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INNOVATE OR DIE NEW MANTRA OF MODERN DAY BANKING

***Shyam Ji Mehrotra**

Abstract

Competition, convergence and consolidation are key drivers of banking these days. Competition breeds innovation and innovation breed's competitive advantage. To stay ahead of their competitors, banks like any other industry are trying new ideas (innovations) and reinventing existing products (renovations). 'Innovate or die' is new mantra of modern day banking.

'INNOVATE OR DIE' - NEW MANTRA OF MODERN DAY BANKING

- Innovation is application of ideas – new or existing - in new ways or in new fields or in new products. It helps an organization to cut cost, to improve profit and also to improve market share.
- Organizations often associate innovation with a product or process. In fast moving time that we live in, this is not enough. Today innovation means change in business model it-self.
- Innovation happened when TCS began to offshore information technology, or when Dhirubhai Ambani told his son, Mukesh, that only if he can price a call less than the cost of post card will his mobile business has future, or when Jack Welch set up a call centre at Gurgaon to answer queries raised by General electric customers in US, or when Lalit Modi introduced T 20 format in Indian Premier League.
- Winning companies recognize the need of 'out of box thinking' and are, therefore, creating culture where ideas keep flowing continuously. They design and place policy initiative to encourage, facilitate, manage and

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documents innovations by employees. Those who do not innovate, join the list organizations that drive themselves to oblivion. 'Innovation' is 'in' word in corporate philosophy now.

- Competition, convergence and consolidation are key drivers of banking these days. Competition breeds innovation and innovation breed's competitive advantage. To stay ahead of their competitors, banks like any other industry are trying new ideas (innovations) and reinventing existing products (renovations). **'Innovate or die' is new mantra of modern day banking.**

CUSTOMER IS DRIVING INNOVATION

Customers buy not because they understand the product or service because they feel that the bank understand their needs and wants. Customer centric innovation flips traditional **'design – produce - sell'** model into **'design – redesign – innovate – produce - market'** model. In fact it is the changing needs of the customers that drive innovation.

Innovations come in two forms - the quantum leap type innovation and incremental innovation. Quantum leap type innovation in the financial services industry may not come very often but incremental innovation is now order of the day. Engaging with the customer is first step in the innovation process, which provides strong insights for value addition.

'Walking with the customer' is a strategic tool of innovation as strategically companies are now not only generating ideas internally but also open to ideas from customers and alliance partners. As one walk with the customer and is with him right through while selecting, buying and using a product, one can identify great deal of happening that can be used for creating (innovation) new products or modifying the existing products (renovation). Walking with the customer is a strategic tool of (a) mapping the customer's need by analyzing activities that customer performs while selecting, purchasing or using a product, (b) locating *the gap based on unfulfilled or expected needs and wants and (c) closing the gap by introducing new products (innovation) or modifying existing products (renovation) as per identified needs and wants.* Customer thus teaches everything including what you should innovate.

INNOVATE TO STAY AHEAD – A NEW BANKING PARADIGM -

Since each product has its life cycle, banks are required to continuously innovate and renovate products so that new/renovated product can replace the existing product by the time its life cycle is over or new product is launched by its competitors. Creation/ modification of products are done either through value creation (new products) or value addition (new features) or value affordability (less price or no frill products). Of late there is a paradigm shift in product development with regards to process, pricing, place (delivery channel), packaging, people and partnering by the banks.

(Following paragraph will enlighten the readers with paradigm shift taking place in banking industry through innovation. List is only illustrative not exhaustive).

DEPOSIT PRODUCTS

Accepting deposit is basic function of banks. From core deposit products like savings account, current account and fixed deposit, banks have gone a long way in offering value added deposit products like monthly income plan, reinvestment plan etc. Some emerging innovations are: -

- Opening of no-frill savings accounts with zero balance is recent innovation, which has been introduced at the instance of Reserve Bank of India for financial inclusion of poorer section of the society. It is built on the concept of value affordability so that customer can enter the market with cheap entry-level product and thereafter use the product as per his capacity.
- Tax-incentive on term deposit is another recent development. Banks have structured deposit products of specified maturity to attract investors who were hitherto parking their funds in small savings schemes of post office, life insurance etc. for tax savings.
- Floating rate of deposit products where interest rate is linked to some benchmark rates like inter-bank call money rate or base rate have been introduced by some banks. These products assure market related return to depositors. They also help the bank in mitigating interest rate risk and overcoming ALM problem.
- New deposit products with auto investment facility in mutual funds (debt funds or equity funds) are also evolving with objective of maximizing return

to the depositors. Since dividend income (in the hand of investors) and capital gain (long term) is exempted from tax, these products have become very attractive.

RETAIL CREDIT PRODUCTS

Given the microeconomic scenario, it is expected that retail loan segment will grow at 35% CAGR. Seeing big opportunity ahead, banks have become aggressive in retail loans and attracting customers with innovative offerings. Some recent innovations in retail credit products are-

- Pre approved housing loan so that customer can select the property of his/her choice as per his/her financial resources.
- Pre approved personal loan so that customer can draw the amount as per his convenience as and when he needs money.
- Pre approved housing properties that save the borrowers from hassles of going through formalities of title examination and valuation.
- Bridge loan against mortgage of existing house to enable the borrower to buy a bigger house and loan will be repaid from sale proceeds of old house.
- Overdrafts against security of house property, which house owner generally, feel as unproductive.
- Variants of personal loan like loan for purchase of jewellery, loan to meet tax liability, loan to meet festival expenses, loan to meet critical sickness etc.
- Home loan with 'repayment holiday' - to enable the borrower to tide over unexpected financial needs like tax liability, educational expenses of children or expenses of critical illness.
- New home loan product launched is 110% home loan requirement. Extra 10% is for furnishing the house, which comes along with the home loan.
- Overdraft through ATM to privilege customers to meet emergency requirements.

NEW FINANCIAL SERVICES

- Banking to unbanked has become win-win model for the bank and the poor. A recent case study of a bank branch in Dharavi in Mumbai suggested

that how this place in financial capital of the country remained neglected till 2007 when a bank opened the branch there and how this branch mobilized business of Rs. 44 crores in just two years and thereafter many other banks lined up for opening branches and ATM in that area.

- e-Commerce is opening up opportunities for bank to act as intermediaries for authenticating transaction between retailer and consumer through digital signatures. So far banks are issuing guarantee and letter of credit by giving assurance to seller that he will get the payment of goods/services sold and authentication of e-transaction is a logical extension of bank guarantee and letter of credit business.
- Integrated financial services provided by financial advisers who assist customer in executing long term saving and investment plan to achieve individual financial goals is also an emerging area.

RISK FREE INCOME

Banks are innovating by leveraging on their credit dispensation strength to augment risk free income through variety of ways like-

Originator of Loan

Banks mobilizes credit proposal, syndicate the loan but will not carry in their books. Earn income as originator. LIC has huge corpus of funds but cannot directly lend. Here originator has opportunity.

Monitoring Fee

Transfer loan to SPV or other banks through securitization process but continue to earn fee-based income for monitoring of loan. Even in case of sale of distressed assets to ARC, bank has opportunity to earn monitoring fee, as they know the assets better than the buyer.

Take Out Finance

Largely resorted to for infrastructure projects where the loan is taken up by other institution after a specified period to overcome problem of assets liability mismatch.

Money Transfer Business

Money transfer business is growing with the growth of remittance in India which is estimated at \$22 billion annually. And banks are tying up with money transfer companies like Western Union Money Transfer to offer this service to their customers.

Financial Advisors

From relationship manager to financial advisor to private banker- all services are for fee. Banks are now offering discretionary portfolio management services- investment in art, philanthropy, real estate, funds within country and in offshore funds - for its affluent customers all under one roof. Under property advising services bank guide customers about entire process of selecting and buying a house and handle the cumbersome documentation formalities and the registration on his behalf.

Gold Hedging Services

Most Indian gold jewellery manufacturers are now hedging their gold purchases in Dubai Commodity exchange in absence of such facilities in India. A few private sector banks have seen business opportunity here and are offering gold-hedging products. The gold traders and jewellery exporters are expected to avail gold hedging service, which has very lucrative market.

SELLING OF THIRD PARTY PRODUCTS

- Starting from selling free personal accident to holders of credit card, ATM cards, banks have gone a long way of cross selling various insurance products like life insurance to savings banks account holder, credit protection bundled with education loan, housing loan and other loan, loss of baggage and other insurance bundled with NRI accounts. These innovations are offering business avenues of earning fee based income by selling products on behalf of third party where banks have no expertise or product offering is not possible due to regulatory constraints.
- Apart from selling insurance and mutual funds, banks now see opportunity in selling gold coins and bars to earn extra fee based income. Buyers find investment in gold as attractive option since interest income in fixed deposit is comparatively low to increase in the price of gold in the recent past. Since

gold coins and bars are hallmarked and are backed by quality assurance of bank, buyers feel secured.

- Selling of stamp papers, collection of utility bills like electricity, telephone and school fees, collection of taxes for the state and central government, payment of pension of government, railway and defense pensioners, safe keeping of examination papers, credit/debit cards in alliance with other banks etc., are fast expanding fee based services.
- Prepaid cards is recent innovation, which has substituted gift cheques and traveler cheques. These cards act like a debit card, which can be used by the holder for purchasing any article/good from approved merchants up to the value of the card or paying foreign exchange for payment of services for business, studies or medical reasons. Bank earns extra fee based income by selling such cards by way of upfront fee, reload or reassurance charge, refund charge etc.

SALE OF IMPAIRED ASSETS

RBI has made the beginning by putting in place the policy of buying and selling distressed assets in policy announcement of 2005. Indian bad loan market is sizeable and provides immense business opportunity. And the driver of the market is potential profit.

NEW CREDIT PRODUCTS

Commodity Finance Business

Commodity financing business has brought new revolution in credit business. Banks are innovating products to lend to farmers and traders in collaboration with commodity exchanges against demat warehouse receipts of gold, silver and other commodities. Collateral managers are also designing new products to assist banks in undertaking due diligence (credit risk), guaranteeing quality and safety of the commodity (operational and performance risk), documentation (legal risk) and insurance (default risk). India's commodity trading is estimated to Rs. 400,000 crores annually and offers good business opportunity.

Asset Based Financing (ABF)

Asset base financing started from transportation segment (mainly truck

financing) and is gradually spreading into financing of bulk machinery like printing machinery, road building equipments, medical equipments etc. To mobilize business banks are entering into business alliances with the manufacturers and offering credit to buyers backed by security of assets crated out of the bank loan.

Channel Financing

- Channel financing is an innovative finance mechanism by which banks meets the various funds requirements along with supply chain at the supplier's ends itself, thus helping him in seamless cash flow along the arteries of the enterprise. Channel finance ensures the immediate realization of sales proceeds for the client's supplier, making practically a cash sale. Under channel financing, the dealer can leverage on the relationship with reputed companies in sourcing low cost credit with support from their counterparts. Under channel financing following credit facilities are available-
- Discounting of trade bills accepted by the dealer/distributor.
- Limited overdraft facility to dealer/distributor for his business dealing with large corporates.

Micro-Credit through On-line Route

Inspired by global efforts, some websites are providing platform to HNIs and professionals who want to extend credit to rural entrepreneurs and wants to make difference in the life of rural poor. These websites employ crowd-funding techniques, informing and encourage common people online to act as investors in microfinance space aimed at the small borrowers and tries to seek investment from them where business plan inspire and suits them. For example Chennai based Rangde lends mainly to women and Bangalore based Dhanax reaches out to self help group in urban area. They also encourage people to contribute beyond investing, volunteering time and efforts for the social development.

DELIVERY CHANNELS

Banks now have multi channel approach, which add convenience to customers on one hand and cost effectiveness to banks on the other hand. ATMs are now gradually becoming more popular and offering 24X7 facilities to customers. While mobile ATMs are bringing service to customer doorstep, there are specialized ATM for blind, solar powered ATMs for rural areas, Barcode enabled ATM for

payment of bills and so on. Sunday banking and 8 AM to 8 PM banking is other innovation, which has totally transformed the delivery channel.

CAPTIVATING THE CUSTOMER THROUGH INNOVATION – A NEW LEARNING CURVE

Walk in business is the thing of past. The customers are now not only demanding on price (interest rates, service charges etc.), they are also demanding on product (quality), place (home delivery, internet banking), packaging (brand affinity), people (customer service), partnering (business alliances, direct selling agents), and promotion (discount, freebies etc.). Due to this old business model of 'capturing customer through aggressive selling' has given way to new business model of 'captivating the customer through innovation'.

NEW LEARNING CURVE IS

Shift Focus from Product to Customer

- You need to appreciate that the Customer is Queen.
- Anticipate and adapt as per customer's changing need and demand –
- **You need to continuously innovate or renovate your product to stay ahead of your competitors.**
- Take speedy action and decision to **have first mover advantage.**
- Make effective implementation- **Idea alone cannot deliver.**

LOOKING AHEAD

Indians are known to have good culture of innovation but bad for execution. Hence, bank people should learn not only to innovate but also to implement innovative ideas into practice. Next big thing is learning to accept change. The person with the best idea may not win but a person who learns the fastest wins. The lesson is learning the change is as essential as innovation. Next important thing for innovation is speed. The success of innovation lies in speedy implementation of the new ideas before the competitors are able to copy them. Lastly Indian banking industry is hugely under-penetrated industry and it is expected that with innovation, banks will be able to make inroads in the new markets by putting the customers at the centre of everything they do.