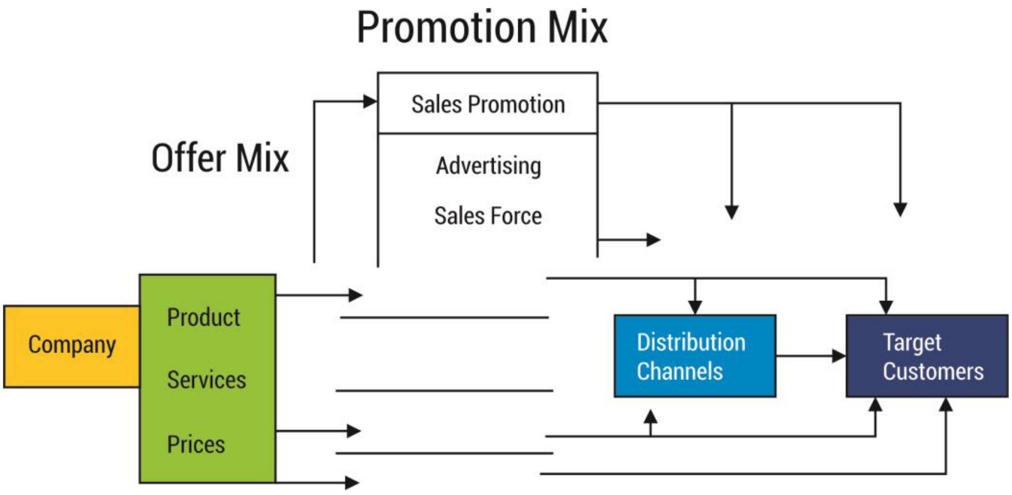

Fig 2.7 Promotion mix

A company may not be able to adjust all the marketing mix variables in the short run. Normally, the firm can change its price, sales force, size and advertising expenditures in the short run. Development of new products and modifications in its distribution channels, are more feasible in the long .run. Thus, the firm typically makes fewer period to period marketing mix changes in the short run than the number of marketing mix variables suggest.

The most basic marketing mix tool is product, which stands for the firm's tangible offer to the market, including the product quality, design, features, branching, and packaging. The company cold also provide various services such as delivery, repair, and training as well as running an equipment leasing business.

Place another key marketing mix tool, stands for the various activities the company undertakes to make the product accessible and available to target customers. The company must identify recruit and link various middlemen and marketing facilitators so that its products and services are efficiently supplied to the target market. It must understand the various types of retailers, wholesalers, and physical distribution firms and how they make their decisions.

Promotions, the fourth marketing mix tool, stands for the various activities the company undertakes to communicate and promote its products to the target market. Thus, the company has to hire, train, and motivate salespeople.It has to set up communication and promotion programmes consisting of advertising, direct marketing, sales promotion and public relations.

It may be noted that 4Ps represent the sellers' view of the marketing tools available for influencing buyers. From abuyer's point of view, each marketing tool is designed to deliver a customer benefit. Rober Lautherboln's suggesting was that the 4Ps correspond to the customers' 4Cs:

4Ps	**4Cs**
Product	Customer needs and wants.
Price	Cost to the customer
Place	Convenience.
Promotion	Communication

Winning companies will be those who can meet customer needs economically and conveniently and with effective communication.

Fig 2.8 P's of Target Market

Let us, therefore, see how each "P" is important in the context of marketing of banking services:

Product: Bank marketing is unique in the sense both product (services) and its delivery is very important. The product has to suit to customers' needs and wants. Customers are andrested in the variety (range) of products that suit to their needs. The quality of product/service is the factor which decides customer preference to select a product from the given range of products that suit to their needs by the same bank or different banks. The returns in terms of interest payable by the bank, the packaging (suitably scheme) its branding etc. like 'Suvidha scheme' or 'kamdhanu' or 'Grihavitta scheme' also count in customers choosing bank products.

Price: In the competitive banking scenario the price of a product is also very important as it reflects/matches with the cost to the customer. Although they know that the interest rate payable has a ceiling by IBAIRBI, the permutation combination of interest rate differentials mean a lot to customer in term of pricing. The interest rates charged on loans (short, medium and long term) and offered on deposits schemes by the banks is the impact of pricing most visible to customer to decide and choose abanks' product. Similarly, service fees, other charges do count to differentiate different products of banks.

Place: The studies by IBA (mentioned in subsequent units) indicate that safe and convenient place of abank (branch location) is perhaps the foremost preference area for a customer to opt for abank's products/services.

Promotion: How the bank tailors, markets and advertises its products is the key to success or otherwise in bank marketing'! Communication by abank with its customers and public at large through advertisements, brochures, and hoardings and through PR exercise in and out of its premises using its well-trained sales force enables it to create better image amongst to get more business. Let see in brief the importance and relevance of balance 3 Ps as well with respect to marketing of banking services:

People: This is the most important of the 7 Ps in bank marketing which includes the entire workforce of the bank i.e. executives, officers, employees and the subordinate staff. The banks policies and systems get converted into service only through people and that is why well-trained and motivated work force which is committed to better customer service as a mission is the back bone of abank's marketing efforts. The appearance of the counter staff, the interpersonal skills of the sales force, the positive behaviour and approach of those coming in contact with customersand reflecting right interest and care towards customers result into positive customer interaction which enables the bank to grow its business successively over the years.

Physical Evidence: With the growing competition, in the banking industry the right ambience which includes proper premises, furnishings, convenient layout, attractive atmosphere, courteous staff and required peripherals to ensure all sorts of help to the customer puts abank in a winning position vis-à-vis other competitors.

Process: Starting with the pro-active polices for better customer service anand simplified procedures/systems to facilitate fast work flow by the employees who are well empowered and who deliver the goods with quality consciousness for pleasing the customer, the process has to have a proper mix of quality, delegation, direction and discretion for effective customer service.

Check your progress 6

1. A company may not be able to adjust all the marketing mix variables in the ____________ run.
   a. Short
   b. long
2. The most basic marketing mix tool is ___________.
   a. price
   b. Product
3. ______________, the fourth marketing mix tool, stands for the various activities the company undertakes to communicate and promote its products to the target market.
   a. Promotions
   b. Place

2.8 Marketing Strategy and Financial Services

The key elements in determination of the marketing strategies tar financial services are the marketing objectives of the organisation, its target segment and its marketing mix. The process would involve the best possible selection of the elements of the marketing mix to enable the greatest degree of fit between the needs and wants of the selected target group and the organisation services offer such that. The exchange process results in value creation for the consumersand the organisation.

Once the organisation, looking at the needs of the target market determines what is sold to whom (decision on the service product), the pricing promotion and distribution will be easier to determine in practice, these determination of these elements involve a thorough understanding of buyer preferences and company capabilities. You will go through some of these inputs in subsequent blocks. In developing a marketing strategy for financial services, marketers would thus need to go through a two steps process: First to select or identify its target market or markets and then to design marketing mix to meet the needs of the target market better than its competitor.

Check your progress 7

1. The ___________ process results in value creation for the consumersand the organization.
   a. exchange
   b. Sale
2. In developing a___________strategy for financial services, marketers would thus need to go through a two steps process.
   a. sales
   b. Marketing

2.9 Let Us Sum Up

In this second unit we covered the topic marketing of financial services in very detail. Here in this unit we discussed about marketing and financial services in very detail, a detailed discussion was even made on the marketing as a functional area of management. Financial services and different marketing orientations were even discussed.We discussed here in very detail about the differences between services and products. The service was even discussed here in detail. The marketing mix of financial services was even discussed here in detail. In this block we discussed the evolution of service in very detail and how the production of services is given very much importance in today's world. After reading this block the readers would have got sufficient ideaabout the topics discussed in the unit above.

2.10 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b), (3-a), (4-b), (5-a)

Check your progress 2

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 3

Answers: (1-a), (2-b), (3-a), (4-b), (5-a)

Check your progress 4

Answers: (1-a), (2-b), (3-a)

Check your progress 5

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 6

Answers: (1-a), (2-b)

Check your progress 7

Answers: (1-a), (2-b), (3-a)

2.11 Glossary

1. **Perishable -** things, especially foodstuffs, likely to decay or go bad quickly.

2.12 Assignment

Discuss the Marketing as functional area of management.

2.13 Activities

Bring out the differences between the services and products.

2.14 Case Study

Discuss the various characterstics of services

2.15 Further Readings

1. Brean Andeston, 1995 "Financial Services", Macmillan Press Ltd., London.
2. Kimball Dietrich, 1996 "Financial Services and Financial Institutions Prentice - Hall, Inc. New Jersey.

UNIT 3: CONSUMER BEHAVIOUR FOR FINANCIAL SERVICES

Unit Structure

3.0 Learning Objectives

After learning this unit, you will be able to understand:

- Explain the importance of consumer behaviour analysis for marketing decision making.
- Describe the variables that affect consumer decision making for financial services.
- Discuss the impact of needs and motivation, perception and learning on buying of financial services.

- Elaborate on the impact of group and social variables like family, reference groups, culture and subculture on consumer decision making for financial services.
- Apply the various models of consumer behaviour for effective marketing of financial services.

3.1 Introduction

Some people regard marketing as an art. Others consider it a science. Actually it is a combination of the two. Marketing involves the effective blending of the behavioural science-anthropology, sociology, psychology with the communication, art writing, graphics, photography, drama, to motivate, modify or reinforce consumer perceptions, beliefs, attitudes and behaviour. To accomplish this, marketing professional must be constantly aware of the consumer's attitudes, beliefs, likes and dislikes habits, wants and desires. And since these are always changing, steps must be taken to monitor them.

As societies change their attitudes towards dress, recreation, morals, religion, education or even other people, marketing techniques also change. Because the behavioural characteristics of large groups of people give the directional force to any marketing 'efforts aimed' it those groups. Marketing tries to use the trends in mass consumer behaviour to effect changes in specific consumer behaviour.

3.2 The Complexity of Consumer Buying Decisions

While making even the simplest purchase, consumers go through a complicated mental process.

For us to appreciate the complexity of the consumer's buying decision, we need to understand the variety of individual influences on consumer behaviour; the impact of environmental factors such as family, social, and cultural influences on the consumer; and how these components are integrated in the consumer's mind.

A firm's marketing efforts interacts with non-commercial sources of information to stimulate the purchase decision process. This process is tempered by the individual in influences of consumer behaviour, including motivation, personality, learning and perception. The process stops when the consumer loses interest or evaluates the product and decides not to make a purchase. If the purchase is made, the consumer has an opportunity to see whether the product satisfies his or her needs. If not, the consumer will discontinue the use of the product.

Check your progress 1

1. While making even the simplest purchase, consumers go through a complicated ____________process.

   a. mental

   b. money

2. A firm's ____________efforts interacts with non-commercial sources of information to stimulate the purchase decision process.

   a. selling

   b. marketing

3.3 Individual Influences on Consumer Behaviour

The effort of all marketing is to influence people's buying behaviour, but it is difficult to foresee the success of planned marketing programs because human beings are all individuals. Each behaves differently, thereby making mass consumer behaviour patterns us see everyday:

- People vary in their persuability. Some are easily persuaded to do something; others are sceptical and difficult to convince.
- Some people have very 'cool heads' and control their emotions. Others are 'hot heads' and anger easily.
- Some people are loners, whereas others need the security of a crowd.
- Many people are oriented towards the acquisition of material things. Some people are motivated mainly by spiritual matters.
- Some people spend their money cautiously. Others spend their money extravagantly.

Many other contrasts in the behaviour of people could be noted such as interests in sports and hobbies, goal orientation, colour preference. All affect consumers' buying decisions.

To further complicate the marketer's goal of influencing consumer behaviour, consider these observations. First, people's attitudes, beliefs and preferences change. What we have liked as children we may not like as adult. That includes products, activities and living conditions.

Second, individual behaviour is inconsistent and difficult to predict from one day to the next. An individual may like to go out and have dinner today, but he may prefer to stay home tomorrow.

Third, people are often unable to explain their own behaviour. A man may say h e bought a shirt because he needed it and it was at a discount of 30%. The real reason may be different.

People often do not understand why they behave as they do. And if they do understand their true motivations, they may fear expressing them.For example, abusinessman who purchases a new Mercedes probably would be reluctant to admit it if the real reason for the purchase was his insecurity amongst his peer group.

Check your progress 2

1. The effort of all ____________is to influence people's buying behaviour,
   a. marketing
   b. selling
2. People vary in their ____________.
   a. structure
   b. Persuability
3. Individual behaviour is inconsistent and ___________to predict.
   a. Difficult
   b. easy

3.4 Needs and Motives

In the study of consumer behaviour, motivation is understood to mean the underlying drives that contribute to the individual consumer's buying action. These drives originate from some conscious or unconscious needs of the consumer.Unfortunately, motivations cannot be directly observed. When we see a person eat, we assume he is hungry, but that may not be correct. We eat for a variety of reasons besides hunger - to be sociable, because it is mealtime, because we are bored, or because we are nervous.

Often a combination of motives underlines our behaviour in making a decision. The reasons (motives) a person switches an account from the city bank to the people's bank may be (I) the people's bank is closer to work (II) it does 11ot charge for overdrafts and/or (III) the staff at the peoples bank are more friendly.

Psychologists have tried to categorise needs to understand them better. Abraham Maslow developed the widely used hierarchy of needs on the theory that the lower biological or survival needs are dominant in human behaviour and must be satisfied before higher, socially acquired needs become meaningful.

1) Physiological needs - food, drink, oxygen and sleep
2) Safety needs – avoidance/protection from threatening situations and economic security.
3) Social needs - friendship, affection and a sense of belonging.
4) Esteem needs - self respect, recognition, status and success.
5) Self-actualisation - self fulfillment.

Although Maslow's hierarchy is a convenient way to classify human needs, it would be a mistake to assume that needs occurs one step at a time. Usually people are motivated by a combination of needs.

The problem of analysing motivation for marketing purposes is aggravated by the fact that people are admittedly moved by both conscious and unconscious needs. To explore the depths of the unconscious, psychologists like Einest Dichter have developed a discipline called motivation research which although limited to very small samples of consumers and hampered by analytical subjectivity, has offered some insight into the underlying reasons for unexpected consumer behaviour.

Check your progress 3

1. ______________is understood to mean the underlying drives that contribute to the individual consumer's buying action.
   a. motivation
   b. leadership
2. Often a combination of ___________underlines our behaviour in making a decision.
   a. money
   b. motives
3. _________have tried to categorise needs to understand them better.
   a. Psychologists
   b. Marketers
4. Maslow's hierarchy is a convenient way to classify ___________needs.
   a. money
   b. human

3.5 Individual Perception

While an individual is motivated by his personal needs for self-esteem, love or social recognition, his behaviour is affected by his particular perception of himself and world around him.

Perception is the sensing of stimuli to which an individual is exposed-the act or process of comprehending the world in which the individual exists. E.g. when an individual looks at an automobile that he needs for transportation, he perceives more than a random collection of steel, glass, tyres and paint. He perceives an integrated entity designed to provide a variety of benefits-transportation, comfort, convenience, economy and even status for the driver

A person's perception of this integrated entity may be affected by the individual's self concept, needs and motivations, knowledge, past experience, feelings, attitudes and personality.

Self-concept and roles: We all carry images in our minds of whom we are and who we want to be. If a man wants to appear successful and wealthy, he may favour a 'Gold' credit card from Citibank of American express rather than from an Indian bank.

Marketers are very concerned with the perceptions that consumers have of their products or services, because to the consumer, the perception is the reality. As marketing consultant Howard Moskowitz says, if the consumer wants a 'natural taste' and if the consumer thinks lemonade with additives tastes natural, that's what we'll give her.

'Lemon flavour' is lemon flavour, whether you get it from .a tree or from chemical ingredients. The constituentsare different but what is perceived as lemon flavour is, lemon flavour. That’s reality, similarly a customer of an old nationalised bank say SBI or BOI will continue will be a valuable customer of that bank as long as his ego is not hurt and motives of security and convenience are satisfied. He would believe 'A bank is abank - why shift to another when he is happy with the present bank'.

Selective perception: One of the major problems that marketers face is the fact that each individual exercises selective perception.

As humans we have the ability to select from the many sensations bombaring our brains those that relate to our previous experience, need and desires.

The average adults are exposed to nearly 10,000 messages a day - twice as many as we, received 10 years ago. Yet most people are hardly aware of most of these, we are limited not only by the physical capacity of our senses but also by our interests. We focus attention on some things and avoid others. A single newspaper may contain hundreds of advertisements but the average reader recalls only few of these and is 50 influenced by even less

Recent research has shown that new automobile buyers are more likely to read advertisement about the brands of cars they have already purchased than about competitive makes.This electivity makes it important marketers to obtain satisfied customers and build brand royalty, and the product to fit the image created by advertising. Satisfied customers will be less likely to obtain information about competing products and probably will not even notice it when it is forced on them. Bank customers often prefer to see/read the ADSL messages of their own banks that re-enforce their perceptions/feelings about security and returns through their banking products. Unless a new bank or its products has something very special and attractive or very unconventional and yet convenient and convincing; such customer may not be diverted easily.

Theory of cognitive dissonance: Selective perception services us in many ways. Besides saving us time by filtering out irrelevant uninteresting data, it protects us from having to face unpleasant realities. Leon Feslinger developed a theory of cognitive dissonance, which states basically that people strive to justify their behaviour by reducing the degree to which their impressions or beliefs are inconsistent with reality (dissonance).

For example, people who use a 'diners club' credit card because they believe it is the most prestigious and widely accepted card, may receive a mailer from 'ANZ Grindlays that proves that their gold card is even more exclusive with many more advantages. This exposure may create dissonance because of the gap between current thinking and 'new evidence'. Marketers such and ANZ Grindlays hope that the recipient experiences dissonance because the 'Diners club' card holder upon seeing the 'proof ' of greater effectiveness or value might than relieve the uncomfortable tension resulting from the dissonance by applying for an ANZ Grindlays card

Check your progress 4

1. ___________is affected by his particular perception of himself and world around him.
   a. behavior
   b. motivation
2. __________is the sensing of stimuli to which an individual is exposed-the act or process of comprehending the world in which the individual exists.
   a. Motivaton
   b. Perception
3. ___________are very concerned with the perceptions that consumers have of their products or services.
   a. Marketers
   b. sellers
4. ___________are more likely to read advertisement about the brands of cars they have already purchased than about competitive makes.
   a. sellers
   b. buyers

3.6 Learning and Habit Development

Another individual influence on consumer behaviour is the way in which consumers learn new information and developed purchasing habits. The major objective of marketing is to teach people about products and where to buy them. So marketers are interested in how people learn. Many psychologists consider learning to be the most fundamental process in human behaviour. The advance, 'higher level' needs, for example, are learned. Learning produces our habits and skills. It also contributes to the development of attitudes, beliefs, preferences, prejudices, emotions and standards of conduct.

Learning is a relatively permanent change in behaviour that occurs as a result of reinforces practices. Theories of learning are numerous but Most Can be classified into two broad categories: cognitive and stimulus-response theory.

Cognitive theory views learning as a mental process of memory, thinking and the rational application of knowledge to practical problem solving. This theory may be an accurate description of the way we learn in school.

Stimulus response theory, on the other hand, treats learning as a trial and error process whereby needs, motives or drives are triggered by some cue or stimulus to cause the individual to respond in an effort to satisfy that need. Satisfaction, then rewards or reinforces the response by reducing the drive and producing repeat behaviour the next time the drive is aroused.

Let us examine how the stimulus-response theory works in marketing. Advertising is a stimulus or cue, while a purchase is a response. The motivation is to satisfy various needs. If the product that the consumer purchases gives satisfaction then there is some reinforcement Additional reinforcement may be given through superior product performance, good service, and the reminder advertising. The advertisements by banks like Citibank or Global trust bank on T.V., in news papers and at public places like airport, railway station or bus stops re-enforces the response to the stimulus created about its products and services with respect to safety, security, utility and status appeal - which is re-enforced by repetition. The publicity campaign and hoarding by banks like UTI or HDFC bank regarding one counter service or service with guidance to meet the needs easily have similar re-enforcing effect on bank customers-both existing and probable.

Through repetition of the cues (advertisements) the learning process, including memory, may be reinforced and repeat behaviour encouraged. Learning may be further enhanced by engaging the consumer's participation in the process through the use of free samples or in-home trials of the product. Finally if learning is reinforced enough and repeat behaviour produced,a purchasing habit may result.

Habit is the natural extension of learning. It is the acquired or developed behaviour pattern that has become nearly or completely involuntary. The old cliché 'people are creatures of habit' is true.

Why most consumer behaviour is habitual: There are three reasons that consumer behaviour is habitual. First we resort to habit when we select products because it is easy. When we consider an alternative to an existing brand choice, we are forced to think, evaluate, compare aid then decide. This is difficult for most of us, not to mention risky. We may be dissatisfied with the new choice.

Second, we rely on habit because of necessity. Consider the person who purchases 25 items at a provision, store. To evaluate all the features and ingredients of competitive, brands would require hours, which no one has the time-or the inclination to do.

Third, we resort to habit because it is the rational thing to do, as we learn through trial and error which brands, serve us well and which do not, we also learn which stores and service outlets satisfy us and which do not. When we find a product or service of abank to our liking we continue to buy the product, patronize the bank branch, because it is the intelligent choice to make.

Marketers have three Habit-related Goals

1) **Habit breaking** - a device to get consumers to break an existing purchase habit that is to stop buying their habitual brand and try a new brand. Many promotional devices are used to attract consumers to a new product or visit a new store once. Giving away free samples, introductory trial offer, limited time price offers, store opening special prices etc. are some of the methods used to generate customer, traffic and new clientele.

2) **Habit acquisition** - to get consumers to acquire a habit of buying from their establishment. To build a product preference habit, marketers may use 'reassurance' advertising to remind customers of an earlier purchase response. Examples of advertising themes designed to build purchasing habits are:

   'The Citi never sleeps' for Citibank’s round the clock services; 'don’t leave home without it' for American express cards.

3) **Habit reinforcement** - once consumersare won over, to get them to remain habitual users. Each time a consumer uses a product and is satisfied with it,

the habit is reinforced. Continued satisfaction may reinforce the habit to such a degree that the purchase decision .is virtually automatic. Examples of second and third generation customers of banks around in each city.

Check your progress 5

1. Learning is a relatively ___________change in behaviour that occurs as a result of reinforces practices.
   a. permanent
   b. temporary
2. ____________theory views learning as a mental process of memory, thinking and the rational application of knowledge to practical problem solving.
   a. Stimulus response
   b. Cognitive
3. _____________theory, on the other hand, treats learning as a trial and error process whereby needs, motives or drives are triggered by some cue or stimulus to cause the individual to respond in an effort to satisfy that need.
   a. Stimulus response
   b. Cognitive
4. ______________is the natural extension of learning.
   a. Buyer
   b. Habit

3.7 Family Influences on Buying Behaviour

We are all aware as to how our needs and expectation change over different stages in our lifecycle.Your priorities as a teenager or a young adult or a family man are very different. These differences are important and marketer as they enable the marketer to fine tune his marketing effort by using family life cycle as a segmentation variables

The family life cycle was developed in 1960, and was based on variables like martial status, number and ages of children, work status and age. It has since then, been widely 'used as a segmentation tool.

Because our age, income and family requirements, except for the basic necessities change over time, the family life cycle and identification of family needs over various stages of the FLE are useful inputs to the marketer. The family life cycle consists of 5 stages, the young bachelor stage, the full nest I, the full rest I1 the empty nest and the solitary survivor stage. Expenditure priorities and need for money at different stages have interesting implication for the demand for various financial services. Figure gives you an idea of varying requirements of consumers for banking services.

Family Life Cycle and Banking Needs

Stage	**Financial Situation**	**Banking Needs**
Young Bachelor Stage	Few financial burdens Per capita income high Income low as compared To future prospects	Credit Cards, auto loan low cost banking services
Fullest Married	Home buying a priority	Mortgage, Credit Card
With young children	liquidity low may have	overdraft savings account
Working couples situation	housing and durables loans	
Fullest Older	Income stabilised. Good	Home improvement loans
Married with older	Financial position, mid equity investments certificate dependent children career, comfortable. Position, money involving Matters	Of deposits money market deposit accounts fixed or flexi deposits other Investments services

Empty nest-Older Couple, with children Now not living at home May be retired	Significantly reduced income	Social security services, few loan services, med claim services

Check your progress 6

1. Our needs and expectation ___________over different stages in our lifecycle.
   a. change
   b. dont
2. The family life cycle was developed in____________.
   a. 1980
   b. 1960
3. _______________life cycle was based on variables like martial status, number and ages of children, work status and age.
   a. Family
   b. product

3.8 Behavioural Models for Analysing Buyers

Four different models of the buyer's 'black box' are detailed along with their respective marketing applications:

- The Marshallian model, stressing economic motivations
- The Pavlovian model, learning
- The Freuidian model, psycho-analytical motivations
- The Veblenian model, psyclto-social factors

The Marshallian Economic Model

Economists were the first professional group to construct a specific theory of buyer behaviour. The theory holds that the purchasing decisions are the result of largely 'rational' and conscious economic calculations. The individual buyer seeks to spend his income on those goods that will deliver the most utility or value' (satisfaction) according to his tastes and relative prices.

Adam Smith set the tone by developing a doctrine of economic growth based on the principle that man is motivated by self-interest in all his actions. Jeremy Benthan refined this view and saw man as finely calculating and weighing the expected pleasures and pains of every contemplated action.

Alfred Marshall was the great consolidator of the classical and neoclassical tradition in economics. His theoretical work, but his method was to start with simplifying and to examine the effect of a change in a single variable (say price) when all other variables are kept constant. Over the years his methods and assumptions have been refined into what is now known as the modem utility theory: economic man is bent on maximising his utility and does this by carefully calculating the consequences of any purchase

Marketing Applications of Marshallian Model

From one point of view the Marshallian model is tautological and therefore neither true nor false. The model holds that the buyer acts in the light of his best 'interest'. But this is not very informative.

A second view is that this is a normative rather than a descriptive model of behaviour. The model provides logical norms for buyers who want to be 'rational'. Although the consumer is not likely to employ economic analysis to decide between abox of 'ship' and 'Shakti’ matched, he may apply economic analysis in deciding whether to buy a new car.

A third view is that economic factors operate to a greater or lesser extent in all markets and therefore must be included in any comprehensive description of buyer behaviour. Furthermore, the model suggests useful behavioural hypotheses such as:

- The lower the price of the product, the higher the sales. In banking context, it applies to increase in advance with lowering of 'interest rates.
- Tile lower the price of substitute products, the lower the sales of this product and the lower the price of complementary products, the higher the sales of this product in case of over drafts and loans.
- The higher the real income, the higher the sales of this product, provided it is not an 'inferior' product holds good regarding medium and long term deposits if perceived as safe and interest rate is reasonable.

- The higher the promotional expenditures, the higher the sale applies to credit cards, consumer loans and ATM cards.

The validity of these 'hypotheses does not rest on whether all individuals act as economic calculating machines in making their purchasing decisions. For example, some individual may buy less of a product when its price is reduced. They may think that the quality has deteriorated or that the ownership has less status value.

If majority of buyers view price reduction negatively, then sales may decrease, contrary to the first hypotheses.

But for most goods a price reduction increases the relative value of the goods in many buyers’ minds and leads to increase sales. This and the other hypotheses and intended to describe average effects. This is observed in respect of reduction of interest rates in case of loans by banks.

The impact of economic factors in actual buying situations is studied through experimental design or statistical analyses of past data. Demand equations have been fitted to wide variety of products. More recently, the impact of economic variables on the fortunes of different brands has been pursued with significant results.

But economic factors alone cannot explain all the variations in sales. The Marshallian model ignores the fundamental question of how product and brand preferences are formed. It represents a useful frame of reference for analysing only one small corner of the buyer's mind the 'black box'.

The Pavlovian Learning Model

This has its origins in the experiments that Russian psychologist named Pavlov conducted on dogs. Pavlov rang abell each time before feeding a dog.Soon he was able to induce the dot to salivate by ringing the bell whether or not food was supplied. Pavlov concluded that learning was largely an associative process and a large component of behaviour was conditioned this way. The model has been refined over the years, and is today based on four central concepts - those of drive, cue, response and reinforcement.

Drive: Also called needs or motives, drive refers to the strong stimuli internal to the individual which impels action. Psychologists draw a distinction between primary physiological drives such as hunger, pain, cold, thirst etc. and learned drives which re derived socially such as cooperation, fear acquisitiveness. A customer of abank once recognised and responded positively will show drive to come again and again.

Cue: A drive is very general and impels a particular response only in relation to a particular configuration of cues. Cues are weaker stimuli in the environment and or in the individual which determine when, where and how the subject responds. Thus, a cold drink advertisement can serve as a cue which stimulates the thirst drive in a child. His response will depend upon this cue and other cues, such as the time of day, the availability of other thirst quenches and the cues intensity.

Response: The process is the organism's reaction the configuration of cues. Yet the same configuration of cues will not necessarily produce the same response in the individual. This depends on the degree to which the experience was rewarding, that is, drive reducing. A bank customer would demonstrate his behaviour satisfied or otherwise depending on his past experience.

Re-enforcement: If the experience is rewarding, a particular response is re-enforced; that is it is strengthened and there is a tendency for it to be repeated when the same configuration of cues appears again. An individual for example, will tend to frequent the same bank outlet so long as it is rewarding convenient, fast friendly, flexible) and the cue configuration does not change. But if a learned response or habit is not re-enforced, the strength of the habit diminishes and may be extinguished eventually. Thus, an individual may acquire a new credit card, if the existing card has some limitations or drawbacks. Or he may change his bank due lo location, timing service standards, facilities etc.

Forgetting, in contrast to extinction, is the tendency for learned associations to weaken, not because of the lack of reinforcement but because of non-use.

Cue configurations are constantly changing. The individual may see a new bank branch near his house, or a special advertising offer for abank credit card. Experimental psychologists have found that the same learned response will be elicited a similar pattern of cues; that is, learned responses are generalised. A housewife wills buy a similar brand of tea when her favourite brand is out of stock.

A counter tendency to generalization discrimination: When an individual uses two banks and finds one more rewarding - in terms of location, timings, speed, courtesy, facilities, etc. his ability to discriminate between similar cue configurations improves.

Discrimination increases the specificity of the cue response connection, while generalisation decreases the specificity

Marketing application of the Pavlovian Model

The modern version of the Pavlovian model makes no claim to provide a complete theory of behaviour such important phenomenaas perception, the subconscious, and interpersonal influences are inadequately treated. Yet the model offers insights about some aspects of behaviour of considerable interest to marketers

Light introductory advertising is a week cue compared with distributing free samples. Strong cues, although costing more, may be necessary in markets characterised by strong brand loyalties.

For example new credit cards issuers frequently resort to waiving membership fees for a limited time promotional offer to attract new members.

To build abrand habit, it helps to provide for a period of introductory offer. Sufficient quality of product or service must be built into the brand so that 'brand experience' is reinforcing. Since buyers are more likely to switch to similar brands than dissimilar ones (generalisation), the company should investigate what cues in the leading brands have been most effective. Outright imitation may not provide the most transference, the question of providing enough similarity should be considered. (Notice the levels of exclusivity conveyed by the colouring/ naming of credit cards as 'silver', 'gold', and 'Platinum')

The Pavlovian model also provides guidelines in marketing and advertising strategy. The Pavlovian model emphasizes the desirability of repetition in advertising. A single exposure is likely to be a weak cue, hardly able to penetrate the individual's consciousness sufficiently to excite his drives above the threshold level.

Repetition in advertising/marketing messages has two desirable effects.In fights forgetting, the tendency of learned responses to weaken in the absence of practice. It provides reinforcement because after the purchase the customer becomes selectively exposed to advertisements of the products.

Tile model also provides guidelines for 'message' strategy. To be effective as a cue, an advertisement must arouse strong drives in the person. The strongest product related drives must be identified. For chocolates, it may hunger' for cars, it may be status, for safety belts, fear. The marketing and advertising practitioners must search his cue box - words, colour pictures and select that configuration of cues that provides the strongest stimulus to these drives.

The Freudian Psychoanalytic Model

According to Freud, the child enters the world driven by instinctual needs which he cannot gratify by himself. Very quickly and painfully he realises his separateness from tile rest of the world and yet his dependence on it. He tries to get others to gratify his needs through a variety of blatant means, including intimidation and supplication. Continual frustration leads him to perfect more subtle mechanisms for gratifying his instincts.

As he grows, his psyche becomes increasingly complex. A part of his psyche-the id remains the reservoir of his strong drives and urges. Another part the ego becomes his conscious planning centres for finding outlets for his drives. An a third part his super ego channels his instinctive drives into socially approved outlets to avoid the shame of pain or guilt

The individual's behaviour, is therefore, never very simple. His motivational wellsprings tire not obvious to the casual observed not deeply understood by the individual himself If asked why he purchased an expensive sports car, he may reply that the liked its speed and shape, Ata deeper level he may have purchased the car to impress others, or to feel young again. At a still deeper level, he may be purchasing the sports car to achieve substitute gratification for unsatisfied sexual strivings.

Many refinements and changes in emphasis have occurred in this model. The instinct concept has been replaced by more careful delineation of basic drives; the three parts of the psyche are regarded now as theoretical concepts rather than actual entities; and the behavioural perspective has been extended to include cultural as well as biological mechanism

Marketing Applications of the Freudian Model

Perhaps the most important marketing implication of this model is that buyers are motivated by symbolic as well as economic functional product concerns. The change of abar of map form a square to a round shape may be more impel-taut in its sexual than its 'functional connotations. A cake mix that is advertised as involving practically no labour may alienate housewives because the easy life may evoke a sense of guilt.

Motivation research has proved some interesting and bizarre hypothesis about what may be in the buyer's mind regarding certain purchases

Motivational researchers have to employ time consuming projective techniques in the hope of throwing individual 'egos' off guard. When carefully administered and interpreted, techniques such as word association, sentence completion, picture interpretation and role playing can provide some insights into the minds of the small group of examined individuals; but a 'leap of faith' is sometimes necessary to generalize these findings to the population.

Nevertheless, motivation research can lead to useful insights and provide inspiration to creative men in advertising and marketing. Appeals aimed at the buyer's private world hopes, dreams, and fears fan often be as effective in stimulating purchase as more rationally-directed appeals

The Veblenian Social - Sociological Model

While most economists have been content to interpret buyer behaviour in Marshallian terms, Thorstein Veblen struck out in different directions.

Veblen was trained as an orthodox economist but evolved into a great social thinker. He was man primarily as a social animal conforming to the general forms and norms of his larger culture .and to the more specific standards of the subcultures and face to face grouping to which his life is bound. His wants are greatly moulded by his present group memberships and his aspired group memberships.

Veblin's best known example of this is in his description of the leisure class. His hypothesis to that much of economic consumption is motivated not by intrinsic needs or satisfaction so much as by prestige seeking. He emphasized the strong emulative factors operating in the choice of conspicuous goods like clothes, cars and houses. Some of his points, however, seem overstated by today's perspective. The leisure class does not serve as everyone's reference group many persons aspire to the social patterns the class immediately above it. And important segments of the affluent class practice conspicuous under consumption. There are many people in all classes who are more anxious to 'fit in' than to 'stand out'. As an example, William H. Whyte found that many families avoided buying air-conditioners before their neighbours did.

Marketing Applications of the Veblenian Model

The various streams of thought crystallized into the modern social sciences of sociology, culture anthropology and social psychology. Basic to them is the view that man's attitude and behaviour are influenced by several levels of society culture, subcultures, social classes, reference groups, and face to face groups. The challenge to the marketer is to determine which of these social levels are the most important in influencing the demand for his product.

Culture

The most enduring influences are from culture. Man tends to assimilate his culture's mores and folkways, and to believe in their absolute rightness until he confronts member, of another culture.

Subculture

A culture tends to lose its homogeneity as its population increases. When people no longer are able to maintain face to face relationships with more than asmall proportion of other members of a culture, smaller units or subcultures develop which help to satisfy the individual's needs for more specific identity.

The subcultures are often regional entities, because the people of a region, as a result of more frequent interaction, tend to think and act alike. But subcultures also take the form of religion, nationalities, fraternal orders and other institutional complexes which provide abroad identification for people who are strangers. The subcultures of a person play a large role in his attitude formation and become another important predictor of certain values he is likely to hold.

Social Class

People become differentiated not only horizontally but also vertically through a division of labour.The society becomes stratified socially on the basis of wealth, skill, and power. Sometimes castes develop which the members are reared for certain roles or social classes develop in which the members feel empathy with others sharing similar values and economic circumstances.

Because social class involves in different attitudinal configuration, it becomes a useful independent variable for segmenting markets and predicting reactions. Significant differences have been found among different social classes with respect to magazine readership, leisure activities, food imagery, fashion interests, and acceptance of innovation. A sampling of attitudinal differences in class is the following with respect to their banking habits:

Members of the upper middle class place an emphasis on professional competence; indulge in expensive status symbols; and more often that not show a taste, real or otherwise, for theatre and the arts. They want their children to show high achievement and precocity and develop into physicists, vice-presidents and judges. The classes like to deal in ideas and symbols. They, besides recurring and fixed deposits also take pride in credit cards and ATM.

Member of the lower middle class cherish respectability, bank savings, college education and good house-keeping. They want their children to who self-control and prepare for careers as accountants, doctors, lawyers and engineers. They prefer to keep amounts in fixed deposits to meet future needs.

Members of the lower class try to keep up with the times, if not with the Mehtas. They stay in older neighbourhoods but buy new kitchen appliances. They spend proportionately less than the middle class on major clothing articles, buying a new suit mainly for an important ceremonial occasion. They tend to raise large families and their children generally enter manual occupations. This class also supplies many local storekeepers, garage owners, politicians, sports stars and labour-union leaders. Such segment keeps their funds in savings banks mainly for getting liquid funds to be available in case of day to day needs.

Reference Groups

There are groups in which the individual has no membership but with which he identifies and may aspire to reference groups. Many young boys identify with test cricket players or astronauts, and many young girls identify with Hollywood stars. The activities of these popular heroes are carefully watched and frequently imitated. These reference figures become important transmitters of influence, although more along lines of taste and hobby than basic attitudes.

Face to Face Groups

Groups that have the most immediate influence on the person's tastes and opinions are face to face groups. This includes all the small 'societies' with which he comes into frequent contact: his family, close friends, neighbours, fellow workers, fraternal associates and so forth. His informal group memberships are greatly influenced by his occupation, residence and stage in the life cycle.

'The powerful influence of small groups on individual attitudes has been demonstrated in a number of social psychological experiments. There is also evidence that this influence might be growing. David Riesman and his co-authors have pointed to signs which indicate a growing amount of other direction, that is, a tendency for individuals to be increasingly influenced by their peers in the definition of their values rather than by their parents and elders

For the marketer, this means that brand choice may increasingly be influenced by one's peers. For such products as cigarettes and automobiles, the influence of peers is unmistakable.

The role of face to face groups has been recognised in recent industry campaigns attempting to change basic product attitudes. For years the milk industry has been trying to overcome the image of mild as a 'satisfied' drink by portraying its use in social and active situation. The men’s wear industry is trying to increase male interest in clothes by advertisements indicating that business associates judge a man by how well he dresses.

Of all face to face groups, the person's family undoubtedly plays the largest and most enduring role in basic attitude formation. From them, he acquires a mental set not only towards religion and politics, but also toward thrift, chastity, human relations land so forth. Although he often rebels against parental values in his teens, he often accepts these values eventually. Their formative influence on his eventual attitudes is undeniably great. Family members differ in the types of product messages that they carry to other family members. Most of what parents know about cereals, candy and toys comes from their children. The wife stimulates family consideration of family appliances, furniture and vacations. The husband tends to stimulate the fewest purchase ideas, with the exception of the automobile and perhaps the home.

The marketer must be alert to what attitudinal configuration dominates in different types of families and also to how these change over time. For example the parent's ideas about the child's rights and privileges have undergonea radical change in the last 30 years. The child has become the centre of attention and orientation in a great number of house holds, leading some writers to label the modern family a 'filliarchy'. This has important implications not only for how to market for today's family but also on how to market to tomorrow's family when the indulged child to today becomes the parent

Check your progress 7

1. ___________were the first professional group to construct a specific theory of buyer behaviour.

   a. Economists

   b. Sellers

2. ___________set the tone by developing a doctrine of economic growth based on the principle that man is motivated by self-interest in all his actions.

   a. Alfred Marshall

   b. Adam Smith

3. ___________was the great consolidator of the classical and neoclassical tradition in economics.

   a. Alfred Marshall

   b. Adam Smith

4. If majority of ___________view price reduction negatively, then sales may decrease, contrary to the first hypotheses.

   a. sellers

   b. buyers

3.9 Consumer Behaviour: Some, Learning Points for Financial Services

It is said, satisfaction suffices, but delight dazzles. Average services set up will compete for the customer by conforming to his/her expectations consistently. Winner will surpass by constantly exceeding expectations, delivering at doorstep additional benefits which the investor would never have imagined possible.

A personal loan to a cash strapped investor, surprises and leading to satisfaction will retain the customer-investor. Telling the investor new opportunities and helping him or her invest, If no cash with the customer, get a loan for him/her under a guarantee you offer to the lender and help your customer invest and help him/her reap benefits. Yes, it is that is where how you can hold your customer with you and the customer is in need of such entrepreneurs who will look after him/her at all times. If you call fill the bill then you are most needed

Reward always your loyal customer before your customer thinks he/she deserves specials from you.

Similarly hold back your potential defector, attract the fence sitters. Serve up unparalleled value to your customer, is the watch word in the new millennium customer psyche. After all why he or she should be with you and for what if you cannot take care, of him or her.

Pradeep Kar, Managing Director of Microland, says:

'Customer delight docs not end at the front-office of a company it (just) begins there.'

Abraham Koshy, a Professor of JIM-A, says:

'Customer delight should add value to both the customer and the company. Don't provide abee lunch'.

What is a delight -- It is a fulfilment of latent needs that the customer is not yet aware of - a quality of service that he/she does not consider possible from marketers compete personalization of a standardized product or service an unexpected benefit that does not result in profits for the company solutions to problems offered, by a company's personnel at personal initiatives.

What justifies a delight only continuously rising satisfaction levels can hold back potential defectors ever-rising value strengthens the loyalist's resolve not to switch to the competition the promise of constant surprise turns experimenters into life long customers entry barriers are raised for new competitors who have to set new standards and the compulsion to innovate constantly leads to pay-offs in cost reductions and quality.

How to generate delight? Strive constantly to provide additional customer value in every transaction, use a flexible service envelope around the core product to generate surprise benefits, constantly surpass expectations that the customer has built around your product or service treat every customer as though he/she is the only customer whom the company wants, look for expectation performance gaps in order to identify opportunities to delight.

R. Sridar of Ogilvy and Mather says -

If you want to drive competition crazy, ignore your competitors and concentrate on your customer one-on-one. You won't find a more potent competitive weapon than that. Hence, it is relevant to know that the only safe way to bet on market is to assess whether a company is capable of creating greater value for the customer than its rivals. The challenge there is to attain a value insight. In fact while the value system is market specific, it is influenced by the level of consumer evolution and the nature of alternatives available as well as the cultural conditioning of customers.

C.K. Prahalad and Garry Hamel's concept is that in emerging markets there is a great need, for foresight because of rapid pace of change which needs an understanding of future drivers of value of three planes, Macro consumer changes plane, competitive offerings plane and the categories codes plane. Value foresight being crucial in the emerging markets, needs an understanding of the likely changes in the value system driven by historical events, fresh competition and the new cultural categories.

Check your progress 8

1. ____________suffices, but delight dazzles.
   a. satisfaction
   b. money
2. ___________always your loyal customer before your customer thinks he/she deserves specials from you.
   a. benefit
   b. Reward

3.10 Let Us Sum Up

In this unit we have focussed on consumer behaviour for financial services. In this unit we discussed the complexity of consumer buying behaviour.

In this unit the various behavioural models for analysing buyers were even discussed in detail.The family influences on buyer behaviour were even discussed here in detail.In this unit efforts have been made to explain every aspect of consumer behaviour in relation with financial services. Some of the very important learning points were even discussed here in this unit.

After this detailed discussion the readers would have got the sufficient knowledge about this topic.

3.11 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b)

Check your progress 2

Answers: (1-a), (2-b), (3-a)

Check your progress 3

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 4

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 5

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 6

Answers: (1-a), (2-b), (3-a)

Check your progress 7

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 8

Answers: (1-a), (2-b)

3.12 Glossary

1. **PLC -** Product life cycle

3.13 Assignment

Write abrief note on needs and motives.

3.14 Activities

Write abrief note on individual perception.

3.15 Case Study

Discuss the family influences on buying behavior.

3.16 Further Readings

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4. National Automated Clearinghouse Association Website (http/www.racha.corn March 1997).
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UNIT 4: BANKING PRODUCTS AND SERVICES

Unit Structure

4.0 Learning Objectives

After learning this unit, you will be able to understand:

- Describe the concept and significance of banking product types and product cycles.
- Explain the concept of product and service.
- Understand the product strategies as applicable to banking.

- Discuss the process of product analysis and product development.
- Evaluate the role of brand in marketing of banking services.

4.1 Introduction

The product/service offering is among the most crucial element in marketing of banking services.

The service is integral part of product in banking and is at timesan indivisible part of any banking product. Similarly whether we talk of brand or selling a product, the institution (bank) is always the deciding factor in product design and delivery as the customers do not look at any product in isolation but look at it as the particular bank's product.

In this unit we will discuss the important concepts of the types of banking products, product life cycle, product strategies, product analysis, product development and innovation and role of brand in marketing of bank's services.

4.2 Nature of Product

A product is defined as: "Anything that has the capacity to provide the satisfaction, use or perhaps the profit desired by the customer." Product and service are the words used interchangeably in banking parlance.

It must be remembered that whatever be the form in which a product or service is provided; the focus willbe on the want and need satisfying aspects of that product or service. Without such a focus on the customer’s wants need satisfaction no product service can exist for long.

For a product or service, when it is marketed the following two aspects are very significant:

i) Offer - what is offered say a product at a price, and

ii) Manner of offering - how it is offered i.e. the manner of product delivery.

The product includes quality, features, accessories, packaging, brand, warrant, etc. As the services are marketed like the products, products also include services.

An organisation may offer different product lines, each product line comprising of different product varieties all of which collectively represent a product mix.

Product planning, as it is called, comprises of the process of developing and maintaining a portfolio of products which satisfy the wants and needs of customer from different segments. Such product planning has to ensure maximum utilisation of skills and resources of an organisation.

This product planning function consists of decisions on:

1) Product Line

2) Product Mix

3) Branding

4) Packaging

5) New Product Development

In the following paragraphs we shall discuss all the above aspects elaborately.

Check your progress 1

1. A ____________is defined as: "Anything that has the capacity to provide the satisfaction, use or perhaps the profit desired by the customer."

   a. product

   b. service

2. The ____________includes quality, features, accessories, packaging, brand, warrant, etc.

   a. service

   b. product

3. An organisation may offer different product lines, each product line comprising of different product varieties all of which collectively represent _____________.

   a. Product mix.

   b. Product range

4.3 Products and Services in Banking

As we have seen, a product is abundle of all kinds of satisfaction of customer's wants and needs.

Products can be goods, a service or goods + service or even just an idea. A product is, in short, all the things offered to a market. It can involve physical objects, design, brand, package, price, services, literature, attractive ideas, personalities or even the image of abank or its branch.

It is thus essential to define a product or service in terms of product functions i.e. what the customer expects from a product or service offered by abank.

The normal connotation to differentiate between the product and the service is that the product is something tangible and service means something intangible. In general marketing terms, word- product is mostly used. Philip Kotler defines a product as:

"A product is anything that can be offered to a market for attention, acquisition, use or consumption; it includes physical objects, services, personalities, places, organisations and, ideas."

The bank's products are its deposit or borrowing scheme or other products like credit card or foreign exchange transaction which are tangible and measurable whereas service can be such products including the way /manner in which they are offered which cannot be shown but expressed.

But if two banks have same or similar products and pricing; it is the service (though abstract) which differentiates between these two banks and the better service (delivery or offering) which wins customer's confidence and satisfies him.

It can, therefore, be said that the better service is even more important than just a good product when we talk about marketing of banking services.

We will discuss more elaborately about various services offered by abank various types of deposits and services offered by abank.

Different Banking Products

The discussion and process of understanding the bank marketing will not be complete unless we know the various products/schemes tailored by different banks to cater effectively to the customers needs. Important among the banking products are the following:

Deposit Accounts

Knowing the human behaviour with respect to wants and needs or rather making wants to be felt as need is the first challenge in marketing of bank's schemes. The second challenge is the resistance to change and/ or new ideas which becomes a touch barrier in the process of marketing products/services of abank.

Banks, therefore, tailor various deposits schemes and market them to either their/ existing customer or the new segments of customers. Before selling the deposit schemes, it becomes necessary to identify the needs and aspirations of the customers to make them most ideal and acceptable to satisfy their needs.

From the marketing angle the different deposit schemes of the bank can be grouped on the basis of:

- The mode of deposit
- The mode of repayment
- Additional benefits
- The end use of accumulated funds
- The calculation and payment of interest
- Need for liquidity, safety, growth, etc.

Let us illustrate a few schemes on these criteria:

Need	Deposit
1. Personal Saving, Liquidity, easy withdrawal	Saving
2. Turnover, many transactions business	Current
3. Interest income required and lump sum saving	Fixed deposit monthly int. Dep. scheme, quarterly int. Dep. scheme, cumulative Deposit scheme

4. Gift to some one	Gift cheque, Festival Deposit Certificates
5. Safe Travel	Travellers Cheque
6. Deposit in small instalments	Recurring deposit scheme, Daily deposit

Let us first discuss the type of 'main deposits' from the broad classification point.

- **Savings Deposit:**

Means a form of deposit which is a deposit account titled as savings account, savings bank account or savings deposit account which is subject to restrictions about the number of withdrawals there from (RBI Directive dt.27.12.85)

Current Deposit Account

Means a form for deposit from which withdrawals are allowed freely, any number of times depending upon the balance in the account or up to a particular agreed amount and Shall be deemed to include other deposit accounts which are neither savings deposit nor term deposit (RBI Directive dt.27.12.85)

Demand Deposit

Means a deposit received by abank which is withdraw able on demand. S.B., CIA and overdue deposits are the examples of demand deposits. Customers having these accounts can withdraw their deposits from their accounts at any time they desire.

Time Deposit

Are deposits which are not repayable on demand. Such deposits are repayable on a fixed date in future which is termed as a due date. Rate of interest for the said period is contracted at the time of opening the account. Deposits held under these following ' schemes are called time deposits.

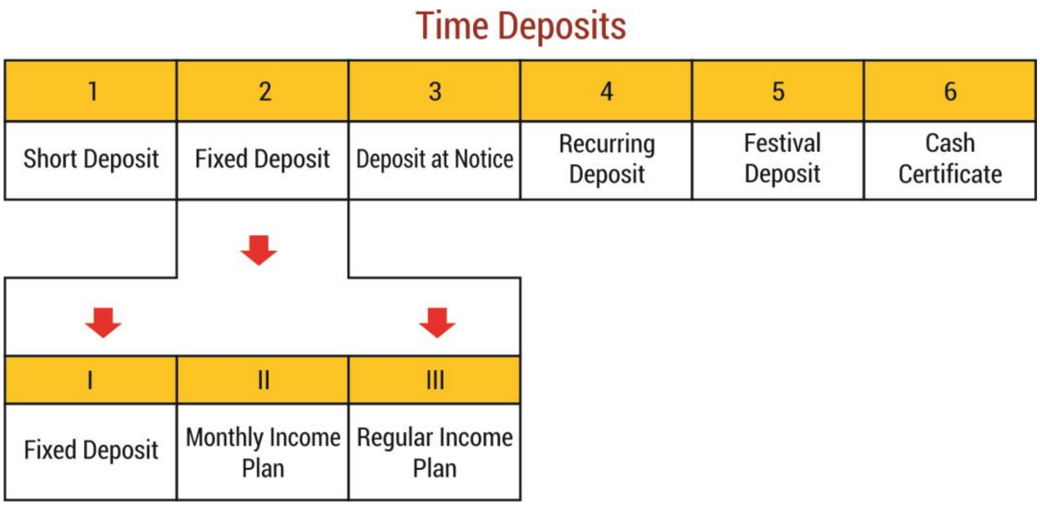

Fig 4.1 time deposits

These deposits are:

1. With due dates
2. Long Tern
3. Higher Interest Rates
4. Each transaction: a separate contract
5. Non negotiable

Let us briefly examine the characteristics of each of the above 'Time Deposits'

1) **Short (Term) Deposit:** Deposits for a period of 15 days and less than 12 months are called short term deposit. Rate of interest is as prevailing from time to time as directed by RBI.

   i. **Fixed Deposit:** Deposits for a period of 12 months and above up to 120 months are termed as fixed deposits. Minimum amount accepted is Rs.100/-. Interest is paid in 112 yearly basis at agreed rate and as directed by RBI from time to time.

   ii. **Monthly Income Plan:** Interest is payable every month. Minimum amount accepted is Rs.500/- and interest is paid at the discounted rate or if depositor agrees to take holiday of 3 months, the bank pays interest at the stipulated rate from 4th month

   iii. **Regular Income Plan:** Interest is paid every quarter to the depositor. Minimum amount stipulated is Rs.500/-. Interest is paid on quarterly basis.

2) **Deposit at Notice:** while keeping the deposit with the bank a depositor stipulates the notice period ranging from 15 days to 90 days. Depositor has to give stipulated notice to bank he intends to withdraw the deposit, Due date will count from the notice date. Minimum amount for 15 days to 45 days is Rs.1, 000/- and for 45 days to 90 days it is Rs, 2,500/-.

3) **Recurring Deposit:** This is recurring in nature. A depositor while opening the account has to stipulate the period of deposit and amount of the agreed monthly instalment - which is normally in multiples of 51- or 101- an for the periods multiples of 12 months up to 120 months.

   Instalment is required to be deposited regularly between any days from first to last date of month. Interest is compounded quarterly and principal + interest (accumulated) becomes payable on due date or one month after payment of the last instalment which ever is later.

4) **Festival Deposit:** Account is opened in the name of festival. Minimum amount stipulated is Rs.251-. This account can be opened for a minimum period of 4 months and maximum of 12 months.

5) **Cash Certificates:** This scheme is meant for persons having seasonal incomes like farmers, artisans, etc. The face value is in multiples of Rs.50 up to Rs.10,000/- and maturity period from 24 months to 120 months.

Some schemes combine recurring deposit and fixed deposit schemes benefits.

The prepayment of deposits at the desecration of bank attracts penalty i.e. 1% less interest than due for that period. When loan is allowed e.g. such deposits (where allowable) interest on that loan is charged 2% above the rate of interest payable on these deposits which is a price to cover the cost involved in that transaction.

It is interesting to observe that there is not a very large difference/variation in the lowest and highest deposit rates of deposits offered by a small co-operative bank, a nationalised bank, a private bank or a foreign bank. What differ are the presentation, pricing strategy, labelling and marketing style which projects quality and professional friendly approach which makes all the difference in customer making a decision to bank with such banks using professionally marketing.

It is equally interesting to know that although benefits are same or similar as to interest rate or maturity value, the titles vary very much in their 'catchy' value.

One more shifts is, earlier most brochures highlighted only interest rate or benefits but now service charges are also advertised in a subtle and friendly manner,

Non-Resident Account

We have seen the types of deposits maintained by bank of Resident Indian in Rupees.

Banks authorised to deal in foreign exchange also maintain various non-resident accounts which bring the non-resident Indian segment in their portfolio and ensure both business and exchange profit in the conversion process.

Due to the special consideration in cash reserve calculations and the exchange communication/profit involved, many banks have been competing with each other to attract and retain such non-resident accounts.

Who is a Non-Resident Indian?

As per FERA, 1973, an Indian Citizen staying outside India (except in Nepal or Bhutan) for employment or carrying out business or vocation outside India or for any other purpose in circumstances indicating his intention to stay abroad or for an uncertain period I s called 'non-resident'.

a) Indian citizens who proceedabroad for higher studies, business visits and medical treatment continue to be treated as persons resident in India even during their temporary absence from India.

b) Indian citizens staying abroad on foreign government/government assignment, world bodies or officials of Central, State Government, and Public Sector undertaking and deputed/posted abroad to their offices including Indian Diplomatic missions are treated as non-resident during their stay abroad.

Non-Resident Account can be opened by the names of non-resident persons and persons of Indian origin residing abroad., Persons of Indian origin means a person who himself or either of his parents or any of his grand-parent was an Indian citizen or a permanent resident in undivided Indiaat anytime.

OR

A wife of an Indian Citizen or a person of Indian origin shall also be deemed to be of Indian Origin even though she may be of non-Indian origin.

However, non-resident (E) accounts can also be opened in the names or overseas companies, partnership firms, societies and corporate bodies which are owned by non residents of Indian nationality/origin or trusts, wherein these persons have irrevocable beneficial interest to the extent of 60%.

These non-resident accounts have to be properly introduced.

The following types of non-residential accounts can be opened in Rupees.

a) Current Account

b) Saving Account

c) Term Deposit

d) Special Term Deposit

e) Recurring Deposit

f) Cash Certificates

g) Annuity Deposits

Such N.R.I. accounts can be even jointly opened if:

1. All the account holders are N.R.1.s
2. All are of Indian Nationality or origin
3. All are resident in the same country if belonging to bilateral group (now modified. in the same or different countries in Ext. group)

Funds in N.R. (E) accounts can be accepted in any currency if they are transferred to India in an approved manner from the country of residence of the account holder or from any other foreign country if the country of residence of the account holder and the country from which remittance is received are both in same group (now modified).

The following local credits are accepted' in N.R. (E) account:

1. Interest/Dividend/sales proceeds of units of UTI, National Plan, Savings Certificates, and Share provided these are purchased out of external funds
2. Interest on Term Deposit of account holder
3. Transfer from accounts to account holder ad the same/another branch of bank.

The following is difference in N.R. (0) and N.R. (E) Account:

N.R. (0)	N.R. (E)
1. Conversion of resident accounts as account holder becoming non-resident Or new account in the name of N.R.	Conversion not allowed from resident account to N.R. (E)
2. Source of credit resident as well as foreign	Source foreign credit only
3. Repatriation not allowed	Repatriation allowed
4. Joint account with Resident Indian - close relative allowed	Joint account with N.R. only
5. No Tax exemption	Eligible for tax exemption

N.R. (E) accounts are eligible for:

1) Tax Exemption
   - Income tax
   - Wealth tax
   - Gift tax
2) Repatriation of balances held in N.R. (E) account including interest is allowed without prior reference to RBI.
3) Interest rates payable are higher for N.R. (E)
4) Reconversion facility is available Funds from NR (E) can be transferred to N.R. (Ext) Term Deposit Account Loans 1O.D. Against N, R. (E) Term Deposit is allowand up to specified limit for approved purpose and repayment has to be made either by adjusting the deposit or by fresh remittances in Forex from abroad,
5) Premature payment is allowed like conditions for domestic deposit
6) When the account holder changes his status from N, R to resident the account should be changed to resident on getting intimation from account holder.

Types of Loans/Advances

Like the deposit accounts are life bleed or raw material for the bank, the advances are essential to deploy those funds are to earn revenue for the banks.

In order to balance liquidity and profitability properly, banks have to use their available (lonable) funds judiciously, keeping in mind all the statutory requirements imposed' by RBI.

The employment of funds is made generally as:

1) Cash-certain portion has to be held to meet day-to-day demand of customers and to hold certain portion in QRR with RBI.

2) Money to call or short notice-Refers to inter-bank borrowings. In day-to-day requirement banks borrow from each other, the interest whereon varies day to day.

3) Investments-The investment by bank depend upon statutory requirement as per Sec. 24 of Banking Regulation Act, 1949 and Sec. 42 of RBI Act, 1934.

4) Advances-As banks have to pay interest on various types of deposits received from customers, in addition to salary cost, rates, taxes, insurance, stationery cost and other administration costs, they have to earn adequate profit to meet all these expenses by deploying funds profitably.

   This is done depending on RBI guidelines and bank's own policies.

The advances are granted to eligible borrowers as per bank's policy, available lonable funds, bank's corporate plan, its performance budget and borrowers' character, capacity, capital and credit needs.

The following principles are kept in mind:

1) **Safety -** the advance should be safe.

2) **Liquidity -** as the time deposits are slowly reducing, advances should be liquid and not blocked for long period.

3) **Profitability -** Interest and charges be remunerative.

4) **Speed -** decided on security, risk, type of industry, etc. which is the pricing decision linked to bank rate prevailing.

5) **Purpose -** The advances are generally granted for productive purpose after verifying utilisation and repayment capacity.

6) **Security -** This is the safeguard to fall back upon in case of emergency and recovery by sale of assets. The stock or Fixed Assets or collateral securities

are insisted upon.

7) **Margin -** Depending on the security a cushion is required in case of recovery by sale of asset and this is normally dependent on the type of security - which is marketable, ascertainable, saleable and transferable.

8) **Repayment -** the period of repayment and quantum is linked to type of security, life of security and fund generation capacity (cash flow).

Main Types of Advances Granted by banks:

As the bank's function is to accept deposits from customers and lend money to borrower, the advances are granted on short-term, medium. Term or long term basis depending on the fix deposit, lonable funds, exposure to industries and bank's business policy and profitability requirement.

The types can be classified as

a. Funded

Short Term	Long Term
1. Overdraft	Short term loans
2. Cash credit	Medium Term Loans
3. Bills purchased/discounted	Long Term Loans

b. Non-Fund:

Bank Guarantee and Letter of Credit

Let us briefly touch each of these types as a product by the bank:

a) Fund Facilities

1. Over draft-under this type of facility, bank permits aborrower to overdraw his current account up to a decided limit. The borrower is allowed to draw in excess of the amount of deposits up to a specified sum. Normally, it is short term and for specified purpose to finance current assets,

2. Loans-The loan is normally for acquiring fixed assets and repayable within 12 months, 1-3 years, 5-7 years or 10 years.

   In loan there is usually only one debit and several credits (repayment) in a phased - predefined manner.

3. Cash Credit - It is a, form of advance to meet the demand of trade, industry etc. Operations are conducted similar to the overdraft. The difference is that while in O.D., CIA is necessary and it is usually temporary or short term, in cash credit limit is assessed based on projected sales level and required inventory. (C/A) level. A limit for 1 year is allowed and balance fluctuates with in the range. This is given for working capital requirement of a corporate borrower.

   Technically, it has to be brought in credit once a year.

4. Bills purchased and bills discounted - A bill of exchange coines into being when business transactions take place on credit basis.

A bill of exchange is an unconditional order in writing, addressed by a person (drawer) to another (drawee) signed by the maker, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a certain sum of money to or to the order of a specified person or the bearer. Banks grant advance against such bills by purchasing or discounting these bills

b) Non-fund limits

1) Bank Guarantee

A guarantee is a contract to perform the promise or discharge the liability of a third party in case of his default. In such contract when the bank undertakes the function of guaranteeing it is known as a Bank Guarantee, where abank issues a guarantee on behalf of its corporate customer to a third party. There are generally 3 parties:

- The principal debtor
- The creditor
- The surety

In abank guarantee the liability of surety is secondary and depends on the principal debtor. In bank guarantee the surety undertakes the obligation at the request of the principal debtor.

This like L/C is called as non-fund facility as immediately parting with funds is not required and it earns good commission to the banks.

2) Letter of Credit

A letter of credit is the undertaking given by bank at the instance of its corporate customer addressed to a seller saying that it (bank) would honour the drafts drawn there under subject to the terms and conditions stipulated therein.

An Inland LIC is when both buyer and seller are in Indiaand Foreign L/C is issued on behalf of Indian buyer (importer) to the Foreign Seller (exporter).

The L/C is opened on the basis of the contract between buyer and seller and the bank undertakes to honour the commitment on behalf of the buyer to pay the, amount In case of satisfying stipulated condition.

The buyer gets credit and seller gets an assurance from the bank and the corporate client either buyer or seller gets the benefit of this arrangement.

Banks earn commission for issuing L/Cs.

Products in Demand

We have seen in the earlier paragraphs, different types of deposits advances and non fund facilities. In the context of products of Banks in recent day Bank marketing it is essential to take a look at the following two products which attract the middle 'class customers and also are profitable to the banks

a) Consumer Loans

b) Credit Cards

Due to the restrictions of loanable funds and the less demand for loanable funds by industry the profits of banks were affected during the period when stock market and industrial scenario was slack. Merely mobilising deposits do not mean sound marketing policy. It becomes necessary to market the loans as well as to improve profitability. Similarly, taking into account the customers need to buy things in the open market either products of high value of moderate value consumer loans and credit cards serve the purpose of satisfying such need adequately thereby matching consumer's demand and supply of bank's loanable funds.

a) Consumer Loans

Like financing the needs of working capital (for current assets) and loan (for fixed assets) of an industrial customer or a trader, banks also finance 'consumer loans' under different captions to its individual customers. The middle class being the largest segment of bank depositors (savers) and their purchasing power being tapped by various companies in consumer durable industry, the job of identifying credit needs of such already tapped segment makes it easier for the banks to market the consumer loans. As such customers have ready needs to buy consumer durables like fridge, TV, stereo, two-wheeler, etc, for which they have comfortable cash flow but not the capital (ready cash balance) to purchase such items of their own.

Let us examine the modalities of such 'consumer loan' scheme

For whom-

- For existing consumers of the bank
- For customers with proven ability and willingness to repay and who are interested in starting relationship with the bank.

Salient Feature

- It can be availed by individual who are 18 years of age.
- It is offered for worthwhile purchase or approved purpose to purchase an article, TV/Video, AC etc
- The amount can be minimum of Rs 5 ,00 to Rs 5 Lacs
- The security taken while advancing such loan is hypothecation of asset so purchased or lien over another asset of adequate value to cover the loan amount
- The repayment is in equated monthly instalments (EMI) which is to be repaid over a period of (minimum) 12 months to (maximum) 60 months. This is arrived at after verifying the customer's income, saving/repaying potential and the life of asset so purchased
- The repayments can be through a standing order or by collecting post-dated cheques from the customer.
- Interest rate charged for such loans is as per bank's policy and RBI guidelines from time to time

Although such loans have very good potential demand from middle class customers, it becomes obligatory for the banker to do a thorough scrutiny of the customer and his credit worthiness and repaying capacity as well. For this purpose a probing scrutiny is made to cover the following important aspects

1. Age-Proof like ration card or school leaving certificate.
2. Address-Should be in bank's command area, can be checked from ration card, electricity bill, proof of salary/income.
3. Income proof - Salary slip or salary certificate regarding employees in service and income proof/certificate copy of I.T. Return in case of person on their own (self employed, professionals).
4. Creditworthiness - Satisfactory confidential reports from the employer.
5. Security-The customer's personal worth is calculated by taking into account :
   - Average balance in account.
   - Shares/Debentures (M.V.).
   - Life Insurance Policies (S.V.).
   - Real Estate Property.
   - Gold/Jewelry.

   The minimum value of such assets blocked should nor be less than Rs.50,000 for salaried customers and not less than Rs. 1.00 Lacs for professional customers.
6. Repayment-In EM1 within 12-60 months.
7. Costing-Let us take an example of a consumer loan say for Rs.1 Lack.

Loan amount	-	Rs. 1,00,000
Repayment period	-	36 months
Interest rate	-	15% (say)
Therefore, EMI	-	Principal component + Interest componenets

Principal component of EMI = 1,00,000/36 = Rs. 2778 p.m.

Interest component of EMI = 1,00,000 * 15 * 3136 = Rs. 1250 p.m.

Therefore EMI = Rs. 2778.00
+ Rs. 1250.00
Rs. 4028.00

Besides interest:

i. Processing fees of 1% of loan amount subject to a minimum of 5001- and maximum of Rs. 1, 5001- is charged.

ii. For post dated cheques Rs.101- per cheque is charged.

Banks have had very good experience about these consumer loans in terms 01 customers demand and as nationalised banks were not encouraging such loans (except loans, FD), Co-operative banks, private sector banks and foreign bank have tapped this segment very well and have deployed the funds and broadened customer base on one hand and have earned good income as well..

Credit Cards

'Plastic Money' or credit cards have become very popular as bank's product and have wide acceptance in Indian Market.

The credit card allows a holder to make purchases (upto his sanctioned credit limit) without making purchases in lending shops/markets to make payment of bills-electricity or telephone--or to withdraw funds (cash upto a pre decided limit) as and when required.

The credit cards widely accepted are

Visa cards

Who can have it?

The profile for the prospective visa card holders can be wide i.e., persons of 18 years to 60 years of age. Higher middle income, professionals and financially mature segment is the largest segment for credit cards

Salient Features

- It is open even for non-customers (non-account holders) .
- No entrance fee is charged
- Annual subscription fee of Rs.250/- is charged
- Family add-on cards are issued @ Rs.200/-- each
- These are affiliated to visa international
- It is valid for transactions in a chain of over 8 - 10000 merchants
- Minimum amount payable can be as low as 1120th (5) of the principal outstanding.

- Cash advance of upto a certain limit is allowed on which 2% (porn.) service charges are charged.
- For purchases, no service charge is applied if a payment comes within 15 days.

Benefits

- It is safe and convenient
- It facilitates easy purchases
- It provides confidence while traveling
- The owner of the card is sanctioned a resolving credit facility which satisfies his 'Ego Needs' and also 'purchases -anywhere, anytime-need as well.
- Cardholder's limit is enhanced every year.

This enables bank to have higher profits and more holders who can be non customers, in its wings)

Check your progress 2

1. A____________can be goods, a service or goods + service or even just an idea.
   a. Product
   b. satisfaction
2. A __________is anything that can be offered to a market for attention, acquisition, use or consumption.
   a. satisfaction
   b. product
3. If two _________have same or similar products and pricing; it is the service (though abstract).
   a. banks
   b. consumers
4. ____________Deposit Are deposits which are not repayable on demand.
   a. current
   b. Time

4.4 Elements of Product Mix

By product mix is meant the total range of products offered by a bank.

In marketing terminology the product mix has three main characteristics:

1) Width
2) Depth
3) Consistency

These can be shown as a diagram in the following way -

Product Group		Depth			
Line	1	1---a	1---b	1---c	1---d
Line	2	2---a	2---b		
Line	3	-----	3---b	3---c	3---d

Fig 4.2 product mix charecteristics

Width of a product-mix depends upon the number of product groups or product lines whereas the depth depends upon the number of products in each line. The consistency means whether the products have production affinity as well as market affinity.

For the purpose of diversification, frequent changes are made in the product mix. Broader product mix enables better business turnover 10 minimizes the risk of failure.

The following factors affect any product-mix:

1) Cost of production/delivery
2) Demand from customers
3) Advertising/distribution cost
4) Policy of the bank

Acceptability of any product or product mix depends upon:

1) Consumer acceptance
2) Satisfactory Performance
3) Adequate distribution

4) Effective Packaging/Branding

5) Good service/delivery

It can thus be seen from the foregoing details that in marketing of banking services, product mix consists of product lines which mean similar products or services like I deposits, loans, investment counseling services. In each product line there can be different products like example under category of deposits there can be saving or checking accounts, The width depends upon such number of product lines whereas the depth means how many product types are offered in a particular product line. To cite an example abank giving 12 different types of loans like education loan, housing loan, industrial finance, consumer durable loan etc. has abroader product mix. Depending upon the market demand i.e. customer's needs this mix has to be widened or deepened as a prudent marketing strategy.

Check your progress 3

1. By _____________is meant the total range of products offered by abank.
   a. product mix
   b. product range
2. ___________of a product-mix depends upon the number of product groups.
   a. length
   b. Width
3. For the purpose of diversification, frequent changes are made in the ___________.
   a. product mix
   b. product range

4.5 Product Life Cycle and Product Strategies

As the products volume (sales) and sales revenue follow a typical pattern, the concept of product life cycle has been one of the important concepts in marketing which must be properly understood.

As each product passes through certain typical but definite stages in its life-span, we will look up into the important stages:

i) Introduction

ii) Growth

iii) Maturity

iv) Decline

It must be borne clearly in mind that the growth or decline of products depends not on product alone but the market in which it is launched.

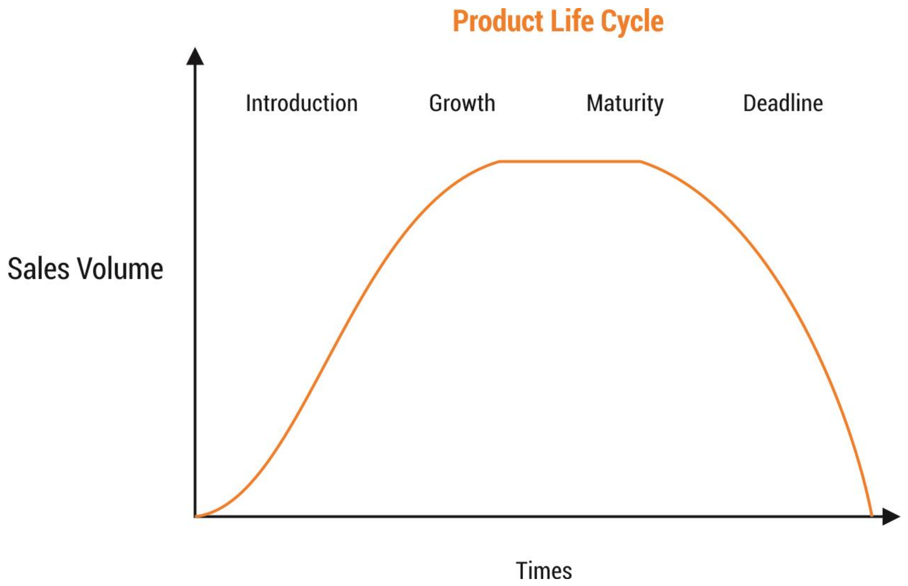

Fig 4.3 Product life cycle

A key concept on which marketers rely is the concept of PLC i.e. Product Life Cycle. It in essence means the stages in product life from its conception to obsolescence as mentioned earlier. From strategic view point it provides important guidelines about product management

The figure given above depicts a typical PLC where the Y-axis shows volume of sales (business), X-axis shows the time scale.

Introductory Stage/phase

This is the stage when a new service or product has just been introduced in the market. This stage in the product's life cycle is characterized by low sales and most pf the times negative profits which may be due to lack of awareness about the product or limited distribution or unfamiliarity with the product.

In banking industry, however, it is different from consumer goods industry as the products have been regulated for long and prices were also controlled by statutory agencies. Promotion being the only variable which could be manipulated, advertising and personal service were the options for enabling rapid product growth

Growth Stage

After a product survives the introductory stage, it passes into the growth stage. At this point, competitive strategies by other banks can affect the growth. The promotional strategies tend to change during this stage to keep up the sales. The product/services are fine tuned during this stage. Sales tend to grow and profits increase during this phase. Market acceptance of the product is the key factor at this stage

Maturity Stage

Having continued, at the growth stage, the product reaches a plateau in it growth curve and thus into the maturity stage. The most notable indicator of this phase can be the initial stability and then slowdown in volume of sales/profit

Products in maturity stage can give indications about changes required in product strategies. The competition at times may tend to thin up, the margin to stabilize the p w t h at maturity phase. It may force to lower the price of the product or additional cost in promotion and distribution of the product.

Decline Stage

After maturity, with increased competition on change in consumer preferences a downward shift/drift in sales or reduction in profit May start. Except in case of new diversified products in banking industry, such sudden decline cases are not many. We will see the application in the foregoing paragraphs with respect to decline, death or obsolescence of bank products.

In real life, in banking - being a financial service industry, all products need not follow such a cycle but still the concept of product life cycle has important place in product marketing strategy. The bank, knowing what happens to different products and services at different stages in a given economic scenario in a market can decide and improve its planning. In fact the trial balances, monthly MIS dataand quarterly business figures compiled by tlie planning divisions can indicate the demand and supply position of various products as inter-se composition (vis-a-vis budgeted pattern) and as a percent share of the total market vis-a-vis the potential for each product. A suitable flexible plan with a matching pricing strategy can ensure sustained growth of all the products ensuring growing business and matching profits – of course with growing customer satisfaction.

Understanding product life cycle may provide inputs for strategic planning at various stages

Check your progress 4

1. A key concept on which marketers rely is the concept of ____________.
   a. PLC
   b. DLC
2. ____________stage is the stage when a new service or product has just been introduced in the market.
   a. maturity
   b. Introductory
3. After a product survives the ___________stage, it passes into the growth stage.
   a. introductory
   b. maturity
4. After____________, with increased competition on change in consumer preferences a downward shift/drift in sales or reduction in profit may start.
   a. maturity
   b. introductory

4.6 Using Product Life Cycle to Manage Marketing of Banking, Products

The introductory stage of the product's life cycle is characterized by low or negligible sales and .negligible or no profit. When allnew account or product which is designed to suit to a particular segment of customer is launched after research by R and D or marketing department, if the same is not properly advertised or promoted by the staff, initial launching costs will be higher and due to unawareness resulting in low or no response. Initially it may show very low or negligible sales.Credit card or ATMs when introduced initially in India shared similar response.

The products like consumer loans or housing loans or automobile finance shared a very high growth when the market was booming due to high growth rate in consumer durable, car and housing (Real Estate) market.

It ensured both growing demand, very good sales and also very good profit due to lucrative lending rates charged to such customers who had smooth cash flow but not lump sum money to buy the much needed car or home or TV/VCR which were strongly marketed by the seller of these products. In this growth phase, aggressive marketing by product launchers in these industries enabled bank to fulfill the needs created by them through their (banks') own products and services. Here, so to say the growth phase of real estate, consumer durable and automobile industry coincided (matched) with growth phase of products/services marketed by banks which was a very good timing to launch and continue provision of such products as loans and credit limits or loans/advance against deposits, shares etc.

When all the banks started giving liberal loans for products marketed by these 3 sectors, the competition went up although the demand was growing, which resulted in maturity or saturation of banks' products/services and compelled some banks to adjust the pricing (lending rates) downwards to continue their products/services to be attractive to buyers so as to ensure the business growth.

The saving accounts or pass book accounts have also reached the maturity phase as the growing awareness amongst the customers for higher yield make such low yield products less attractive. Due to the change in interest rate structure which is linked to the demand and period of (short term) deposits, customers don't like to block more funds in such type of accounts except for basic safety and liquidity criteria to meet urgent/unforeseen expenses. To overcome the decline in such accounts some banks have started flexi accounts giving a combination of saving and short term investment to provide mobility at the same time ensure retaining of low cost funds for the bank.

There has been a clear-cut decline in current account of traders who don't block any funds in such '0' yield accounts and arrange funds to get the cheques passed as and when the clearing cheques are received.

Due to tax-saving option in the market the short term deposits are getting diverted to such schemes which provide safety, short term liquidity, comfortable yield and tax concessions.

A close watch of economy, government policies, industrial scenario and the middle class habits provide an insight to the banks to study and watch the shift in saving/borrowing habits of its customers. The change in macro-economy affect the customer's behaviour at the micro-level due to which proper research and analysis of the trends of demand and supply as well as the shifts in pattern of various deposits gives an idea and opportunity for the bank to change its products with respect to the design, pricing and need to launch new or innovative products/services to ensure customer's interest and loyalty to their bank accounts.

Through observing and monitoring the product life cycle it becomes easier to decide and implement the product development strategy.

Generally, these are four strategies recommended for growth in business and profits which are-

1) Market Penetration
2) Market Development
3) Product Development
4) Product Diversification

It can be shown through the following Figure

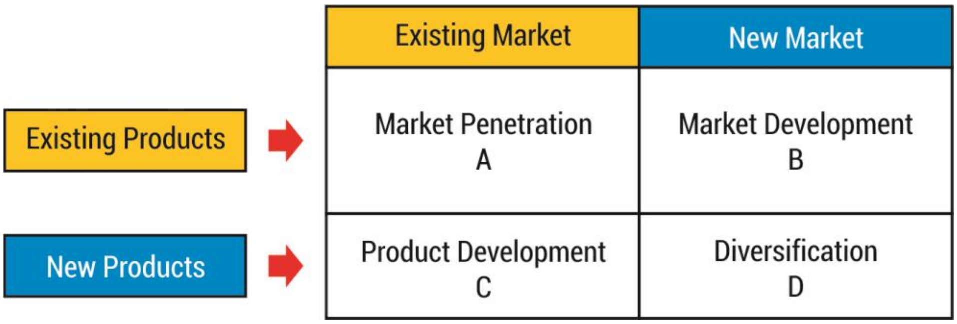

Fig 4.4 growth strategies

Market Penetration

Market Penetration strategies involve increasing the sales for an existing Product in an existing market. This, generally, involves an increase in marketing effort. These can be possible through three strategies -

i) Increasing current rate of use of a product
ii) Attracting competitor's customers.
iii) Attracting non-users of a product

Increasing rate of usage is strategy normally used by many marketers in consumers durable industry. Banks can use this strategy to promote increased usage of certain services. Of course, not all services are conducive to this type of strategy

Attracting competitor's customers is the second option in market penetration strategy making a SWOT analysis of abank and its competitors with respect to consumers' needs and place, promotion, price of bank's own products enables abank to attract customers to its products.

The third strategy is to attract the non-users. Cross-selling of a product of abank is an example of such market penetration strategy. Providing trust/advisory services can be another example of such strategy

Market Development

Market Development strategies involve the increase in marketing effort for existing products in new markets. The one option can be to attract new customers for existing products and the second expanding areas (branch expansion policy).

Managing bank's product/service mix in increasingly competitive market determines the success or survival of banks in the volatile market situations

Check your progress 5

1. The ___________ stage of the product's life cycle is characterized by low or negligible sales and negligible or no profit.
   a. introductory
   b. maturity
2. Market____________strategies involve increasing the sales for an existing Product in an existing market.
   a. demand
   b. Penetration
3. _____________rate of usage is strategy normally used by many marketers in consumers durable industry.
   a. Increasing
   b. Decreasing

4.7 New Product Development

The new products can be developed for a new market or existing market.New product can also be launched in improved market or in the new market, Innovating a product essentially means developing a product resulting in an increase in the product line.This enables diversifying business risks, continuing life cycle of a product and also ensuring profits.

Such Ideas are subjected to discussions and examination by expert bankers, economists, experienced field staff and marketing experts within abank to validate the applicability of such ideas to lead to new and salable product

Normally such ideas for new products pass through following stages:

Fig 4.5 New product stages

The very modern manifestation of new product development has been the consumer convenient-credit card. The major impetus of bank charge account plans began about 3 decades ago when the Franklin National Bank near New York city sponsored a plan which received massive publicity within the banking community. By mid 60's, seventy five commercial banks had set up such credit plans. However, risks of recovery and lack of quick profits let to gradual withdrawal of new entrants from the plan. It took almost a decade to establish credibility amongst merchants regarding acceptability of credit cards and streamline recoveries. As time passed revolving credit and shift of charges to consumers was acceptable and then credit cards became abuzz word. This innovation has thereafter proved to be of convenience to customers, enabled merchants in sales promotion and proved to be profitable for the banks as well

Role of Product in customer satisfaction

Any product or service developed by abank has to satisfy the needs of the customer. In fact, the product development, positioning, launching etc, is decided based on customer needs only. It is, therefore, necessary that the strategies keep the customer needs and satisfaction as the focal point.

General Need of customersare:

- Financial Security
- Quick Service
- Convenience
- Attractive yield
- Low cost loans
- Personalized service
- Advice/Counseling
- Easy Access
- Simple Procedure
- Attractive Package
- Friendly Approach
- Variety of Products

This list is only illustrative.

The product conceptualization and development has to bear these needs in mind.E.g. Using the PLC approach seen earlier abanker may group these needs into following segments

Young Customer	**A Family with teenage children**	**A retired couple**
Would prefer a bank which provides security, convenience and quick, friendly service at convenient hours.	Would have need for proper saving with safety of funds, reasonable yield and availability of low cost loans for children's education, convenient location and convenient hours.	Would prefer for high safety, higher yield counselling advice and personalised service at convenient location.

Thus some needs like safety, liquidity, better yield, personalized service and convenient location and timing are the common factors which have to be satisfied by any bank's product.

As we have seen in the earlier inputs, proper matching of market segments and needs is the key factor in deciding product strategies for existing as well as new products. An ongoing market research about positioning strategies by other banks vis-a-vis changing needs of customers would positively supplement such exercise to design and launch new products which lead to customer satisfaction and also more business for the bank.

The following are some of the real life examples of new products developed by banks to meet the needs/expectations of its customers:

1) Flexible deposits
2) Debit cards
3) Credit cards with ATM card
4) Cumulative deposits
5) Facility of over drawing and saving bank account.

Such new products are developed keeping in mind the growing/new demands arising out of customers' needs/expectations within the guidelines/directives of IBAIRBI with permutation combination of interest payable on deposit accounts

Check your progress 6

1. ____________a product essentially means developing a product resulting in an increase in the product line.
   a. Innovating
   b. promoting
2. The very modern manifestation of new product development has been the consumer convenient-_____________.
   a. aadhar card
   b. credit card

4.8 Branding In Bank Marketing

You have already studied this concept in your earlier unit on branding in MS-6 in detail. However, to focus the concept with specific reference to bank marketing let us re-look at the same.

A brand is the name or design which identifies the products or services of a manufacturer and distinguishes them from those of competitors.

Brand names may be given to each product or to a complete product line. Branding is the process of deciding what brands the company should offer.

Branding also differentiates a product which invites the attention of customers. It gives details as to benefits and quality and ensures the loyalty of customers. It enables abank to do the market segmentation as each product from out of a product line can attract a distinct segment of customers.

Branding decisions are taken based on market research and assessment of customer needs and preferences.

Generally before deciding brands, the following questions have to be answered satisfactorily:

1) Is the brand name essential?
2) What brand name would suit?
3) Should products be branded separately or as a product line?
4) It is necessary to segment the market for each brand?
5) Is the brand needed for strengthening existing market segment form a new market?

While selecting abrand name abank should,

i) Chose a short and simple one.
ii) Prefer one which is easy to pronounce and remember.
iii) Avoid confusing or negative connotations.
iv) Ensure that it suits the characteristics of a market.
v) If the bank's name is highly established and accepted the brand name should include that (bank's) name also like 'citicard' or 'Indbank' fund or 'Bobcard', etc.

Advantages of branding to buyers (customers)

a) Brands are dependable guides to contents, processes, qualities, etc.

b) They make shopping of various products feasible and convenient.

c) They assure satisfaction.

d) They satisfy the status needs or the emotional needs of the customers.

Advantages of branding to sellers (Bank)

a) It ensures repeat sales through identification.

b) It ensures product stability through customer loyalty.

c) It helps segmenting a market.

d) Customer may even pay a higher price for branded product than an unbranded one.

e) It shields the product from price competition.

f) Successful brands add to the corporate image of the bank.

The brand establishes after undergoing following chain-

Non recognition----- Recognition--------Preference--------Loyalty-------- Repeat buying

Role of Brand in Bank Marketing

As the brand enables seller bank to build up a certain image which in turn ensures receptivity of advertising as well as repeat business and consumer loyalty, brand plays an important role in marketing of banking services.

In banking industry as the competition is 'cut throat' and products are quite similar as to the basic nature and benefits/returns to the customers, the service delivery and branding are excellent tools which enable abank to create and maintain an image among the customers.

Like the brand names 'TATA" or "Godrej" or even "Lijjat Papad" or "Zandu Balm" customer loyalty goes to products which are linked to' the brand names of their established and well known producers.

Brand name has to give a positive message and create pleasant associations.

In USA there are more than 5 Lacs brands registered. In Indiaalso thousands of brands are registered. It become important even here in India where products of widely different nature are entering the selling channels. Branding is significant and essential in banking until faith and confidence of the customers are firmly established.

In fact at the macro level or corporate level the positioning provides abank framework to' view itself in the industry concerning the totality of its orientation towards the marketplace strategy and as micro application with respect to a specific product or service brands call help to establish its products in the competition market. Some of the examples of brands are:

BANK	**PRODUCT**	**BRAND**
Citibank	Credit card	Citi bank card
State Bank of India	Mutual Fund	SBI Mutual Fund
Canara Bank	Growth Fund Schemes	Can Growth Can Share
Indian Bank	Housing Loan	Ind Shelter
Citibank	Car loans	Citimobile

It can be, therefore, said that brands are very important as product (marketing) strategy in marketing of bank's services as branding indicates how the organisation chooses to use branding as an integral part of its overall marketing strategy. To the customer such brand name means a way to identify the product and differentiate the product from other similar products in the market

In the context of bank marketing it is important to note that as the customer loyalty and patronage is built around bank's name and image, the bank's position and consumer's perception of abrand in customer's mind makes it easier to market the product brands.

Logically, it is very few products which sell as brands irrespective of bank's name if they have distinct advantage and benefits and have been so advertised constantly. In majority of cases, the bank's overall image is what counts in the selling process and the customer comes to know about the specific brands more beneficial to him. It is, therefore, clear that with all its product range and brand of distinctive products/services, the bank has to develop an image among the customers and then encashing this 'whole' brand-image, has to market the products branded for specific customer segments to win over other bank's products.

In a customer's language, two questions have to answer satisfactorily in this branding effort:

i) What is it in this bank which is different from other banks in terms of its position, sign off and product range?

ii) What are the product brands which are more beneficial to me which this bank offers distinct from other bank's products. In summary, both bank's brand and product brand are important in the marketing strategy for more clientele, more customer satisfaction and more business in the long run.

Check your progress 7

1. A ___________is the name or design which identifies the products or services of a manufacturer and distinguishes them from those of competitors.
   a. brand
   b. product
2. ___________names may be given to each product or to a complete product line.
   a. product
   b. Brand

4.9 Process and Product' Development Cycle for Banking Services

In the 7 'P's of marketing of banking services, the product related decisions are very important. To know about the concept of product/service delivery, it is necessary to know the process cycle concept. In order to have effective marketing or selling, proper understanding of the concept of product/service delivery is essential.

The products have to be launched through a well thought product development strategy. Launching a product or delivering a product to customers depends on whether it is a totally new and innovative product or just modification of an existing product. Equally important is the timing and market situation when a product is launched. It, then, becomes necessary to have suitable pricing and/or promotion strategy

Process Cycle in Product Development

The product development in banking depends on many factors which together with the steps in the process decide the success or otherwise of a product launched.

The process cycle is the stages of product while it is given in the hands of a customer. It is like a flow-chart of steps involved in this process. Let us take a simple example of a savings bank deposit account. The following aspects are involved before opening the account.

- New customer approaches with a request to open the account.
- He has to establish identity/bring introduction.
- Account opening documents/forms have to be completed duly signed.
- Pay-in-slip has to be filled in to pay deposit/required amount in cash.
- Specimen signature card/forms have to be signed.
- If cheque book is required, the requisite application form/slip has to be completed and signed.
- The pass book issued has to be collected.

Thus the Savings Deposit as a product develops from the cash brought in by the customer and deposited in his account opened after passing through the aforesaid process.

The acceptability of the product is facilitated by simplification of the process so that the customer, find it easier and convenient to go for that product.

In service organisation like banks, the system by through which service delivery takes place is called the 'Process'. This process of delivering a product or service is akin to the operation management in a manufacturing industry where the raw material gets converted into a finished product i.e. an input passing through a mechanism or process becomes an output.

The three processes applicable in delivery of service products can be indicates as:

- Line Operations- e.g. self service hotels.
- Job Shop Operations-combination of operations using different sequence e.g. Hospitals or Educational institution.
- Intermittent Operations- i.e. service is rarely repeated e.g. consultancy for projects.

In application of these concepts of process in banking situations abanker will have to ask some pertinent questions.

- What are the steps involved in delivery process of a product/service?

- What can be the logical sequence of event?
- What modifications are necessary to smoothen the process?
- At what point and how much consumer contact is involved/desirable?
- Can the technology be useful to speed up the process?

The marketing can be successful if the product development, packaging and delivery are properly synchronized from the view point of the bank as well as the customer.

It becomes quite necessary in reviewing the process cycle to consider:

- Customer's benefit
- Concept of service as seen by customer
- Method of offering the service
- Service delivery system

These can be shown as in the following manner:

Consumer Benefit Concept

↓

Concerned with consumer's view point

↓

Translated to service concept

↓

Concurred with the benefits offered by service

↓

Translated in to a service offer

↓

Concerned with greater details

↓

Translated into a service delivery system

↓

Concerned with people and process

In such delivery of service, the process cycle and a specific market segment' has to be considered specifically.

Packaging and Delivery

Packaging in the context of marketing of banking services means the art, science and techniques of selling the products and services to the customers ensuring their satisfaction, keeping in mind two salient aspects:

a) Actual delivery and sale of product.

b) Packaging as a function should consider.

 (i) Selecting proper material.

 (ii) behavioural aspects.

Functions of Packaging

Packaging in normal marketing parlance should do the following functions:

1) Protection

2) Appeal

3) Perform

4) Convenience

5) Cost-effectiveness

The packaging must be attractive and attracting the customer, should build confidence and indicates real intrinsic value of the product. Consumer research indicates that the colour and design of packaging is very important as it affects the consumer purchase decisions. Packaging also should be convenient, useful and cost effective.

Delivery: Packaging, it must be borne in mind, is much more than just packing. It is ' a marketing necessity. As the customer doesn't just want a product, he wants an integrated, combined, pleasant and eye catching package "get it on the top to gain action" at the close of a sale. Packaging so to say completes the sale (process) cycle triggered off by advertising.

A simple example can be of the Piggy Bank or Pigmy Deposits popularized by Syndicate Bank giving small Saving Bank Boxes in the shape of Pigs or 'minty' similar scheme by Bank of Maharashtra in the shape of a squirrel which promoted the product fast among children due to the novelty and toy value of the packaging.

Colorful and Crisp plastic envelops of FDRs by many banks facilitate the close of sale on a very positive note and attract other customersas well. It serves as a means of publicity and has retention value and multiplier effect to popularize not just the product but the image of the bank as well.

Service Delivery: When you go to abank with an intention to withdraw your money from S.B. Account, either with the cheque book or a withdrawal slip, it is given to a clerk - who verifies the instruments and balance in your account and then given the monthly corresponding to the withdrawal amount, Here the check, withdrawal slip, become the delivery system. In product/service delivery the physical evidence and the people are very important elements.

Check your progress 8

1. In the __________of marketing of banking services, the product related decisions are very important.
   a. 7 'P's
   b. 4P’s
2. The___________have to be launched through a well thought product development strategy.
   a. brand
   b. products

4.10 Product Development

Product Development and Delivery: Some Examples

To understand better about the concept of product development and stages of delivery of a product in banking situation let us take three illustrations-

i) The Flexi Limit Deposits

To know product development

ii) The Easy Access Deposit

iii) The classical example of fixed deposit - to know the stages of delivery of abank product.

Let us first take the example of a Flex Units Deposit Account of a Private Sector Bank.

It is the facility that provides a customer freedom of transferring the excess funds in saving bank account to a Term Deposit Account of his choice. It also ensures the flexibility in transferring a portion of the term deposit back to savings bank account in case of a need with this type of facility (product), the bank can offer higher interest to customers without affecting their liquidity position which gives the attractive option to customers to have both liquidity as well as higher yield.

Let us first understand how this scheme works as a product and then try to see the intricacies involved in such product development:

i. Balance in excess of the minimum required sum in Savings bank account is automatically transferred to a term deposit of customer's choice.

ii. In case of need, to meet the cheques drawn by the customer, his term (Flexi) deposit gets transferred to his S.B. account.

iii. On maturity as per customer's instructions the (Term) Flexi Deposit is either renewed automatically or the entire amount (principal + interest) is transferred to S.B. account.

iv. The transfer of funds from SB Account to term deposit account is made at a minimum of 5 units of Rs.10,001- each and a further in multiples of Rs.10,001- each.

v. A statement giving details of outstanding balances under SB (Term) Flexi deposit is furnished as and when required.

Now as a product when such a scheme is developed it requires a close co-ordination between the following departments:

a) **Corporate office** - to approve such a product as a concept as a policy-taking into accounts RBI/IBA guidelines.

b) **Marketing Dep't** - to study the demand and products developed by other banks.

c) **Operation Dep't** - to decide suitable transactions and required accounting for the same.

d) **Accounts Department** - to streamline the inter department transactions smoothly and effect the funds properly under respective heads to decide the interest accrued and payable from the date of opening of account of passing (converting) a transactions.

Thus the product development in case Flexi Deposit Account requires close co-ordination between the following departments:-

Corporate Office------ Marketing Dep't ------- Operation Dep't--------- Accounts Dep't ----------- Delivery

If we take another example of easy access deposit of a foreign bank, following aspects are important:

- Minimum deposit accepted is Rs. 10,000
- Deposit is accepted under any scheme of term deposit (except R.D.)
- Rate of interest and period of deposit is as per RBI guidelines.
- An overdraft of upto 75% is available through current account at a chargeable interest.
- If such overdraft is taken, interest is paid on full deposit amount and interest is charged only on amount of O.D. for the actual period of use.
- The period of deposit is 46 days to years.
- A cheque book is given with current account.
- Depositor can avail cash advance upto Rs.3,000/- from any branch of the bank.
- "Interest on O.D. can be recovered from the customer's current or savings account.
- Transaction charge of Rs.11- per transaction is charged on all transactions CIA.
- OD is made available @ 2% higher interest than the simple base rate payable on deposit.

Benefits

- The customer pays no service charges.
- Withdrawals take place through CIA cheques.
- Freedom to avail 75% of deposit as withdrawal.
- Despite withdrawals, deposit continues to earn interest.
- The customer's money is safe.

Now if we look at this scheme a product development it is a deposit as well as advance scheme and close co-ordination between following departments is essential from conceptual state to actual delivery of product.

Corporate Office------ Marketing Dep’t ------- Operation Dep’t--------- Advance dep’t ------ Accounts Dep’t ----------- Delivery

Fixed Deposit Account

Product Attraction: It is a deposit for a fixed amount of money, for a specified period and at a fixed rate of interest. The rate of interest opted may be simple or compound. It being higher than interest payable on S.B. account it becomes an attractive feature.

The term deposits are accepted as short term, simple fixed deposit or reinvest deposits.

Features

- Deposits can be 46 days or 5 years
- The term of deposit is fixed initially
- Rate of interest is decided as per term
- Premature withdrawals though allowed attract a penal rate of interest

Benefits

- the customer earns higher interest
- funds are secure
- Funds can be saved for specific purpose
- Funds can be withdrawn in emergency
- Free remittance of interest is allowed
- Irrespective of fluctuations, guaranteed earnings are assured
- Term Deposit (fixed deposit) is transferable to any branch of the bank in India

Process of Delivery

1	Customer Approaches with cash/cheque/instruction for fixed deposit
2	Application made on fixed deposit voucher/record
3	Account opening form and signature/authority card is completed
4	Pre-numbered certificates of deposits are issued
5	Customer’s instructions regarding renewal/repayment are obtained
6	Fixed deposit receipt prepared/signed/entered
7	F.D. actually – delivered to the customers

Thus the above stages involved in delivery of a simple case of bank fixed deposit enables to visualize how the product delivery process has many stages from the time a customer approaches for a particular product (being attracted/convinced by its use in fulfilling his specific need) till it is actually delivered

Check your progress 9

1. ______________Account is the facility that provides a customer freedom of transferring the excess funds in saving bank account to a Term Deposit Account of his choice.

   a. Flex Units Deposit

   b. Current deposits

2. The ______________deposits are accepted as short term, simple fixed deposit or reinvest deposits.

   a. saving

   b. term

4.11 Let Us Sum Up

In this unit we have focussed on the banking products and services. Here the main area of discussion was banking services. In this unit we discussed the nature of products that are offered by the banking sector and we studied in very detail about the various services offered by the banking sector.

In this unit the marketing mix for banking sector. We even studied the product life cycle of banking product. Basically the banking is a service industry so all the marketing principles are very similar. Branding and bank marketing were also discussed here in very detail. The various stages of product development were even explained in a very detailed way.

After this detailed discussion the readers would have got the sufficient knowledge about this topic.

4.12 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b), (3-a)

Check your progress 2

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 3

Answers: (1-a), (2-b), (3-a)

Check your progress 4

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 5

Answers: (1-a), (2-b), (3-a)

Check your progress 6

Answers: (1-a), (2-b), (3-a)

Check your progress 7

Answers: (1-a), (2-b)

Check your progress 8

Answers: (1-a), (2-b)

Check your progress 9

Answers: (1-a), (2-b)

4.13 Glossary

1. **FDRs -** Fixed deposit receipts are where amount is deposited with the bankers for a definite period of time. Rate of interest is more as compared to saving bank interest.

4.14 Assignment

Write abrief note on products and services in banking.

4.15 Activities

Discuss the elements of product mix in banking industry.

4.16 Case Study

Discuss the product development cycle for banking services.

4.17 Further Readings

1. Dynamics of Bank Marketing, R.K. Madhukar, UBS Publisher-1990.
2. A Handbook o j Management Techniques, M. Armstrong, Excel Books-1995.
3. Principles of Bank Management, Vasant Desai, Himalaya Publication-1993.
4. Elements of Marketing Management, Pradeep Kumar, Kedainath and Co. Meerut, 1995.

Block Summary

In this block we have discussed on services in very detail. This block focused on services and marketing of services in very detail.

In this block we have studied about financial services and marketing of financial services in very detail. In the first unit we discussed about the financial services in very detail. We discussed here in this unit about the service. What are the roles of this sector in our economy? Here we discussed the evoloution of this sector in detail. We even discussed the characterstics of this sector in very detail. Later in the second unit we discussed the marketing portion of this sector in very detail. In this block we discussed in very detail about the marketing aspect of financial services. Here in detail we discussed the marketing mix of services.

The difference between the product and services was even discussed here in very detail.In this block we had a detailed discussion on consumer behavior for financial services, where we studied the behavior of consumer in regards to the financial services and how does he have here in this sector. In this block under unit 4 we had a detailed discussion on the banking productsand services; here we even discussed the product mix for banking industry and even the product life cycle of the product of banking industry. After going through this block the readers will certainly feel confident in the topics of the block and would have understood the basic concepts and objectives of this block.

Block Assignment

Short Answer Questions

1. Marketing Mix
2. 4 Ps of Marketing
3. Product mix for financial services

Long Answer Questions

1. Discuss the characterstics of Financial Services.
2. Discuss the Impact of Technology on financial services.
3. Discuss the marketing mix for financial services.

Enrolment No. [   ]

1. How many hours did you need for studying the units?

Unit No	**1**	**2**	**3**	**4**
Nos of Hrs				

2. Please give your reactions to the following items based on your reading of the block:

Items	Excellent	Very Good	Good	Poor	Give specific example if any
Presentation Quality	☐	☐	☐	☐	________
Language and Style	☐	☐	☐	☐	________
Illustration used (Diagram, tables etc)	☐	☐	☐	☐	________
Conceptual Clarity	☐	☐	☐	☐	________
Check your progress Quest	☐	☐	☐	☐	________
Feed back to CYP Question	☐	☐	☐	☐	________

3. Any Other Comments

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Education is something which ought to be brought within the reach of every one.

- Dr. B. R. Ambedkar

Dr. Babasaheb Ambedkar Open University
'Jyotirmay Parisar', Opp. Shri Balaji Temple, Sarkhej-Gandhinagar Highway, Chharodi,
Ahmedabad-382 481.

FINANCIAL MARKETS

PGDF-103

BLOCK 3:

DISTRIBUTION, PRICING, RETAINING CUSTOMERS AND CONSULTANCY SERVICES

Dr. Babasaheb Ambedkar Open University
Ahmedabad

FINANCIAL MARKETS

Knowledge Management and
Research Organization
Pune

Acknowledgment
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The content is developed by taking reference of online and print publications that are mentioned in Bibliography. The content developed represents the breadth of research excellence in this multidisciplinary academic field. Some of the information, illustrations and examples are taken "as is" and as available in the references mentioned in Bibliography for academic purpose and better understanding by learner.'

ROLE OF SELF INSTRUCTIONAL MATERIAL IN DISTANCE LEARNING

The need to plan effective instruction is imperative for a successful distance teaching repertoire. This is due to the fact that the instructional designer, the tutor, the author (s) and the student are often separated by distance and may never meet in person. This is an increasingly common scenario in distance education instruction. As much as possible, teaching by distance should stimulate the student's intellectual involvement and contain all the necessary learning instructional activities that are capable of guiding the student through the course objectives. Therefore, the course / self-instructional material are completely equipped with everything that the syllabus prescribes.

To ensure effective instruction, a number of instructional design ideas are used and these help students to acquire knowledge, intellectual skills, motor skills and necessary attitudinal changes. In this respect, students' assessment and course evaluation are incorporated in the text.

The nature of instructional activities used in distance education self-instructional materials depends on the domain of learning that they reinforce in the text, that is, the cognitive, psychomotor and affective. These are further interpreted in the acquisition of knowledge, intellectual skills and motor skills. Students may be encouraged to gain, apply and communicate (orally or in writing) the knowledge acquired. Intellectual-skills objectives may be met by designing instructions that make use of students' prior knowledge and experiences in the discourse as the foundation on which newly acquired knowledge is built.

The provision of exercises in the form of assignments, projects and tutorial feedback is necessary. Instructional activities that teach motor skills need to be graphically demonstrated and the correct practices provided during tutorials. Instructional activities for inculcating change in attitude and behavior should create interest and demonstrate need and benefits gained by adopting the required change. Information on the adoption and procedures for practice of new attitudes may then be introduced.

Teaching and learning at a distance eliminates interactive communication cues, such as pauses, intonation and gestures, associated with the face-to-face method of teaching. This is particularly so with the exclusive use of print media. Instructional activities built into the instructional repertoire provide this missing interaction between the student and the teacher. Therefore, the use of instructional activities to affect better distance teaching is not optional, but mandatory.

Our team of successful writers and authors has tried to reduce this.

Divide and to bring this Self Instructional Material as the best teaching and communication tool. Instructional activities are varied in order to assess the different facets of the domains of learning.

Distance education teaching repertoire involves extensive use of self-instructional materials, be they print or otherwise. These materials are designed to achieve certain pre-determined learning outcomes, namely goals and objectives that are contained in an instructional plan. Since the teaching process is affected over a distance, there is need to ensure that students actively participate in their learning by performing specific tasks that help them to understand the relevant concepts. Therefore, a set of exercises is built into the teaching repertoire in order to link what students and tutors do in the framework of the course outline. These could be in the form of students' assignments, a research project or a science practical exercise. Examples of instructional activities in distance education are too numerous to list. Instructional activities, when used in this context, help to motivate students, guide and measure students' performance (continuous assessment)

PREFACE

We have put in lots of hard work to make this book as user-friendly as possible, but we have not sacrificed quality. Experts were involved in preparing the materials. However, concepts are explained in easy language for you. We have included many tables and examples for easy understanding.

We sincerely hope this book will help you in every way you expect.

All the best for your studies from our team!

FINANCIAL MARKETS

Contents

BLOCK 2: FINANCIAL SERVICE, CONSUMER BEHAVIOUR AND BANKING PRODUCTS

UNIT 1 FINANCIAL SERVICES: AN INTRODUCTION

Introduction, Meaning and Concept, Characteristics of Financial Services, Evolution of Financial Services in India, Significance of Financial Services, Types of Financial Services, Impact of Technology, Challenges before the Financial Services Sector

UNIT 2 MARKETING OF FINANCIAL SERVICES: A CONCEPTUAL FRAMEWORK

Introduction, Marketing and the Financial Services, Marketing as a Functional Area of Management, Financial Services and the Different Marketing Orientations, Difference between Services and Products Physical Goods, Characteristics of Service, Marketing Mix for Financial Services, Marketing Strategy and Financial Services

UNIT 3 CONSUMER BEHAVIOUR FOR FINANCIAL SERVICES

Introduction, The Complexity of Consumer Buying Decisions, Individual Influences on Consumer Behaviour, Needs and Motives, Individual Perception, Learning and Habit Development, Family Influences on Buying Behaviour, Behavioural Models for Analyzing Buyers, Consumer Behaviour Some Learning Points for Financial Service

UNIT 4 BANKING PRODUCTS AND SERVICES

Introduction, Nature of Product, Products and Services in Banking, Elements of Product Mix, Product Life Cycle and Product Strategies, Using Product Life Cycle lo Manage Marketing of Banking Products, New Product Development, Branding in Bank Marketing, Process and Product Development Cycle for Banking Services, Product Development

BLOCK 3: DISTRIBUTION, PRICING, RETAINING CUSTOMERS AND CONSULTANCY SERVICES

UNIT 1 DISTRIBUTION, PRICING AND PROMOTIONS STRATEGY FOR BANKING SERVICES

Introduction, Banking Services and Issues in Delivery, Channels of Distribution for Banks, Types of Branches, Electronic Methods of Distributing Financial Services, Pricing of Banking Products/Services, Pricing Objectives, Pricing Methods, Pricing Reviews and Committees, Price Setting in Practice, Promotion of Banking Products/Services, Guidelines on Advertising by Public Sector Banks, Sales Promotion, Internal Communication, Marketing Information Systems (MIS)

UNIT 2 ATTRACTING AND RETAINING CUSTOMERS IN BANKING SERVICES

Introduction, Defining Customer Value and Satisfaction, Factors Influencing Consumer Behaviour in Banking, Relationship Marketing and Attracting Customers, Customer Relationships Management, Retaining Customers Through Quality, Service and Values , Delivering Customer Value and Satisfaction, Image as a Managed Perception, Fulfilling Promises : Internal and Interactive Marketing, Customer Service and Customer Care, Bank Marketing : Future Challenges

UNIT 3 ADVISORY AND CONSULTANCY SERVICES

Introduction, Portfolio Management, Credit Rating, Takeovers and Mergers, Trustee Services, Depository Services, The Marketing Approach for Merchant Banking Services

BLOCK 4: MARKETING OF PENSION FUNDS AND GLOBALIZATION

UNIT 1 MARKETING OF PENSION FUNDS

Introduction, Emerging Dimensions Relating to Investment Services, Pension Funds: A General Overview, Why Pension Plan?, Types of Pension Plan, Pension Fund Risk, Funds Management, Pension Fund Investment: General Guidelines, Pension Funds and Capital Markets, Pension Funds: Some Related Statistics

UNIT 2 GLOBALISATION AND ITS IMPACT ON FINANCIAL SERVICES MARKETS

Introduction, Globalisation of Financial Markets and its Impact on Local Markets, Globalisation of Markets: The Main Drivers, Globalisation of Markets: The Road Ahead, Some Asian Trends, Globalisation and Consumer Orientation, The Emerging Imperatives for Financial Services

Dr. Babasaheb
Ambedkar
Open University

PGDF-103

FINANCIAL MARKETS

BLOCK 3: DISTRIBUTION, PRICING, RETAINING CUSTOMERS AND CONSULTANCY SERVICES

BLOCK 3: DISTRIBUTION, PRICING, RETAINING CUSTOMERS AND CONSULTANCY SERVICES

Block Introduction

As we are progressing the area of production has been increasing, gone are the days when only products which are tangible in nature used to be produced. Now a day the production of services is immensely rising and because of this the importance of this subject can never be underestimated.

In this block we will be discussing about the distribution, pricing, retaining customers and consultancy services. In this unit we will be discussing in very detail about the meaning and importance of distribution, pricing, retaining customers and consultancy services. In this block we will be studying the banking Services and Issues in Delivery; we will be focussing on the banking services in very detail and the various types of banking branches shall be discussed in this block in detail. Here we will be discussing the various pricing objectives, methods. We will be discussing the about sales promotion and management information system in very detail. In this block we will also be discussing in very detail the topic how to attract and retain customer in banking industry. Thereafter in the third unit we will be discussing the advisory and consultancy services sector in which we have discussed in very detail about portfolio management and credit rating.

After going through this unit the students will be confident enough about the basics of financial services the marketing of this sector.

Block Objective

After learning this block, you will be able to understand:

- The basic concepts of distribution, pricing and promotion for banking services.
- Relationship marketing in the banking sector.
- Customer's relationships management.
- The process of creating service differentiation through service quality.
- The marketing approach for merchant banking services.
- The depository services.
- The takeovers and mergers.

Block Structure

UNIT 1: DISTRIBUTION, PRICING AND PROMOTIONS STRATEGY FOR BANKING SERVICES

Unit Structure

1.0 Learning Objectives

1.1 Introduction

1.2 Banking Services and Issues in Delivery

1.3 Channels of Distribution for Banks

1.4 Types of Branches

1.5 Electronic Methods of Distributing Financial Services

1.6 Pricing of Banking Products/Services

1.7 Pricing Objectives

1.8 Pricing Methods

1.9 Pricing Reviews and Committees

1.10 Price Setting in Practice

1.11 Promotion of Banking Products/Services

1.12 Guidelines on Advertising by Public Sector Banks

1.13 Sales Promotion

1.14 Internal Communication

1.15 Marketing Information Systems (MIS)

1.16 Let Us Sum Up

1.17 Answers for Check Your Progress

1.18 Glossary

1.19 Assignment

1.20 Activities

1.21 Case Study

1.22 Further Readings

1.0 Learning Objectives

After learning this unit, you will be able to understand:

- Explain the concepts of distribution, pricing and promotion for banking services.
- Apply these concepts in bank marketing.
- Discuss issues in delivery of banking services.
- Describe the effect of pricing policies in marketing of banking services.
- Appreciate the role of promotion strategies in the banking services.

1.1 Introduction

In an organization engaged in marketing, channels of distribution for financial services should be thought of as a means to increase the availability and/or convenience of services that help satisfy the needs of existing users or increase their use among existing or new customers. The marketers of financial services have to ensure facilitating right product for the right people at the right place and at the right price. Pricing can be strategically used as the tool to reduce the competition. Pricing is equivalent to the total product offering which includes the brand name, package, product benefits, service delivery, credit extended. It can be described a sum of expectations and satisfactions. Promotion is a generic term used for the communication efforts of the firm that are directed towards achieving the objectives of a marketing strategy. You will see in this unit how the promotion means conscious efforts towards integrating its marketing strategies with business plans.

1.2 Banking Services and Issues in Delivery

Let us now attempt to see what effect the special nature of services has, on the formulation of banking delivery systems:

1. **Tangibility:** It is not often possible to illustrate, demonstrate or display the services on offer, and therefore storage, transportation and inventory control are not relevant for the bank marketer. This partly explains the relative absence of intermediaries’ ox middlemen in the delivery of banking services. As a result it severely limits the alternatives available to the

financial services marketer and often necessitates the use of direct channel for distribution

2. **Inseparability:** Because of the simultaneous production and distribution of financial services, the main concern of the marketer is usually the creation of time and place utility that is that the services are available at the right place and at the right time. This implies that direct sale is almost the only feasible channel of distribution. But as we shall discuss later one way of overcoming the inseparability factor is the use of credit cards, whereby the service is transferable.

3. **Highly individualized marketing system:** When selecting channels of distribution the goods marketer will usually have a marketing system that contains several established middle persons. This is not always the case with financial services with a few traditional distribution channels. 1n many bank transactions a client relationship exists between buyer and seller, as distinct from a customer relationship: This is especially true in the case of in any corporate and trust accounts, although it not extends more and more to other retail customers as well. Where such a close personal and professional client relationship must exist direct channels may be only feasible choice.

4. **Lack of special identity:** To the public often one financial service is very much like the other. The reason why a particular financial institution or branch is used is often related to convenience. As the competing products are similar, the emphasis is on the 'package' reputation, advertising and from time to time new services. As major competitors offer similar services, the emphasis will be on the promotional aspects rather than on the inherent uniqueness of a particular financial institution's service.

5. **Geographical dispersion:** There has to be a branch network in any financial. Institution of size and scope, in order to provide benefits of convenience and to meet international, national and local needs. Therefore, all services or promotion must have both appeal and wide application.

Barriers to Provision of Delivery System

Barriers to the provision of delivery systems in financial service can be considered to fall under two broad categories:

- Business barriers, and
- Technological barriers.

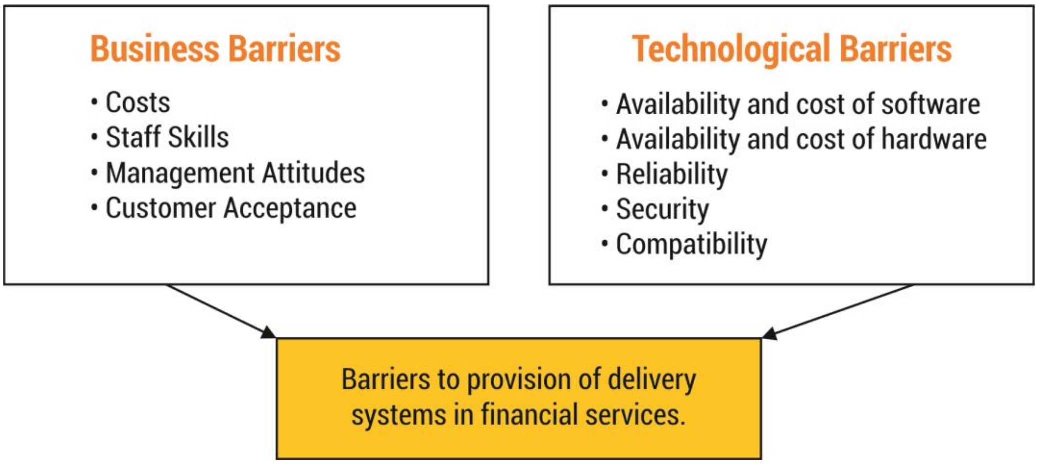

Fig 1.1 Barriers to Provision of Delivery System

Check your progress 1

1. The main concern of the ____________is usually the creation of time and place utility.

   a. marketer

   b. seller

2. When selecting channels of distribution the goods marketer will usually have a marketing system that contains several established __________persons.

   a. end

   b. middle

3. To the ______often one financial service is very much like the other.

   a. public

   b. seller

1.3 Channels of Distribution for Banks

The channels of distribution in financial services perform a number of key functions, as follows:

- Sale and offer of services and products, as well as advising customers.
- Contact and liaison with advertising and public relations agencies to assist in designing more effective advertising/promotional campaigns.

- Gathering of information necessary for planning marketing activities, strategy decisions and product development.

In distributing financial services, firms employ a number of channels. The advantages of direct distribution channels - for example branches, used to be lower operational costs and more efficiency. In comparison, the selling through indirect channels offers convenience to the customers and more 'impartial' advice, as in the case of agencies.

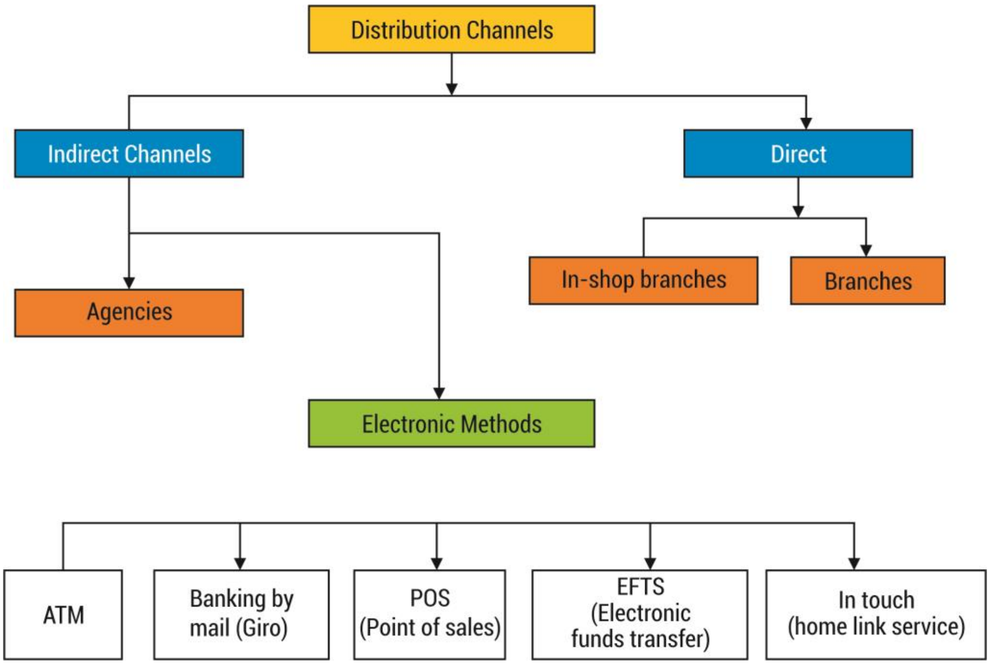

Fig 1.2 Distribution Channels

The Branch Network

Bank's major distribution outlets are their branches. The design and development of the branch network will be affected by:

- **Characteristics of the products** - importance of service quality, inseparability of the product, intangibility of the product.
- **Customer needs** - convenience, opening hours, availability of ATM, telephone banking, home banking and so on.
- **Environmental factors** - legislation, development of information technology.
- **Competitors** - if a branch network is efficient, it will be a competitive advantage, keeping up to date with changes made by competitors.

Advantages of the branch network include:

- Its accessibility for customers.

- It keeps a bank's name in the public eye
- The prime sites
- Banks become accepted as important members of the community

Disadvantages of the branch network include:

- It is costly to maintain premises
- The staff costs
- The major investment involved - the amount of capital tied up in it
- It is old fashioned, difficult to modernize
- Small branches can be difficult to enlarge when expansion is necessary

Branch Location and Distribution

As the roles and functions of financial services continue to grow in most countries, pressures are building up for more efficient distribution systems. Historically, for financial services branches have essentially been retail outlets. Although in the last few decades or so the roles of the branches have changed, financial services customers still regard convenience of delivery as being decisive when choosing a financial organization. Moreover, location decisions involve long-term commitment of resources and as such have implications on the long term profitability of the banks.

In distribution of banking service the marketer is faced with a huge market that should be duly served. For e.g. in recent years many banks, have already grown and diversified through acquisition, they have had to face the necessity of developing profitable services for mass business. This market falls into two broad categories:

1. **The mass (retail) market:** Standard products, relatively inflexible in performance and cost, can be offered to this market. It spells out the requirements of geographical decentralization, standardized services, heavy advertising and promotion, attractive services and above all cost effective processes.
2. **The individual (corporate) market:** This market constitutes single orders of sufficient size of importance to be profitably singled out for individual treatment. It requires individualized services and counselling, such as comprehensive financial advice, the availability of research services and contact brokerage to the customer, negotiated terms and so on.

Banks are now changing the image of their branches. Bank branches used to be serious, dull places that often intimidated customers. All the staff used to work behind security screens and this created an unfriendly atmosphere. Now, some security screens have gone, banking halls are brighter and a friendly atmosphere has been created that is less daunting for customers. Branches are more like a financial services shop Newly designed branches are open, planned and many staff have moved into the banking hall to tables, to advise a customers in a friendly way about financial matters, opening of accounts, solve problems or answering queries.

It is expected that by the end for this millennium, the most important aspects of branch workload will be ATMs, telebanking and the retail counter in that order. Currently, the developed countries' bank branch workload is in reverse order, the retail counter demanding the most time and effort from the branch staff and management. In Indian conditions, the lion's shares of service are through retail counter only. The other components in the delivery system have just begun to catch up.

As mentioned, branches still continue to be the most important channel of distribution for banks although demand for electronic systems has been registering high growth rate.

The traditional reasons for establishing branches were to collect deposits, arrange loans and provide convenience in conducting transactions. Technological development has meant that there is less need for customers to go to branches for their business transactions. This reduces the possibility of any 'impulse' cross service sales.

Check your progress 2

1. Bank's major distribution outlets are their__________.

   a. branches

   b. customers

2. For financial services _______________have essentially been retail outlets

   a. customers

   b. branches

1.4 Types of Branches

Branches of different financial institutions deliver different types of service for different types of customer as explained in following section:

1. **Full service branch:** The full service branch has been the conventional delivery system, providing a full range of the products and services offered by the institution to both corporate and retail customers, however, in the developed countries, the services provided by banks have increased immensely as deregulation has led them to extend their range of conventional financial service variants. In India, too with the liberalization and deregulation in the financial sector, similar position is set to be evident soon.

2. **Specialty branch:** Specialty branches now serve as alternatives to full service operation. Specialty branches focus on either retail or corporate business but not both; for example real estate specialist branches focus on mortgage finance. Thus the time devoted to withdrawal and deposit transactions is reduced. On the domestic scene, we have many SSI branches, industrial finance/corporate banking branches, NIU branches, Hi-tech agricultural branches, service branches, commercial and personal branches, recovery branches, leasing branches, housing and finance branches.

3. **High net worth' branches:** These branches are located' in appropriate socio-demographic areas and they distribute a range of financial services for up market customers. These services are often based on minimum account balance criteria, and they emphasize personal financial counsellor services rather than conventional bank teller services.

4. **Corporate branches:** These aim at middle-market corporate accounts and do not usually handle retail financial services. The services provided are on-line foreign exchange, letters of credit, asset-based financial specialization and corporate cash - management services and so on.

5. **Hub and spoke banking:** The status of each branch is determined by the area and customers it serves. There is little point for a branch in a small rural village to have a business advisor. It is more beneficial for the bank to ignore this service when the market is very small and to cater for it at a larger branch in the nearest larger town. This system of providing a limited service in the smaller branches, backed up by a nearby, larger core branch, that is' able to carry out all the services 'the bank offers, is called 'hub and spoke' branch banking. The smaller satellite branches provide a limited and

mostly highly automated service, dealing mainly with the personal banking. These are linked to a key branch that offers a full range of services and often co-ordinates the activities of its satellites. Normally there can be between four and 15 satellites to one key branch. The hub is responsible for corporate business and has overall jurisdiction for the network as a whole. In India such an organizational arrangement is not common.

The hub and spoke structure has many benefits. One very important benefit is that it is part of a rationalization strategy. The new structure reduces the large amount of replication that was occurring at every site (including expensive equipment and personnel) and which was not being used in an efficient way anyhow. This reduction and regrouping at the key site has vastly reduced the excessive duplication in a move towards getting the bank to provide the correct range of services in an area

The advantages of hub and spoke branching are: -

- Costs are reduced by concentrating specialized (and expensive) staff in key branches;
- Duplication of management skills is avoided
- The processing function in centralized in a limited number of branches; and
- Banking are able to pursue simultaneously both product and relationship strategies, for example identifying good customers in satellite branches, who are then served by product managers (bankers) located in key branches.

Overall the tendency is towards fewer bank branches. The reason for this is that, the high operational and staffing costs of running a branch, the increase in scale and benefits of automation and technology, the advent of direct banking (via telephone, home link and in-touch services offered to larger financial customers), and the mergers and /or acquisitions by banks, have given rise to rationalization reduction) of the number of branches.

It often happens that a financial product that might be unprofitable when delivered through one type of branch-say a satellite branch-might be successful when it is distributed through a central, regular branch. The selection or emphasis on one type of distribution outlet rather than another depends on the personal service required, service content (for example information, advice, personal attention and so on) financial product complexity and its customization requirements, purchase frequency and level of customer sophistication.

There are three perspectives that determine distribution profitability in financial services:

1. Channel profitability
2. Branch profitability
3. Customer profitability

Branch profitability is particularly important, as the costs of managing and operating branches tend to increase. Obviously, the profitability of a branch is affected by its, administration. Research has shown that the profitability of a branch depends largely on the volume of deposits, that is high volume/economies of scale approach is usually profitable. To handle this problem banks have developed a number of different types of branch, as mentioned above and depicted in figure below:

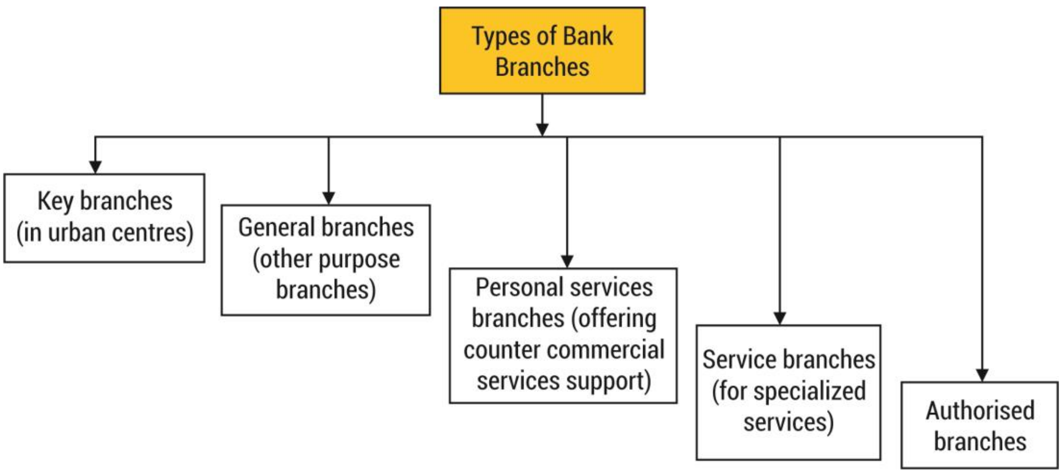

Fig 1.3 Types of bank branches

Branch Location and Shopping/ Commercial Centers

Branch locations often tend to be concentrated in larger shopping centers because if financial institutions seek to attract personal savings and past experience indicates that these are the most advantageous locations, especially for banks. The advantages of locating branches in shopping centers include easy market entry since many shoppers and potential customers frequent the Height Street and shopping centers. Generally, availability of parking and transport facilities as well as proximity makes the location ideal for customer contact.

A few of the distinct limitations for such branches are:

1. They might not be able to expand because of limited adjacent space General branches
2. They might lose their special identity because of the many competing

branches around

3. In certain areas, shopping centers have restricted opening hours which might affect the branch's activity.

The Indian experiments of opening rural branches, service area approach and directed lending uniquely combined both the marketing and social responsibility roles for bankers. The liberalization and deregulation may focus more on the viability of operations more than in the past and hence, the aspects that go to make a branch profitable will need to be addressed more effectively.

Check your progress 3

1. The ___________branch has been the conventional delivery system, providing a full range of the products and services.

   a. full service

   b. speciality

2. ____________branches now serve as alternatives to full service operation.

   a. full service

   b. speciality

3. ___________are located' in appropriate socio-demographic areas and they distribute a range of financial services for up market customers.

   a. branches

   b. head office

4. __________locations often tend to be concentrated in larger shopping centers.

   a. ATMs

   b. Branch

5. Branch ___________is particularly important, as the costs of managing and operating branches tend to increase

   a. profitability

   b. business

1.5 Electronic Methods of Distributing Financial Services

The need to make branches and distribution more efficient has led to the introduction of electronic methods in financial services. The first ATMs (automated teller machines) were introduced in the UK in the form of cash dispensers by Barclays Bank in 1968. The main objectives of this distribution facility were to save costs and staff time, and to provide greater customer convenience (that is service outside normal banking hours). Since the system was introduced, there have been four main features associated with ATMs: reliability, security from fraud, volume generation at any particular location, and the relatively high costs per machine network.

The decision whether or not to install an ATM depends on a number of factors, as follows:

- Its impact on branch staffing levels, branch business and costs. (Recent research suggests that paying out money via cash dispensers is about 65% cheaper than counter withdrawal).
- The cost of investing in a large network of ATMs including service support and reciprocal arrangements with other financial institutions.
- The impact of ATM installation on a financial institution's image and its ability to differentiate its services/products.

The distribution of financial services has been further affected by development of the electronic funds transfer systems (EFTS), whereby money can be exchanged between the consumer, retailer and financial institution in the form of electronic data rather than being transferred physically which involves the processing of paper. ATMs form part of EFTS and have been used to provide the customer with a quick, convenient and safe service 24 hours a day, seven days a week

Financial services today are making determined efforts to make use of the latest technology is changing the market rapidly and this will have a major impact on financial services branches. ATMs and EFTPOS (electronic fund transfer at point of sale) are much more efficient in cost savings, time and labour.

Calculations, show that on an average an ATM equals (or leads to) a total net labour savings of 1.33 full time staff. There are a number of important reasons for installing ATMs.

- To increase customer convenience,
- To increase customer traffic,
- To reduce cheque volume and consequently cheque processing costs,
- To reduce labour cost,
- To reduce cash security problems, and
- To provide the bank with clear strategic advantages (for example entry barriers, greater economies of scale, and product differentiation).

There is now a trend to establish ATMs in satellite or away from branch locations in shopping centers and in commercial complexes. ATMs can be used to absorb extra customer demand during peak hours or outside branch business hours. They also save staff time. ATMs now perform as many as 150 functions ranging from cash dispensing to accepting split deposits to trading in stocks, to buying mutual funds.

Future electronic payment systems in financial services will consist of a flexible telecommunications network that will join terminals situated on the premises of retailers in customer's homes, and on the counters of branch offices, and ATMs. The network will then link these terminals via microcomputers to financial service computers. All these new electronic methods will eventually make cash and cheque less necessary but it will take some years for their full potential to be achieved. In the meantime, it is essential for financial services to have branches with full payment facilities so as to maintain their strong competitive edge. Some of the electronic banking methods in use are:

Telemarketing: Consider the case of the largest 'branch' of the manufacturer’s bank in the USA. No customer visits it. Its customers reside throughout the USA and their business is solicited by long distance telemarketing or direct mail. There has been substantial growth in both loans and deposits via telemarketing and direct response to newspaper advertising. These systems 'can be much cheaper than full branch operation and are especially useful to institution that do not have a large network of bricks and mortar outlets.

ATM’s: Many banks now have ATMs outside their branches. Those outside ATM’s offer 24 hours banking to customers. Some banks also have an ATM in the lobby and customers use their security card to enter the lobby and then use the machine in the normal way. These machines can be used to withdraw cash, pay money and cheque into an account or to order statements balances or information packs. ATMs are also now located at many of the larger retail stores and at factories. The machines are maintained by the local branch. The development of the ATM network may mean that at some point of time in the future, cashiers will be replaced by the ATM machines.

EFTPOS: EFTPOS offers a cashless method of payment to the customers at the point of sale and is important in all areas of retail transactions. In many countries, the EFTPOS schemes proposed by bank have run into difficulty as the banks have endeavoured to charge more than retailers have been prepared to pay. While trends show that EFTPOS will become an important payment mechanism, it is not expected wholly to replace cheque, although successful EFTPOS systems are likely to reduce cash payments and in particular stimulate the use of debit rather than credit cards. As with ATMs, EFTPOS also reduce the need for customers to visit their branches.

Intelligent Terminals: In the corporate market, developments in electronic banking have led to the introduction of intelligent terminals. With these, and backed up with their own central processing units, corporate treasures can interact with the bank's own mainframe computers to undertake cash management, transactions, letters of credit and the like, receiving timely transaction data and other economic and financial information services.

Telephone Banking: Some banks are now offering home or telephone banking. This may reduce the need for branches in the future. An example of this is Midland's first direct service which is a new concept in banking. It does not operate through a branch network but entirely by the use of the telephone and the postal system, it also provides all the usual banking services - current accounts, loans, A'TM facilities. Customers can, contact first direct service 24 hours a day. Midland have spent a lot of money advertising this new venture. The market they have tried to attract is the younger market particularly the age group 20-35, who are more financially aware and are used to dealing with matters by phone.

Home banking or in-touch Financial Services: Another innovative means of distributing bank service has been pioneered in the USA through the application of computers. Computerized facilities have been used in supermarkets to record each transaction with the respective customer's account with the bank. The Seattle- first National bank has promoted an in-touch home service that provides customers with access to a talking computer from touch-tone phones at home. By calling up the bank computer, the customer can instruct it to perform financial services such as:

- Paying bills by transferring funds from his bank account to that of a creditor.

- Aiding family book-keeping by reporting expenses with a biweekly budget analysis broken down into several categories (food, housing, clothing, etc.)
- Computing income tax data

Normally, home banking is likely to be just one of a range of services provided as part of a home information system which also offers shopping, news, entertainment and information data. The home banking service itself will usually permit account interrogation; inter account transactions, bill payments, loan generation and electronic mail. In addition some systems are adding brokerage, insurance and mortgage banking facilities. Home banking is expected to become a significant alternative delivery system to conventional branch systems in due course.

Internet Banking: Security First Network Bank, an Atlanta (US) based savings bank, is one of the first international banks to go operational on the internet. Within 10 months of its launch in October, 1995 it garnered 5550 accounts and US$ 15 million deposits I across the world. The services being envisaged by Indian Banks include:

Customers with PC and net connectivity can-

- View transactions in their accounts, exchange messages with the officers concerned in the bank through a mailbox, request cheque book and get printed account statements, structure loans by asking a series of what if questions and getting answers.
- Request for funds transfer between accounts, issue stop payment requests and standing instructions and do deposit modelling.
- Have on-line connectivity providing the customer with the ability to directly debit and credit the account without the bank's intervention, etc.

A recent study estimates that in a full service branch, the cost per transaction is US$ 1.07 as against US$ 0.54 for telephone banking, US$ 0.27 for ATM full service, US$ 0.015 for PC banking and US$ 0.ol for internet based banking.

Check your progress 4

1. The need to make branches and distribution more efficient has led to the introduction of ___________methods in financial services.

   a. electronic

   b. manual

2. ATMs and EFTPOS are ________efficient in cost savings, time and labour.

a. not much

b. much

1.6 Pricing of Banking Products/ Servings

No discussion on marketing mix for banking services can be complete without understanding the concept of pricing and its importance in detail. Pricing can be strategically used as a tool to meet/ reduce the competition

Pricing affects the product cost and also plays a key role in decision making of the buyers (customers). Pricing is affected by competitions, seasonality and general trend of demand and supply. In short, it can be said that the price is determined by cost, demand and competition in the market.

Price in the eyes of the consumer is the evaluation of the total product offering which includes the brand name, package, product benefits, service, delivery, credit extended, etc. Price can be defined as the money value of a product or service agreed upon in a market transaction and can be shown as –

PRICE = sum of expectations + satisfactions.

Pricing for Profitability:

In a competitive market, price is determined by free play of demand and supply. Price will increase or decrease depending on increase or decrease in the demand for product.

Pricing decisions link the marketing actions with the financial objectives of organizations.

Pricing affects:

1. Sales Volume
2. Profit Margin
3. Rate of return on investment
4. Product position
5. Image of the organization

Pricing is the key decision through which the other marketing strategies have to consider in order resulting into profit or revenue like:

Other Marketing Strategies	➔	Price Strategy	➔	Revenue

See the relationship of pricing with profitability in a manufacturing concern. We can see the following break-up:

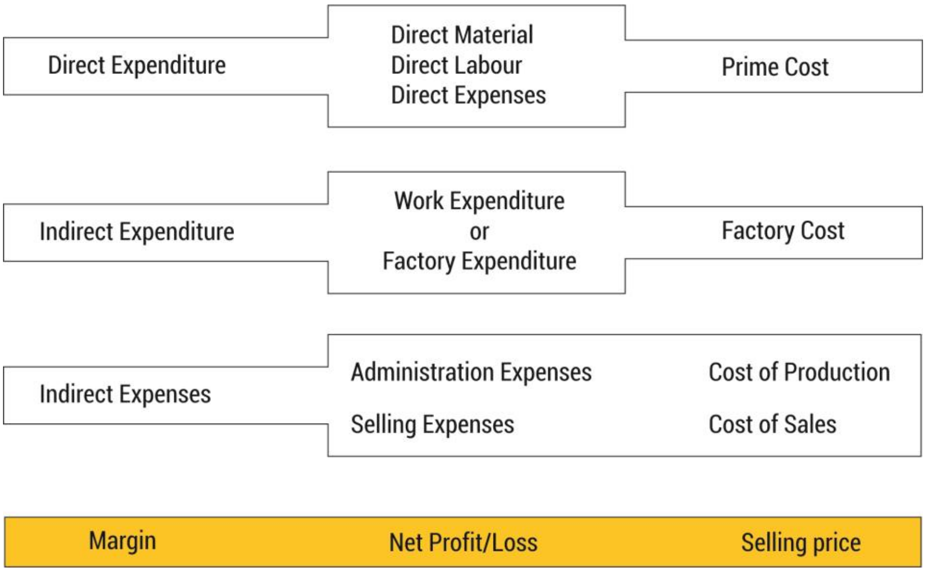

Fig 1.4 Relationship of pricing with profitability in a manufacturing concern

Price simply read can be described as 'cost plus profit'. Therefore, proper analysis of cost and proper decision regarding profit level has direct impact on pricing decisional strategy

Normally direct expenses which vary with volume of production/sales are variable cost and indirect expenses are fixed cost.

Check your progress 5

1.____________ affects the product cost and also plays a key role in decision making of the buyers (customers)

a. Pricing

b. selling

2. In a competitive market, ___________ is determined by free play of demand and supply.

a. cost

b. price

1.7 Pricing Objectives

Before we review the pricing theories in detail, it is essential to know the typical pricing objectives. Important among which are:

1. **Growth in Sales** - A low price can achieve higher growth in sales volume but may affect the profit level adversely.
2. **Market Share** - The customer acceptance is reflected by market share of a product and. is an indicator of acceptability of price.
3. **Competition** - To face the competition, prices can be lowered to maintain sales or in the absence of it, prices can be revised but stable prices help in maintaining image or brand name and quality.
4. **Pre-determined Profit** - If a profit level is pre-decided as a policy, the price has to be maintained at a particular level despite other factors as to ensure attaining that objective.
5. **Corporate objectives** - to have pay-back in a specific period also can affect the pricing and price level

Check your progress 6

1. A __________price can achieve higher growth in sales volume but may affect the profit level adversely.

   a. low

   b. high

2. If a __________level is pre-decided as a policy, the price has to be maintained at a particular level despite other factors as to ensure attaining that objective.

   a. danger

   b. profit

1.8 Pricing Methods

Market Based Pricing System:

In order to understand consumers based inputs on pricing system, we should also take into account the market related pricing systems, which adopt one or more of the following approaches:

- Perceived value pricing
- Psychological pricing
- Promotional Pricing
- Skimming

Perceived value pricing: These are based on the belief the consumers have about the value of products and pricing is based on these assumptions. This is supplemented by market research and if price is more than buyer – recognized value, it may affect sales whereas if price is less than buyer - recognised value, the revenue will suffer.

Psychological Pricing: In many pricing systems, pricing is based on prestige - and can be kept higher to promote the idea of status and quality. Many other times the price will be just below a round figure say Rs.59.20 (to show it is less than Rs.100) or Rs.499.00 (i.e. not Rs.5001- or above).

Sometimes instead of giving a 20% discount, the price per unit per-se will be constant (uncharged) but it will advertised that on purchase of 4 units one unit will be free.

Promotional Pricing: This is used for promoting high level of sales or to clean excess stock which although is with a reduced profit margin improves sales and reduces holding cost.

Skimming: This strategy is to, 'skim the cream' i.e. adopting a high price approach. When the product is new and innovative and in a monopolistic or less competitive market, the price will be higher, (like in mobile phones) which can be progressively reduced with entry of more producers and skimming the cream sufficiently.

Cost based Pricing:

There are four main cost based pricing methods which are:

1. Standard cost pricing
2. Cost-plus pricing

3. Break-even analysis

4. Managerial Pricing

Competition Related Pricing Strategies

The competitive pricing means pricing to compete with the leader in the market with respect to the price

It can be either to set higher price initially and then to offer discounts known as 'discount pricing' or to significantly increase sales volume by competing with others already leading in the market by undercutting the prices significantly with the sole idea of penetrating the market.

Pricing Decisions as applied in Banks

Decisions in pricing are generally taken in view of the market opportunities. Pricing decisions are differently handled by different organization as a policy or as a strategy.

The factors such as economic, social, political affect pricing decisions. In small organisations pricing decisions are taken by the top management whereas in big organisations the divisional or product line heads have the authority to decide/fix the price. In some other organisations, committees are set up to fix the price.

As we focus our attention to marketing of banking services and further on the pricing aspects, these are two major costs which have to be considered and they are:

- Interest cost
- Servicing cost

The interest rates for banks in India have been administered for decades by the Reserve Bank of India and the service charges have been advised and administered by the I.B.A. with which although in funds management market forces and demand and supply do play a role, in respect of interest or service charges, the market forces did not affect to any considerable extent

Pricing policy and strategies, however, is equally relevant in banking due to the fact that it affects the demand as well as profitability and after a considerable stress on social banking in Indian context, due to the guidelines regarding capital adequacy by Narasimham Committee, once again profitability has become an important consideration of bank viability.

Now, even the public sector banks have freedom to stipulate rate schedules for such activities which are not covered under uniform schedules. The interest rates on domestic deposits can also be fixed by banks, within the stipulated range, for deposits with different maturities.

With the winds of globalisation and liberalisation flowing freely in India and the competition faced due to aggressive marketing strategies and innovative products by private and foreign banks, the banks have to re-think their marketing policies - more so the pricing strategies.

Check your progress 7

1. Decisions in ___________are generally taken in view of the market opportunities.

   a. pricing

   b. profit

2. In ___________organisations pricing decisions are taken by the top management.

   a. big

   b. small

3. In some organisations, committees are set up to fix the______________.

   a. price

   b. quality

4. The interest rates for banks in India have been administered for decades by the _____________

   a. State Bank of India

   b. Reserve Bank of India

5. __________and strategies, however, is equally relevant in banking due to the fact that it affects the demand as well as profitability.

   a. Pricing policy

   b. profit policy

1.9 Pricing Reviews and Committees

It is well known that the banks in U.K. and USA have already diverted their attention to service and non-fund activities for improving revenue.

With regulated interest rates and uniformity in service charges for a long time, customers too are now aware and many accept the service fees/transaction fees charged by banks in giving better and prompt service.

- There have been many studies to analyse the ways and means to improve profitability of banks.
- The very 1st report on cost aspects of Indian Banks was published in 1972.
- Traditionally, interest or finds activities were the only source of profit for the banks.
- The remittance business and bills business did not prove to be of much help in increasing profit/ revenue.
- Besides profit from forex business and exchange profit, there were not enough amounts under other income which now is increasing steadily.
- Before standardization efforts by IBA, banks were using different methods for service charges like
  - Flat Service Charge
  - Measured Service Analysis
  - Complete Analysis Method
- On bill business the fees charges were not very adequate compared to the service rendered.
- In 1985 IBA efforts for rationalization and standardization of service charges met with success to bring about uniformity in several banking services, while public sector banks are governed by IBA guidelines, the foreign banks and the private, banks had the freedom to decide their own charges

The committee, of public sector banks for service charges was set up to provide guidance, check costing and decide the implementation schedule.

- Sinha Committee was constituted by IBA with Mr.T.K.Sinha as Chairman to give report on costing of services.. The report was submitted to IBA on

April 1987. This was a very useful study providing a firm basis to all the banks to decide pricing strategies.

The steering committee set up by RBI advised commercial banks to undertake costing studies in two phases.

The banks were advised to collect data on deposits, advances, foreign exchange business, bill business; govt. business, etc.

In the second phase exercise was given by RBI to each bank to work out cost in following fields:

1) Transfer pricing

2) Pricing of different services

3) Analysis cost trends

4) Cost benefits analysis for concession, etc.

5) Break-even analysis of branches to categories and monitor profit making and loss making branches and to decide strategy.

With the advent of new departments and products, like merchant banking, investment, counselling, project consultancy, etc. pricing of new products, services was required to be based on cost assessment and commercial (viability) criterion.

Even at the branch level awareness was created to be in tune with macro level.

(Corporate) planning and decide selective recommending/selling of bank's products at branch for better pricing mix and better overall revenue.

Check your progress 8

1. It is well known that the banks in ____________have already diverted their attention to service and non-fund activities for improving revenue.

   a. U.K. and USA

   b. India

2. The steering committee set up by__________advised commercial banks to undertake costing studies in two phases.

   a. SBI

   b. RBI

1.10 Price Setting In Practice

We have seen from the discussion on earlier pages that in Indian Banking it has been a regulated pricing system, till recently regarding 'interest as well as the service costs.

If we take a look at the following table (taken from the consumer federation of American report) it will be clear as to how bank fees/services vary and customers accept such a variety of service fees.

Saving	Low	High
Minimum balance for interest		
Monthly fee if below minimum	0.00	200,00
Regular chequing	0.00	3.00
bounced cheque	7.00	20.00
returned deposit		
Now A/c	0.00	12.00
Minimum to avoid charge monthly service charges	50.00	2500.00
Pre-cheque charge if below minimum	2.00	3.00
Other checking	0.20	0.50
Holds on non-payroll cheques from out of state	2 Days	20 Days

Banks have to develop better strategies and understanding with customers to convince regarding the cost by way of service fees as essential for good quality service.

Traditional Bank Pricing Approach:

Primarily two types of approaches are being adopted by banks abroad to set prices:

- Bundling
- Auction

Bundling involves the aggregation of bank product 01- services offered i.e. combination of deposit and loan account or credit and non-credit accounts and bundling these with respect to the compensating balances and a prime rate.

In auction mechanism, banks desirous of making loans to both retail and corporate sectors auction, their loans in a (restricted) competitive market.

These are further based on considerations like relationship with credit worthiness of the client and average balance maintained, etc.

Price Determination:

It is not just the interest rates alone that determine pricing, it is also the fee-based pricing (for services rendered) that is fast gaining momentum. As each deposit/product or service has potential to achieve certain marketing goal to satisfy a particular customer segment, the pricing must be set with respect to the said objectives and customer needs ability and level of satisfaction

Target Pricing:

This is decided by keeping in view a pre-decided target level of business (volume) or profit (revenue). This depends on the level of investment and degree of risk involved.

If we look at the factors determining the 'base' price level for any organisation, its relevance to banking can be judged.

Some Limitations in Pricing for Banking Services

In banking the concepts determining prices have been

Bank Rate

MNR - Minimum Lending Rate

MLR - Maximum Lending Rate

PLR - Prime Lending Rate as a reference rate

Loan Able Funds - Banks have to work within the framework of RBI guidelines due to which a bank can lend only a certain portion of mobilized deposits after providing for cash reserve ratio and statutory liquidity ratio i.e. out of Rs.100 funds only about 58% can be lend as loans/credit. It becomes obvious, therefore, that the revenue by interest on lending should be enough to cover the cost of interest paid on deposits and administration cost.

Spread - Due to the limitations of CDE (Credit Deposit Ratio) and lack of sufficient demand for borrowings in the money market all banks are consciously considering the service fee concept to improve their profitability on the SPREAD is not quite enough to improve the profit planning in view of higher administrative costs and non-interest bearing advances (non-performing assets).

Transfer Pricing Concept and Mechanism

Simply speaking if we take profit as excess of income over expenditure, the same has to be re-thought in branch level system where some branches will be predominantly deposit centers and some branches will be predominantly advance centers where deposit centers will have mostly interest payable and show losses. The advances branches will have large demand and all profits by way of interest on advances but these will not be deposits available as loan able funds.

This means in one branch there will be high supply (deposits) and high interest payable and no demand or interest receivable whereas as in other branch there will be high demand and high (profitability) interest receivable but no supply.

A view is, therefore, taken to compensate this demand and supply of funds and interest payable/receivable by transferring pricing concept where high deposit branches are taken as fund supplies and certain interest is payable to them and high advances branches' have to pay certain interest to such supplying branches.

Check your progress 9

1. ____________have to develop better strategies and understanding with customers to convince regarding the cost by way of service fees as essential for good quality service.

   a. Banks

   b. Government

1.11 Promotion of Banking Products/ Services

Promotion is a generic term used for the communication efforts of the firm that are directed towards achieving the objectives of a marketing strategy.

The promotion efforts include the marketing communication through-

- Advertising
- Publicity
- Sales Promotion
- Person-to-person' communication
- Banks internal communication process, etc.

These elements of promotion serve as the links between the Bank and the target segment of its market (customers).

In this section we will discuss the communication theories and their application in banking organisations through the promotional mix-aspects. You may note that. Promotion does not mean only advertisements but a Bank's conscious communication efforts towards integrating its marketing strategies with business plans.

Promotion thus means the Bank's well organized, planned and goal oriented communication efforts which must be in congruence with its overall business goals and objectives in the desired market area keeping specific needs of customer in mind.

Table Composition of Promotion Mix

Mass Communication	Person - to - communication
Advertising	Person sale
Publicity	Internal Communication
Sale Promotion Public Relation	

In the service industry like Banking, promotion assumes all the more important position as what we really sell is 'abstract' thing i.e., service with the interest rates, range of product, etc. being more or less same, the service given through proper promotional channel makes all the difference between two Banks in marketing context.

Promotion can thus mean 'communicating with the buyer (customer), in order to strengthen his attitudes that are favourable to the (Bank's) sellers' offering and to change his attitudes which are unfavourable to the sellers. This presupposes ensuring that such buyers become satisfied customers of the Bank, now or later.

The objectives of "Promotion" are:

- Informing/telling/educating potential customer about the banking service and its value to them.
- Informing existing customers about new products/services.
- Following up with existing/potential customers for schemes introduced.
- Approaching a new segment of customers to attract them to buy new scheme.

It can thus be briefly said that the objectives of "PROMOTION" are product/service information, persuasion and re-enforcement so as to create and/or keep up Bank's image among its existing and potential customers. In the traditional wheel of marketing as after the '3 Ps' viz. Product, Place and Price; Promotion is the 4th important "P" in marketing.

Advertising (Budget) Expenditure:

Advertising Expenditure in relation to total market costs (cost of promotion and distribution) has to be decided as the first step. This budget is decided after an extensive market research. The Advertising cost may vary from 112 % to as high as 40% depending on the anticipated business, profit margin and the positioning of product in a given market

Joel Dean in his paper published in 1966 had raised a very significant question-"Does advertising belong in the Capital Budget? 'Dean's thesis is as follows, "Most advertising is, in economic essence, an investment. Mow much to spend on advertisement is, therefore, a problem of investment economics. A new approach is required economic and financial analysis of future. This approach focuses on future after-tax, cash flows and centres around the profit productivity of capital."

Check your progress 10

1. _______________ is a generic term used for the communication efforts of the firm that are directed towards achieving the objectives of a marketing strategy.

   a. Promotion

   b. selection

2. __________thus means the Bank's well organized, planned and goal oriented communication efforts.

   a. Selection

   b. promotion

3. In the ____________industry like Banking, promotion assumes all the more important position as what we really sell is 'abstract' thing.

   a. service

   b. production

4. ___________Expenditure in relation to total market costs has to be decided as the first step.

   a. selling

   b. Advertising

1.12 Guidelines on Advertising by Public Sector Banks

In view of the social commitments of Nationalized Banks and comparatively limited budgets of advertising, the policy related to advertisement expenditure by Public Sector banks has been examined by Reserve Bank of India periodically. This has been done with a view to improve effectiveness on one hand and reduce the cost on the other.

November 1970 - Banks were instructed to show the expenditure on Advertising as a note to P & L A/c.

July 1982 - It was advised that the total advertising expenditure should not exceed 0.1 (1110) % of Bank's Gross Earnings.

April 1984 - There was a sort of ban on incurring expenditure on publicity and advertising up till September 1984. However, the foreign banks were allowed to incur Advertising Expenditure to the extent of 50% of their expenditure under this head during the previous year.

October 1985 - These norms were relaxed.

1987 - Public Sector Banks were permitted to incur expenditure upto 0.05 (1/20)% of their gross earnings from Domestic Operations on Domestic Publicity. For publicity abroad, banks were allowed to incur additional upto 1 (1/10)% of their Gross Earnings on Advertising and Publicity.

The Joint Publicity Committee (JPC) of Public Sector Banks constituted in 1971 with Government approval played active role since February '1976. In 1980 all the 28 Public Sector Banks were brought under its preview and joint action was proposed as follows:

- Ensure considerable savings in expenditure on advertising by joint publicity.
- Ensuring non-controversial advertisements
- Improving overall image of public sector banks
- Taking up the matter regarding distorted advertisements with concerned bank.

JPC recommended use of following media:

- Press
- Hoardings/posters
- Radio/TV sponsored programs.
- Cinema (slides)
- Films
- Direct Mail

JPC emphasized on areas of common interest for advertising and publicity.

i) Deposit mobilization

ii) Customer education

iii) Priority sector advances

iv) Performance highlights of public sector banks

v) Borrower's responsibilities to repay obligations.

Advertisements by Foreign Banks

Unlike the Public Sector Banks, leading Foreign Banks had liberal approach and higher budgets to regularly advertise in leading newspapers, newsletters, catchy brochures and attractive hoardings in prime locations of metropolitan cities. This enabled them to continuously build a positive and brighter image in the eyes of customers - which also reflected in their multi fold business achievements and high profitability vis-à-vis public banks.

Effectiveness of Advertising:

Although advertising is a very effective and most frequently used promotional tool in marketing of banking services, it is desirable to measure the effectiveness (impact) of an advertisement campaign. For this there cannot be any one criterion to assess the effectiveness. These are multiple objectives to asses such an aspect.

Normally below mentioned methods are used to measure results of Advertising:

1) Usage Measurement: This is done through measuring business growth, interviewing consumers.
2) Measuring Recalls: This can be either unaided recall or aided recall – which assesses the extent to which advertisements are retained by customers' mind.
3) Psychological measurements: Through interviews or inventories this can be measured.
4) Attitude Measurement: This is done through structured interviews or attitude scales.
5) Measuring Awareness: This is done through simple YES/NO type questionnaires.

The success of advertising affects successful launching of product/schemes, customer's positive response or increase in business share. This can reflect in the business figures like Deposits, Advances, Profitability, etc. and the comparison of pre and post advertisement figures can reveal the visible effect of advertising campaigns.

It can thus be summed up that effective advertising is the technique of creative communication. It ensures co-ordination and application of various batches of the art and profession to achieve a, pre-determined end i.e. to communicate a message to the public in general or to the desired segment of public/market in particular. Advertising is significant both as a social and economic force. Advertising serves as 'mouthpiece' for the organization's objectives to be made public.

In simpler words, advertisement makes use of communication process with in-built psychological and sociological contents which influence the buyer's behaviour in Advertiser's favour through a process cycle of - stimuli, response, motivation and reward.

Check your progress 11

1. In ____________banks were instructed to show the expenditure on Advertising as a note to P & L A/c.

   a. November 1970

   b. November 1980

2. In _________________it was advised that the total advertising expenditure should not exceed 0.1 % of Bank's Gross Earnings.

   a. November 1970

   b. July 1982

3. The __________of advertising affects successful launching of product/schemes, customer's positive response or increase in business share.

   a. success

   b. failure

1.13 Sales Promotion

Advertising and Sales Promotion as parts of the marketing mix are integrated with the marketing objectives and they are often coordinated with other selling efforts.

As the name suggests, sales promotion is a collective name given to all measures used to promote the sales. Any sale by an intending seller of a product presupposes a corresponding buyer and, therefore, to sell anything the buyer has to be made aware about the product and its advantages to the buyer. The visible benefits of the product have to be demonstrated to facilitate buyer's decision to buy that product.

In a controlled economy and market if the competition is low or less, sales promotion may not be necessary if there is only one seller and many buyers but in a competitive market place, the importance of sales promotion cannot be undermined.

In the banking context due to severe competition between different types of banks, sales promotion assumes lot of importance.

For much sales promotion, three essentials have to be borne in minds:

a) Product knowledge

b) Market information

c) Reaching the desired customer segment

In the context of a company/firm, the sales promotion serves as a 'link' between the advertising and its sales force's impact as the trade and public in the retails stores. There is generally a triumvirate of selling forces-advertising, sales promotion and personal selling. The sales promotion, measures gives the salesman a cutting edge in his selling activities.

The main difference between advertising and sales promotion can be described as - while the advertising moves the consumer to the product; sales promotion moves the product to the consumer.

The following activities are usually the part and parcel of sales promotion activity:

1) Designing and preparing advertising and sales promotion material.
2) Purchasing/arranging different types of material for display/distribution.
3) Organizing direct mail to customers.
4) Organizing exhibitions/trade shows.
5) Arranging demonstrations in sores, factories and homes.
6) Arranging lectures for public, academia, trade and industry.
7) Sales meetings and conventions.
8) Sales training to sales people and dealers/retailers.
9) Sales contests/dealer contests.
10) Sales bulletins.
11) Preparing bulletins/magazines.
12) Giving sales manuals.

13) Preparing sales-films.

14) Organizing seminars/training for customers.

15) Display in trade outlets.

These multi/various activities under sales promotion induce a temptation among buyers to buy the product on the spot.

From the above discussion it can be understood that the sales promotion is an activity which enthuses the sales force and distributors to sell more products and also makes the potential buyers eager to buy, use or consume a product more frequently.

Steps Required In Sales Promotion

Sales promotion pre-supposes a planned and sustained activity involving systematic steps which includes:

1) Product promotion and image building.

2) Selling the idea.

3) Selling the idea of comprehensive promotion involving all forms of publicity.

4) Selling the idea that the salesman is enthusiastic colleague and helps the people in promoting campaigns.

5) Ensuring right product for right buyers at right times.

Some of the foreign banks do the sales promotion jobs through information booklets and brochures sent with credit cards, etc. in an excellent manner.

Sales Promotion Strategy:

In Indian context in general and in marketing of banking services i11 particular during the launching of product, distribution channel sales promotion is an important task.

Before deciding promotion strategy it is important to keep in mind three essentials, as already mentioned earlier.

- **Product Knowledge:** This is the first essential. The employees and specialized staff promoting a scheme/product must have the thorough knowledge of both the advantages and disadvantages of the product. Only after ensuring the market demand and specific needs of customers, the product/scheme has to be launched with full details made available to staff beforehand to promote this product in a better way.

- **Market information:** This means knowing who will buy the product, when he wilt buy and why he will buy? This gives an idea about the probable market share and enables to decide promotion (selling) strategy to specific segment of the market. This also enables the seller to decide on the advertising through proper media keeping in view the specific needs of the potential buyers.

- **Reaching the customer:** After ascertaining the market and ensuring proper product knowledge to all concerned when it's time to reach the customer, the campaign has to take into account:

  a) TIMING-to launches the product;

  b) APPEAL-to target audience; and

  c) GEOGRAPHICAL TIMING-to ensure that when the customers respond, in adequate quantity, product will be available at all probable locations of demand.

- **Personal Selling:** Sales promotion also can be done through personal selling. In banking context, it is the clerk at the counter who is the primary contact point with both existing and potential buyers (customers). Well informed and well-trained staff at the counter eager to explain the schemes to the customers using smile, courtesy and proper communication process can ensure successful sales promotion through personal selling, within the branch, across the counter.

The pro-active approach of the staff and projecting a harmonious image of the bank taking keen interest in customers' interest can do wonders to boost the image and increase business of the bank.

- Seminars
- Exhibitions
- Deposit mobilization-month/fortnight
- Branch anniversary, etc. is some of the other special sales pro1.notion measures taken by banks.

The effectiveness of sales promotion depends upon the following four variables:

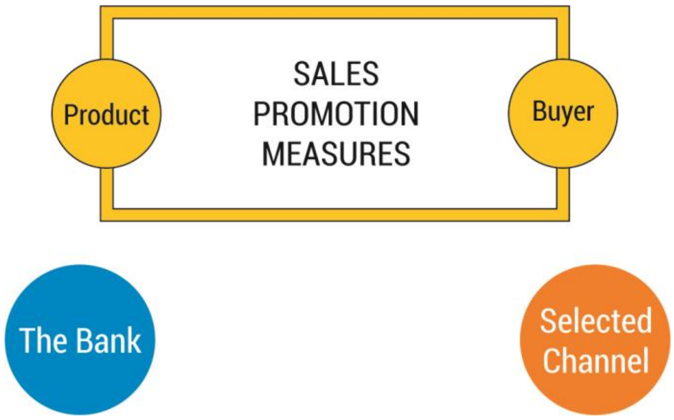

Fig 1.5 Sales promotion measures

The sales promotion is very important instrument which smoothens the process of selling a product to the customer successfully. A well thought strategy of sales promotion, like planned advertising, should be looked at as an investment and not just expenditure. Sales promotion is a bridge between advertising and actual selling in the field. Like the sum 2 + 2 = 5, when proper advertising is added with sales promotion, publicity and personalized service it can bring rich dividends in promotional efforts.

Strengths of Sales Promotion

	Strengths		**Weaknesses**
1	Developing favourable customer attitude	**1**	The impact of a promotion campaign can
2	Flexibility for use at any stage of product life	**2**	It is supplementary to advertisement and
3	Inducing instant purchase behaviour of the buyer	**3**	Un-trained staff can create obstacles in promotional efforts
4	It ensures continued brand loyalty by customer	**4**	Over doing may result in adverse effects.

Having looked into the details of advertising and sales promotion we can make comparison as under:

	Advertising	Sales Promotion	Personal Selling
Strategy	Pull strategy useful for consumer durables	Pull as well as push	Push useful for individual

Activity	Promotion is important in consumer durables	Promotion is important in both consumer and individual goods	More in individual goods
Efficiency	High.	High	Low
Effectiveness	Low	Low	High

In marketing of banking service combination of all three ensures success,

We have just discussed the role of advertising and sales promotion at some length. ‘Publicity' is a generic term used for a wide range of activities ranging from antics of stars in films or media to genuine methods of getting a product, service or even an organisation (or even an individual) 'talked about' and more widely known to the public.

The Oxford English Dictionary gives definition of the word 'Publicity' as: "The quality of being public, the condition or fact being open to public observation or knowledge. The business of making goods or persons publicly known is called as 'Publicity'.

The publicity differs from Advertising not in its aim but in its techniques. Whereas the latter has a more specific job to do i.e. inform and motivate, publicity seeks to interest and draw attention, without essentially motivating or informing the public.

Publicity can be good or bad. With high customer expectations and presence of various consumer councils these days it is just possible that a branch of a bank can get wide bad publicity for some mistakes/flaws or inadequacies in giving service.

The publicity hand-outs or press releases are the commonest form of publicity. Such a press release must

i) Give specific facts

ii) Not give any sales promotion suggestion

iii) Be accompanied by photographs

iv) Be prepared/sent well in advance of the function/event Publicity normally is not paid for by the organisations. It comes through good liaison with press reporters, journalists and column writers. Good public relation strategy (P.R. strategy)

Publicity does the job of reducing ill effects of bad news and also positive effects of good news if properly backed by proper public relation.

Check your progress 12

1. Advertising and Sales Promotion as parts of the marketing mix are Integrated with the marketing objectives and they are often coordinated with other _______________efforts

   a. selling

   b. marketing

2. In a ___________economy and market if the competition is low or less, sales promotion may not be necessary.

   a. uncontrolled

   b. controlled

3. ___________serves as a 'link' between the advertising and its sales force's impact as the trade and public in the retails stores.

   a. sales promotion

   b. advertising

4. The ___________moves the consumer to the product.

   a. sales promotion

   b. advertising

5. ___________moves the product to the consumer.

   a. Sales promotion

   b. advertising

1.14 Internal Communication

Thus far we have seen the various promotional measures that are required in the communication process to achieve the corporate goals and objectives of the banks.

In order to supplement such external communication measures, most of the banks also have internal communication strategies in the form of an Annual

Budget or business and corporate plan which spells out its goals, objectives and targets during the financial year.

For such a budget or business plan, Head offices of the banks assess the business targets of various branches, divisions, zones and regions in the past with reference to the achievement rate (of deposits and advances targets) and the market shares vis-à-vis branches of other banks in that command area. Field Managers, Planning Officers and P.R. or marketing specialists assist in this function to assess the projected levels of business at micro (branch) and macro (corporate) levels.

Internal communication used for this purpose uses 'Top to Bottom' and 'Bottoms up' approach as shown below-

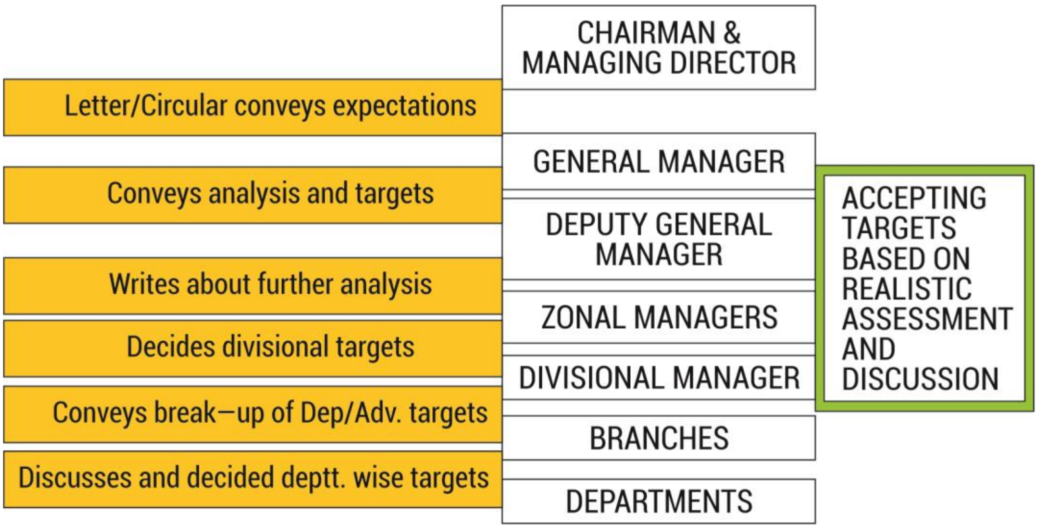

Fig 1.6 Organisational Communication Matrix

In this manner the expectations of the CMD are conveyed with respect to corporate goals using data in the past and changes in economy and business environment appealing to the managers/staff to realistically assess the business potential in the common area of their branches and to arrive at revised business targets as expected by corporate goals based on analysis of market and potential of branches. Motivational Techniques and Recognition measures are used in such an exercise of budget or business plan.

The success of such an exercise largely depends on the realistic assessment of past data and realistic targets set. The utilization of positive strokes and empathy in the top-bottom communications ensures positive feedback/response from bottom to top.

The response and involvement by each level in deciding/accepting and implementing business plan decides the success of such an important internal marketing communication.

Besides business plan exercise, internal communication also involves:

1) House Journals

2) Circular

3) Corporate objective1Business plan booklet

4) D.O. letter for encouragement/appreciation

5) Posters, etc.

Integrated Marketing Communication

The integrated marketing communication is used through corporate strategy as can be represented through the following diagram:

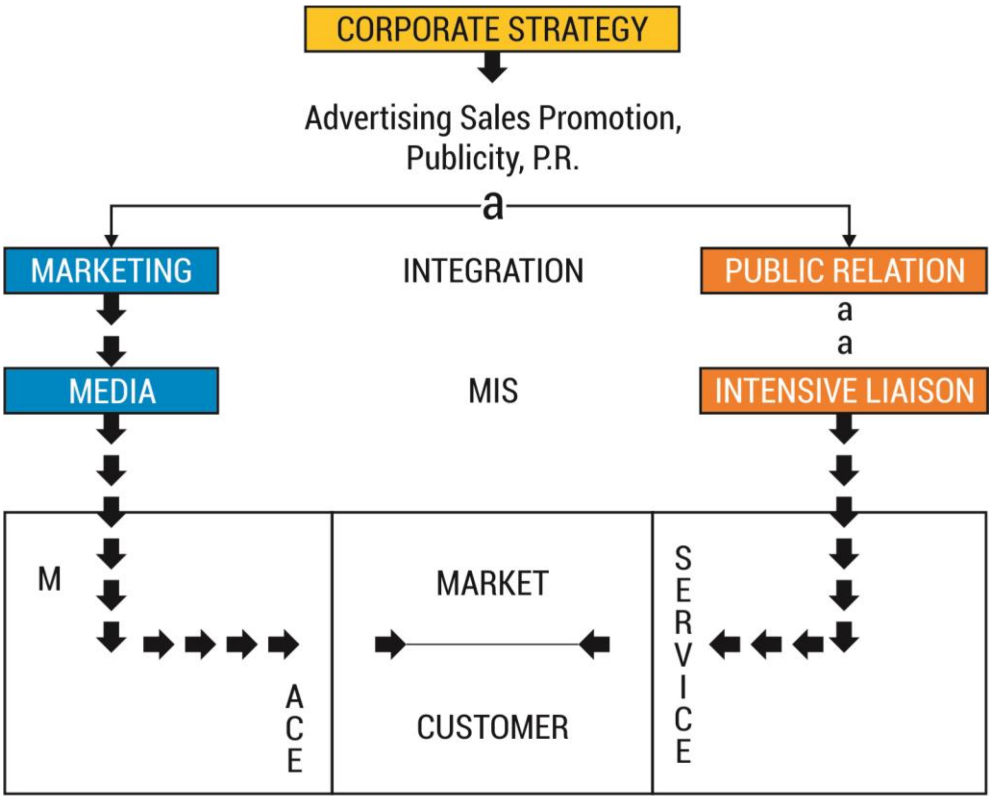

Fig 1.7 Corporate Strategy

In order to know about steps in integrated marketing communication, we will now look into the finer aspects of approaching the market (customer) through media keeping in mind the various promotional plans as the extension of an Integrated Marketing Process.

	Advertising	Sales Promotion	Publicity	Personalised Service
	It should cover	The sales promotion	A publicity	This should cover
1	Objectives	Objectives	Objectives	Business Goal/
2	Targets	Business (Sales)	Targets	Targets
3	Action Plan	Action Plan	Deciding productsl services to be	Proper implementation strategy
4	Theme/Contents	Scheduling/Sequencing	Budget	Privitising
5	Selecting Media	Budget	Evaluation	Budget
6	Budget	Evaluation		Review of *mica given
7	Feedback/ Evaluation of			Evaluation

As a shrewd marketing communication strategy, the promotion plan under aforesaid four major categories must be:

1) Relevant

2) Implementable

3) Specific

4) Thorough

The integrated marketing communication should aim at:

1) Improving market share.

2) Increase sales/Business turnover.

3) Create Awareness.

4) Create Brand loyalty.

5) Create conducive climate for future sales.

6) Establish a positive image.

7) Reach untapped segments.

8) Win over competitors.

9) Highlight special aspects of products.

10) Educate the customers.

Such an integrated marketing communication should be hand-in-hand with the broad corporate objectives and policies so as to ensure that it becomes effective by meeting the necessary purpose.

Proper co-ordination and integration of selling, advertising and sales promotion coupled with due publicity and personalized service results in a better image of the bank and ensures achieving business targets efficiently and effectively.

Check your progress 13

1. The __________of such an exercise largely depends on the realistic assessment of past data and realistic targets set.

   a. success

   b. profit

2. Proper co-ordination and integration of selling, advertising and sales promotion coupled with due publicity and personalized service results in a better image of the _________.

   a. RBI

   b. bank

1.15 Marketing Information System (MIS)

Since having accurate data and information regarding Buyers' (Customers') needs and wants is a very crucial requirement and also the feedback and evaluation after implementing the integrated marketing communication; the MIS i.e. Marketing Information System becomes another vital re-requisite of an integrated communication system.

This system (MIS) simply speaking, is an arrangement for on-going and regular collection of relevant market linked information. This is nut shell can be shown as the computer system i.e.

Fig 1.8 MIS

This generally includes:

a) Internal Report System: In company information

b) Market Intelligence System: Information from outside

This serves TWIN objectives i.e. analysis 'of data for marketing opportunities and locating grievances/problems and offering solutions to them.

MIS can consist of storing data in a compartmentalized fashion i.e.

1) Customers' details
2) Product range
3) Place (location)
4) Pricing details
5) Promotional needs and avenues
6) Competitors' details
7) Changes in external market conditions
8) Required changes in internal policies/operations
9) Newly identified product needs
10) Budgetary allocation and utilization with respect to each aspect of promotional mix, etc.

MIS is essential in the integrated marketing communication because the opportunities existing in the market and the nature of problems cannot be properly known without having such data and its proper analysis.

MIS serves the purpose of marketing support decision system and provides means for selection, adoption and speedy operation with reference to emerging market opportunities.

How to design a MIS?

Designing adequate and proper marketing information system involves three important steps.

1) Defining the required information needs
2) Collecting, collating and storing required information
3) Utilizing the information through retrieval whenever required.

Thus, MIS has to be designed taking into account the business needs.

It should be put to operation and data should be processed by appropriate persons. The systems should be monitored on an on-going basis and periodic review should be taken for improving it whenever necessary.

With reference to the Integrated Marketing Communication it can be said that the highly competitive nature of banking business in the recent years is in a way compelling banks to give their competitive edge in the marketing. In such an effort is not a single arm of promotional strategy or integrated communication which should be effectively used but rather all of them duly blended.

In addition to using all the above types of promotional measures' and MIS, the bank has to be prompt to launch a product or service at proper time to suit to the customers' requirement.

To sum up, the Integrated Marketing Communication involves well-planned strategy of using all types of promotional ways viz. advertising, publicity, sales promotion, personal selling etc. in tune with its business goal to launch the products/service to meet the customers' demands. Proper blend of different strategies and use of a specific media ensures achieving the business goals efficiently and effectively.

Some important pointers to be kept in mind while communicating with the consumer are summarized in the Table below:

Dos	**Don'ts**
Maintain your cool	Be angry
Listen	Shift responsibilities
Be positive	lntempt
Be humble	Neglect a customer
Call customer by name	Criticise
Ensure details	
Follow up till customer is satisfied	

Check your progress 14

1. _________becomes another vital re-requisite of an integrated communication system.

   a. Marketing Information System

   b. internet

2. ________is an arrangement for on-going and regular collection of relevant market linked information.

   a. database

   b. MIS

3. MIS serves the purpose of marketing support _________and provides means for selection.

   a. decision system

   b. information

1.16 Let Us Sum Up

In this unit we have studied that the success of marketing of banking services apart from the service product itself, depends upon distribution, pricing and promotion strategies.

Here in this unit we have studied that in the changing scenario of Indian Banking the concept of pricing is also undergoing fast changes. There has been a shift from fixed rates link to PLR and MLR to flexible rates to induce more healthy competition and better customer service. The fee-based service or service based fee concept is gaining ground and banks have to make this concept more consumer friendly backed by improved quality of customer service. Various objectives, strategies and techniques of deciding proper pricing is the bed rock of marketing of banking services. A proper understanding and application of these will certainly sharpen your skills as professional bankers. Pricing should be used as an effective tool to strike a balance between additional satisfaction to customer and additional revenue for the bank.

After going through this unit the readers would certainly be benefitted in understanding the basics of this unit.

1.17 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b)

Check your progress 2

Answers: (1-a), (2-b)

Check your progress 3

Answers: (1-a), (2-b), (3-a), (4-b), (5-a)

Check your progress 4

Answers: (1-a), (2-b)

Check your progress 5

Answers: (1-a), (2-b)

Check your progress 6

Answers: (1-a), (2-b)

Check your progress 7

Answers: (1-a), (2-b), (3-a), (4-b), (5-a)

Check your progress 8

Answers: (1-a), (2-b)

Check your progress 9

Answers: (1-a)

Check your progress 10

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 11

Answers: (1-a), (2-b), (3-a)

Check your progress 12

Answers: (1-a), (2-b), (3-a), (4-b), (5-a)

Check your progress 13

Answers: (1-a), (2-b)

Check your progress 14

Answers: (1-a), (2-b), (3-a)

1.18 Glossary

1. **MIS -** System that provides information to management.

1.19 Assignment

1. Explain the role of distribution in the marketing mix. Elucidate the influence of the characteristics of services, in restricting the delivery system of banking service essentially to bank branches.
2. Technological advancement has enabled the introduction of various models of delivery for banking services'. Please discuss.
3. Explain the development of different types of bank branches and other models of delivery of banking service.
4. Explain the process of communication in marketing. Give illustration with reference to bank marketing.

1.20 Activities

1. Explain briefly various methods of pricing financial products.
2. Illustrate the concept of breakeven analysis and its relevance in pricing.
3. Pricing is the backbone of profitability in banks, Comment.
4. Define Promotion. What should be the "Ideal Promotion Blend" for marketing banking services?

1.21 Case Study

1. Based on your experience of the bank branches that you are familiar with respect to a specific branch, enumerate the components of distribution functions carried on by the branch.
2. In addition to task mentioned above in our study material does the branch carry out any other activities in relation to the distribution function. Describe.
3. You may have noticed changes in the layout and placement of various services within the bank. Briefly list these changes in respect of your own bank.
4. Talk to at least 10 long standing bank customers and take their feedback on these changes. Report on the feedback received by you. What do you think is the impact of these changes on service delivery?
5. Through a visit or on the basis of your experience, compare the banking services offered at personal service branches, service branches and automated branches. Briefly enumerate the differences in type of services offered.

1.22 Further Readings

1. Marketing Concepts and Strategies, Dr. S.J. Bedekar, Oxford University Press-I991.
2. Marketing Management, S.A. Sherlekar, Himalaya Publication House-1986.
3. The Formula for Successful Marketing, Ralph Mroz, Galotia Publication-1991.

UNIT 2: ATTRACTING AND RETAINING CUSTOMERS IN BANKING SERVICES

Unit Structure

2.0 Learning Objectives

After learning this unit, you will be able to understand:

- To explain the importance of customer's satisfaction and customer service in the context of the banking services.
- Discuss the need for relationship marketing in the banking sector.
- Identify the basic levels of customer's relationships management.
- Describe the process of creating service differentiation through service quality.

2.1 Introduction

In the earlier units of this block you looked at the various elements of the marketing mix for banking services. This unit deals with the strategies for generating consumer satisfaction and retaining bank consumers.

In times past, management could arrive at a fair understanding of its buyer groups through the regular experience of selling to them. But the growth in the size of companies and markets has removed many decision makers from direct contact with consumers. Decision makers increasingly turn to statistical data and to behavioural theory and spend large amounts of time and money to study and understand their consumers.

Mr James E. Turner during the 11th International Retail Banking Conference, at London, November 1992, opined:

For many financial institutions, profits are down;

Growth has slowed or stopped, Competitors are targeting the most profitable segments of your customer base.

He continued: It is just the right time to think about Service Quality.

He argued that operating with a high level of service quality made sense because it saved money instead of costing it. This rationale was based on the fact that it was less costly to do a job right at the first time.

It is also less expensive to keep a current customer than to attract a new one, as various studies have shown. Premium quality always brought premium price from the most profitable but demanding and heavy financial service user customers, who generally did not switch banks at the slightest lure.

That a satisfied customer is not only more likely to stay with the bank, but may also recommend it to others, was good and sufficient reason for Mr. Turner to advocate service quality even in times of recession, even when profit margins were at strain. The more affluent the customer is, the more. Influential he is in referring other customers who are high users of financial services.

Institutions that make service quality a high priority tend to have high employee morale and low employee turnover.

The situation prevailing in Indian financial markets is no different now, particularly in the deregulated and liberalized environment. A lot of interest has been generated by the terms service quality and customer service in different contexts; in a market economy, the very survival of the organisations depend on their ability to attract and retain their profitable clientele and in a regulated economy, the power-groups of the consumers glamour for qualitative performance when the protected firms fail to meet the group's expectations. India is in a transitional stage now, and for certain, the financial institutions will need to address the issue for their own benefit rather than as an imposition from the regulatory authorities or power-groups

2.2 Defining Customer Value and Satisfaction

Today's in their choice of banking services customer face a vast array of product and brand choices, prices and suppliers. While making a choice, customers form an expectation of value and act on it. Then they learn or experience whether the offer lived up to their value expectation. Customers' satisfaction and their repurchases or continuance with the product are directly dependent on this experience.

Customer delivered value as defined by Kotler, is the difference between total customer value and the total customer cost.

Total customer value is the bundle of benefits customers expect from a given product or service. The customer adds values li.0111 sources like - product, services, personnel and image and may perceive an offer to be of more total customer value, if additional value is perceived through some of these sources.

Total customer cost consists of more than the monetary cost. As Adam Smith observed two centuries ago, 'the real price of anything is the roil and trouble of acquiring it'. It includes the buyer's anticipated time, energy and psychic costs. The buyer evaluates these costs along with the monetary cost to form a picture of total customer cost.

A rational buyer's addition would be to buy from whoever offered the highest delivered value.

In bank marketing context, we may say that the following values are the most sought after:

1. **Safety:** Since keeping money at home is very risky and creates a sense of insecurity, every customer treats safety of funds as the primary value and looks up to banks as safe place to keep their hard earned savings.
2. **Convenience:** The customer looks to branch location, timing and procedures from convenience point of view and prefers that bank which keeps this value as prime thing to suit to customers' expectations.
3. **Growth:** With growing needs of people and growing inflationary trends of the market, customer assign priority to growth of their funds as important value and banks have to ensure that this value also is sufficiently taken care of to meet customers' expectations.
4. **Speed:** Customers rate time as high as money and due to automation and rapid progress of technology and IT, speed is becoming yet another value.
5. **Relationship:** In marketing of banking services, service concept itself rests on relationship between banker and customer and it grows with positive approach and pro-active schemes marketed with care and personal touch Awhile selling the products to the customers.

Check your progress 1

1. Customer delivered value as defined by__________, is the difference between total customer value and the total customer cost.

   a. Kotler

   b. Robbins

2. Total ___________consists of more than the monetary cost.

   a. producer cost

   b. customer cost

2.3 Factors Influencing Consumer Behaviour in Banking

In a survey of customers' expectations done by Indian Banks' Association for rural and urban market revealed the following:

Customer Expectation

Criteria	% Preference/Response	
	URBAN	RURAL .
Suitable location	46	65
Quality of service	24	09
Variety of service	11	02
Interest rate	02	02
Canvassing	03	03
Security	03	06
Credit	07	03
Emergency need	0=1	07
	100	100

Each segment of customers has a different perception of a good bank and quality of service.

Research and a study conducted by IBA/NIBM of factors that influence behaviour of customers in banking indicates the following

a) **Location:** Where a bank branch is located often influences the choice of the bank. Subconsciously the consumer is looking for convenience and what matters is whether the location of the branch is close to his home or office, Very often the 'bank next door' often win on that basis alone.

b) **Safety:** Depositors are very often placing their hard earned money in bank and worrying factor for them is “is Bank Safe?” To quell the fear the background of the bank, its promoters, international associations and the years it has been operating in the country, all influences the choice.

c) **Returns:** A consumer having satisfied himself that his money is safe wants to be sure that the returns being earned are attractive.

d) **Customer Service:** The experience of the customer when he has been within the branch will influence a strengthening or a weakening of the relationship. Speed, politeness and friendliness in the service are factors which do matter.

e) **Range of Services:** With greater sophistication in the environment a consumer gets more demanding and would like his bank to offer a variety of services and products which increase convenience for him, Example, phone billing + ATMs or offer him greater choice - a range of term deposit products which offer him high returns and liquidity.

f) **Easy Documentation and well-defined Eligibility Criteria:** When a consumer wants to borrow from a bank, what bothers him is 'Will I qualify for the loan? So a bank will do. well to clearly establish the eligibility criteria and simplify and make loan documentation easy

Check your progress 2

1. _______________are very often placing their hard earned money in bank and worrying factor for them.

   a. Depositors

   b. bankers

2. A _____________having satisfied himself that his money is safe wants to be sure that the returns being earned are attractive.

   a. banker

   b. consumer

2.4 Relationship Marketing and Attracting Customers

The term 'Relationship Marketing' was introduced in the 1980s and is a relatively new and evolving concept. One definition is:

'Relationship marketing is the attraction, maintaining relationship with customers in a multi service organisation aimed at enhancing customer relationships'.

There are three primary objectives for the study of relationship marketing-

1. Companies have changed their perspectives as regards their relationship with customers. Emphasis has changed from a transaction focus to a relationship focus aimed at long-term customer retention.

2. In addition to customer markets, the organisation is concerned with the development and enhancement of enduring relationships with other external markets including suppliers, potential employees, opinion leaders and influences and people providing referrals, as well as internal publics.

3. The integration of marketing activities, customer service and quality standards is essential to achieve a strong and stable relationship marketing orientation.

Customers have become more individualistic, quality conscious and impulsive in their buying behaviour, any service organisation which wants more than one-off sales has to nurture the relationship with existing customers, various intentional studies have proven that retaining existing customer, and building loyal repeat buyers, costs only one-fifth as much as acquiring new ones

So companies need to monitor customer service at every lave1 including internally, because personnel who treat one another well serve customers better. Successful companies listen to everyone in the distribution chain-dealers, distributors, retailers, etc. They know that the relationship does not end with the sale, so they try to stay as close as possible to their customers. That is how they get to the next sale.

With the costs of generating and maintaining databases dramatically decreasing over the last decade, the age of relationship marketing is rapidly reaching both maturity and sophistication. As databases collect and store the right information about your customers and prospects, through the sales force, branch network, letters and telephone calls, the database becomes the focal point for all marketing activities from customer loyalty programmes to internal communications.

To build productive and profitable relationships with target consumers, the marketer needs to tailor general mass marketing messages into several different messages, targeted directly at individuals. The marketer then can reward regular customers and cement their loyalty. Also reactivate lapsed customers, tempt away competitor's customers and cross sell new products and services to the existing customers. You can also reach critical audiences such as your sales force and your shareholders to motivate and inform them about issues that affect them personally

There are simultaneous and major long-term benefits both to the marketer and the consumer. Firstly, accurate targeting produces fewer communications with less wastage and better results. Incorporating a relationship marketing strategy allows for the fine tuning of the marketing communications plan and schedule.

Secondly, a data based marketing strategy can create a stronger company and/or stronger brand image. This is because; the mass communication and direct promotion efforts work together and result in both sales and awareness increases.

As Theodore Levitt says, "The sale merely consummates the courtship. Then the marriage begins. How good the marriage is depends on how well the relationship is managed by the seller".

Customer Markets

Customer must, of course remain the prime focus area for marketing activity. But the focus needs to be less on 'transactional marketing' and example on the one-off sale or hooking a new customer and more on building of long-term client relationships.

As companies are starting to recognize that existing customer are easier to sell to and are more profitable - the lifetime value of the customer - the retention of existing customers become even more critical. As mentioned earlier, it costs five times more to hook a new customer as it does to retain an existing one.

This is not to say that new customers are not important - indeed they are vital to the future of most financial service businesses. A delicate balance needs to be maintained between the efforts directed at existing and new customers

Transaction Marketing and Relationship Marketing

The critical differences between transaction and relationship marketing can be contrasted as below:

Transaction	**Relationship**
Single sale focus	Customer Retention focus
Product feature orientation	Product benefit orientation
Short time frame	Long time scale
Low emphasis on customer service	High customer service
Moderate customer contact	High customer contact
Moderate quality concern	High quality concern

Some service organisations have adopted the relationship focus, but it is noticeably absent in many others. Unfortunately, many companies still take the transactional route which has both limited utility and profitability. The investment made in winning a new customer, once successful, is immediately transferred to the next potential customer. Little effort goes into keeping that customer and the economic benefits of customer retention are often ignored.

Many marketers put their main efforts on the initial activities of identifying prospective customers and attempting to convert them into customers, rather than on both deepening and widening the scope of the relationship. It is ultimately more rewarding to ascertain the needs of customers and cross sell additional products and services which will subsequently result in strong supporters and active advocates for the company and its services. For example an ANZ Grindlays Bank current account holder could well be receptive to applying for a credit card as car loan, loans against assets, etc.

Moving customers up the consumption and loyalty ladder is not easy. Marketers need to explicitly know, in great detail, what each customer is buying and how every customer is different and how the marketer can continue to offer additional product benefits and service advantages that will distinctively differentiate its offerings. Essentially, one of the ways to change a casual customer into a committed customer is to replace customer satisfaction with customer delight that is by providing service quality that exceeds customer expectations.

Referral Markets:

The best marketing is that which is carried out by the company's own customers; that is why the customer loyalty ladder and the creation of advocates is so important. But existing markets are not the only sources of referral. Referral markets to under many names intermediaries, connectors, multipliers, agencies and so on.

An example from a bank will serve as an example here. Referral sources from the bank included insurance companies, real estate brokers, accountancy and law films as well as existing customers and internal referrals. An internal study was conducted for a bank which reflected the amount of businesses that originated from referral sources. It showed how important these sources were, although the bank had done little in the traditional sense to promote itself in this area.

A strategy retreat was subsequently organized which included sessions. On referral sources including presentations from several important intermediaries.

The bank received a lot of criticism during these presentations. Made aware through it research of the importance of this business, the bank established a task force to develop better relations with referral sources and establish a marketing plan to deal with referral markets. The result was noticeable and continued improvements in business generated by referral sources.

Most organisations will need to take similar action. The current and potential importance of referral sources should be established and a plan developed for allocating marketing resources to them. Efforts should be made to monitor results and cost benefits. However, it is worth emphasizing that developing these relationships take time and that the benefits of increased marketing activity this area may to come to fruition immediately.

Supplier Markets

The relationship between an organisation and it suppliers is undergoing fundamental changes mainly under the influence of the Japanese. The old adversarial relationship where a company tried to squeeze its suppliers to its own advantage is going way to a relationship that is based more on partnership and collaboration. One can sense good commercial value in this. Manufacturers in the Asia-Pacific region typically spend over 60% of total revenue on goods and service from outside suppliers.

This new relationship has been termed differently at different places. For example, at AT&T, it is 'vendor ship partnership'; at electronics group Phillips in Europe it is called 'co-makership'. In the US, it is referred as reverse marketing. Whatever the term, however the aim is close co-operation between customer and supplier from a very early stage, mutual concentration on quality, commitment to flexibility, lowest costs and long term relationships.

Recruitment Markets

The key scarce resources for business is no longer capital or raw materials - they are skilled people, a vital perhaps the most vital element in customer service delivery. A situation is not getting easier, even if unemployment climbs to historic levels. The reason is demographic trends. The new skilled workers entering the labour market originate from the following key groups: 16-24 and 25-34. If demand outstrips the supply, which is quite possible then effectively marketing an organization to its potential employees will become vital success factor. A brief case study shows the kind of effort that may have to be made:

Several years ago a large and well known accountancy practice was having problems attracting new recruits. The reasons were hard to discover. Its recruitment was old fashioned and lacked visual impact. A marketing plan to try and improve the situation involved redesigning recruitment literature (with the help of recent graduates), sending the brightest partners on university visits with managers with interesting experiences to recount, and sponsoring awards and prizes at target universities. As a result of this marketing plan, the firm's offers to acceptances ration increased by nearly 200% within two years.

Check your progress 3

1. The term 'Relationship Marketing' was introduced in the__________.

   a. 1980s

   b.1990s

2. _______________have changed their perspectives as regards their relationship with customers.

   a. banking

   b. Companies

3. The integration of marketing activities, customer service and quality standards is essential to achieve a strong and stable ____________orientation.

   a. relationship marketing

   b. customer marketing

2.5 Customer Relationships Management

All markets require equal levels of attention and in that respect the customer market cannot be excluded. This is where the role of customer relationship management comes into play.

The seven activities that constitute customer relationship marketing/after marketing' are the following:

1) Establishing and maintaining a customer information database
2) 'Blue Printing' or planning customer contact points
3) Analyzing informal customer feedback
4) Conducting customer satisfaction surveys

5) Managing communication programmes

6) Hosting special events or programmes for customers

7) Auditing and reclaiming 'Lost Customers

Successful 'After marketing' has direct impact on the customers. It shows the customers that the marketer:

- Appreciates their business
- Is interested in maximizing their satisfaction
- Cares about their problems
- Is interested in their suggestions and inputs
- Wants their repeat business

So we find that acceptance and relevance are the key twin concepts of successful 'after marketing'.

Customer Information database

The customer information database should include data-on the following:

- Current customers
- Prospective customers
- Lapsed on lost customer

'Conversion' ratios and 'loss' ratios should be calculated and targets established.

Customer Satisfaction Measurement

Organisations that develop and implement customer satisfaction programmes derive

Several benefits by delivering value addition

- A deeper understanding of the buyer-seller relationship can be developed, for both party's benefit.
- The organisation/bank focuses on delivering measurably high standards of customer satisfaction not in just being competitive.
- A customer satisfaction audit can also monitor how 'front line' employees affect customer satisfaction.

Managing Customer Communication Programmes

Every organisation has a set of priority communication goals. They are

- To position the bank in a distinctive manner
- To keep customers informed on what is new
- To educate customers about the banks products and services and usage conditions.
- To reaffirm the customer's purchase decision, and lower post purchase dissonance
- To stimulate cross-selling; promote the bank's range of products and services to potentially eligible customers

Banks with a large retail branch network use a variety of communication vehicles to promote their products and services to both existing and potential customers, some of these are

- Individualized letters on new product introductions.
- Special offers for affinity products, e.g. gold, credit cards to high net worth customer’s auto loans for corporate, etc.

Special Events and Programmes for Customer

Banks that have carefully segmented their customer universe can use a host of methods to address key customer groups, as below-

- Bank newsletters
- Corporate videos
- Special interest magazines
- Invitations to cultural and other events
- Affinity product introductions

All these devices seek to create a deeper relationship with customers and also communication a sense of belonging to an exclusive club. For example, a Citi gold credit card holder may receive complimentary copies of a specially conceived-and produced quarterly magazine; invitations to exclusive music and theatre performance; discounts at five star hotels, etc.

Lost Customer' Programme

Banks should also implement on-going studies to track the status of lost customers so that appropriate actions can be taken to stem the attribution rate.

The key issues monitored through these studies are the following:

- Know who your lost customers are, Find out 'why they are left out
- Establish if the problem can be fixed
- Apologize if it's the bank's fault
- If the problem can be fixed, fix it
- If the problem cannot be fixed, monitor the situation to see if:
    - The banks' ability change
    - The customer's preferences or personnel change

Lost customer programmes are becoming more critical in a highly competitive environment because customers that have deserted the organization play often have a residual loyalty and some inclination to be won back. The bank already has customer information files on this sub-group, and knows them, so these customers can be reconverted cost effectively and can be more profitable than new customers

Check your progress 4

1. All ____________require equal levels of attention and in that respect the customer market cannot be excluded.

    a. markets

    b. buyers

2. __________should also implements on-going studies to track the status of lost customers so that appropriate actions can be taken to stem the attribution rate.

    a. Financial institutions

    b. Banks

3. Lost customer programmes are becoming ____________critical in a highly competitive environment.

    a. more

    b. less

2.6 Retaining Consumers through Quality, Service and Values

'Satisfaction is the level of a person's felt state resulting from comparing a product's perceived performance (or outcome) in relation to the person's expectations".

Therefore, the satisfaction level is a function of the difference between perceived performance and expectations. If the performance falls short of expectations, the customer is dis-satisfied. If the performance matches expectation, the customer is satisfied. If the performance exceeds expectations, customer may be highly pleased or delighted.

What factors decide or influence 'expectations'?

Expectations get formed, on the basis of the buyer's past buying experience, statements made by friends and associates and marketer and competitor information and promises. If the marketer raises expectations too high, and the company cannot match its delivery with the expectation level, the buyer is likely to be disappointed. On the other hand, if the company sets expectations too low, it won't attract enough buyers although it will satisfy those who buy.

Most successful companies raise expectations and deliver matching performances. These companies are aiming at 'Total Customer Satisfaction' (TCS). Another observed characteristic of the market place is that those who are just satisfied find it easy to switch suppliers when a better offer comes along. Those who are highly satisfied are much less ready to switch.

Defining Service Quality

One of the difficult aspects of managing service quality is establishing a common understanding of what we all mean when we talk about it. A one sentence description of what constitutes acceptable service quality will be significantly different from one person to the next. The definitions given even by the staff within a bank may vary, depending on the level of the staff in the organisation. Here are just a few ways in which individuals define quality:

- Courtesy
- Problem-solving ability
- Environment
- Speed

- Accuracy
- Range of Service

Differentiation through Quality

Competing on the basis of service quality is very appealing from the marketing perspective, because prime consumer segments seek it and because competitors cannot. Match it as easily as they can match pricing or product change. There are several reasons why service quality is so difficult to match or even so difficult to achieve:

Service quality is culture, not equipment, adding a new ATM system is relatively easy when compared with the task of taking the diverse range of your employee's attitudes and moulding them into a cohesive and consistent service culture. Unlike equipment, their performance can vary significantly between good days and bad days. Furthermore, they cannot simply be reprogrammed to change old habits into the new customer - oriented actions: altering behaviour takes time, In short, people are human;

In the past, we have focused more 'on the operations and security activities of delivering financial services than on the human side of the equation. We may, for example, try to teach tellers to be friendly and thank customers but at the end of the day, the only things we monitor are their technical errors and drawer count. In turn, tellers are rewarded, or not rewarded, based only on how they perform the operational aspects. It is therefore not surprising that customer service is difficult to improve; and there is a difficulty in communicating what we mean by high quality service from the top ranks of the institution, down through middle management to the people who deliver service on the front-line the tellers, receptionist personal bankers and lending staff for example. All bank chief executive, presidents or directors say that high quality service is a main priority in their institutions. At the same time, this is often not translated into the service that customers actually receive when they do business with the bank

The research by A. Parasuraman has focused on developing a procedure for quantifying customer's service quality. The research suggested that service quality can be measured on the following five dimensions:

Reliability: The ability to perform the promised service dependably and accurately.

Tangibles: The appearance of physical facilities, equipment, personnel and communication materials.

Responsiveness: The willingness to help customers and provide prompt service.

Assurance: The knowledge and courtesy of employees and their ability to convey trust and confidence.

Empathy: The caring individualized attention provided to the customer.

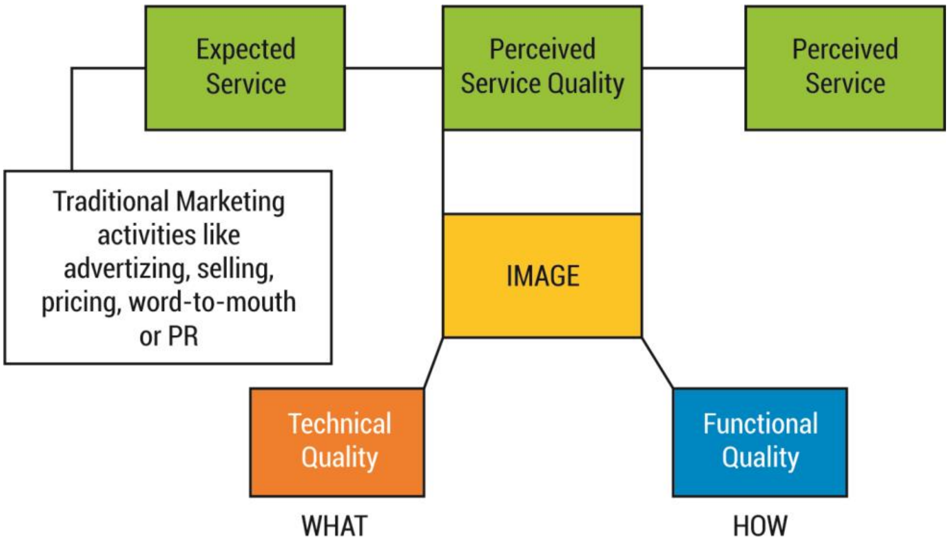

Fig 2.1 Service quality

In order to develop greater understanding of the nature of service quality and how it is achieved in an organization, a service quality model was developed by Parsuraman and et a1 in 1985. Their model clearly indicated that consumer's quality perceptions are influenced by a series of five distinct gaps occurring in organizations. These gaps which can impede delivery of services that consumers perceive to be of high quality are-

Gap1 Difference between consumer expectations and management perceptions of consumer expectations.

Gap2 Difference between management perceptions of consumer expectations and service quality specifications.

Gap3 Difference between service quality specifications and the service actually delivered.

This gap depends on the size and direction of the first gaps associated with the delivery of service quality.

Another work of the same team of researchers identified an exhaustive set of constructs that could affect the magnitude and direction of Gap 4. Most of these construct involved communication and control processes used to manage employees, as well as consequences of these processes.

They summarized by stating that the service quality is a subjective assessment that customers arrive at by comparing the service level they believe an organization ought to deliver to the service level they perceive is. Being delivered. Extensive qualitative research conducted in the recent past by Parsuraman and et al suggests that service-quality deficiencies perceived by' customers, i.e. the gap between their expectations and perceptions, are caused by a series of organizational gaps.

- Marketing information Gap: inadequate or inaccurate management understanding of customer's service expectations.
- Standards Gap: Management's failure to develop performance specifications reflecting customer's expectations.
- Service Performance Gap: Discrepancy between service communication to customers describing the service actually delivered

Developing Better Service

To use quality effectively as a marketing strategy, Bank managements should play a pivotal role in the service design and implementation. Their function is to guide the Programme to fulfill consumer expectations, which also change from time to time. This is done through such activities as evaluating your competitors to see how you compare, and researching consumers to identify your strengths and weaknesses.

In managing the human side of quality service, it is typically most efficient to plan from the top down, and implement from the bottom up. This means the quality imperative is defined by the highest level of management, but implemented in waves, starting at the front line of the bank - their tellers. The reasons to start there is that they create more customer contact than any other of the bank, When Jan Carlozn embarked on the service quality Programme for Scandinavian Airlines in the mid-1980s, he defined these types of contacts as "moments of truth', during which the success or failure of his airline would ultimately be determined, These "moments of truth" will be positive, neutral or negative for the customer depending on how he perceives to have been attended to by the person with whom he had to have, interaction.

A quality programmer can be effectively started at counters where more of the transactions are relatively straightforward and routine, and where basic standards distinguishing high quality form low quality service can be easily identified. Furthermore, the initial training required can be completed in a matter of days or weeks, and measurement can be achieved directly and accurately.

From there, the Programme should be rapidly extended to reception and telephone service, new accounts or personal bankers, extending upward through the organization to commercial lending, trust and private banking,

Counter personnel should be rapidly extended to reception and telephone service, new accounts or personal bankers, extending upward through the organization to commercial lending, trust and private banking.

Counter personnel with little service can pose a special challenge because; their perception of what constitutes a superior level of service can be radically difference from what your customer has in mind. Thus, when senior managers talk among themselves about high quality service, they may all have a common concept in mind, but their ideas of quality will probably be different from those of lower staff levels in the bank. Tellers may not, for example, be totally confident when dealing with the public, so they may speak softly, keep eyes averted from the customer, forgets to smile and almost never thank the customer by name. These are all actions which could lead the customer to feel unwelcome.

Check your progress 5

1. The__________is a function of the difference between perceived performance and expectations.

   a. satisfaction level

   b. satisfaction

2. Most__________companies raise expectations and deliver matching performances.

   a. failed

   b. successful

3. Competing on the basis of___________is very appealing from the marketing perspective.

   a. service quality

   b. quality

4. Service quality is________, not equipment.

   a. output

   b. culture

2.7 Delivering Customer Value and Satisfaction

'Moments of Truth'

The metaphor of the "moment of truth' is a very powerful idea for helping people in services business shift their point of view and think about the customer's experience. Donald Porter as Director of customer service quality assurance for British Airways, points out:

If you are a service person, and you get it wrong at your point in the customers' chain of experience, you are very likely erasing from the customer's mind all the memories of the good treatment he or she may have had up until you. But if you get at right, you have a chance to undo all the wrongs that may have happened before the customer got to you. You are really the moment of truth.

Every time a service organization performs for a particular customer, the customer makes an assessment of the quality of the service, even if unconsciously. The sum total of the repeated assessments by this customer and the collective assessments by the customers establish in their minds the organization's image in terms of service quality

Three features outstanding service organizations have in common-

1. A well-conceived strategy for service: This service concept the attention of the people in the organization toward the real priorities of the customer.
2. Customer-oriented front-line people: The effective front-line person is able to maintain an "otherworldly" focus of attention by tuning o the customer's current situation, frame of mind, and need. This leads to level of responsiveness, attentiveness, and willingness of help that marks the service as superior in the customer's mind and makes him or her want to tell others about it and come back for more.
3. Customer-friendly systems: The delivery system that backs up the service people is, truly designed for the convenience of the customer rather than the convenience d f the organization. The physical facilities, policies, procedures, methods, and communication processes all say to the customer, "This apparatus is here to meet your needs".

The Triangle of Service

Karl Albrecht (1984) suggested that the relationship between the company and its customer be represented by the service triangle model as shown below

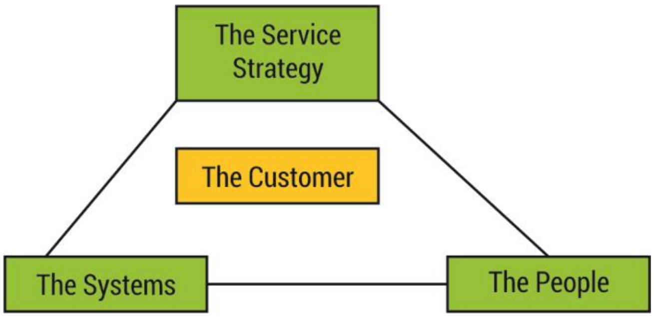

Fig 2.2 The Service Strategy

This triangle model is radically different from the standard organization charts in that it represents a process rather than a structure, and it forces us to include the customer in our conception of the business.

A customer-driven organization has to start with the customer as the basis for defining the business. That the company exists to serve the customer is perhaps never disputed. But the company has to consciously and deliberately, organize and manage for service.

They suggest that first and foremost, a clear conception of the motivational structure of the customer needs to be in place. Some kind of workable model for service can be attempted only thereafter. The aim would be to agree upon a basic business strategy that will service to differentiate company from its competitors, in the mind and in the experience of the customers. In many cases, it is a very challenging task to formulate a nontrivial philosophy of service that can really make a difference. The service strategy must mean something concrete and valuable to the customer, something he or she is willing to pay for.

Armed with an understanding of the customer's buying motivations and concept for service that will position the bank advantageously in the market-place, the marketer must explore the interplay between the strategy, the people of our organization, and the systems that are available to them to get the job done.

It is instructive to take each of the parts of the service triangle arid to explore some of the obvious interactions. Each of the lines in the diagram can represent an important dimension of impact.

1. The Customer-Service Strategy connection.

a) It can be taken to represent the critical important of building the service strategy around the core needs and motives of the customer. This is no place for guesswork. We need to find out, if we don't really know, what goes on in our customer's mind when he or she thinks about out kind of service.

b) Conversely, the line that flows from the service strategy to the customer represents the process of communicating the strategy to our market. It is not nearly enough that we give good service, or that our service is uniquely better in some way; the customer has to know that fact for it to do us any good.

2. The Customer-People in Organisation connection

This line connecting the customer and the people of the organization explains itself. It is the crucial point of contact, the continuation interplay that accounts from more of the moments of truth. It is this interplay that presents the greatest opportunity for gain or loss, and for creative effort.

3. The Customer-Systems connections

Another very interesting line on the service triangle figure connects the customer to the systems that presumably help to deliver the service. These systems can include abstract procedural systems as well as physical hardware. Many negative moments of truth in the business world arise because of system peculiarities and malfunctions. When the customer's interest is treated as an afterthought in the design of service delivery systems, the situation is virtually programmed for mediocrity and dissatisfaction. Forms that don't make sense and are impossible to fill out, illogical or confusing building layouts, and administrative process that burden the customer with tasks that could be handled by service employees all make it more' difficult for the people to provide service effectively

4. Systems-People; Strategy-Systems; Strategy-People connections

a) The three outer lines of the service triangle tell their own individual stories as well. For example, think about the interplay between the people and the systems. How often have you seen highly motivated people prevented from giving the quality of service they really wanted to give because of nonessential administration procedures, illogical tasks assignments, regressive work rules, or poor physical facilities? In situations like these, the service concept is nothing more than normal procedure. Front-line people are usually much better prepared than their manager to find ways to improve the systems they use every day. The big question is do, their managers realize that facts, and are they willing to invite the people to contribute what they know?

b) The line connection the service strategy with the system suggests that the design and development of the physical and administrative systems should follow logically from the definition of the service strategy. This seems obvious, but given the inertial resistance to change found in most large organisations, it sometimes seems like an Uptopian precept.

And finally, what about the line which flows between the service strategy and people? That line suggests that the people who deliver the service need to have the benefit of a clearly defined philosophy from management. Without some sense of focus, clarity and priority, it is difficult for them to keep their attention on service quality. The moments of truth tend to deteriorate and regress to mediocrity

Check your progress 6

1. ________ is a very powerful idea for helping people in services business shift their point of view and think about the customer's experience.

   a. moment of truth'

   b. Truth

2. A________driven organization has to start with the customer as the basis for defining the business.

   a. producer

   b. customer

2.8 Images as a Managed Perception

What are some of the factors that come to your mind when you hear the word image? These might include terms like goodwill, credibility, honesty, ethics, reputation and trust, a sense of permanence, consistency, quality, and integrity. These are some of the images a bank can have. But what is an image?

A practical definition of the term image from the standpoint of business strategy is "a managed perception on the part of the customer of the way the company does business." How do we want our customers to perceive us? What kind of an image do we want to earn by the way we conduct out affairs?

Banks reflect their mission or values to project such image in their literature like brochures and in advertisements like:

- A bank that helps

- A bank that cares
- A bank with the personal touch
- Why go to 10 counters for one work, get 10 works done at 1 counter.
- A bank to bank upon
- A bank for all needs, etc.

Understanding how a bank's image is created is critical to the process of building one. The moments of truth concepts remind us that our image improves or deteriorates, moment to moment and day by day as a result of the sum total of our customer's experience in dealing with us. We manage the customer's perception - our image by managing the moments of truth.

Let's return now the concept of the service triangle (See Figure). When we can find the elements of (1) a meaningful service strategy (2) customer-oriented front-line people and (3) customer-friendly systems working in self-reinforcing interplay, we are doing what is n6cessary to earn a positive image. We are creating such an image indirectly by managing the customer's experience. We are reinforcing his or her perception of our organization by making things come out right at the moments of truth

Check your progress 7

1. An ________managed perception on the part of the customer of the way the company does business.

   a. image

   b. picture

2. Understanding how a__________ image is created is critical to the process of building one.

   a. producer's

   b. bank's

3. The moments of______concepts remind us that our image improves or deteriorates.

   a. truth

   b. false

2.9 Fulfilling Promises: Internal and Interactive Marketing

Employee’s abilities and motivation to meet the expectations of customers as created by external marketing efforts are backed up by internal marketing efforts. By creating and maintaining a service culture through marketing campaigns and activities directed towards the employees the organization may prepare its employees for the moments of truth.

Personnel management policies based on detailed understanding of employees' personal needs of jobs, life and career path, role ambiguity, role conflicts and job conflicts, employee motivation, etc. would have a definite impact on employees' performance in the moments of truth of buyer-seller interactions.

Marketing effort is towards establishing developing and commercializing long term customer relationships, so that the objectives of the parties involved are met. This is done by mutual exchange and keeping of promises. According to one definition the most important issue in marketing is to establish, strengthen and develop customer relations where they can meet business objectives. And the marketing functions envelops the total organization, even outside the marketing department, (called part time marketers) and also covers activities (beyond Ps) which exercise an impact on the current and future customers. Another point in a service organizational is that the effective or ineffective operations management influences the perceptions of the organization and therefore both HRD 'and operations management need to be integrate with marketing.

It is perceived that there is a need to achieve integration between marketing, operations, human resource, R & D, etc. It is in this context Regin McKenna remarked that in service organization "marketing is everything and everything is marketing". The underlying idea is that everyone in the organization who is in customer contact (personnel) should be oriented towards customer relations. It implies that the firm has to manage the business from the customer's point of view. The business processes are to be such as would meet customer needs and technologies of service delivery are to be harnessed to improve customer satisfaction.

Quality in service industries would imply, executing customers' expectations, timeliness, accuracy, responsiveness, performance, etc. A higher quality would obviously generate brand loyalty, word of mouth publicity and willingness to pay higher.

The relationship has to be kept vibrant to remain attuned to customer's changing expectations. Scheduling of service augmentations to meet the specific need of the customer, at the precise moment when these needs get developed, would definitely enhance the customer's delight.

Managing service recovery is also important in building customer satisfaction. Exceeding customer expectations when things go wrong, may leave a stronger positive impressions on customers.

If these suggestions are followed by each functional department and personnel, then an organization can create and keep loyal customer for a profit

Check your progress 8

1. __________'s abilities and motivation to meet the expectations of customers as created by external marketing efforts are backed up by internal marketing efforts.

   a. Employee

   b. Employer

2. ____________is towards establishing developing and commercializing long term customer relationships, so that the objectives of the parties involved are met.

   b. Marketing effort

   a. Selling

3. Managing service recovery is also important in building customer_______.

   a. satisfaction

   b. trust

2.10 Customer Service and Customer Care

Financial services involve the continuous delivery of service and a strong membership relationship. Hence relationship management is extremely important. It in turn depends on the quality of the service offered. If the perceived quality of the financial service exceeds Collsa1ller expectations, there is a basis for building a relationship. IF the reverse prevails the relationship tends to deteriorate. Service quality is of strategic importance in the marketing of financial services, and is considered by some as one of the most important elements in the mix, relationship management is dealt with in greater detail in later module.

If is not generally accepted that financial services consumer's expectations of quality are increasing, and that people are becoming increasingly critical of the service they experience. In addition, financial service organizations are becoming more aware of the importance of 'looking after' their client base, especially in the light of the increasingly competitive environment.

It is not just the competitive environment that is changing consumer attitudes to service, technology also pays a role. Kreitzman sees technology as an opportunity to increase service; however it is also accepted that technological developments such as electronic banking and direct line insurance make banks and insurance companies more impersonal, and less customer contact could make customers less loyal. Marshall (1985) found that leadership in technology was not such an important quality that customers want it in a financial service company. Indeed customers are more concerned with quality of services than with innovative features such as home banking.

Service Quality

The most recent trend in many service industries has been their emphasis on quality as a vehicle for sustaining competitive edge. Berry et a1 (1989) believe that service excellence is key strategic weapon, highlighting that service quality is the marketing strategy for the financial service industry

Service quality must have the full commitment of every echelon in the organization, but essentially it is the commitment of top management that yields the initial quality orientation. 'Effective quality strategies should involve all levels of staff and should be supported, planned and directed by managers at the top to the organisation'.

Many definitions are applied to the concept of service quality, and phrases such as 'meeting customer expectations', or 'providing customers with what they want, when they want and at an acceptable cost' are well-known explanations of the meaning of quality. Essentially, quality is a judgmental issue relating to an individual's perceived expectations of service and actual service performance.

It service organizations care about their employees as well as their customers, the result should be increased motivation and satisfaction, and a higher level of service quality compared with the quality expected by customers, and therefore increased customer satisfaction and loyalty.

Customer Care

Customer care is an extension of customer service, but is wider in context. Customer services implies and immediacy of actions, the focal point being a tactical response to customer requirements. Customer care, on the other hand is more strategic: it is the planned provision of services in anticipation of customer requirements. As already mentioned, customer care is essential if financial organizations are to maintain their customer base.

Heinz Pekarek, Creditanstalt Bankverrein, says thus:

A major criterion, in making a product or rendering a service, is creating more value while using resources economically. For the banks, quality is a means of differentiating an otherwise homogeneous range of service in order to obtain a "unique selling position" in the competitive environment.

A service or product is of high quality if it meets the demands and expectations of the customer’s i. e. if the service or product can be matched with customer's actual needs and expectations e.g. housing loan, car loan or consumer durable loans by banks which help a customer to meet his growing social needs and improve his status.

The satisfaction of customer needs depend on how far the bank optimizes its internal procedures. Decisive factors or internal quality are technology and organizational aspects. The following requirements must be met:

- Speed (Same day processing of transfers)
- Security (ensuring that transactions are handled correctly)
- Accuracy and Punctuality.

Check your progress 9

1. Customer care is an extension of customer service, but is ________in context.

   a. wider

   b. narrower

2. A service or product is of high quality if it meets the demands and expectations of the _____________.

   a. producer

   b. customer

2.11 Bank Marketing: Future Challenges

Under the fast pace of liberalisation, Indian economy is gradually opening up. The globalisation of financial services is creating a 'pressure' effect on the financial firms and companies making them more effective and productive.

Coupled with socio-economic changes, the I.T. related changes is bound to change the complexion of Indian financial market and banking and marketing of banking services is no exception to that. They are now required to design new customer friendly products to cover the emerging needs of changing preferences and the risk factor. As it is the slack in demand for credit has in itself made all banks to come out in the arena of marketing their services 'with easier terms and attractive packages. More and more banks are labelling their products more effectively as only getting deposits is not going to generate any field. The prudential norms are creating positive pressure on banks to be more transparent, effective in recovery and to strengthen their capital base. From just social angle, banks are now compelled to focus on optimum profits not only for growth but even for healthy survival amidst the competition all around.

If we review the changes in financial markets on the backdrop of 'future challenges', it is realised that the financial services, in general, have undergone a sea-change.

In the first phase of development, the emphasis was on setting up and functioning of investment institutions, insurance business, leasing and merchant banking firms.

In the second phase, the focus shifted on hire purchase, factoring, venture capital funds and reforms in stock market and capital market.

In the third phase, the emphasis was on computerization, paperless trading and depository’s innovative use of new financial instruments and integration of financial services with the rest of the world.

Since there is strong emphasis on development of infrastructure sector as a priority area of Govt. policy it would need massive outlay and how the financial institutions cater to its need will be a great challenge. The foreign exchange market amidst the currency fluctuations and the trend of rupee weakening will be another challenge to be faced. The increasing expenditure vis-à-vis thinning margin and its compelling effect on controlling human resources – in terms of not many fresh recommitment and schemes like VRS are the challenges to HRD and their socio-economic effect has to be closely monitored.

Effect on Banking and Latest Trends in Banking Marketing

Let us now review the latest glimpse of the latest trends in bank marketing which will give a glimpse of the changing fabric of banking services and its effect on marketing of banking services.

Latest Trends in Banking Marketing

The banking business is becoming more and more complex with the changes emanating from the liberalisation and globalisation, with UTI, NSC, Company Debentures and NBFCT competing in deposits and new private banks and foreign banks competing in advances, with aggressive marketing strategies, bankers are becoming growingly aware about the need for marketing.

With the restricted (though now free to decide) rates of interest on deposits and advances the main emphasis is being given on:

i) Efficient and courteous customer service

ii) Attractive and innovative schemes

iii) Developing subsidiary services

iv) Aggressive personalized selling strategy

Marketing has not remained just a strategy but many banks - like Citibank, Hong Kong Bank in Foreign Bank Sector and State Bank of India, Canara Bank among the nationalised bank sector adopted a pro-consumer philosophy.

The 'customer is a king' - thought is getting more and more deep-rooted. If we take a look at the tables which give reasons as to why a customer leaves a bank (a) in India and (b) in. USA, it will be clear as to why banks are giving top priority to quality of people (through continued training) and quality of service (through continuous improvement) as the bedrock of a good promotional strategy:

Why a Customer leaves a Bank?

In India	%	In USA	
Death	01	Poor Service	20
Move away	03	Moved away	45
Forms other relationship	05	Loan related problems	05
For competitive reasons	09	Services charges	10
Dissatisfied with products	14	Changed jobs	10
Indifferent attitude	68	Changed travel pattern	10

Since nationalization, the Indian Banking scenario has been successively changing each decade and the banking system today through more transparency, is showing signs of maturity,

The changing environment directly affects bank's marketing strategy with respect to the following categories

1) Political/legal dimensions

2) Technological dimensions

3) Socio-cultural dimensions

4) Economic dimensions

5) Competitive dimensions

With computerization on a large scale, the traditional concept of communications are undergoing sea change. The letters are now replaced by E-Mails. In place of cashiers and even tellers, ATMs are responding quickly and for 24 hours. 'Plastic Money' is gaining more acceptance and popularity. Home Banking, tele-banking, room service are the new catchy concepts which attract the customer to appeal to his valuable time factor and convenience.

The following Table will indicate the effect of changes in economy on saving pattern which too is a very important dimension leading bankers to reorient their marketing strategy

Table Progress Card of the Banking sector

Bank Group wise financial Performance of scheduled commercial bank : Some

Important Financial Indicators: 1997-98,1998-99 and 1999- 2000

	Opening Profit	Net add	Income Income	MIRE income	Other Expended	Expenditure Expenses	Interest Bill	Operating & Contingatiet	Wage (Na)	Provisions	Spread
Stn664 daimon,' Bann	18,423.36	7,30636	1,15,386,00	99,936.85	15,879,15	1,01,01964	69,317.04	27,645.60	18,467.38	11,117.00	30,189.82
1999-2300	[1.66]	[0.66]	[10.391	18.96]	[1.43]	[9.73	[6.24]	[2.491	[1.661	[1.001	[2.721
Fut& Sector Banks (27)	13,064.03	5,113.87	90,900.44	79,459.71	11,440.73	85.786.57	5537328	22,461.13	16,361.57	7,950.16	24,034.43
1999-2030	L2.471	[031	[10.20]	(8.92I	0 .28]	[9.63]	[6.22]	[2.521	[124]	[0.891	12.701
1tploualler.4.1 Banks (19)	7,22428	2,43720	56,883/16	30,273.04	6.61182	54,448.86	35,478.22	14,182.76	10,435 IS	4,787,81	14,794.22
1959-2000	[130]	[0441	(16.26]	p26)	[I.193	(9.823	[6A0]	12.561	[1.88]	[0.861	[2.67]
Mince Bud. Group (3)	5,839.15	2,676.87	34,014.51	29,186.67	4;827.91	31,337.71	19,297.06	8;27837	3,024.39	3,167.23	9,229.62

1999-2000	[1.74]	[0401	[10.11]	[8.61311	[1.44]	[9.321	[5.92]	12.461	[1,761	[0.941	[2.76]
Indhn Neale Sector Banks (24)	1,428.86	655.09	13349.88	7,441511.	1,307.97	8;094.79	5,628.95	1,692.07	1,080.24	773.77	1,812.96
1999-2000	(1.841	(0i4)	[11.26)	I9381	(1.68]	110.421	(7.24]	p.18]	ie.391	on0'	[2.33J
blip Rime Sector Banks (8)	1.242.24	569.41	3,407.47	4,4292/	978.26	40628.06	3,326.61	837.02	163,18	674.43	1,102.60
1999-2000	[2.11]	[0.971	[931	[7431	[1.66]	[322]	[3.45]	[1.41]	[0.28]	[1.151	[1.27]
Boragn Bath (42)	2,686.63	967.99	1032821	8,176.02	2,152.19	9,360.22	4,916.20	2,645.12	862.37	1,718.64	3,189.85
1999-2000	[3.24)	(1.171	[12.47]	(921	[2.69	[1130]	[6.02]	[3.21]	[1.041	12071	pi59

Bank Group. Wise Financial Performance of Scheduled Commercial Bank:

Some Important Financial Indicators: 1997-98, 1998-99 and 1999-2000

The latest statistics in Economic Times indicate that the saving rate has been 26% of, GDP. Household being 76% of overall saving and 10.6% of that is into financial assets. Percentage of household contribution sector as GDP (1996-97) is 19.1%. The private corporate sector is 4.1% and public sector is 1.9% of GDP.

The money supply (M-3) has been affecting growth of banks' deposits which is, in fact, the raw material for banking services. These is almost perfect co-relation between money supply and deposit growth. Due to changing rates of interest on deposits, there is also shift in the patters of short term, medium tern1 and 1o11g term deposits with Banks. Due to large supply of bank credit to government and the corporate sector preferring to raise money through the share market, it has also been affecting the growth of advances. This exerts pressure on profitability which compels bank to go for low cost deposits and higher rates on advances. This leads to more emphasis on selling to corporate clients.

The growth of market and vide spread of debenture and share culture provides the corporate sector a direct access to saver causing dis-intermediation. This too forces the banks to provide new types of services in the investment area. The money market instruments also have shown innovative additions like (CP) Commercial Paper (CD) Certificate of Deposit, Stock invest, Mutual Money Market Fund, etc.

In the corporate sector, despite easy access of credit which enabled the small and medium industries to widen their entrepreneurial base, the adoption of, Tandon and Chore Committee norms for credit decision and credit monitoring (which had the objective of orienting the corporate borrower to gain more and more for self-reliance in equity), has been a compelling factor for corporate sector to turn to capital market to raise additional funds equity.

Now with more liberalisation of bank credit to corporate sector against the present slack state of affairs in the capital market, banks can 'aggressively utilise their marketing strategies to market their products/schemes to corporate sector borrowers whereby the resources can be gainfully employed. This can ensure comfortable profit margin for the banks and more importantly higher economic growth through better industrial output.

Changing banking scenario in India is causing changes in the marketing strategies of commercial banks.

The need for being more competitive and also transparent, to be socially committed without sacrificing profits has compelled the banks to be more conscious about quality customer service and to be sensitive to their changing needs and expectations. The changing patterns of household and corporate sector have affected the saving-borrowing patterns,' this makes banks to think of more assertive promotional strategies to attract new customers and maintain the existing ones as satisfaction

Due to the freedom to decide interest rates on deposits and advances vis-à-vis the shifts in demand and supply of deposits of loan able funds, banks are turning more towards relationship (bank) marketing and selling to corporate clients. Instead of concentrating on high cost deposits and more number of customers with low deposit, banks prefer the corporate clients. Banks are also devising new and innovative schemes to attract corporate borrowers. Such an exercise has to be carried out to ensure that the cost of finds is kept low and return are better so that profitability is maintained and banks can strengthen their capital base as required by the Narasimham Committee.

With relationship and transaction banking banks are also becoming more quality oriented and offer quick and courteous customer service. To facilitate this swiftly and selling to corporate clients better banks also have to have a pro-active work culture and a flexible structure. The concept of venture teams can be useful for the banks for selling suitably to the corporate customers as it has the combination of line and functional type of organisation. The banks organizational structure for selling to corporate customers must be flexible with motivated personnel who are properly empowered so that they can mobilize the customers for long term banking relations. A corporate marketing department can also be set up to cater to the corporate clients. All this requires proper promotional strategies.

The bank marketing has, therefore, become a very complex and yet interesting subject as it requires the knowledge of economics, sociology, psychology, banking and also marketing concepts. The buyer behaviour and socio-economic situation being constantly changing, an on-going monitoring and reorienting the promotional strategy is the essence of effective marketing of banking services.

Check your progress 10

1. The globalisation of financial services is creating an _______ effect on the financial firms and companies making them more effective and productive.

    a. 'pressure'

    b. demand

2. The _________market amidst the currency fluctuations and the trend of rupee weakening will be another challenge to be faced.

    a. money

    b. foreign exchange

2.12 Let Us Sum Up

In this block we have studied about the competition has been eating into the profit margins of banking industry.

In this unit we have studied that Improvement of service quality is what will keep a customer and the cost in doing a thing right at the first time is cheaper than the process of recovery. IT is proved be far more expensive to win a new customer than to retain an existing one and hence it is big business sense to keep the service standard at high enough levels as per the perceptions of the client so that he does not get tempted to look the other way. Therefore the clear need of a banker is to understand the meaning of customer satisfaction and the way in which this can be achieved through the management of three crucial parameters viz. quality, service and value. Satisfaction level is a function of the difference between' perceived performance and expectations. If the performance falls short of expectations, the customer is dissatisfied. If the performance exceeds expectations; he may be highly pleased or delighted. Expectations get formed on the basis of buyer's past experience, marketer and competitor information, etc.

Successful companies raise expectations and deliver matching performance, always aiming for Total Customer Satisfaction (TCS).Customer's experiences of moments of truth are based on certain expectations created by the service provider. The traditional marketing efforts give promises. Employee's motivation and abilities to meet customer expectations are backed up by internal marketing. So by creating and maintaining a service culture through marketing campaigns and activities directed towards the employees, the organization may prepare its employees for the moments of truth.

So after going through this unit the readers would be feeling confident in the topic discussed.

2.13 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b)

Check your progress 2

Answers: (1-a), (2-b)

Check your progress 3

Answers: (1-a), (2-b), (3-a)

Check your progress 4

Answers: (1-a), (2-b), (3-a)

Check your progress 5

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 6

Answers: (1-a), (2-b)

Check your progress 7

Answers: (1-a), (2-b), (3-a)

Check your progress 8

Answers: (1-a), (2-b), (3-a)

Check your progress 9

Answers: (1-a), (2-b)

Check your progress 10

Answers: (1-a), (2-b)

2.14 Glossary

1. **Globalization -** It is the process of international integration arising from the interchange of world views, products, ideas and other aspects of culture.

2.15 Assignment

1. Explain the terms relationship marketing in the context of banking services. How is relationship marketing different from loyally programmes?
2. What are the 'essential factors affecting customer choice for bank customers? How do banks try to meet some of these expectations?

2.16 Activities

With respect to banking services, explain the concepts of service quality, customer value and customer satisfaction. Briefly identify the sources of the five gaps with respect to the discussion on gap analysis in the unit.

2.17 Case Study

The criteria listed above have been researched with respect to individual customers. Talk to at least 3 organisation, elicit from than the criteria they would consider most important to their definition of a "good bank". List these criteria and comment upon how different, if at all, are these from the criteria considered important by individual consumers.

2.18 Further Readings

1. Management Techniques, R. Mittal, G.K. Publications- 1996.

2. Essentials of Management, J.L. Massie, Prentice Key, 1994.

UNIT 3: ADVISORY AND CONSULTANCY SERVICES

Unit Structure

3.0 Learning Objectives

After learning the unit, you will be able to understand:

- Describe the various advisory and consultancy services provided by merchant bankers.
- Explain the various legal and regulatory provision in respect of providing qualitative and professional services.
- Know the marketing approach for merchant banking services.

3.1 Introduction

In addition to the services discussed in the earlier units, merchant bankers today provide an impressive range of advisory and consultancy services, which have assumed critical importance in present day competitive business environment, by providing facilitation to business organisations. This unit describes the various services and allows you to have a general overview of the range of services

3.2 Portfolio Management

Portfolio Management refers to management of investment portfolio by an expert or professionally qualified person for the maximum benefit of the investor.

All the transactions are done by the portfolio manager in the name of the investor under the Power of attorney.

SEBI (Portfolio Managers) Rules 1993 defines- Portfolio means the total holdings of securities belonging to any person.

Portfolio Manager means any person who pursuant to a contract, agreement or arrangement with a client advises or directs or undertakes on behalf of the client the management or administration of portfolio of securities or the funs of the client as the case may be.

Discretionary Portfolio Manager means a manager who exercises or may under a contract relating to portfolio management exercise any degree of discretional as to the investments or management of the portfolio of securities or the funds of the clients as the case may be.

While selecting the Portfolio Manager an Investor should take in to account the authorization of the Portfolio Manager with SEBI, his qualifications and experience, the 50 research base and time period for which he is to be appointed as Portfolio Manager.

The Objective of the Portfolio management should be specific, because each objective has a different element of risk involved. A Maximum return objective has maximum risk, Optimum return hears optimum risk, capital appreciation, safety objectives may bear comparatively less risks. From the return angle the securities may be classified as under:

Fixed Income Securities

1. Debentures, PCD, NCD’s or Debentures with tradable warrants
2. Preference shares, Government securities, bonds, fixed deposits
3. Bank deposits, Mutual funds, Tax savings schemes, etc.

Variable Income securities

1. Equity shares,
2. Money market securities such as bills, commercial papers, etc.

Functions of Portfolio Manager

1. Advise on new investments, review existing investments,
2. Research: Markel research about the new issues, their comparative profitability to the investor and the analysis of the performance of the companies which are listed the new trends in the stock and securities market, the dealings in derivative instruments, Government Directives, Study of the Industry for the industry profile for investment.
3. Study of the Market for understanding the bearish or bullish trends, and the demand and supply of securities,
4. Decide the objective for the investor,
5. Decide the size and split up of portfolio of the investor as per size of investment,
6. Decide strategies to have optimum return, by diversification of the portfolio.

Check your progress 1

1. ________refers to management of investment portfolio by an expert or professionally qualified person for the maximum benefit of the investor.

   a. Portfolio Management

   b. investment

2. _________Manager means a manager who exercises or may under a contract relating to portfolio management exercise any degree of discretional as to the investments.

   a. portfolio

   b. Discretionary Portfolio

3.3 Credit Rating

It may he defined as the science of estimating the creditworthiness of a person or a business, or the value of security, on various parameters about business, such as turnover, repayment capacity, profitability, asset quality, risks, etc. The credit rating represents, the opinion of the rating agency on the relative ability and willingness of the issuer of financial instruments to meet service obligation as and when the same arises.

In India the credit rating agencies rate bonds, debentures, preference shares, structured obligations, commercial papers, certificate of deposits, equity stocks, LPG suppliers, real I estate developers. Credit rating of individuals, or entities,' is also done by the banks to decide the rate of interest to be charged on borrowings.

In India, it is mandatory to get the debt instruments rated such as:

a) Issue of commercial paper (must have a rating not below A-2 of ICRA grade)

b) Company fixed deposits

Credit Rating provides information to the investor to measure the risk investing into a particular security. It also provides comparative information about various securities, and their associated risks. Represented by words such as AAA+, AA+, A+, BBB+, BB+, B+, CCC+, CC+, C+ in order of increasing risk of the securities, credit rating allows the investor to apprehend the risk involved. The return on the investment and take a decision. These ratings represent opinion of the company, which is formed after a very careful study of the company and the market conditions. It provides a good tool to the investor. It is security credit rating specific and time specific

Quality of Rating: The quality of rating depends upon the expertise with the rating agency, 'and the factors taken into account for rating.

The Credit Rating Analysis: While studying the credit rating of a particular security being issued by a company, the Rating agency considers all the business details about the company, and the promoters, and board of directors, as depicted through their balance sheet, and general market position. The Market condition, competitors, Government Policies, the position of the Market Leader, and such other conditions are also taken into consideration while making credit analysis. The analysis of the instrument to be issued, the time period of its redemption, the method of redemption or conversion into a share, and similar relevant factors are also taken into consideration while doing this exercise.

The analysis is focused on these fundamental risks: Industry Risk, Financial Risk, Rate of Interest Risk, Management Analysis, and Fundamental Analysis.

Credit Rating Agencies: The Credit rating agencies floated by three premiers financial institutions ICICI, IFCI, and IDBI presently working in India me:

1. CRISIL Credit Rating Information services of India Ltd
   1988
2. CRA Investment Information and Credit Rating Agency
   1990
3. CARE Credit Analysis and Research Ltd
   1993
4. Duff and Phelps India Pvt Ltd 1997

CRISIL Debenture rating Symbols

a) High Investment Grade: Highest Safety MA, High Safety AA,
b) Investment Grade: Adequate Safety A, Moderate safety BBB,
c) Speculative Grade: Inadequate Safety BB, High Risk B, Substantial risk C, In default D

+ Or - symbol may be attached to AA to D to reflect comparative standing within the Category.

CRISIL Rating for Fixed Deposits

The symbols, FAM, FAA, FA, FB, FC, FD stand for: Higher safety, High safety, Adequate safety, Inadequate safety, High risk and In-default, ratings respectively

CRISIL Rating for Short Term Instruments

The Symbols PI, P2, P3, P4, P5 represent decreasing degree of safety of timely payments of the short term instruments.

Similarly other rating agencies also make ratings by using standard symbols for easy understanding.

Which Schemes/ Instrument are rated?

Debentures, Bonds, Fixed Deposits schemes, Equity shares, Commercial papers, Municipal Bonds, Debt Funds, Mutual Fund schemes, Plantation schemes, Infrastructure related debt, Cellular and basic telecom services, ADR/ GDR issues, are the instruments schemes rated for benefit of investors.

Check your progress 2

1. _____________may he defined as the science of estimating the creditworthiness of a person.

   a. Credit Rating

   b. Risk taking

2. ________provides information to the investor to measure the risk investing into a particular security.

   a. Risk bearing

   b. Credit Rating

3.4 Takeovers and Mergers

Merchant Bankers are best suited to negotiate on behalf of the companies in cases of amalgamation and mergers. A merchant banker can be an effective catalyst in deciding the price, time and quality of mergers, and for complying with all the legal provisions. Maintenance of secrecy, which is highly essential in such cases, can be done by the merchant bankers, who are professional bankers. Merchant banker is well equipped 'to do the Pre take over investigations, analysis of the values of the tangible and intangible assets, arranging the financial syndication, etc.

The shareholding pattern, the capital structure, the borrowing pattern and the term liability structure, position of the company in the market, are decided by the size of its assets and liabilities. A company needs to orient itself in the direction of either of the methods of takeovers, or merger, for the mutual benefit of the Stock holders, owners and the society. Merchant banker can help the companies in taking decision in respect of the under mentioned types of mergers.

Amalgamation: Joining of two or more companies to form a new business. The existing entities no more exist, a new entity emerges.

Merger: means takeover of companies by a bigger company. The companies which are taken over lose their identity while the one which takes them becomes a larger company.

Consolidation: Means fusion of two or more co-existing companies into a new company to form a new company.

Reconstruction: A company transfers its undertakings and assets to a new company in consideration of the issue of the new company's shares to the first company's members and if the first company's debentures are not paid off in further consideration of the new company issuing shares or debentures to the first company's debenture holders in satisfaction of their claims.

Acquisitions in India are prevented under various statutory provisions as under:

Section: 108 of the Companies Act 1956, on transfer formalities,

Section 391 and 394 on mergers and rearrangement

Section 370 and 372 on limits on borrowing and investments,

Rules 40A and 40B of the listing agreement,

Monopolies and Restrictive Trade Practices Act 1969.

However the Amalgamations may be permitted under the following circumstances:

Directions or order from the concerned High Court, Approval of High Court under section 391-394 of Indian Companies Act,

Approval by creditors and financial institutions and banks who have approved the scheme, RBI approval for shares to NRI’s.

Check your progress 3

1. ___________Bankers are best suited to negotiate on behalf of the companies in cases of amalgamation and mergers.

   a. Merchant

   b. foreign

2. Merger means takeover of companies by a __________company.

   a. foreign

   b. bigger

3. _________means joining of two or more companies to form a new business.

   a. Amalgamation

   b. merger

4. ____________means fusion of two or more co-existing companies into a new company to form a new company.

   a. amalgamation

   b. merger

3.5 Trustee Services

A Debenture trustee is defined in SEBI Debenture trustee Rules 1993 as: "a trustee of a trust deed for securing any issue of debentures of any 'body corporate".

This definition does not at all give the full responsibility of the Debenture trustee. A debenture trustee is a link between the Company which raises a loan from the Public in the form of Debentures, and also acts as a trustee for the investors. It is given various regulatory powers by SEBI, and can exercise a good control over the actions of the Company, in the interest of the investors in debentures raised by various companies.

Who can act as a Debenture Trustee in India?

As per SEBI regulations (article 7); A scheduled commercial bank, a public financial institution, an insurance company or a body corporate only can do the business of Debenture trustee, in India.

The Obligations and Responsibilities of Debenture Trustee

The Debenture trustee must hold a certificate from SEBI (which is valid for a period of 3 years), pay the necessary fees for registration, and must abide by the directives of SEBI,

The duties of the Debenture trustee specified in articles 13,14,15 or SEE1 regulations are as under:

a) The debenture trustee must enter into a written agreement with the company which intends to issue the debentures, the agreement should be specific about the amount to be floated, the period within which amount to be raised,

b) If the debentures certificates are to be issued only after registration of charge, the Debenture trustee must ensure the necessary charge has been so registered before dispatch of the certificates,

c) Ensure that the interest warrants on these debentures have been dispatched on or before the due dates,

d) The redemption of the debentures is made to the debenture holders on maturity,

e) Exercise due diligence to protect the interests of the investors, and not allow deterioration in the value of the assets against which the debentures are raised,

f) Ensure that the company, complies with all the guidelines issued by various Govt authorities,

g) Inform the SEE1 about any act of breach of trust by the Company, e.g. Appoint a nominee director on the Board of the Company, in case of 2 consecutive defaults in either of these

   i) Payment of interest to the debenture holders,

   ii) Default in creation of security for the debentures, or

   iii) Default in redemption of debentures

h) Make periodical verification of accounts, records, and registers of the company, take possession of trust property, and enforce security in the interest of the debenture holders

Debenture trustee can Call or cause to be called by the company, the meeting of all the debenture holders, if requested by debenture holders of least 10 % in value.

Check your progress 4

1. A ______trustee is a link between the Companies which raises a loan from the Public in the form of Debentures.

   a. debenture

   b. share

2. _________can Call or cause to be called by the company, the meeting of all the debenture holders.

   a. share trustee

   b. Debenture trustee

3.6 Depository Services

Depository is an agency to whom securities are deposited by the investors, for: a) timely collection of all the benefit such as dividend, rights issues, bonus, redemption, etc. b) settlement of sale purchase transaction through computerized accounting system instead of physical movements) safekeeping of the securities, d) and handling/dealing on behalf of the owner or the depositor, e) collecting funds from the companies, and settlement of sale purchase transactions of securities

The Working of the Depository

Investor (owner) of security transfers the same in the name of the Depository. The depository sends this security to the issuing Company for transferring it in the name of ' itself, It issues a Receipt to the Investor (beneficial owner) for holding the security. This enables the Depository to perform its functions smoothly. The investor can then advise the depository to sell some portion of his security at a specified rate, or to a specified person. The depositories will then sell it, realize the proceeds, transfer the interest in the name of the new purchaser and continue to hold the securities, of course on behalf of the new beneficial owner and all this without the actual movement of papers.

The Depository gets fees for each of the transactions, the investor gets 10 protect his interests, and is free Prom caring about the legal issues and other formalities.

The SEBI has issued Rules, regulations and code of conduct for the depositories.

Check your progress 5

1. ________ of security transfers the same in the name of the Depository.

   a. Investor

   b. creditor

3.7 The Marketing Approach for Merchant Banking Services

Despite the recession, which is affecting various industries in different countries with varying intensity, the merchant banking and allied activities continue to grow in terms of turnover and profits and thus have a paramount impact on other spheres of the economy.

The main characteristics of merchant banking services-

1. **Intangibility:** They meet a general rather than a specific need. Particular benefits from one rather than another institution are not readily apparent and therefore are dependent on effectively getting their message across 'to the public and ensuring that their image and services are attractive.
2. **Inseparability:** The main concern of the market is usually the creation of time and place utility; this implies that direct sale is almost the only feasible channel of distribution.
3. **Highly individualized marketing system:** Since a close personal and professional client relationship must exist, direct channels are the only feasible choice.
4. **Lack of special identity:** Each organisation must find a way of establishing its identity and implanting this in the mind of the public. As the competing products are similar, the emphasis is on the "package" rather than the product, the package consists of branch location, staff, services, reputation and advertising and from time to rime new services. As major competitors offer similar services the emphasis will be on the promotional aspects rather than on the inherent uniqueness of a particular institution's service.
5. **Heterogeneity or a wide range of products/services:** A wide range of products and services are offered to meet a variety of financial and related needs from different customers in different areas. On the one hand they provide a special one-off management service for corporate customers and on the other, retail services for individuals. The implication is very seldom can a service be standardized.
6. **Geographical Dispersion:** Branch network is necessary so that all services or promotions must have both appeal and wide application.
7. **Growth must be balanced with risk:** There has to be a well-controlled balance between expansion and prudence.

8. **Fiduciary responsibility:** The organisation must guard the interests of its customers.

9. **Labour intensiveness:** Personalized service versus automation is an important issue. Because of relatively high personnel costs as well as to enhance customers' convenience use of technology is increasing

The main objectives of merchant banking services-

1. **Flexible goals:** Increasing or decreasing certain type of products, services and customers.

2. **Fixed objective:** Increasing profitability, high return on investment, achieving certain market share/growth rate, achieving a spread of customer types in order to minimize risks and business fluctuations.

The marketing function of merchant banking services is one of five subsets of management controllable variables. The management system comprises of four major sets of variables:

1. Organisational objectives
2. External environnements (non-contrôlable variables)
3. Controllable (or management) variable sets
4. Organisational and control variables

The four facets of variables are interrelated and operate together as a system.

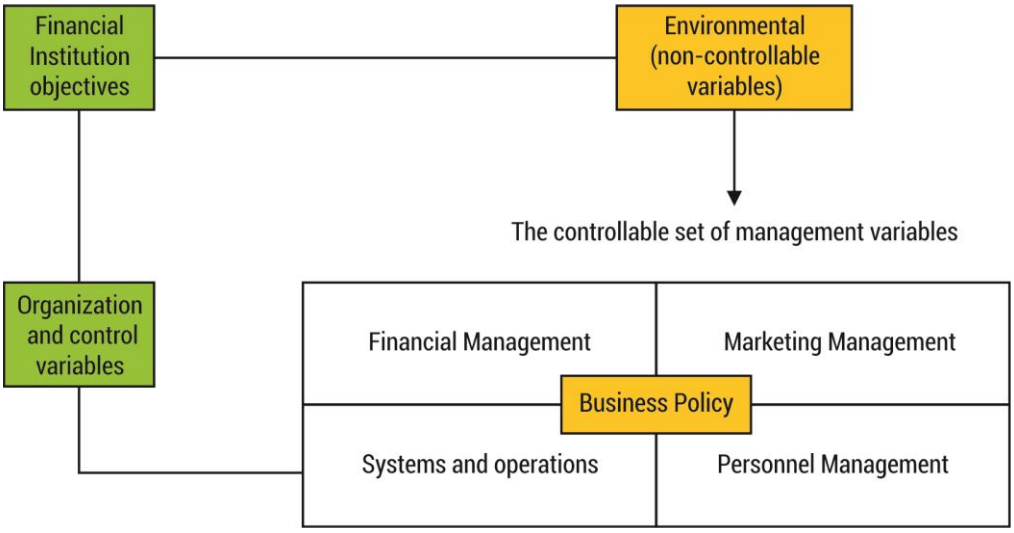

Fig 3.1 The controllable set of management variables

Marketing function focuses its attention on the following activities:

- Customer behaviour, attitudes and segmentation

- Marketing research that attempts to collect, investigate, analyse and interpret customers' attitudes and market developments in order to contribute to the maximum attainment of objectives in the light of existing non-controllable factors, and in consonance with the other four major functions mentioned earlier
- Products/service development
- Branch management; location and distribution of services
- Advertising, communication, promotions and publicity
- Pricing of services

Defining marketing strategies, administering and controlling the marketing program

Figure below illustrates the dual marketing task for financial institution.

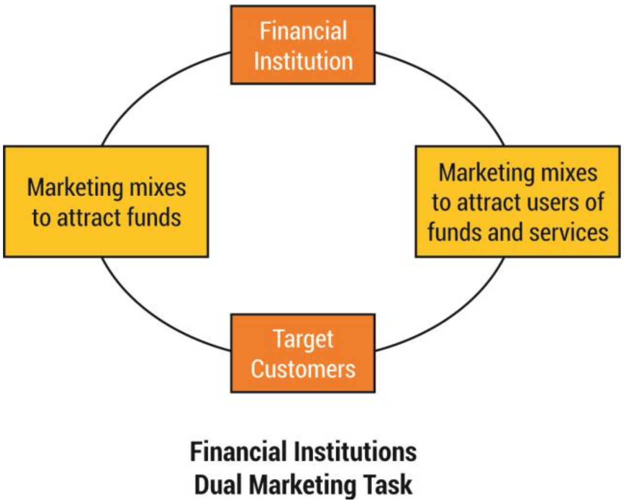

Fig 3.2 Dual Marketing Tasks

The marketing approach refers basically to four steps:

1. Determine customers' requirements;
2. Design new services or update old ones according to the findings;
3. Market services (at a profit) to the customers for whom they were researched and designed (this includes pricing, promotion and distribution);
4. In doing so, satisfy the customers' needs.

The marketing approach for financial services can be diagrammatically illustrated

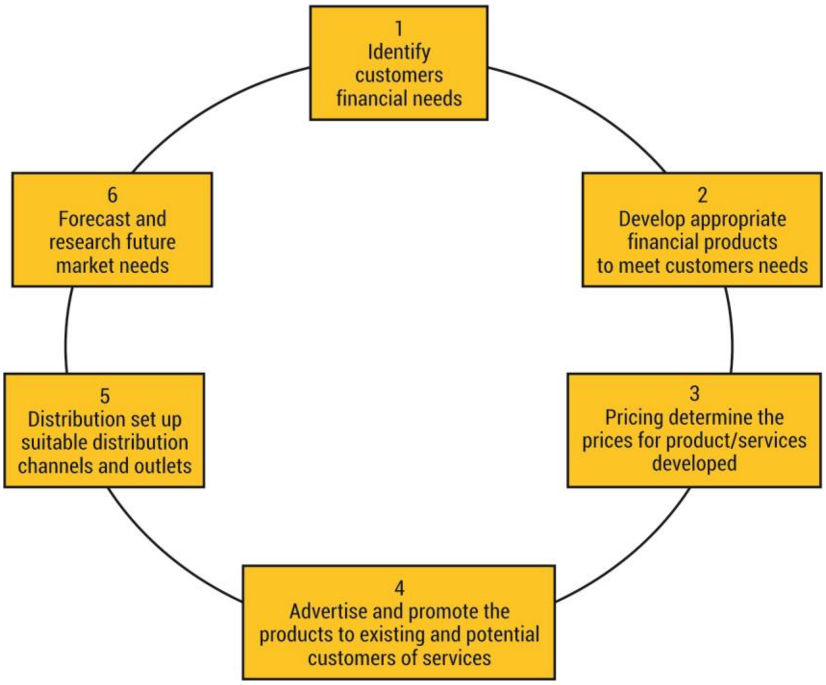

Fig 3.3 Marketing approach to financial services

In the coming years the developing trend will be more in line with an increase in computerization and information technology, In the twenty-first century the trend onwards further liberalisation and deregulation will lead to tremendous growth in the volume of business, This is likely to lead to a restructuring of the services industry. The strategies will have to change in order to enable institutions to benefit from the expected growth, or example by strengthening the marketing function (including development of problem solving skills at branch level), improving information systems, increasing strategic alliances and simplifying the decision making mechanism.

Check your progress 6

1. _____________ function focuses its attention on customer behaviour, attitudes and segmentation.

   a. Marketing

   b. selling

2. In the twenty-first century the trend onwards further _______and deregulation will lead to tremendous growth in the volume of business

   a. liberalisation

   b. globalisation

3.8 Let Us Sum Up

In this unit we have studied about the consultancy and advisory service sector in very detail.

Here in this unit we have studied about a large number of services can be rendered by the Merchant Banker. The services are required to be marketed because of many reasons such as increasing need of investor clients, largeness of amount of turnover in Investment transactions, monitoring the activities of the corporate clients, providing liquidity to the various instruments for the profit to the client, increasing own fee based income. The merchant banker however has to observe the legal framework and work within the business ethics. Increasing number of Non-resident investor, foreign investors, foreign institutional investors, and globalisation of the trade transactions, necessitates proper institutional focus to the advisory and consultancy services provided by the merchant Banker.

Portfolio Manager: Manages the investment portfolio of his customer client. This means, that he will sell, retain or purchase securities which may yield long term or short term or both types of yield for the full satisfaction of the customer, The portfolio Manager takes the decision about the time of sale/purchase, price of sale/purchase, and company in which investment is to be made. He is guided by the SEBI guidelines on the his role and responsibilities. While raising funds, from the general public, it is essential that the investor knows the risks involved in his investment decision. Credit Rating of various instruments educates the investor on the risk and return aspects of his decision. This service is therefore beneficial to the investor. It also a good source fee based income to the Merchant banker. Corporate clients need to expand their business. This can be done through various methods of raising capital or funds, or through takeover, merger, amalgamation with existing bodies engaged in the same or parallel activity. Since this involves a substantial amount of legal and technical skill, which the merchant banker possesses, these services are provided by him.

After going through this unit you must have got the sufficient idea about contents of this unit and would be confident enough in this topic

3.9 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b)

Check your progress 2

Answers: (1-a), (2-b)

Check your progress 3

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 4

Answers: (1-a), (2-b)

Check your progress 5

Answers: (1-a)

Check your progress 6

Answers: (1-a), (2-b)

3.10 Glossary

1. **Debenture -** Instrument used to raise long term debt from creditors.

3.11 Assignment

1. How can the depository services be marketed by you? Give your answer with reference to The Place, Price, Promotion and Product angles of marketing.
2. Write down the advantages of-
   a) Depository Services to the Investor,
   b) The Company issuing the securities,
   c) The Merchant Banker who handles the Depository Services
   d) The Stock Exchange, and
   e) To the Money Market/ Capital Market.

3.12 Activities

Write down the strategies adopted by your bank/institution for promoting merchant banking service?

3.13 Case Study

How do you distinguish between the Services offered by the Portfolio Manager and Depository Service?

3.14 Further Readings

1. Sandra Vandermerwe and Micheal Chadwick, "The Internationalization of Service", The Service Industry Journal, January 1989.
2. Micheal E. Porter, "Changing Patterns of International Competition", Ccdgornin Management Review. Vol. 26, Winter 1986.
3. George S. Yip, "Total Global Strategy: Managing for Worldwide Competitive Advantage", Englewood Cliffs, N.J. Prentice Wall 1992.
4. Pei-Yuan Chia, "Citibanking the World", Bank Management, July-August 1995.

Block Summary

This block focused on Distribution, Pricing, Retaining Customers and Consultancy Services.

This block was divided into three units, where unit one discusses on distribution, Pricing and Promotions Strategy for Banking Services. Here in this unit we made a detailed discussion on banking services, we discussed on various types of branches, pricing of banking services. On the other hand unit second discusses on the topic Attracting & Retaining Customers in Banking Services i.e. how would a bank attract and retain its customers. Here a detailed discussion was made on Factors Influencing Consumer Behaviour in Banking, and on Customer Relationships Management. Unit three discusses Advisory and Consultancy Services. Here a detailed discussion was made on portfolio Management, Credit Rating, Takeovers and Mergers, Trustee Services, Depository Services.

After going through this block the readers will certainly feel confident in the topics of the block and would have understood the basic concepts and objectives of this block.

Block Assignment

Short Answer Questions

1. Sales promotion
2. Promotion
3. Advertising
4. Marketing communication
5. MIS
6. Customer Value and Satisfaction
7. Relationship Marketing
8. Customer Relationships Management
9. Customer Care
10. Bank Marketing
11. Portfolio Management
12. Credit rating
13. Takeovers and Mergers
14. Trustee Services
15. Depository Services

Long Answer Questions

1. What is sales promotion? Explain its role in marketing.
2. Write a note on publicity measures taken in banks.
3. What is integrated marketing communication?
4. What is advertising? Illustrate its role in marketing of banking services. Quote advertisements by a few banks and what appealed you most in it as a banker and as a customer?
5. What do you understand by the term "Moments of 'Truth”?", How can a bank manage to convert most of its moments of' truth into winning transactions. Explain with reference to your own bank.

Enrolment No:

1. How many hours did you need for studying the units?

Unit No	1	2	3	4
Nos of Hrs				

2. Please give your reactions to the following items based on your reading of the block:

Items	Excellent	Very Good	Good	Poor	Give specific example if any
Presentation Quality	☐	☐	☐	☐	______
Language and Style	☐	☐	☐	☐	______
Illustration used (Diagram, tables etc)	☐	☐	☐	☐	______
Conceptual Clarity	☐	☐	☐	☐	______
Check your progress Quest	☐	☐	☐	☐	______
Feed back to CYP Question	☐	☐	☐	☐	______

3. Any Other Comments

…………………………………………………………………………………………

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"Education is something which ought to be brought within the reach of every one."

- Dr. B. R. Ambedkar

Dr. Babasaheb Ambedkar Open University
'Jyotirmay Parisar', Opp. Shri Balaji Temple, Sarkhej-Gandhinagar Highway, Chharodi,
Ahmedabad-382 481.

FINANCIAL MARKETS

PGDF-103

BLOCK 4:

MARKETING OF PENSION FUNDS AND GLOBALIZATION

Dr. Babasaheb Ambedkar Open University
Ahmedabad

FINANCIAL MARKETS

Knowledge Management and
Research Organization
Pune

Acknowledgment
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The content is developed by taking reference of online and print publications that are mentioned in Bibliography. The content developed represents the breadth of research excellence in this multidisciplinary academic field. Some of the information, illustrations and examples are taken "as is" and as available in the references mentioned in Bibliography for academic purpose and better understanding by learner.'

ROLE OF SELF INSTRUCTIONAL MATERIAL IN DISTANCE LEARNING

The need to plan effective instruction is imperative for a successful distance teaching repertoire. This is due to the fact that the instructional designer, the tutor, the author (s) and the student are often separated by distance and may never meet in person. This is an increasingly common scenario in distance education instruction. As much as possible, teaching by distance should stimulate the student's intellectual involvement and contain all the necessary learning instructional activities that are capable of guiding the student through the course objectives. Therefore, the course / self-instructional material are completely equipped with everything that the syllabus prescribes.

To ensure effective instruction, a number of instructional design ideas are used and these help students to acquire knowledge, intellectual skills, motor skills and necessary attitudinal changes. In this respect, students' assessment and course evaluation are incorporated in the text.

The nature of instructional activities used in distance education self-instructional materials depends on the domain of learning that they reinforce in the text, that is, the cognitive, psychomotor and affective. These are further interpreted in the acquisition of knowledge, intellectual skills and motor skills. Students may be encouraged to gain, apply and communicate (orally or in writing) the knowledge acquired. Intellectual-skills objectives may be met by designing instructions that make use of students' prior knowledge and experiences in the discourse as the foundation on which newly acquired knowledge is built.

The provision of exercises in the form of assignments, projects and tutorial feedback is necessary. Instructional activities that teach motor skills need to be graphically demonstrated and the correct practices provided during tutorials. Instructional activities for inculcating change in attitude and behavior should create interest and demonstrate need and benefits gained by adopting the required change. Information on the adoption and procedures for practice of new attitudes may then be introduced.

Teaching and learning at a distance eliminates interactive communication cues, such as pauses, intonation and gestures, associated with the face-to-face method of teaching. This is particularly so with the exclusive use of print media. Instructional activities built into the instructional repertoire provide this missing interaction between the student and the teacher. Therefore, the use of instructional activities to affect better distance teaching is not optional, but mandatory.

Our team of successful writers and authors has tried to reduce this.

Divide and to bring this Self Instructional Material as the best teaching and communication tool. Instructional activities are varied in order to assess the different facets of the domains of learning.

Distance education teaching repertoire involves extensive use of self-instructional materials, be they print or otherwise. These materials are designed to achieve certain pre-determined learning outcomes, namely goals and objectives that are contained in an instructional plan. Since the teaching process is affected over a distance, there is need to ensure that students actively participate in their learning by performing specific tasks that help them to understand the relevant concepts. Therefore, a set of exercises is built into the teaching repertoire in order to link what students and tutors do in the framework of the course outline. These could be in the form of students' assignments, a research project or a science practical exercise. Examples of instructional activities in distance education are too numerous to list. Instructional activities, when used in this context, help to motivate students, guide and measure students' performance (continuous assessment)

PREFACE

We have put in lots of hard work to make this book as user-friendly as possible, but we have not sacrificed quality. Experts were involved in preparing the materials. However, concepts are explained in easy language for you. We have included many tables and examples for easy understanding.

We sincerely hope this book will help you in every way you expect.

All the best for your studies from our team!

FINANCIAL MARKETS

Contents

BLOCK 2: FINANCIAL SERVICE, CONSUMER BEHAVIOUR AND BANKING PRODUCTS

UNIT 1 FINANCIAL SERVICES: AN INTRODUCTION

Introduction, Meaning and Concept, Characteristics of Financial Services, Evolution of Financial Services in India, Significance of Financial Services, Types of Financial Services, Impact of Technology, Challenges before the Financial Services Sector

UNIT 2 MARKETING OF FINANCIAL SERVICES: A CONCEPTUAL FRAMEWORK

Introduction, Marketing and the Financial Services, Marketing as a Functional Area of Management, Financial Services and the Different Marketing Orientations, Difference between Services and Products Physical Goods, Characteristics of Service, Marketing Mix for Financial Services, Marketing Strategy and Financial Services

UNIT 3 CONSUMER BEHAVIOUR FOR FINANCIAL SERVICES

Introduction, The Complexity of Consumer Buying Decisions, Individual Influences on Consumer Behaviour, Needs and Motives, Individual Perception, Learning and Habit Development, Family Influences on Buying Behaviour, Behavioural Models for Analyzing Buyers, Consumer Behaviour Some Learning Points for Financial Service

UNIT 4 BANKING PRODUCTS AND SERVICES

Introduction, Nature of Product, Products and Services in Banking, Elements of Product Mix, Product Life Cycle and Product Strategies, Using Product Life Cycle lo Manage Marketing of Banking Products, New Product Development, Branding in Bank Marketing, Process and Product Development Cycle for Banking Services, Product Development

BLOCK 3: DISTRIBUTION, PRICING, RETAINING CUSTOMERS AND CONSULTANCY SERVICES

UNIT 1 DISTRIBUTION, PRICING AND PROMOTIONS STRATEGY FOR BANKING SERVICES

Introduction, Banking Services and Issues in Delivery, Channels of Distribution for Banks, Types of Branches, Electronic Methods of Distributing Financial Services, Pricing of Banking Products/Services, Pricing Objectives, Pricing Methods, Pricing Reviews and Committees, Price Setting in Practice, Promotion of Banking Products/Services, Guidelines on Advertising by Public Sector Banks, Sales Promotion, Internal Communication, Marketing Information Systems (MIS)

UNIT 2 ATTRACTING AND RETAINING CUSTOMERS IN BANKING SERVICES

Introduction, Defining Customer Value and Satisfaction, Factors Influencing Consumer Behaviour in Banking, Relationship Marketing and Attracting Customers, Customer Relationships Management, Retaining Customers Through Quality, Service and Values , Delivering Customer Value and Satisfaction, Image as a Managed Perception, Fulfilling Promises : Internal and Interactive Marketing, Customer Service and Customer Care, Bank Marketing : Future Challenges

UNIT 3 ADVISORY AND CONSULTANCY SERVICES

Introduction, Portfolio Management, Credit Rating, Takeovers and Mergers, Trustee Services, Depository Services, The Marketing Approach for Merchant Banking Services

BLOCK 4: MARKETING OF PENSION FUNDS AND GLOBALIZATION

UNIT 1 MARKETING OF PENSION FUNDS

Introduction, Emerging Dimensions Relating to Investment Services, Pension Funds: A General Overview, Why Pension Plan?, Types of Pension Plan, Pension Fund Risk, Funds Management, Pension Fund Investment: General Guidelines, Pension Funds and Capital Markets, Pension Funds: Some Related Statistics

UNIT 2 GLOBALISATION AND ITS IMPACT ON FINANCIAL SERVICES MARKETS

Introduction, Globalisation of Financial Markets and its Impact on Local Markets, Globalisation of Markets: The Main Drivers, Globalisation of Markets: The Road Ahead, Some Asian Trends, Globalisation and Consumer Orientation, The Emerging Imperatives for Financial Services

Dr. Babasaheb
Ambedkar
Open University

PGDF-103

FINANCIAL MARKETS

BLOCK 4: MARKETING OF PENSION FUNDS AND GLOBALIZATION

BLOCK 4: MARKETING OF PENSION FUNDS AND GLOBALIZATION

Block Introduction

As we have already discussed the importance of studying the subject financial market. In the world of globalisation when there are no boundaries left in the countries it becomes even more important to study this subject because now the financial market has not been restricted to the national level but moved at international level.

In this block we shall be discussing in very detail about the pension funds and globalisation. As we all are aware of pension, here we will be discussing in very detail the need or requirement of pension, what are the various types of pension plans available, how globalisation has affected the pension schemes and what is the future of this system. This whole block has been divided into units; the first one focuses on marketing of pension funds, whereas the second one focuses on globalisation and its impact on financial market

After going through this block the readers would get a sufficient idea about the pension, its role and need in the society, what are the various kinds of plans available? In short the utility and future of pension would be known through this block.

Block Objective

After learning this block, you will be able to understand:

- Requirement of Pension plans.
- The type of Pension plans.
- The risk associated with Pension funds.
- Globalisation of financial markets on local providers.
- The future trends for financial services in respect of globalisation.
- Changing consumer orientation in the forthcoming scenario.

Block Structure

UNIT 1: MARKETING OF PENSION FUNDS

Unit Structure

1.0 Learning Objectives

After learning this unit, you will be able to understand:

- Describe the need and requirement of Pension plans.
- Distinguish between the types of Pension plans.
- Identify the type of risk associated with Pension funds.
- Explain the fund management process for Pension funds.
- Comment upon the Financial Market Implication of Pension funds.

1.1 Introduction

Since the volume of International business and capital flows are increasing, the commercial banks are likely to be exposed to different types of risk and there is a need to hedge these exposures. The emerging derivatives in foreign countries are increasingly used by banks to bring variations in the sensitivity of their funds and also the underlying portfolio; it is the right time that forex dealers, specially the commercial banks, in India, familiarize with the complexity of these instruments and acquires skills to manage these emerging challenges.

Establishment of foreign banks and non-banking companies have played a very key role in introducing the technology cult in the financial sector in India. In the light of the diversified product range the banks and financial institutions are offering to public various types of financial services in a global perspective. Hence, in the aspiration towards becoming major player in the modern financial service sector, commercial banks and various investment institutions will have to evolve appropriate strategies for technology integration for providing faster and efficient financial services.

The pension funds are playing a very important role in U.S.A. and other European countries in ensuring challenging of savings into fruitful diversified investment portfolio.

Different types of financial services are being provided by these pension funds. The aim of finallcia1 sector reforms in India has been to encourage the foreign institutional investors to invest in India and, it is hoped that in the changing global business scenario, ignore and more pension funds will, enter in India to provide wide variety of financial services. Presently some of the investment schemes in the same of pension funds investment have been started by IDBI, ICICI and by some other financial institutions.

1.2 Emerging Dimensions Relating To Investment Services

Over the years, with the changing scenario in Indian economy, new challenges are emerging, which the banks have to face with suitable strategies. The major challenges in the nineties relating to investments and other financial services are likely to be in the following areas.

a) Growing importance of the corporate sector and its diversifying needs,

b) Development of capital markets, the disintermediation phenomenon and their impact on commercial banks,

c) Development of factoring and commercial paper,

d) Need for export promotion and disintermediation in international business, and

e) Universal banking.

Check your progress 1

1. One of the major challenge in the nineties relating to investments and other financial services will be of ________banking
   a. Universal
   b. National

1.3 Pension Funds: A General Overview

A Pension is an agreement to provide regular income during a person's post-retirement life. During the past decade, people have wanted to be provided after their retirement due to rising life expectancy and the earlier retirement. The profound social changes have also an impact on the growing population to seek some sort of regular income after retirement instead of depending upon their children in their old age.

In the U.S. the first pension plan was established by the end of 19th Century by Railroad. (The earliest one set up in 1875 by American Express Company was later on closely associated with Rail road). At that time the pension plan was quite informal and that too at the discretion of [he employer and used as a disciplinary devise. During depression in 1930's, the many pension plans failed to make payment to the beneficiary. These wide spread collapse of pension plans led to more regulations and it was also a major factor for the establishment of government sponsored pension plan and social security.

The World War II brought a major expansion or pension plans. This was necessitated due to scarce labour, government imposed wage control and social security benefit. In 1949, the U.S. Supreme Court upheld decision of National

Labour Relation Board that pensions were a legitimate part of collective bargaining. Since then, the pension funds have grown rapidly.

Changing Demographic Structure

- Although the proportion of people who are old is highest in OECD countries and transitional socialist countries, most of the growth is in the world's old population - from half a billion people in 1990 to almost 1.5 billion people in 2050.
- About one old person in four is "very old" (over age 75) and of these almost two thirds are women. The economic position of the very old is very different from that of the younger old, and the position of old women is very different from that old men.
- The proportion of the population that is old rises with per capita income. In low income countries, less than 7 per cent of the population is over 60. This proportion rises to 12 to 16 per cent in middle-income countries and to 17 per cent or more in most high income countries. The ratio of old people to working age people (old age dependency ratio) also rises with per capita income a relationship that sterns directly from the lower fertility rate in richer countries and the ability to lengthen life span through medical intervention.
- Most old people live in poor countries (which is also the most populous), a pattern that will intensify towards 2030. By then, more than three-quarters of the worlds' old people will be in areas not now industrial more than half in Asia and more than a quarter in China alone.

Indian old age population would increase from 6.5 per cent in 1990 to the extent of 7.58 per cent in 2000, 13 per cent in 1030, 28 per cent in 2100 and 30 per cent in 2150.

Table in 15.9 gives details on percentage of old people over the years as projected by tile World Bank, while Table summarizes the percentage of population in India by age groups.

Need for Reforms in Social Security

- Political pressures lead to tax financed benefit formulas that are not sustainable.
- High payroll taxes that are not closely tied to benefits discourage employment.

- Early retirement provisions reduce the supply of experienced workers.
- Financial methods misallocate capital and may reduce national saving.
- Workers often evade contributions but manage to qualify for benefits.
- The failure to index benefits means that pensioners in many countries have not been
- Protected from inflation.
- The growing deficits of old age programs are passed on to general treasury, requiring higher taxes and higher public borrowing less public spending for other important purposes.
- Publicly managed pension reserves are invested unproductively, earning low, even negative, rates of return.
- Large income transfers go to upper-income old people, while many of the lower income old are not helped.
- Occupational pension plans have not been adequately regulated.
- Today's children and young workers may pay the price of higher taxes, lower pensions, and therefore lower living standards, as old age dependency rates raise and growth declines.

Check your progress 2

1. A ___________is an agreement to provide regular income during a person's post-retirement life.

   a. Pension

   b. gratuity

2. In the ________the first pension plan was established by the end of 19th Century by Railroad.

   a. B U.S.

   b. India

1.4 Why Pension Plan?

Pension plans receive special tax treatment and are subject to eligibility, coverage and the benefit standards. For individuals, it would be indifferent-pension benefits and personal savings if it provides some retirement benefit at the same cost of forgone current consumption. Tax advantages create favourable savings through pension plan. For firms, it provides of substitute for wages and pension can provide firms with a source of financing at a cheaper cost Pension cost of a firm is tax deductible.

The investment income of pension plan is tax exempt. Pension benefits are taxed when the benefit paid to the beneficiary not when earned by them. There are three options available to the employee for their retirement benefit

- Employer does not make any contribution but he pays full amount lo the employee. Employee himself saves that amount for his retirement benefit.
- Employer does not make any contribution but he pays full amount to the employee. Employee himself takes a life insurance policy for his retirement benefit.
- Employer makes a contribution to the pension fund for the retirement benefit of the employee.

Before considering the comparative advantage of above three options, let us make assumption that:

- Employee is in tax bracket.
- His marginal rate of tax throughout his life is assumed to be 30 per cent.
- Return earned on his saving assumed to be 14 per cent.

In case of option No.1, employee receives only after tax income of 0.7 (1.00 - 0.3). This after tax income is deposited in a bank which earns rate of interest of 14 per cent. His effective rate of return would be 9.8. In this case, employee receives Rs. 7001- after paying 30 per cent tax on gross income of Rs. 10001- and depositing in a bank for 35 years. The interest earned on savings again reinvested after paying the tax' for that income for each year. Therefore, his return after 35 years will be Rs.18,457.8 after 35 years. This amounts to a rise of 26.37 times over his initial investments.

In case of option No. 2, employee receives after tax income and takes an insurance policy of Jeevan Dhara at a single payment of Rs. 31.50. It will accrue and would receive an amount of Rs. 1,0001- after 35 years. It amounts to 31.75 times over his initial investment.

In case of option No. 3, employer contribute Rs. 1,0001- to the pension plan instead of paying him after tax income of Rs. 7001-. The pension plan accrues an assumed rate of 12 per cent, the amount returned to the beneficiary would be Rs. 52,8001-. It comes to 52.8 times over his initial investments.

Considering the above three options, it is obvious for an individual to opt for a pension fund which accrues 52.8 times over his initial investment even at a lower rate of return of 12 per cent.

Check your progress 3

1. _________ plans receive special tax treatment and are subject to eligibility, coverage and the benefit standards.
   a. Pension
   b. Investment
2. _______advantages create favorable savings through pension plan.
   b. Tax
   a. Money
3. _______benefits are taxed when the benefit paid to the beneficiary not when earned by them.
   a. Pension
   b. Investment

1.5 Types of Pension Plan

There are two basic types of pension plans:

a) Defined Benefit Plan

b) Defined Contribution Plan

Defined Benefit Plan: This plan assures the contributors a predefined pension payment system depending on the final contribution structure. The plan usually has a formula which will be worked out and paid accordingly to the employee upon his retirement. In essence tile pension payment will depend upon the length of the service of the employee and the earnings of the employee. The pension obligations are effectively the debt obligations of the sponsor of the fund, which assumes the risk of having insufficient funds in the plan to meet the contractual payments to the retired employees. Thus all the investment risk is borne by the plan sponsor.

Defined Contribution Plan: This plan specifies the contribution and pension income depends upon the amount of contribution, numbers of years in which contributions made and the performance of the fund. Thus risk of investment is transferrer1 to the investors in the pension fund. Defined contribution pension plans come in several legal forms: Money Purchase Pension Plans, 401(k) plans, Employee Stock Ownership Plans (ESOPs)

With a defined contribution plan, employer merely passes pension fund management to the insurance company arid stops making contribution to the plan upon the termination of the plan by employee. With the defined benefit plan, it become more complicated and controversy. The pension fund assets do not necessarily equal the present value of promised benefit. If assets are greater than the benefit the excess assets are transferred to the employer. If the assets are lower than the benefits then it falls short of obligation.

Hybrid Pension Plans: These combine features of both defined benefit and defined contribution plans. It appeals to both employee as well as employers, since bearing of investment risk by the employee in case of defined contribution plan, while it is expensive and complex to implement defined benefit plans for employers. Thus there will be risk sharing between sponsor and members of the plans. Floor-Offset Plan is one of the hybrid plans. Employee contributes a certain amount each year to a fund as in defined contribution plan. The employer guarantees a certain minimum level of benefits, depending on the employee's number of years of service as in a defined benefit plan. The employer manages the fund and informs the employee periodically of the value of his investment. If the managed fund does not generate sufficient growth to achieve the present levels of benefit, the employee is obliged to contribute an additional amount to bridge the gap.

Factors Affecting Contributions

An organisation must evaluate on actuarial funding projection designed to accumulate assets to provide benefits to the retiree. An actuarial funding programme combines the data on plan specification, employee characteristics and pension fund size with assumption about future interest rate, salary turnover and death and disability ratio. Given these assumptions and data, an actuary estimates both future pension obligation and the annual payment schedule to satisfy those obligations. Different interest rate and salary assumptions have an impact on annual contribution. A rule of thumb is that rising annual interest rate by 1 per cent point will lower pension liabilities by 15 per cent holding all the factors held constant. Similarly, different actuarial funding method can substantially alter required and allowable contribution in any given with even a same plan characteristics and actuarial assumption features the state pension in selected OECD countries which follow different number of years for full pension, indexation and pension benefits.

Check your progress 4

1. Defined Benefit Plan assures the contributors a predefined pension payment system depending on the final_______.
   a. contribution structure
   b. payment
2. ________Plan specifies the contribution and pension income depends upon the amount of contribution, numbers of years in which contributions made and the performance of the fund.
   a. Defined Contribution
   b. Fixed investment
3. _______Pension Plans combine features of both defined benefit and defined contribution plans.
   a. Hybrid
   b. variable
4. A _________must evaluate on actuarial funding projection designed to accumulate assets to provide benefits to the retiree.
   a. Organization
   b. employee

1.6 Pension Fund Risk

The pension funds generally face the following risks:

- Coverage Risk
- Replacement Risk
- Investment Risk
- Longevity Risk

- **Coverage Risk:** Employee failing to participate in the pension schemes which in turn leads to impossibility of economies of scale of operation in the funds management. It call be avoided by mandatory contribution by employee as well as plan participant.
- **Replacement Risk:** Employee who retires will not be able to maintain the standard of living after retiring comparable with same standard of living during pre-retirement periods. Tax benefit should be given for employee to contribute more to funds as well as to contribute longer time so that replacement risk can be reduced.
- **Investment Risk:** The investment made by pension funds may perform poorly due to market risk and other risk inherent to assets in which the investments are made. Better diversification across assets and across countries would help reduces the investment risk which partly depends upon the fund management.
- **Longevity Risk:** Risk that the retiree will live longer than expected and thus exhaust the amount saved for retirement before he dies. This risk can perfectly be hedged against insurance, since longevity risk is 'beneficial to insurance companies and mortality risk is beneficial to pension funds. The life insurance companies would be more beneficial by floating pension funds and pension fund institutions would be more benefited by floating life insurance companies.
- **Inflation Risk:** The risk of price increases, which erode the purchasing power of the lifetime savings. These risks were entirely depending on government policy, fiscal deficit and central bank's monetary policy. The government must bring a regulation similar to ERISA in USA and form the Pension Benefit Guarantee Corporation (PBGC). The corporation would guarantee at least inflation risk by charging insurance premium for eligible pension fund. The corporation liabilities should be guaranteed by central government and central bank which are accountable for inflation

Risk Sharing

- Certain risks that are uncorrelated across individuals, such as longevity risk, are minimized by pooling across the largest number of people including everyone in a single insurance pool or reinsuring across several smaller pools since the average outcome for the group is much more certain than the experience of any particular individual.
- Other risks, such as disability risk, are subject to moral hazard problems, which should be constrained to keep costs down.
- Some degree and type of indexation, shifting part of the inflation risk to younger workers, is needed to prevent the very old from living in poverty duping inflationary periods
- Investment, insolvency, and political risks are real and potentially large, but they cannot be reduced through risk pooling because they are correlated across individuals and subject to moral hazard problems. Diversification is the solution here. Diversification across several managerial and financing mechanisms protects pensioners against exposure to extreme failure of any one arrangement, reducing overall risk for the old.

Check your progress 5

1. The risk of price increases, which erode the purchasing power of the lifetime savings, is called _______risk.
   a. Inflation
   b. investment

1.7 Funds Management

Long-term vs. Short-term

Pension fund benefits from regular inflow of funds on contractual basis and for long-term liabilities which together imply little liquidity risk. Pension funds are contractual annuities meaning that the lump sum withdrawals are precluded each during the period their claims are payable after retirement. The members of the pension funds are willing to accept low liquidity, giving potential for higher returns at a greater risk and liberal portfolio regulations are also responsible for better management and growth of pension funds. Time also needs to be taken as an important variable in the investment decision process. Long-term investment could reduce risk significantly and increase return. Madhusoodanan (1997) found that taking longer tern view of the market definitely pays rich rewards. That is, buy and hold strategy is likely to be better than any trading strategy on long-term basis this is in conformity with several stock markets. Thus it is very important to look beyond asset allocation strategies based on the risk-returns trade-off of different asset classes

Asset Classes and Diversification

How much fund the pension plan should raise and what kind of assets to invest in are the questions which hove different implications depending upon the types of plan. For defined contribution plan, employer has to make a promised contribution .each year and has no other funding decisions to make. The only question with defined contribution plan is how to invest the assets. The standard portfolio theory that it would be best with some well diversified combination or stocks, bonds and treasury bills. More risk employee wants to take higher the proportion will be in the stocks. In practice, most pension plans in U.S. are fully funded meaning that assets equal the present value of benefits already earned by employee. Pension plan is equally split between stocks and bonds. This fifty-fifty ratio gives possible explanation for the pension fund. There are number of factors which determine the appropriate asset mix policy. The factors are long-term prospects of the capital markets, short-term fluctuations in economic values, plan assets and liabilities, the impact of returns on employers' contributions and riskiness of the portfolios. Most pension funds choose the mutual funds to rely on the investment expertise from mutual funds. In table it is elaborates compositions of pension funds in select developed countries; Table gives real total returns for those countries for different assets, while Table summarizes the returns for selected assets in India

Further, real returns on pension funds show that privately managed funds do better than publicly managed funds. Table 8 shows gross average annual investment returns after inflation for privately as well as publicly managed pension funds in the selected countries.

Domestic vs. International Diversification

International diversification reduces risk faster than domestic diversification because domestic securities exhibit stronger correlation as a result of their joint exposure to country-specific stocks. International diversification' should cover both stock and bonds; efficient portfolios made up only stocks display a substantially higher risk for the same' level of returns than efficient portfolios made up of both stocks and bonds. (Solnik and Noetzlin, 1982) (See also Sliashikant, Uma 1998).

Funding Liabilities

How much funds the pension plans have has different implications depending upon the types of plan. The firms owing pension fund shall chose the funding and the portfolio strategy with higher net present value. This leads to two opposite solutions. Under funding needs to buy risky assets, over funding facilitates to buy high grade bonds. Ambachtsheer points out that pension funds can be classified on the basis of liability goals. It can run on the basis of termination liability goal or going concern goal. A termination liability definition assumes that goal of the fund is to meet current accrued liabilities. The going concern liability reflects an assumption that the pension benefits accruing will actually be paid out over time and that the nominal pay-out value will reflect actual inflation experience. The investment implications vary according to the selection of goal of the pension fund. If the pension obligations are termination obligation, then passive fund management is enough. If the duration of the liabilities is known, investments are to be made in the portfolio of assets that matches the duration of the liabilities. An immunization strategy is constructed through a portfolio of zero coupon long dated paper or coupon paying fixed income securities. The immunization strategy is subject to an element of interest rate risk. If the pension liabilities are going concern Basis, investments in stocks could be worth considering. Then the element of market risk will be with the fund. If the termination liability view is static view of the world then the going concern is a dynamic view of the world.

Passive vs. Active Management

The Management of pension fund depends on the efficiency of the asset market in a particular country. Table summarizes the active investment management and passive management in different assets in different markets. Arumugarn (1997) found day of the week anomaly (high stock returns on Friday) and Arumugarn (1998) found high stock returns before holidays in Indian equity market. The institutionalized investing could exploit the inefficiencies and anomalies present in the market. However, Monday-buy and Friday-sell trading strategy can be used to exploit the day anomaly in the Indian equity market, since any reversal of timing of investment (Friday-buy and Monday-sell) would incur loss of 20% p.a. as against the profit of 6% pa. in the Monday-buy and Friday-sell strategy. Table 10 shows returns on day anomaly trading strategy in Indian equity market. Exhibit 1 elaborates how to choose management style in a given environment.

Exhibit 1: Choosing Management Style

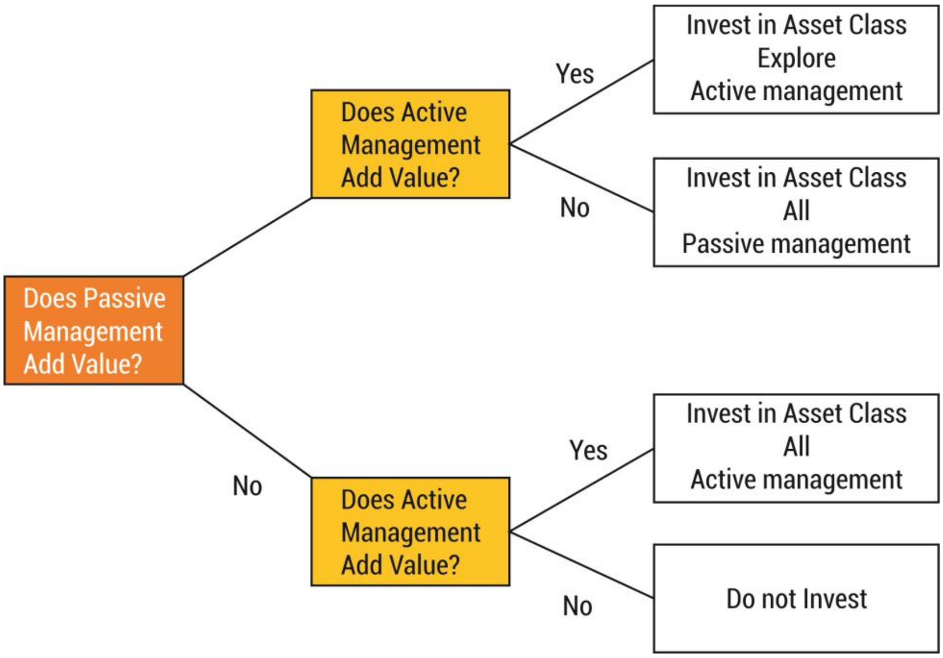

Fig 1.1 Choosing Management Style

Personal Finance

It makes sense as a way of reducing taxes for shareholders. Shareholders can reduce his taxes by shifting his portfolio by stocks into pension funds. The firms allow the workers to own pension funds because it is safe for' them to make long-term commitments to the firm. Further, shareholders can increase their wealth by buying bonds from companies (interest on bonds are tax deductible) are investing those interest in pension plans. Table in 15.9 summarizes the attributes of investment environment in 1980s and 1990s which will have an impact on the management of pension fund.

Check your progress 6

1. Pension funds are contractual ________meaning that the lump sum withdrawals are precluded each during the period their claims are payable after retirement.
   a. Annuities
   b. Perpetuities
2. _________diversification reduces risk faster than domestic diversification.
   a. International
   b. national
3. ________returns on pension funds show that privately managed funds do better than publicly managed funds.
   a. Real
   b. actual

1.8 Pension Funds Investment: General Guidelines

Prudent man Rule

The pension funds should invest the money in the way how prudent man invests in the asset of the portfolios. The onus of being prudent is put on the fiduciary investment committee - the committee that oversees the pension funds. They would have to basically ensure that they review all the investments properly, having all the documents properly and all due diligence that a normal prudent man would, in order to take a decision. This is the process which would have major impact on the pension fund industry.

Sole Benefit of the Plan Participant

All investments have to be made on the basis of providing benefit to the plan participants. In a framework of the decision making in pension funds which has help up to the test of the time, and the pension fund industry generally speaking has been free of scandal

Management Structure of the Pension Fund

Fiduciary Committee at the top (like the board of governors, or board of trustees) takes action on specific investments, on investment policies, the asset allocation, and administration of the fund. These investment activities, administrative actives, oversee any external investments or managers are being done by Chief Investment Officer on behalf of the trust. The officer reports to the fiduciary committee. The Chief investment officer and mutual funds or investments managers are fiduciaries and are liable for any malpractice. This is the kind of structure in US pension industry and have been really good success.

Asset Classes

While most of the pension funds follow prudent man rule, Table exhibits stipulated investment limit for the pension and provident funds in India. Investments are not fairly diversified as it holds only of bond portfolios, nor any foreign investments

Foreign Investments

Though international diversification' ensures reduction of risk and maximize the expected returns, in any pension funds are biased towards domestic investments either by prudent man rule or restrictions by the government.

Performance Measurement

Let us now see how the performance of a given pension fund can be measured. To take an example, cost Effectiveness Inc. (CEM) have created a seven-point GAAP for measuring pension fund management operation (Source: Ambachtsheer, 1994)

- Total fund returns must be decomposed into policy and implementation-related components before any peer-relative comparative analyses me performed. Funds may have different investment polices because of differences in such factors as inability structure and risk tolerance, so policy-related return components across different funds contain no information about management skill.
- To understand the sources of implementation-related fund return, it is useful to decompose it into within-asset-class and across-asset-class (mix) segment. Ideally, return (and risk) decomposition continues down to the level of individual portfolio management mandates within the fund.
- When peer comparisons of fund returns are made, only implementation-related fund returns (and risk) components calculated with identical decomposition procedures ace comparable.
- Total fund operating costs must be decomposed into minimum-required and incremental components before any comparative analyses are performed.

Because funds have different asset values and different investment policies, minimum-required operating. Costs across different funds will differ and will contain no information about management skill.

- To understand the sources of incremental operating costs, it is useful to further decompose them into those directly related to investment management and those related to governance and administration. Ideally, the costs directly related to investment management should be further decomposed down to the level of individual portfolio management mandates within the fund.
- When peer comparisons of fund operating costs are made, only incremental operating cost components calculated with identical decomposition procedures are comparable.
- When peer comparisons of fund return-operating cost combinations are made, only implementation-related fund return and incremental operating cost combinations calculated with identical decomposition procedures are comparable.

Check your progress 7

1. The pension funds should invest the money in the way how __________invest in the asset of the portfolios.
   a. prudent man
   b. Bank
2. All investments have to be made on the basis of providing___________to the plan participants.
   a. benefit
   b. opportunities
3. Most of the pension funds follow___________rule.
   a. prudent man
   b. Keyman
4. International diversification' ensures reduction of risk and__________the expected returns.
   a. Maximize
   b. Minimise

1.9 Pension Funds and Capital Markets

Investment policies of pension funds have a profound effect on the capital markets, affecting the rate and direction of financial innovation, the behaviour of security prices and the policies of the corporations whose securities they hold.

Fiduciary role in pension's management and a large increase in the volatility of interest rates modest it important for pension funds to hedge their liabilities.

In response to the hedging demands of pension funds, the financial markets have produced a variety of innovative products.

Pension funds have also pioneered in the development of index trading. Pension funds having a substantial option of the stock in corporations and their voting powers can profoundly affect corporate policy. Growth of funds has influenced international capital flows. International diversification is a means to reduce systematic risk in domestic markets and beneficial effects on the efficiency of global capital markets

Opportunities for Growth of Pension Funds

- More than 60 per cent of the household savings are in the form of currency and deposits, which can be canalized through pension fund reforms
- Provident and pension fund assets in India constitutes only below 20 per cent of GDP as against average of 30 per cent for developed countries though percentage of household savings are almost similar.
- The government must bring a regulation similar to ERISA in USA and form the Pension Benefit Guarantee Corporation (PBGC).
- The corporation would guarantee at least inflation risk by charging insurance premium for eligible pension fund.
- The corporation liabilities should be guaranteed by central government and central bank, which are accountable for inflation.
- The regulations should encourage wide diversification across assets and countries although to a smaller extent in the initial periods.
- Vesting rules should be simplified so that participant can change the funds depending upon the performance of the funds to encourage competition among pension Funds.

Check your progress 8

1. Investment policies of pension funds have a profound effect on the ________markets.
   a. capital
   b. money
2. In response to the ________demands of pension funds, the financial markets have produced a variety of innovative products.
   a. Hedging
   b. Investing
3. Pension funds have also pioneered in the development of _________.
   a. index trading
   b. market

1.10 Pension Funds: Some Related Statistics

In order to understand the scope and dimensions of Pension Funds and the manner in which they are operated. Let us look at some relevant statistics

Table Percentage of Population over Sixty Years Old 1990-2150

Countries	1990	2000	2010	2050	2100	2150
OBCD	18.2	19.9	23.1	31.2	30.4	31.0
Latin America and Caribbean	69	7.7	9.3	23.5	29,3	30.6
Eastern Europe and Fanner Soviet Union	15.3	17.0	18.2	26.5	192	30.8
Middle Bast and North Africa	7.0	7.3	81	18.1	23.6	30.5

Sub-Saharan Africa	4.6	4.4	4.5	9.9	27.7	29.4
Asia	74	8.3	9.3	22.1	28.3	30.3
India	6.9	73	53	20.4	27.9	30.2

Table Main Features of State Pension in OECD Countries

'DOW 4: Main Features or State PCIISiOn in OECD Countries

Countries Retirement Age women / men		No of year required for full pension	Payroll tax for pensions, workers/ Employers combined	Indexation	Benefit Type
Australia	60/65	0		Prices	MT
Austria	60/65	15	22.9	Wages	CR
Britain	60/65	40	18.8	Prices	CR
Canada	65/65	1	4.6	Prices	OF-MT-CR
France	60/60	37.5	19.8	Wages	CR
Germany	65/65	5	17.8	Net Wages	CR
Ireland	65/65	3	17.7	NA	CR-MT.
Italy	55/60	15	26.2	Prices and Wages	CR
Japan	65/65	25	16.9	Prices	CR
Holland	65/65	49	15.2	Wages	CR
Spain	65/65	15	16.7	Prices and Wages	CR
Sweden	65/65	3	21.0	Prices	CR-UF

United States	65/65	10	124	Prices	CR

CR - Contribution Related

T - Means Tested

UF - Universal Flat

Table Characteristics of Pension Funds' Portfolios

Asset	Year	USA	UK	Germany	Japan	Canada
(a) Marketable Securities	1970	93	85	23	21	77
	1980	86	79	34	64	73
	1988	90	85	44	87	92
(b) Real Assets	1970	45	61	17	37	23
	1980	41	70	18	16	20
	1988	48	77	24	30	35
(C) Capital Assets	1970	93	93	36	51	76
	1980	82	94	42	70	79
	1988	86	92	48	85	86
(c1) Lang-term	1970	51	32	80	14	65
Fixed-interest	1980	43	24	76	54	66
bearing assets	1988	38	15	73	54	58

Table Characteristics of Real Total Returns 1967-90

Assets	US	UK	Germany	Japan	Canada
Loans	3.5	1.4	6.5	0.9	4.0
Mortgages	2.0	2.0	4.7	3.0	2.4
Equities	4.7	8.1	9.5	10.9	4.5.
Bonds	-0.6	0.8	2.7	0.2	-
Short term assets	2.0	13	3.1	-0.5	25

Property	3.4	6.7	4.5	7.2	4.6
Foreign Bonds	1.5	-0.3	3.2	1.5	-1.1
Foreign Equities	9.1	6.5	10.4	7.8	6.6
Inflation	6.0	8.9	2.1	55	6.4

Table Asset Returns in India between 1964-65 and 1996-67

1964/97				1964-81			1981-97	
Asset	Excess	Real	Nominal	Excess	Real	Nominal	Excess	Real	Nominal
Gold	5.3	5.8	13.4 '	13.6	13.3	19.4	-3.0	-1.6	7.5
Silver	2.0	2.4	10.3	8.4	7.9	14.4	-4.4	-3.0	6.3
Equity	15	1.4	9.7	-2.4	-3.7	.4.2	5.1	6.6	152
Call Rate	0.5	0.5	8.7	0.5	-0.7	6.9	0.4	1.7	10.6
Book	0	-0.04	8.3	0	-1.3	6.4	0	1.2	10.1

Table Gross Average Annual Investment Rclurns for Selected Pension Funds

Countries	**Real Rate of Returns**	**Years**
Privately Managed Funds		
Chile	9.2	1981-90
U.K	8.8	1980-90
U.S	8	1980-90
Netherlands	6.7	1980-90
Publicolly Managed Funds		
US (OASI)	4.8	1980-90
Malaysia	4.6	1980-90
Singapore	3	1980-90

India	0.3	1980-90
Kenya	-3.8	1980-90
Ecuador	-10	1980-86
Egypt	-11.7	1981-89
Venezuela	-15.3	1980-89
Zambia	-23.4	J980-S8
Turkey	-23.8	198488
Peru	-37 4	1981-88

Table Asset Market Characteristics and Investment Management

Asset	Market is Efficient	Market is Inefficient
Investment	Passive	Active
Futures/Cash Portfolio	Passive	Active
Physical Commodity	Active	Active

Table Return on Daily and Day Anomaly Trading Strategies

No Trading Cost				With Trading Cost		
Returns	Day	Day	Day	Day	Day	Day
	Unadj.	Adj.	AdJ.(p.a.)	Unadj.	Adj.	Adi(pm.)
Daily	0.088	0.056	20.3,	-0.162	-0.142	-51.19
Mon Fri	0339	0.072	2199	0.089	0.016	5.93
Fri-Mon	0276	0.005	1.93	0.027	-0.056	-20,27

Check your progress 9

1. No government limits to foreign investment.
   a. Austria
   b. Australia
2. 4% limit on foreign assets holdings.
   a. Germany
   b. Japan
3. Foreign investment is prohibited
   a. Portugal
   b. Norway

1.11 Let Us Sum Up

In this unit we had a detailed discussion on pension funds. Here we discussed the importance of pension in our society, how is a pension fund needed in our society, what are the various kinds of funds available.

Here we discussed that countries like India have clearly specified, for the Government Provident Fund avenues in which the pension funds can be invested in addition to the providential norms which have been prescribed. This unit explain the need and significance of pension funds and the type of pension funds across countries that are in vogue today. The type of risks associated with pension funds and the general guidelines for investment of service funds have been discussed.

Important statistics in relation to pension funds have been provided to enable to you to have an overall view of this market across countries. Growth of funds has influenced international capital flows. International diversification is a means to reduce systematic risk in domestic markets and beneficial effects on the efficiency of global capital markets. Here all these points have been covered in very detail and you would learn a lot after going through this unit.

1.12 Answers for Check Your Progress

Check your progress 1

Answers: (1-a)

Check your progress 2

Answers: (1-a), (2-b), (3-a)

Check your progress 3

Answers: (1-a), (2-b), (3-a)

Check your progress 4

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 5

Answers: (1-a)

Check your progress 6

Answers: (1-a), (2-b), (3-a)

Check your progress 7

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 8

Answers: (1-a), (2-b), (3-a)

Check your progress 9

Answers: (1-a), (2-b), (3-a)

1.13 Glossary

1. **Financial Services -** Are services rendered by financial institutions, facilitating the smooth flow of financial activities in the economy of the financial system.

1.14 Assignment

How does the changing demographic profile influence the scope of pension funds?

1.15 Activities

Describe the different types of pension plans.

1.16 Case Study

Discuss the utility of pension for the society.

1.17 Further Readings

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UNIT 2: GLOBALISATION AND ITS IMPACT ON FINANCIAL SERVICES MARKETS

Unit Structure

2.0 Learning Objectives

After learning this unit, you will be able to understand:

- Discuss the impact of globalisation of financial markets on local providers.
- Explain what the main drivers of globalisation are?
- Describe the future trends for financial services in respect of globalisation.
- Elaborate upon the requirement for changing consumer orientation in the forthcoming, Scenario.
- Apply some of the imperatives indicated for financial services.

2.1 Introduction

Globalisation is making boundaries to yield to create boundary-less state in the interest of Internationalizing Markets for free trade situation without any sort of restrictions whatsoever.

In the past when you look at the foreign trade front, you will find every country was vying with one another to get the foreign exchange to help the country to have better balance of payment, but this has been a very difficult task for every country since every country wanted to save its foreign exchange resaves or surpluses and no country liked the idea of foreign exchange deficits but that became very much inevitable. As a result, it in every country's own interest OPENING UP MARKETS became a necessity. Thus Globalisation became a reality. In this unit we will look at the impact of Globalisation on ' financial services in general.

2.2 Globalisation of Financial Market and its Impact on Local Markets

By Globalisation, we mean opening up market opportunities anywhere in the world and there are no borders that means we are living in borderless world. Kenichi Ohmae, a former Managing director of Mckinsey and Company wrote on the power and strategy of Markets in early nineties and he found semi-conductor industry was becoming a high fixed cost process industry and that had generated a lot of criticism that he was behaving somewhat like an agent for MITI (Ministry of International Trade and industry of Japan) though what he wrote was a great fact which the industry did not want to accept at that time and interestingly enough, many of his own colleagues in Mckinsey did not share his views but what he said was realised as an important fact later in the economic environment surrounding the world. A nuclear engineer could outpace many professional economists, as a management consultant. His logics were and are simply better than a normal economist's logic.

A deregulation of financial markets complicated several situations and that could' not be stopped as deregulation of financial markets was really very important even for the very survival of industries and that is how Globalisation started, on comparative advantages 'and that could be possible only in global open markets systems, The principle laid down in this is that resources should not be scarce and that should be available at comfortable costs while nobody loses meaninglessly. You will see today, the new costumer does not believe in scarcity and the very concept of economics taught in the past has undergone a metamorphic change. As Ohamac said in 1990, after deregulation corporations could use alternatives to create wealth in key regions of the world in addition to key manufacturing and selling. He further said, "To help then gain a market share it was necessary to learn about macroeconomics as well as currency and financial markets".

Protectionism has to die a natural death in favour of the consumer. After all why should the consumer pay for the inefficiencies and ineffective manufacturing of products? This has become the consumer driven market, popularly known as Buyer's market globally. This is further well contributed by the innovative software development to cause prompt instantaneous connectivity world over, due to advancement in computer hardware technology and the telecommunication technology to the consternation of protagonists of ' protectionism today. No doubt fixed costs are increasing under various heads in the software industry, Sooner or later, this industry will also face same problems like that of semi-conductor process industry. After all, cost ineffective industries will have just short runs of euphemistic growth. But that is not the concern today, somehow because if the industry matures sooner or later, it will have to work strategies only for short runs and swiftly move over to new thought provoking innovation and creative dreams conducive to the consumer. Care should be taken not to put all your eggs (investments) in one basket.

So it means a lot of product development in financial services and moving out of export oriented stage of organisation. Also one should move out of single head-quarters stage to several head-quarters stages. This will help cut down a lot of governmental levies to the best benefit of the consumer. In this process, several multi-nationals like Micro-soft have opened establishments in different parts of the world with local headquarters mechanism. This also reduces fixed costs phenomenally.

Check your progress 1

1. By__________, we mean opening up market opportunities anywhere in the world.

   a. Globalisation

   b. Nationalisation

2. A ________of financial markets complicated several situations.
   a. deregulation
   b. regulation
3. Protectionism has to die a natural death in favour of the _________.
   a. Consumer
   b. Producer

2.3 Globalisation of Markets: The Main Drivers

Some financial services have been global in scope and practice long before the term came in vogue, Services like banking and insurance have facilitated and supported early trade routes for' centuries with telecommunication and information technology a fresh boost has been given to the pace of internationalization of financial service. Some of these services have simply followed their customers in new and increasingly global markets; others have used new opportunities 'through technology or channels becomi8g available to enhance their access to worldwide customer bases. In order to understand the reasons for Globalisation, let us look at some of the important 'drivers' for Globalisation in the context of financial services. The term was first used by Yip in his research on Globalisation in the context of manufacturing firms but the work can be generalized for financial services too. In terms of the leading imperatives for Globalisation, these 'drivers' can be categorized into five classes. Let us discuss each of these briefly.

Market drivers: This class of imperatives include common customer’s needs, spread of consumers globally emergence of global channels and transferable marketing. The emergence of global customers who demand consistent service from suppliers of financial services whenever they conduct their own business, has in turn caused financial services like credit cards, banking, foreign exchange services, auditing, insurance, securitization, etc. to globalize in order to serve their customer well.

Competition drivers: 'As business customers globalize their operations, competing suppliers of financial services tend to compete on the basis of worldwide access and spread. This has important implication for local suppliers of financial services as an incoming business may also herald in the entry of an overseas competitor in the form of financial services supplier of that incoming business entity.

Technology drivers: Financial services rely heavily on maintenance and movement of data for enhancing their capabilities for Tran's border operations. The availability of broad band telecommunication channels and information superhighways, now capable of moving vast amount of data at great speed, had helped providers of financial service to rapidly internationalize. Emergence of the worldwide web as a major communication tool and its usage in large number of countries has facilitated internet banking and globally usable credit cards

Cost drivers: The impact of the cost driver for different services would vary according to the level of fixed costs required to establish operations in a country and the resultant possibility of cost efficiencies. The lowered costs of tele-communication and international travel, possibilities of organizing regional hubs for business operations for financial services, the round the clock availability of services like foreign exchange and transfers in real time and at lower operational costs have also encouraged Globalisation of financial services.

Government drivers: Among the most important facilitation of Globalisation has been provided by lowering of regulatory barriers by the governments of most nations. Fuelled by the developments in world trade and the impending world trade regime, wide spread liberalisation and lowering of trade barriers including opening up of financial service markets for important sectors like insurance, have created encouraging impetus for the growth of financial services

Worldwide banking, based as it is on information processing has been particularly affected by all these drivers. The practice of banking has been revolutionized by advances in information technology through far reaching developments like electronic funds transfer, automated teller machines, telephone and internet banking and global network of all major credit card services. These developments today allow consumers to enjoy banking services at great distances from the location where such services are provided.

Fast changing technology and its consequent high cost equipment also become components of the cost drivers in the globalisation-of financial. Services

International trade has been the major market driver for global banking. The government driver has always been very important for banking because economic and political reasons have necessitated tight regulation of domestic banking. Bankers in many countries including India were nationalised to enable governments to have lighter control over banking activities. The policy is under revision in most countries today as winds of liberalisation buffet government policy in these countries

The growth and worldwide spread of the multinational corporation have been till important market driver of globalisation in banking, as corporate customers, such MNC's seek global coordination and delivery of worldwide corporate banking services.

The growing needs of business travellers on the other hand are being met by globally branded traveller's cheque and credit cards, issued by both head offices and local franchises, as well as globally networked ATMs that issue money in local currency. Most MNC's today use a combination of both local and international banks, but the larger the geographical spread of a bank, the better its competitive ability to serve clients with translational business.

Check your progress 2

1. Emergence of the ________ has facilitated internet banking and globally usable credit cards.
   a. www
   b. http
2. The lowered costs of ________and international travel, possibilities of organizing regional hubs for business operations for financial services.
   a. Tele-communication
   b. communication
3. Fast changing ________and its consequent high cost equipment also become components of the cost drivers in the globalisation.
   a. technology
   b. organisation
4. The growth and worldwide spread of the multinational corporation have been till important market driver of ________in Banking.
   a. globalization
   b. nationalization

2.4 Globalisation of Markets: The World Ahead

By strategy one should create sustaining value for the consumer. Commercialize inventions and discoveries. Globalisation, it is the turn to invent, innovate and create. Accept the nature law. Old should yield to the new. Never become me - too. If you do, you will be no where the message of the globalisation is. No longer me - too band - wagon can sell. More informed and highly demanding customers are increasing day by day, today. So they have the power in their hands. Multinational really turned out to be the organisations accepting what the customer wants, in the borderless world. So you are seeing today, a lot of products are just sold out at much lesser than manufacturing costs just to avoid finished goods warehousing and interest costs. These companies have to pay, if they do not understand the Mind of the consumer, as he turned out to be super strategist cash rich. He will not part with his cash unless the thing he buys gives him several times satisfaction over his investment on anything. This means that the customer can never be taken for granted. Barriers and artificial controls will have no meaning with the new consumer. So even Governments are just failing today, inter linked economies are much superior to old macro economists view - that exchange rate should change to adjust for the difference in purchasing power of tradable goods, and in rates of inflation and interest between two countries. Inter linked economy has about 1 billion people and above in its net, with the average capacity to a per capita of $.10,000.- GNP, This is growing and most of the wealth is created, consumed and re-distributed. Inter dependence of economy is helping build better security and that is going to be the governing principle in the years to come. So globalisation has taken a great grip on the industry and governments as also on all hues of politicians and their political economic thinking

In this context one has to study what shall be the global asset and liabilities management. That will vividly give chances of working. Also one should take into account sustainable energy availability and exploitation to help reduce energy costs on every manufactured goods. It becomes perforce a necessity to run for alternate sources of energy, consumer is not willing to pay for your energy costs and he will need heavy discounts everywhere possible except in most sought after product or service, for which the consumer might pay any price, as long as it is not a kind of ransom price.

Today, consumer is the king because what you care about most is the product's quality, price, design, value and appeal as a consumer, Young people today are least concerned about a Nation or Country and hence call be called as

Nationality less. Today's products have to rely upon so many different critical technologies. Interestingly enough today you sell your products to your own competitors for comparative advantages so that you can ' supply to your consumers your products at most affordable prices and that is the trend setting in the Beyond Tomorrow, as you know fully well, consumer will not just accept your products at high price one hand but also that what you give should be useful to him, You should be always in the lookout for newer technologies so that your products are in tune with the new technology development. Otherwise you will soon become obsolete in the markets.

You should have continuous research and development in your area of product development and also ensure that you’re R and D takes cognizance of technological advancement so that your product development is consumer friendly and price competitive in the eye of the consumer. He will not accept anything inferior at all. Managers have to amortize fixed costs over a much larger market base and this really drives them. New concept of low labour does not mean you will pay low wages to your people but ' you will get best work from your work force and it meals your work force will produce, best products and quality product and from his it should be clear consumer will not accept second best product but really be best and that you cannot produce from cheap labour! So the concept of low cost of labour has to undergo a tremendous change! Winner will be always focusing on the best or on becoming the best. It is also important to note that concern for shareholders value is vital. Equally important is to sustain leadership, put unmatched value in be market place and back it up with superior operating capability. Best companies are re-inventing competition in their markets.

In the Beyond Tomorrow, if the company is willing to cannibalize its hottest product with a risky and untested one you are the company for tomorrow. Offer a service at a cost hoping to establish a long term relationship. Link up with an adversary to drive its cost even lower, as you have some insight of tomorrow. Your chances of survival are then much superior to the traditionally driven companies.

In the tomorrow situation, you will strategize, Cross border operations are the' in-thing again. Interestingly, you will work on international partnering mechanism just to cut do costs. Dis-investments will be the order of the day. Only future is for the strategist. International trade will grow several folds. Foreign exchange transfers will be on the balance of credit arrangement. Trade boom is certain. Only intelligent players with sound comm. sense will survive. There will be very few common currencies - Euros, Dollars, and some currency will emerge in Asia, South-East Asia, may be some Afro-Asian currency. This will keep currency fluctuations under control or minimum volatility, a thing which is very new today. This will cause to make foreign exchange transactions not a gamble.

Change, challenge and crisis have all become clichés. Many nations and banks, companies did not give adequate concern for these and hence they all failed miserably. So the today nations and companies should know the trend by all means prevailing or suddenly appearing. New customer or consumer is just a challenge-in-total in the world. Even the mightiest have to fall flat before him and that is the message of this democratic world. Citizen really assumes power, in the form of consumer or customer. This spread will strengthen the citizen. Once he has tasted this power, he will take umbrage under this. He deserves this is provided to him, in the Beyond Tomorrow.

Check your progress 3

1. By __________one should create sustaining value for the consumer.
   a. strategy
   b. policy
2. _____________, it is the turn to invent, innovate and create.
   b. Globalisation
   a. Technology
3. Today, _________is the king because what you care about most is the product's quality, price, design, value and appeal as a consumer.
   a. consumer
   b. producer

2.5 Some Asian Trends

Stanley Fisher, deputy managing director of IMF in an interview to Asia Week's senior correspondent Alejandro Reyes, in the September 1,2000 issue of Asia Week, said, to a question "Is Asia's recovery solid. The recovery is impressive. We are expecting growth rates to 6% to 7% range from Asia as a whole for 2000-2001." HZ further added, “You have pretty solid growth in the range of 6% to 8% entrenched in two developing giants - China and India. That is very big source of stability". He further added, Korean ' recovery looks set to continue. Malaysia looks to be doing pretty well. Thailand is a bit slower, while Indonesia, because of political uncertainty (will grow at) around 5%. 'In the Philippines, it is a pity that there has been fiscal slippage, because it managed monetary and exchange rate policy well during the crisis. It is slightly disappointing that in recent years, it has had difficulty keeping its budget on track. Obviously, what it takes to get consistent economic policies is political backing for then and that has been difficult of late."

IMF assesses Japan will grow a little more rapidly next year than this year. There is a fear lingering around of significant slow-down, as there is tremendous uncertainty. There is a declining trend of slowdown in U.S. also.

Reforms in Asia varies a great deal, Korea did real progress in dealing with corporate debt problem and the banks (India should take cue from that experience). Malaysia had 48 done well in the banking sector (India should learn From Malaysia) Thailand moved clearly, progress seemed to have flagged, especially on corporate side. Yes, Indonesia is a bit uncertain, is the view of the deputy managing director of IME

In the Beyond Tomorrow, investors will not take kindly on governments not following proper procedures and would not like innocents being punished due to political interference. That is politician and political governments and governance would have to meet the citizen standards. Otherwise, politicians will lose their grip for ever: and independent citizens representatives will emerge from among the elite's are the message of tomorrow, since the old adage - "politics is the last refuge of a scoundrel" will die a natural death, sooner or later, as there can never be continuous "Peaks" in anything.

Banks and corporate re-structuring are very important for mechanisms and' appropriate re-engineering has to be done in this area and that will light a candle in darkness

Malaysia is dismantling controls pretty steadily and other nations should closely see and assess issues in what way they too can do that, just for sheer survival. Malaysia has got 30% exit levy on repatriating of portfolio funds and they will have to' get rid of them soon. It is a matter of conjecture how long fixed exchange rates will continue in Malaysia. Fluctuation is normal phenomenon and that should be allowed for any economic growth, in monetary policy.

Japanese economy is far from near-capacity points of constraints. Inflation is no risk at all. In terms of risks confronting Japanese economy any raise in interest rates cannot be useful, as per monetary economic theory and in close cohesion with monetary economic practitioners like IME only restructuring can save economies. Japan has started that but now; consumer confidence has to be built up at all costs. Risks of slowdown in Japanese economy are looming large.

There was a slowing down in the last three months (of year 2000) in growth rate in U.S. But growth is returning to sustainable levels and there exists very few signs of inflation. Growth will continue in the range of 3.25% to 3,75% much better than one could have anticipated, in the last five years, is the view of the IME

IMF is now working on debt-relief, an under-lying work of reforming systems, particularly on the very difficult issue of private sector involvement in the resolution of financial crisis. IMF vision statement deliberated upon a more focused fund in IMF meet held at Prague in October, 2000. Fund with more/focused conditionality – structural conditions will work in areas of essential interest to the fund elements central to Macroeconomic stabilization, including governance

On August 11, 2000, Bank of Japan raised interest rates from its zero interest-rate policy to 0.25% interest rate, while Federal Reserve Bank of U.S. as on 22 August, 2000 kept U.S. interest rates unchanged, for its own strategic reasons

In an interview given recently to Laxmi Nakarmi of Asia Week, at Seoul, global chief economist of giant Zurich Financial Services David Hale said Federal Reserve's concern is on productivity in U.S. specially when economy is slowing down, but in the second quarter productivity might stay high, the numbers were spectacular and it might contain inflationary pressures for a few months. Yet there is uncertainty in future monetary policy

Implications of Asia according to David Hale, if U.S. interest rates increase will have negative impact on emerging markets - Asia is an emerging market, in the first half of this year. Asia is a two-tier region, Korea, and China type and laggards like Indonesia and South-East Asia with its continued political problems, languid sense of recovery in Taiwan, lack of confidence in leadership in Philippines.

China's recovery is real. Its membership in WTO (World Trade Organisation) will help encourage further reforms. China is expected to be in the centre stage is about five years' time, with a dramatic foreign direct investments from international companies in Europe, North America and Australia besides non-resident Chinese. Global CEOs frequent turn out to China is impressive, as all of them hope great hopes in China. South Korea has a strong and robust stock market, good export growth, and resurgence in confidence cyclical recovery is just begun thought president Kim Dae Jung's term is winding down. North Korea re-unification with South Korea will not only he dramatic if it really takes place and chances are indeed greater Re-building North Korea alone will cost at least $1 to $2 trillion. Gradual opening of the market will be in 2 to 3 times, by normalization of relations with U.S.A, and Japan by the North Korea part. Money will just pour in if there are right gestures from North America, feels the chief economist David Hale.

David Hale is straight to state, "we don't have the kind of leveraging and capital flow excesses that we had in mid-1990s and the problem is the sense of paralysis, of stagnation and lack of momentum at a time, when the world economy offers a lot of opportunities. In Asia, the issues will remain the same for some time. Attracting foreign investment in the banking system to both revitalize and restructure, Further improvement in corporate governance will force organisations to allocate resources more efficiently. Political systems supportive of these reforms should be in place. Then there is ray of hope. This is what Beyond Tomorrow needs.

Check your progress 4

1. _________economy is far from near-capacity points of constraints.
   a. Japanese
   b. chinese
2. Banks and corporate___________are very important for mechanisms and' appropriate re-engineering has to be done in this area.
   a. re-structuring
   b. re-engineering

2.6 Globalisation and Consumer Orientation

Docile and stoic customer of the past is changing his face as New customer, today and tomorrow, that is Beyond Tomorrow is unforgiving at the market place, as highly empowered customer will decide the corporate' fate. He will demand competition, global, quality and look for new economic realities, as a highly focused customer. So companies have to continuously and constantly monitor and should be willing to meet the changing customer. Needs and his demands, is the clear message for tomorrow. Corporate should have unmatched competitive edge just to be in place, in tomorrow's market place, though he i s trying to satisfy even today the customer's demands but that is just a drop in the ocean of uncompromising demands of the New customer

Harish Manwani, director of personal products of FLL said, “the marketer must constantly upgrade the consumer and the product by finding new dimensions." In the same way, David Thomas of Proctor and Gamble opined, “what we have been learning and relearning is that consumers look for quality and value for money." Suresh Rajpal of Hewlet-Packard-India, said, "There are many companies that have not yet woken up to the reality that to be competitive, you have to be customer 'focused".

Deepak Parekh of HDFC said, "All the employees of our organisations have to be the trustees of our customers". KK Noria of Crompton Greaves said, "Customer intimacy has to be built not by a few, but by employees across the organisation". PK Mittal of Ispat Group said, "You have to get all parts of a corporation talking to the customer. For Indian ' companies, that has to be the Mantra", Mrutunjay Athreya a management consult4mt of repute said, "All the rewards accruing to a company come from only one source: the rupee of the customer."

Ashok Chandarlok of Siemens said, "When you create working cells people can see more of each other and work better with each other."

So to deliver value to the customer the financial service provider will have to

1. Realign organizational roles and resources around processes that deliver.
2. Introduce customer value by integrating suppliers and customers.
3. Promote multiple competencies in individuals by encouraging creativity.
4. Transform management roles, from command and control to process leadership.
5. Recast assessment systems to evaluate customer-driven performance.

6. Restructure the organisation; Found teams within and across processes.
7. Integrate the support functions into high-performance core processes.

For attaining the above goal, customaries -

- Redefine every employee as a customer for everyone else in the organisation.
- Treat the owners of every stage in the work flow as the customers to the previous stage.
- Create several chains of internal customers, leading up to the external customer.
- Use internal customer satisfaction\ion as a gauge for measuring effectiveness.
- Appraise and reward every employee in his success in servicing the internal customer.

The above becomes as suitable training, ground or company employee to fit themselves in real life situations with real customers. This is very much important to tune up one's mind to be with the customer.

This customization helps as follows:

1. Ensures that every employee realize the importance of new ideas and concepts.
2. Builds enough flexibility into individual goals to inject innovation in problem solving.
3. Empowers employees to solve customer problem on their own initiative.
4. Uses customer feedback and participates, to keep the innovation customer focused.
5. Measures the success of all ideas in terms of the value they add to the customers.

In the third stage, the implementation should be to:

1. Ensure that every employee interacts directly with the customers and the end user.
2. Allow the customer access to every person and function within the organisation.
3. Turn every encounter with the customer into a platform of interactive

communication.

4. Involve the customer in designing and fine tuning key products and processes.
5. Set up systems to facilitate interactions between suppliers and customers.

Check your progress 5

1. __________customer of the past is changing his face as new customer, today and tomorrow.
   a. Docile and stoic
   b. Faithful
2. Use ___________customer satisfaction as a gauge for measuring effectiveness.
   a. Internal
   b. external

2.7 The Emerging Imperatives for Financial Services

Financial institutions and, banking institutions will have to deal in the following areas in a most innovative way, if the Indian financial or banking institution have to compete with the foreign counter parts since opening up is gradually accelerating:-

- The evolution of risk management - to cover volatility of foreign exchange, volatility in interest rates, volatility in commodity prices, impact of increased financial risk on firms, Exchange rate risk, interest rate risk, commodity price risk,
- In futures, Swaps, Options and Hybrid Securities, and related contracting
- Risk management markets - derivatives in' every area a
- Futures
- Financial price risks,
- Taxonomy of options-pricing models and so on and so forth.

Similarly attention will have to be given on measuring on and managing default risks, managing of price risks in a portfolio of derivatives, and so on.

If one wants to get some perceptions of creative and innovative corporate management of today, one has to look at the various advertisements floated by the corporate for recruiting people to man their new functions and also to handle marketing functions for domestic and international marketing.

This clearly shows how each company and its board is trying to visualize the new millennium trends, and this will indicate the aggregates of these kinds of perceptions world over. Such a focus on skills and, qualities required will lead to a new exceptional paradigm, after all, man conceive things and then he tries to put strategic positions which we call managing today.

Let us see some advertisements recently published by the companies.

HSBC - The Hong Kong and Shanghai Banking Corporation Ltd - advertised on the appointments page of Economic Times recently, reading as under:

“HR Opportunities with HSBC"

In this advertisement HSBC talks about itself.

"The HSBC group is one of the world's largest banking and financial services organisation with about 6000 offices and around 170,000 employees in 81 countries and territories. Headquarters 'in UK, it has major PERSONAL, COMMERCIAL and INVESTMENT BANKING operations in Europe, the Asia-Pacific region, the Americas, The Middle East, and Africa.

This Hong Kong and Shanghai Balking corporation Ltd., is a principal member of the HSBC group and is a leading multinational bank in India with a significant presence in personal banking, credit cards, corporate banking, custodian services, trade finance treasury, and capital markets, and financial institutions

It further says, "Our human resources function has always played a pivotal role in SUPPORTING BUSINESS OBJECTIVES and is globally recognised as having, institutionalized some of the best HR practices across industries. We are the acknowledged leaders in resourcing through assessment centers, and for career and succession planning through development centers. We also provide a structured executive career development Programme for management trainees and are reputed for our structured job evaluation process.

HSBC is looking for HR, people to contribute for operations and systems driven roles in compensation, employee relations, and career development activities of the bank. Further, these personnel are expected to have ability to work under pressures, manage change as t' well as conflicting priorities, which assumes essential priorities, at a senior level. While at the junior level, the junior HR men should be effective communications, below 30 years of age, should rapidly establish credibility and build working relationships. It also claims, hat this junior position will provide challenging career and a rewarding career. It presumes knowledge of labour laws is essential. An analytical and systems driven background may be an advantage

A trading house, MRF Limited, says it has 50 years of corporate leadership in diversified fields and it is one of the most successful Trading Houses in India with trade links established all over the world. It is said that this value reputation earned global markets that had provided the logical impetus to the growth of its exports. Today, more than 70 countries across the globe ke witness to the quality excellence of MRF products. MRF expects its exports executives should be graduates below 30 years of age preferably with a degree (additional) diploma in Foreign Trade and with minimum 6 years of experience in exports marketing of consumer durable be positions demand hard-core selling, prospecting new markets and involves extensive overseas travel to widen export markets."

In this advertisement one can clearly see, people pin hope on youngsters and on also those who are from specialised institutions of learning, giving the clear impression, only these youngster have some grip on the export markets, especially because the corporate find it difficult to allocate budgets for internal training programmers, for their own relevant needs, and thee is exclusive dependability for specialised education, by outsourcing and this also lead us to believe that the general education pattern developed by the universities, say in India over 160, excluding deemed ones give terrestrial education leaving specialisation in the hands of the users. If the present recruiting trend countries, naturally, we will have to wind up present universal. education pattern, yielding to specialization, since it is not meaningful to go on increasing' The number of years in one institution or the other at the cost of the National exchequer on the one side and unnecessarily reducing the potential working time of d e youth on the other.

We should also consider, in this mercurial global situation, there cannot be consistency of systems and procedures even in the short-term perspective. So corporate cannot get away from their own internal training mechanism since each business needs a particular way of focusing depending upon the business environment. So it will be clear that there is no short cut to success in the future but definitely it calls for intelligent kind of reading the situations, from time to time that no school or college and institution can give, unless the corporate adopt these college and institutions by developing endowments and grants while simultaneously interacting with those institutions by providing feedback on the core experience, This is called using the case basis.

That apart, all people today are at cross roads, and are not clear which direction to move, as every direction is a free for all kinds of direction. That is the reason why now consulting companies like Arthur Anderson (India) country head - global corporate finance Mr. Munesh Khanna says in an interview to Economic Times to Pallab Dutta “major revenues will come from advising on e-commerce architecture for existing as well as new clients. Not to forget the big and diversified brick and - mortars that are web enabling their processes and scale of business operations." He also says "media is disseminating research and in - depth information about the New economy. Mere increase in bandwidth and net penetration alone won't speed up the progression to the information age.

Logistics and distribution channels also need 'to be in place, and this means more road highways, airports, ports, etc." Public finance experts are no longer there today and their areas are taken over by the corporate finance specialists / analysts and they are of some assistance to the government and in this process in India. Fiscal management is wobbling and playing tunes with the corporate finance wizards. There is less accountability to the tax payers and super friendliness with the corporate world which never bothers about the agriculture and farmer. This trend will continue for some more time.

Check your progress 6

1. ___________is looking for HR, people to contribute for operations and systems driven roles in compensation, employee relations, and career development activities of the bank.
   a. HSBC
   b. ICICI
2. ___________Limited says it has 50 years of corporate leadership in diversified fields and it is one of the most successful Trading Houses in India.
   a. MRF
   b. JK

3. ________channels also need 'to be in place and this means more road highways, airports, ports, etc.

   a. Logistics and distribution

   b. Connecting

2.8 Let Us Sum Up

In this unit we had a detailed discussion on globalisation and its impact on financial services.

In this unit we studied that a very large number of financial services providers are now conducting business across national borders. Some financial services, by their very nature have been global for a time now. Some of the stimulus for globalisation has come from markets, technology, competition, costs and governments themselves. This unit discusses the impact of globalisation on financial services and outlines the charges that financial service provided would need to bring about in order to compete effectively in the new world order. Emerging Asian trends and their impact on financial services have also been discussed enable you to have a clear idea about the pervasiveness if; the impact of globalisation.

After this detailed discussion the readers would have certainly got a good idea about globalisation and how it has affected the financial services sector.

2.9 Answers for Check Your Progress

Check your progress 1

Answers: (1-a), (2-b), (3-a)

Check your progress 2

Answers: (1-a), (2-b), (3-a), (4-b)

Check your progress 3

Answers: (1-a), (2-b), (3-a)

Check your progress 4

Answers: (1-a), (2-b)

Check your progress 5

Answers: (1-a), (2-b)

Check your progress 6

Answers: (1-a), (2-b), (3-a)

2.10 Glossary

1. **Fund Based Services -** Financial services firms that cater the short-term term needs of funds of corporate sector and others are in the funds-based services.
2. **Terrestrial -** Wordily.

2.11 Assignment

What are the key drivers for globalisation of financial services? Discuss with respect i to the Indian scenario.

2.12 Activities

1. How has rapid globalisation affected the local providers of financial services?
2. What are some of the trends discernible in the Asian Markets in the wake of globalisation? Briefly discuss.

2.13 Case Study

Enumerate the opportunities that globalisation provide for financia1 service provide.

2.14 Further Readings

1. Sandra Vandermerwe and Micheal Chadwick, "The Internationalization of Service”, the Service Industry Journal, January 1989.

2. Micheal E. Porter, "Changing Patterns of International Competition", Ccdgornin Management Review. Vol. 26, Winter 1986.

3. George S. Yip, "Total Global Strategy: Managing for Worldwide Competitive Advantage", Englewood Cliffs, N.J. Prentice Wall 1992.

Block Summary

This whole block revolves around the pension funds and there role in the society. After going through this block we understood what pension fund is and how it plays a very important role in the society.

In this detailed study we understood the need and importance of pension in our society, not only the need and importance but we also studied the various kinds of pension funds policies that are playing a significant role into our society. In unit 1 we went through the general fund investment guidelines. In the same way under unit 2 we had a detailed discussion on the effect of globalization on the financial service markets. What has been the effect of globalization on the local market; some of the recent trends have even been discussed here in very detail.

The readers would certainly get benefitted after going through this block and they will learn a lot about the topics.

Block Assignment

Short Answer Questions

1. Pension Funds
2. Need for Reforms in Social Security
3. Pension plan
4. Asset classes and diversification
5. Pension Funds And Capital Markets
6. Globalisation
7. Globalisation of financial market
8. Types of globalisation drives
9. Financial services
10. Globalisation and consumer orientation

Long Answer Questions

1. What are the risks associated with pension plans? Can these risks be managed? How?
2. How is the consumer orientation of financial service provider likely to change in times to come?
3. In terms of evolving effective marketing practices, what are the main imperatives the financial service providers should follow?

Enrolment No. ____________

1. How many hours did you need for studying the units?

Unit No	1	2	3	4
Nos of Hrs				

2. Please give your reactions to the following items based on your reading of the block:

Items	**Excellent**	**Very Good**	**Good**	**Poor**	**Give specific example if any**
Presentation Quality	☐	☐	☐	☐	______
Language and Style	☐	☐	☐	☐	______
Illustration used (Diagram, tables etc)	☐	☐	☐	☐	______
Conceptual Clarity	☐	☐	☐	☐	______
Check your progress Quest	☐	☐	☐	☐	______
Feed back to CYP Question	☐	☐	☐	☐	______

3. Any Other Comments

……………………………………………………………………………………………

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Education is something which ought to be brought within the reach of every one.

- Dr. B. R. Ambedkar

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'Jyotirmay Parisar', Opp. Shri Balaji Temple, Sarkhej-Gandhinagar Highway, Chharodi,
Ahmedabad-382 481.