INVESTMENT & MERCHANT BANKING

GUIDELINES FOR ANSWERING ASSOCIATE EXAMINATION - FEBRUARY 1999

INVESTMENT AND MERCHANT BANKING

SECTION I

Q 1. **Select the correct answer**

(a) **If the real rate of return on capital is 9% expected rate of inflation is 5% and risk premium is 2%, the investor should earn return on investment @ --**

i) 5% ii) 7% iii) 9% iv) 16%

(b) **Growth funds is a mutual fund that**

i) assures growth in income ii) Invests in fixed income securities

iii) invests primarily in equities iv) gives fixed return

(c) **Normal yield curve is**

i) downward sloping ii) flat

iii) upward sloping iv) inverted

(d) **When interest rates go up, the current yield on fixed rate bond**

i) does not change ii) rises iii) falls

(e) **The principle of diversification of investment enables the investor to eliminate**

i) unsystematic risk ii) systematic risk

iii) investment risk iv) economic risk

Q 1 a **If the real rate of return on capital is 9% expected rate of inflation is 5% and risk premium is 2%, the investor should earn return on investment @ --**

Ans 1a 16%

Expected return on investment = Rate of return on capital (9%) +

Expected rate of inflation (5%)

and risk premium (2%)

Q 1 b **Growth funds is a mutual fund that**

Ans 1 b Invests primarily in equity

Growth Fund is mutual fund which is primarily meant for investment in equity shares and give the benefit of appreciation in capital.

Q 1 c **Normal yield curve is**

Ans 1 c Upward sloping

Short term interests are lower and the long term interest rate is higher. Hence the yield curve is upward sloping.

Q 1 d **When interest rates go up, the current yield on fixed rate bond**

Ans 1 d Answer not given

Q 1 e **The principle of diversification of investment enables the investor to eliminate**

Ans 1e Unsystematic risk.

Unsystematic risk is the risk arising from firm specific factors like production, availability of raw material, new substitutability products, etc., which is non market risk and can be reduced by diversification of portfolio into several securities.

SECTION II

Q 2. **Answer in 3 to 4 lines why the following statements are true or false.**

- **(a) Mutual funds work on the principle of diversification of risk.**
- **(b) Increase in the Cash Reserve Ratio can cause yield curve going inverted.**
- **(c) Credit rating agencies determine the rate of interest on debenture instruments.**
- **(d) Badla is a method of financing stock market transactions.**
- **(e) Increasing dematerialisation of stocks will remove small investors' problems.**

Q 2 a **Mutual funds work on the principle of diversification of risk.**

Ans. 2. a True - Mutual Funds mobilise savings of large number of investors to invest in both debt and equity securities. A large pool of funds enables the Mutual Funds to diversify risks into different companies and industries and thereby minimise risk and optimise return for investors.

Q 2 b Increase in the Cash Reserve Ratio can cause yield curve going inverted.

Ans. 2. b True - The normal yield curve is an upward sloping curve. Increase in the Cash Reserve Ratio reduces short term liquidity of commercial banks. Hence, the call money rates and other short term interest rates tend to go higher than the long term interest rates turning the yield curve from upward sloping into downward sloping and becoming inverted.

Q 2 c Credit rating agencies determine the rate of interest on debenture instruments.

Ans. 2. c False - Credit rating agencies do not determine interest rates on debenture instruments. The agencies give credit ratings in a pre-determined scale to companies and their debt instruments.

Q 2 d Badla is a method of financing stock market transactions.

Ans. 2. d True - In a stock market transaction, if the delivery is not given or taken on the settlement day, the participants can carry forward their transaction by paying a rate of interest on borrowed funds which is known as badla.

Q 2 e Increasing dematerialisation of stocks will remove small investors' problems.

Ans. 2. e True - Dematerialisation of stocks have made the clearing, settlement, delivery and transfer of shares on electronic system. Hence all the problems relating to settlement, delivery and transfer involving bad delivery do not arise and the transfer is instantaneous and quick. Similarly electronic clearing does not require any stamp duty to be paid. Hence small investors will benefit immensely from this.

SECTION III

Q 3. Write critical notes with practical illustrations/graphs on any three of the following.

(a) Price Earnings (PE) Ratio and valuation of equities.

(b) Capital Asset Pricing Model (CAPM)

(c) Yield Curve and Treasury Management

(d) Certificates of Deposits (CDs)

(e) Convertible Debentures

Q 3 a Price Earnings (PE) Ratio and valuation of equities.

Ans. 3 a Financial analyst use the price earnings multiple approach to reach the intrinsic value of the share as one of the tools.

The P/E multiplier is defined as the market price of the stock divided by the last reported earnings per share. This referred as the historical P/E. The prospective P/E is the closing market price divided by the next years estimated earnings per share (EPS). As the market price changes the P/E ratio (PER) also changes every dya. Many of financial dailies carry the PER numbers, some of them also incorporate the unaudited annualised half yearly profit after tax figure in the calculation.

For example the firm XYZ, financial numbers are :

Face Value = Rs. 10

Market Price = Rs. 220

Profit After tax = Rs. 12 crore

1996-97 (March end)

Estimated Profit After Tax= Rs, 15 crore

1997-98 (March end)

Equity Capital

Then Historical EPS (1996-97) = Rs. 12

Historical P/E (1996-97) = Rs. 18.33

And Prospective EPS (1996-97) = Rs. 15

Prospective P/E (1996-97) = Rs. 14.66

The PER or the P/E multiplier is primarily used by the analyst as a thumb rule. The ratio is dependent on the riskiness of the firm and the rate of growth of earnings. High PERs are associated with companies which are large in size and have created sustainable entry barriers in the business. Companies which have hidden values like brand owned or technological expertise also trade at high PER multiples. On the other hand the low PER are associated with companies in industries having low rates of growth or are cyclical in nature. Also players which are small in size and are exposed to greater business risk are traded at low valuation multiples.

Some of the major factors which are taken into account to get the PER multiplier for a company stock are :

- Estimated Growth Rate
- Quality of Management
- Dividend Payout Ratio
- Size of the company
- Quality of Earnings
- Stability of Revenue
- Nature of Business
- Extent of Institutional Ownership

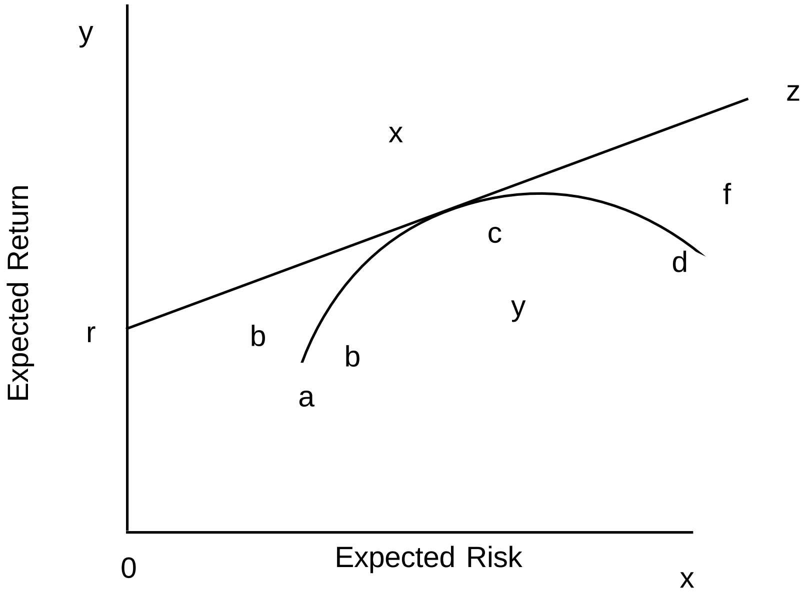
Q 3 b Capital Asset Pricing Model (CAPM)

Ans. 3. b Capital Asset Pricing Model : Every investment is concerned with return thereon and risk attached thereto. Returns tend to be lower where the risk is lower and vice versa. The objective of an investor is to achieve the optimal combination of risk and return. Capital asset pricing model helps an investor to achieve optimal portfolio position.

There are protfolio combination of investments A, B, C, D and F that will produce the lowest levels of risk at each of these levels of expected return. The set of protfolio combinations that produces the lowest possible levels of risk at each possible level of expected return is called the **efficient frontier.** The efficient frontier is the set of optimal or dominant portfolios that provides the lowest levels of risk at a given level of expected return. the efficient frontier graphed below. The efficient set, or the set of optimal portfolios, will nearly always be composed of well-diversified portfolios; therefore individual investments below ABCDF will generally not be on the efficient.

Through diversification, the investor can achieve a higher level of expected return at the same risk level afforded by individual investments. Because different investors may choose different levels of desired returns, there is an infinite number of optimal portfolios that can be constructed from a given set of investments and their risks and expected retruns.

Once an investor has chosen an optimal portfolio, it should be evaluated periodically to determine if it still meets the risk and expected return objectives. If it does not, then a restructuring of the portfolio may be required. One technique commonly used to evaluate portfolio performance is the capital market line. The capital market line **(CML)** is a theoretical equilibrium pricing model that sets forth the required relationship that should exist between the expected return and risk of efficient portfolios. RZ is the CML where OR is the risk free rate of return.



The CML relationship, states that the expected or required return on a portfolio should equal the sum of two elements : (1) the return on a risk-free investment, r, and (2) the risk premium. The CML is a tool, or benchmark, by which an investor can gauge the risk-return performance of a particular portfolio. For example, if the actual return exceeds the sum of these two components, such as is illustrated in figure by Portfolio X, whose risk / expected-return combination lies above the CML relationship, then the portfolio has earned a return in excess of what is requires. On the other hand, Portfolio Y has earned a return that is less than what the CML predicts as appropriate; hence its risk/expected return combination is below the CML lime.

The CML as described above reflects the relationship of total risk and expected return. Total risk includes both systematic and unsystematic risks. It may also include the risk free assets to reduce the total risk. This has two components of the capital market return, which are reward for waiting or riskless return, and the reward per unit of risk borne as measured by the slope of the CML line.

The investors will have their choice of efficient portfolio somewhere along the line of CML, as all efficient portfolios would be on it. Those which are less efficient will be below the CML, in the chart above. The internal rate can be thought as the price of time and the slope of the capital market line as the Price of Risk. The investor would prefer investment portfolio which would be the optimum portfolio for risk-return trade off. CAPM then helps in identifying the optimum investment portfolio.

Q 3 c Yield curve and Treasury Management

Ans. 3. c **Yield Curve :** The relationship between long term and short term rates of a similar risk asset/ bond is known as Term Structure of Interest Rates. Yield Curve is a graphical representation that compares the interest rate of securities with different terms to maturity. To construct an Yield curve a set of bonds in the same risk category but with different maturities is selected. On the 'x' axis term to maturity is plotted and on the 'y' axis, their respective yields. If we join the points, we have a yield curve ready. There are four types of yield curves as follows :

i) Positive yield curve or an upward sloping yield curve. Here the interest rates show an upward trend as maturity increase. hence this is known as Positive yield curve or normal yield curve. This curve indicates that market expects yields to rise on account of the economic activity and to get overheated.

ii) Inverted yield curve or a downward sloping yield curve is formed when the short term interest rates are higher than the long term interest rates. As this situation is unusual, this curve is called 'inverted yield curve'. This curve indicated that the market expects the yields to fall on account of economic recession.

iii) If short term and long term interest rates are the same, the curve formed is a flat yield curve (a straight line). This situation rarely happens.

iv) A humped yield curve forms where there is a rise in the short term rates and then a fall in the medium term and the rate gradually tapers off in the long term. This indicates an uncertainty / aberration in the maturity where the hump occurs. If the treasury is accurate in forecasting and finds any opportunity in such maturities, he can take advantage by shifting his trading portfolio partially to advantageous position.

Regarding some major functions and operations of the treasury

Maintenance of Reserves is one of the major functions of the treasury. This is mainly because the Reserves are maintained on the overall financial figures of the Bank and no other department of the Bank other than Treasury will be able to handle it effectively. On account of Treasury's role/active involvement in bank's major day to day operations, Treasury can manage the Reserves Maintenance more effectively than others. While CRR management is directly related to the overall liquidity position of the Bank on day to day basis, SLR Management is nothing but management of more than 30% of the Assets of the banks.

Selecting the Portfolio Strategy

Almost 30 to 40% of the asset base of the banks now consists of Govt. stock and other Bonds/

debentures. The types of Bonds are varied - Fixed income, floating rate, zero coupon, step up/ down, Liquid, option embedded, Indexed, Staggered / bullet repayment, Flexi - and some of them are on private placement, unrated, unlisted etc. Since a huge proportion of Bank funds are deployed in these debt instruments, its management assumes a very important factor in the overall profitability/risk exposure of the bank. As some of these instruments are traded/ tradable in the secondary market, treasury has a major role in the management of this portfolio. Bank Treasury has to manage the portfolio with strategies that can play an integral role in meeting overall Assets and Liability managements goals. With Treasury's trading and distribution skills, non-fund based income can be generated apart from providing liquidity to the portfolio. An Active Treasury should shuffle the Investment portfolio of the Bank - by adjusting maturities, changing the composition of the securities (taxable versus tax free, Gilts vs. debentures etc.) swapping the securities - and achieve the objectives/policies in the changing market environment. Treasury that targets to earn a rate of return that consistently exceeds the opportunity cost of funds will create long term share holder value.

Treasury has to consider many factors while determining which securities to buy or sell. Risks arise because it is very difficult to outperform the market when forecasting interest rates. Treasury must also be aware of the bank's overall interest rate risk position to make investments that offset the prevailing risk or enhance returns as targeted. A treasury with passive strategy, - passive because of the internal policies restricting its powers, its risk taking decisions, etc., just adopt 'buy & hold' strategy. Because of this they select maturities that generate average retruns over the entire business cycle. Whereas an active treasury shuffles the portfolio based on the forecasts, hedges the portfolio from risks it is exposed, trade in securities and generate non-fund based income.

Riding the yield curve

Riding the yield curve is a common active strategy adopted by the Treasury when the yield curve is upsloping (positive) and rates are relatively stable. It involves buying securities with a maturity longer than the planned holding period and selling the security at a gain prior to its maturity. It has three basis steps.

i) Identify the preferred investment horizon.

ii) Buy a par security with a maturity longer than the investment horizon, for which the coupon yield is high in relation to the overall yield curve.

iii) Sell the security when the preferred time elapses with still more time remaining until maturity. If yields remain relatively stable, the overall return will exceed that from simply buying the security that matches the planned investment horizon.

Q 3 d Certificate of Deposits (CDs) :

Ans. 3 d The CDs are negotiable term-deposits accepted by commercial banks from bulk depositors at market related rates. The CDs can be issued by scheduled commercial bank (excluding RBBs) at a discount to face value for a period from 3 months to one year. The CDs can be issued for a minimum amount of Rs. 25 ;lakhs to a single investor in the minimum denomination of Rs. 5 lakhs. There is, however, no limit on the total quantum of funds raised through CDs. The discount on CDs is deregulated and is market determined. The CDs can be negotiated only after 30 days from the date of issue to the primary investor. The CDs are to be reckoned for reserve requirements and are also subject to stamp duty. Banks are prohibited from granting loans against CDs and buyback their own CDs.

As stated earlier, CDs are issued at discount to face value. The discount is offered either front end or rear end. In the case of front-end discount, the effective rate of discount is higher than the quoted rate while in case of rear end discount, the CDs maturity yield the quoted rate. This can be explained as under :

1) CDs issued at front-end discount

Amount of Issue	:	Rs. 100/-
Period	:	3 months
Rate of discount	:	15%

$$\text{Discount} = 100 \times \frac{15 \times 3}{100 \times 12} = \text{Rs. } 3.75$$

Hence CD will be issued for Rs. 100 - 3.75 = Rs. 95.25. The effective rate to the bank will, however, be calculated on the basis of the following formula :

$$ED = 1 + \frac{D \qquad M}{100 \times M} - 1 \times 100$$

where, ED = Effective discount rate

D = Quoted discount rate

M = Period - 12/3 or 365/91

$$ED = \left(1 + \frac{15}{100 \times 3/12}\right)^{3/12} - 1 \times 100$$

= 15.86%

2) CDs issued at rear-end yield

Amount, period and rate of discount being the same, rear-end discount value can be calculated with the help of the following formula :

$$DP = \frac{1200}{1200 + r \times p} \times F$$

Or

$$\frac{36500}{36500 + r \times P_1} \times F$$

where DP =Discounted price of CD

r = rate

P_1 = Period

F = Face value

$$\frac{1200}{1200 + 15 \times 3} \times 100 = \text{Rs. } 96.3855$$

Thus, the issuing bank has reduced its effective cost of borrowing.

The CDs was introduced in June 1989 with the primary objective of providing a wholesale resource base to banks at market related interest rates. The instrument was effectively used to cover certain volatile asset sources and has since emerged as an instrument for effective asset liability management. Free transferability of instrument assures liquidity to the instrument. Banks can invest in CDs for better funds management; such investments besides yielding high return can be netted with liability to the banking system for CRR/SLR purpose. This type of asset also attracts only less risk weight under Capital Adequacy Standards.

The CDs market witnessed a spurt in activities during 1995-96 against the backdrop of liquidity crisis. While the amounts raised through CDs have increased to Rs. 21331 crores as on June 21, 1996, the discount rate on CDs moved sharply to a high range of 18.0 - 19.0% in March 1996. The rates of interest have since then declined substantially due to high rate of deposit growth and poor credit offtake resulting in higher liquidity situation.

Q 3 e Convertible debentures :

Ans. 3 e A convertible debenture, as the name suggest, is a debenture that is convertible, partially or fully, into equity shares. The conversion may be compulsory or optional. In the last few years convertible debentures have assumed tremendous significance in India.

Features of Convertible Debentures:

Convertible debentures in India, for practical purposes, are of relatively recent origin. Yet during this short period the features of these debentures have undergone significant changes. In the early eighties when they became prominent for the first time they were typically compulsory convertible (partially or fully) at a stated conversion price on a predetermined date. The terms of such debenture were fixed by the Controller of Capital issues. Towards the end of eighties, more particularly in 1989, a strange aberration occurred. In that year several convertible debenture issues were made which had the following features : (I) they were compulsorily convertible (fully or partially) in one or more stages, (ii) the conversion price was left open to be determined later by the Controller or Capital Issues, and (iii) the issuer was given some latitude for determining the timing of conversion.

With the repeal of the Capital Issues Control Act and the enactment of SEBI Act in 1992, the rules of the game applicable to convertible debentures have changed. As per SEBI guidelines issued in June 1992, the provisions applicable to fully convertible debentures (FCDs) and partially convertible debentures (PCDs) are as follows :

* The conversion premium and the conversion timing shall be predetermined and stated in the prospectus.
* Any conversion, partial or full, will be optional at the hands of the debenture holder, if the conversion takes place at or after 18 months but before 36 months from the date of allotment.
* A conversion period of more than 36 months will not be permitted unless conversion is made optional with "put" and "call" options.
* Compulsory credit rating will be required if the conversion period for fully convertible

debentures exceeds 18 months.

From the SEBI guidelines it is clear that convertible debentures in India presently can be of three types.

(a) Compulsorily convertible debentures which provide for conversion with 18 months.

(b) Optionally convertible debentures which provide for conversion within 36 months

(c) Debentures which provide for conversion after 36 months but which carry "call" and "put" features.

There are two popular motives for issuing warrants and convertible debentures. (I) They allow companies to issue debt cheaply. (ii) They provide companies an opportunity to issue equity shares in future at a premium over the current price.

To the companies convertible debentures enable raising of funds at a lower cost and to investors it is attractive due to possibility of good capital appreciation and finally higher rate of return. The debentures have been very popular among the companies in India for raising resources. Modern finance offers superior explanation for the popularity of convertible debentures and debentures with warrants. These instruments have appeal because they improve cash flow matching and generate financial synergy, and mitigate agency problems.

Q 4. Answer any two of the following questions.

(a) Discuss the advantages of mutual funds for small investors. What are the Money Market Mututal Funds ?

(b) Discuss the role of National Securities depository Ltd. (NSDL) in the capital market.

(c) Discuss the interest risk and liquidity risk management in a commercial bank.

(d) Discuss the role of merchant banker in a primary market issue management.

Q 4 a Discuss the advantages of mutual funds for small investors. What are the Money Market Mututal Funds ?

Ans. 4 a Mutual funds represent pooled savings of numerous investors invested by professional fund managers as diversified portfolio to obtain optimum return on investments with least risk to the investors.

Mutual fund earns income by way of interest or dividend or both from the securities it holds. It deducts fees, operating expenses and a management income and then passes the remainder to wealth holders through dividends on the mutual fund share. The dividend fluctuates with the income on mutual funds investments.

Mutual Funds can be open ended or closed ended and income funds, growth funds or balanced funds.

Open ended schemes :

Open-ended schemes are available for subscription all the year round excluding the period of book-closing. They may or may not have a specified redemption period. For instance, UTI's Unit Scheme 64 has no prescribed time limit when it would be redeemed. The sale and repurchase prices are fixed by the mutual fund concerned from time to time. Repurchases are generally allowed at specified rates.

Close-ended schemes :

These are open for subscription only during a specified period. Generally the redemption is also specified, and this means that they terminate on certain specified dates when the investors can redeem their units. The duration of the scheme varies; normally it is five to seven years.

Income Funds : Income fund is established to maximise the current income (i.e. interest and dividend) of investors. There are two aspects of income funds viz. Low investment risk generating constant income and high investment risk generating maximum income. Investment is made in various combinations of high yielding common stocks and bonds with a view to extract income on regular basis with safety of the principal amount of investment. Conservative investment strategy dominates the income funds with modest amount of risk.

Growth funds : Growth funds carry principal objective of capital appreciation of the investment over a period of time. The investment is made in equity stock which have above average growth potential. This is high risk investment fund with high capital gain potential and low current income assurance.

Balanced Funds : Some mutual funds are called as 'Balance Funds' where assets are a judicious mixture of industrial stocks and bonds. With a view to embrace modest risk of investment and secure reasonable rate of return the funds are employed in high grade common stocks with 25% to 40% investment in conservative fixed income securities like debentures, bonds and preference shares.

Mutual Funds are advantageous to individual investors in relation to their direct involvement in investment portfolio activity covering the following aspects.

(1) Reduced Risk : Mutual funds provides small investors access to reduced investment risk

resulting from diversification, economics of scale in transaction cost and professional finance management.

(2) Diversified investment : Small investors participate in larger basket of securities and share the benefits of efficiently managed protfolio by experts, and are freed of keeping any records of share certificates, etc. of various companies, tax rules, etc.

(3) Botheration free investment : Investors get freedom from emotional stress involved in buying or selling securities. Mutual funds relieve them from such stress as it is managed by professional experts who act scientifically with right innings in buying and selling for their clients.

(4) Revolving type of investment : Automatic reinvestment of dividents and capital gains provides relief to the members of mutual funds.

(5) Selection and timings of investment : Expertise in stock selection and timing is made available to investors so that invested funds generate higher returns to them.

(6) Wide investment opportunities : Availment of wider investment opportunities that create an increased level of liquidity for the funds holders become possible because of package of more liquid securities in the portfolio of mutual funds. These securities could be converted into cash without any loss of time.

(7) Investment care : Care for securities is available through mutual fund to the investors relieving them of various rules and regulations.

(8) Low investment and easy liquidity : Initial investment in units is as low as Rs. 1,000 in 100 units of Rs. 10 each prompting investors habits which they encash as per the term of the issue either through direct repurchase by mutual fund or through secondary market of listed securities.

(9) Tax benefits : Investors are allowed tax exemptions on investments made in mutual funds with a view to motivate them to invest in mutual funds and provide finance to industry.

Money Market Funds : Money Market Funds are used in short-term liquid assets like Certificate of Deposit (CDs) or commercial papers and for them capital is raised by selling shares to the investing public at a price equal to the asset value of the then existing shares outstanding plus a loading fee or service charge. This is known as high liquid assets funds with very low risk and virtually no capital loss. Interest income fluctuates because of volatile interest rates but investors get better yield than available from pass book saving accounts. In USA, Money Market Funds were step up in November, 1972 and have been very successful vehicle of savings mobilisation.

Eligibility to set-up MMMFs - At present, while scheduled commercial banks and public financial institutions and private sector funds are allowed to set up both Mutual Funds. MMMFs invest in money market instruments of high quality, short maturities and ensure high level of liquidity.

Money market instruments are generally of high denominations and small investors cannot directly invest their savings in them. It is only through MMMFs, their savings are invested in MMMFs instruments like Certificate of Deposits (CDs), Commercial Papers (CPs), 182 days Treasury Bills, etc.

An investor gets following advantages from investment in money market mutual funds.

1. Individual with short term investible funds park their funds temporarily in money market instruments until some long term avenue opens up.
2. Individual investors share through MMMFs the economic advantages of bulk purchases, expertise of professional fund managers and high yield on short term investments.
3. Individual investors are benefitted of high safety and liquidity of their investments which MMMFs provide because of their early redemption features and reduced risk resulting from diversified investments.
4. Individual saving habits get stimulated with readily available investment avenue for the short term.
5. Individual savers along cannot invest huge sums required for money market instruments as the minimum investment requirements for each of the money market instruments are very high because MMMFs are the vehicles of raising huge funds for short term requirements.

Q 4 b Discuss the role of National Securities depository Ltd. (NSDL) in the capital market.

Ans. 4 b India has among the largest number of listed companies in the world today. The large numbers in the capital market have given rise to a large amount of paper work, bringing with it the associated problems. Instances of wrong/forged signatures, stolen shares, forged/fake certificates, etc., pose a threat to security of investment. As a result of this, investors face a lot of inconvenience in effecting registration of securities in their favour and to ensure that they receive their share of divident, bonus, rights and other benefits. Indian as well as foreign investors have become wary of investing in the Indian capital market.

In this scenario, it was felt that the setting up of a depository and the introduction of scripless trading and settlement would improve the efficiency of the markets, thus eliminating the various problems brought about by dealing in physical certificates. This new system of keeping ownership records in the form of electronic holdings has a number of advantages over the existing system of physical securities. In the depository system, the physical movement of securities is replaced by a book entry system, under which the ownership is transferred by electronic entries.

In this backdrop, the Government of India promulgated the Depositories Ordinance in September 1995 , thus paving the way for setting up of depositories in the country. The Depositories Act has since been passed by both the houses of the Parliament in August 1996. SEBI notified Regulations under the Ordinance in May 1996 providing the regulatory framework for the depositories.

The Depositories Act has been framed keeping in mind the concerns of the small investor. Joining the depository system is not mandatory for the investor. The investor has the option to hold his securities in the depository, he can also withdraw his securities from the depository, if he so desires.

The National Securities Depository Limited (NSDL) is an organisation promoted by the Industrial Development Bank of India, the Unit Trust of India and the National Stock Exchange of India Limited to provide electronic depository facilities for securities traded in the equity and the debt market.

The **Industrial Development Bank of India** is one of the largest development banks in the world. It has been set up as the principal financial institution for providing credit facilities for the establishment and development of industries. The **Unit trust of India** is the largest Mutual fund in India established under the Unit Trust of India Act, 1963 with a view to encourage saving and participation in investments. The **National Stock Exchange (NSE)**, established with a view to provide a fair, efficient and transparent securities market to investors all over the country, has emerged as the largest stock exchange in India.

The NSDL has been registered by the Securities & Exchange Board of India on the 7th June, 1996 as India's first depository to facilitate trading and settlement of securities in dematerialised form.

Settlement of securities in dematerialised form will eliminate problems that are normally associated with settlement through physical certificates, like tearing/mutilation of share certificate due to careless handling, loss of certificates by postal authorities or registrars or investors, problems of bad delivery of shares. Cases of foregery of certificates will be eliminated in an electronic environment. Settlement of trades will be faster and hasslefree leading to shorter settlement cycles.

NSDL will perform the following functions through its various participants.

- enable surrender and withdrawal of securities to and from the depository (i.e., dematerialisation and rematerialisation)

- maintain investor holdings in the electronic form
- effect settlement of securities traded on the exchanges
- carry out settlement of trades not done on the stock exchanges (i.e. off-market trades)

Dematerialisation :

Dematerialisation is a process by which the physical certificate of an investor are taken back by the company/registrar and actually destroyed and an equivalent number of securities are credited in the electronic holdings of that investor. This is done at the request of the investor. An investor will have to first open an account with a depository participant and then request the dematerialisation of his certificates through the depository participant so that this dematerialised holdings can be credited into that account.

Electronic holdings can be converted back into certificates by requesting depository participant for the rematerialisation of the same. **Rematerialisation** is the term used for converting electronic holding back into certificates.

- SEBI has come out with a policy decision which requires all institutional trades to be shifted to the depository segment with effect from January 15, 1998 with respect to a select list of securities. SEBI will specify a list of such securities from time to time.
- SEBI has also decided that the depository settlement of trades will be made compulsory in a phased manner and SEBI will specify a list of such securities from time to time.
- Bank of India and Global Trust Bank Ltd. have announced a reduction in interest charges for loans against pledged shares in the electronic form compared to the interest charged for physical shares.
- As the dematerialisation process has gained substantial momentum in the recent past, NSDL has lowered its custody charges to depository participants to j3.5 basis points (0.035%) p.a. w.e.f. August 1, 1997, as against ear; oer charge of 7 basis points p.a.
- BSDL has announced a new scheme under which, if a company makes a one-time payment of 5 basis points (0.05%) of the average market capitalisation during the preceding 26 weeks, then NSDL will not charge any custody fees to the depository participants.
- Future issues by such companies would require a payment of 5 basis points on the new share capital credited. The valuation for the new shares will be done at issue price. Companies would not be required to pay any additional amount, if they make a bonus issue.

The NSDL today has 111 Depository Participants (DPs) with 1,400 service centres across the country, 617 companies which have signed up for dematerialising their shares with a market cap of Rs. 6,29,700 crore (US $ 145 billion) (over 75% of total market cap), and 15.58 lakh accounts, with a custody of 1,205.3 crore shares valued at Rs. 2,67,200 crore (US $ 61 billion) over 30% of total market cap). While the depository was a boon for large investors, even the retail investors have taken to the concept of demat enthusiastically, proving the skeptics wrong.

Q 4 c Discuss the interest risk and liquidity risk management in a commercial bank.

Ans. 4 c There are different techniques for measurement and management of interest rate and liquidity risks. Depending on the propensity of the risk, variety of techniques can be used. The techniques fall under general classification namely Traditional/direct method and Synthetic method. The traditional/direct method relies on changing the contractual characteristic of Assets and Liabilities in the Balance Sheet while Synthetic method depends on the use of innovative market instruments/derivatives like futures, Options, Swaps and Customised agreements. While direct method involving restructuring of the Balance Sheet may not always be possible. Synthetic methods gives flexibility to the Asset Liability Management (ALM) process as they are Off Balance Sheet activities. Moreover process of Asset Securitization can also be used to manage the Balance Sheet.

Three traditional/direct techniques namely Gap Analysis, Duration analysis and Simulation which are used in ALM. This will be followed by brief discussion on Synthetic method in ALM by using hedging instruments like Futures, Options, swaps, etc.

Gap Analysis

Gap analysis focus on managing Net Interest Income (NII) in the short term, objective being to achieve the targeted NII or improve it.

The GAP or mismatch risk is measured by calculating gaps over different time intervals based on aggregate balance data at a fixed point of time. Gap analysis measures mismatches between Rate Sensitive Liabilities (RSL) and Rate Sensitive Assets (RSA). The mismatch, i.e. Rate Sensitive Gap (RSG) is the difference between RSA and RSG. The gap values provide an indication of the effects interest rate movement on NII. In other words, when Assets and Liabilities fail due for repricing in different periods, they create a mismatch. Static Gap analysis considers the range of outcomes when Gap values are held constant. Dynamic Gap analysis allows Gap values to change along with changes in interest rates. A dynamic gap may lead to gain or loss depending upon how interest rates in the market tend to move.

Managing Interest Rate Spreads

GAP model suggests that a Bank which chooses not to speculate on future interest rates can reduce interest rate risk by obtaining a zero GAP. Then Bank is fully hedged because its interest rate risk is negligible. Alternatively, a bank may choose to speculate on future interest rates and actively manage the GAP. If the bank can forecast the interest rates and vary the GAP accordingly, it is difficult to vary the GAP actively and consistently win because interest rate forecasts may frequently go wrong. Many Banks adjusts the GAP only over short intervals while rate are rising or falling as expected relative to the business cycle. By adopting selected strategies, banks can enhance their incomes and values over business cycle.

Duration Gap Analysis

Matching the duration of assets and liabilities instead of matching the time until repricing is another way to approach Gap management. Many of the experts hold the view that measuring and managing Duration Gap is a more effective way to protect the value of an institution from interest Rate Risk than the traditional Gap management. Duration is defined as the weighted average time to maturity to receive all cash flows from a financial instrument.

Immunization

The basic idea of immunization is to manage the gap between the duration of Assets and Liabilities of the Bank. A portfolio of Assets and Liabilities with the same duration will hedge each other against interest rate risk and maintain the spreads of the Bank. In other words, interest rate risk can be eliminated or immunized by setting the duration gap equal to 'O'. However elimination of IRR is not always the best policy. Sometimes ALCO prefers to manage their gaps to take advantage of expected change in market interest rates and accordingly changes/shuffles the portfolio to arrive at the desired duration gap.

Simulations

Simulations are computer generated scenarios about the futures which permit banks to analyse IRR and plan strategies in a synamic framework. The scenarios are based on a number of assumptions like :

i) expected changes in interest rates and the shape of the yield curves

ii) pricing strategies for Assets and liabilities

iii) the growth, volume and mix of Assets & Liabilities

iv) hedging strategies

The data used for modelling the scenarios may include both current data and 'what if' projections.

Synthetic Method/Derivatives for IRRM

Interest Rate swaps

This represents a contract between two parties to exchange cash flows at periodic intervals based upon a notional Principal amount. Most common type of swap involves payment of fixed rate cash (Interest) flows to receipt of floating interest rate cash flows. While the fixed rate cash flows are determined over the life of the swap, the floating rate cash flows is indexed to a specific reference rate and valued at the reset date. Such swaps are used by the Banks/FIs to synthetically convert floating rate liabilities to fixed rate liabilities. This is possible because the floating cost of liabilities is counterbalanced by floating rate receipts associated with the swap. Any change in the liability costs are matched by similar change in the floating rate inflows. The net effect of this strategy thereby locks in the liability cost at a rate equal to the fixed rate of the swap.

Interest Rate futures

Options are traded on a vast array of underlying assets like stocks, Treasury bills, Treasury Notes, Foreign currencies, Interest rates etc.

ALM through Securitization

Securitization is an innovative tool that can be used for managing many of the risks faced by the Banks and also for Balance Sheet management. Securitization of assets, which otherwise be repaid after a long term, enables the originators to widen the funding sources. Origin of the Securitization is traced to the high volatile interest rate environment when the thrift institutions had mismatched positions with long term assets funded by short term liabilities. To avert the losses on account of negative spreads, securitization was engineered.

Q 4 d Discuss the role of merchant banker in a primary market issue management.

Ans. 4 d Merchant banker is the intermediary appointed by companies in the primary market issue. It has to look at the entire issue management and work as the Manager to the Public Issue.

Principal steps in a Public issue are as follows :

Vetting of Prospects : The prospectus is a document to communicate information about the company and the proposed security issue to the investing public. The draft prospectus containing the disclosures has to be vetted by SEBI before a public issue is made.

Appointment of Underwriters : An underwriter agrees to subscribe to a given number of shares in the event the public do not subscribe to them. The underwriter, in essence, stands guarantee for public subscription in consideration for the underwriting commission.

Appointment of bankers : The bankers to the issue collect money on behalf of the company from the applicants.

Appointment of Registrars : The registrars to issue perform a series of tasks from the time the subscription is closed to the time the allotment is made.

Appointment of Brokers and Principal Brokers : The brokers to the issue facilitate its subscription.

Filing of the Prospectus with the Registrar of Companies

Printing and despatch of prospectus and application form : After the prospects is filed with the Registrar of Companies, the company should print the prospectus and the application form.

Filing of Initial Listing Application : Within ten days of filing the prospectus, the initial listing application must be made to the concerned stock exchanges, along with the initial listing fees.

Promotion of the Issue : The promotional campaign typically commences with the filing of the prospectus with the Registrar of Companies and ends with the release of the statutory announcement of the issue.

Statutory Announcement : The statutoty announcement of the issue must be made after seeking the approval of the lead stock exchange. This must be published at least ten days before the opening of the subscription list.

Collection of Applications : The statutory announcement (as well as the prospectus) specifies when the subscription would open when it would close, and the banks where the applications can be made.

Processing of Applications : The application forms received by the bankers are transmitted to the registrars to the issue for processing.

Establishing the Liability Underwriters : If the issue is undersubscribed, the liability of the underwriters has to be established.

Allotment of Shares : If the issue is under-subscribed or just fully subscribed, the company may allot shares applied for by the applicants after securing the formal approval of the concerned stock exchanges(s)

Listing of the Issue : The detailed listing application should be submitted to the concerned stock exchanges along with the listing agreement and the listing fee.

Costs of Public Issue

The cost of public issue is normally between 8 and 12 per cent depending on the size of the issue and the level of marketing effort. The important expenses incurred for a public issue are Underwriting Expenses, Brokerage, Fees to the Managers to the Issue Fees for Registrars to the Issue, Printing Expenses, Postage Expenses, Advertising and Publicity Expenses, Listing fees, Stamp duty.

In addition to the above procedural matter, the most important issue relates to the pricing of the issue. The merchant banker has to see that the issue is priced properly.

Pricing of Public Issues

The salient features of SEBI guidelines with respect to pricing of public issues are as

1. A new company set up by entrepreneurs without a track record will be permitted to issue capital to public only at par.
2. A new company set up by existing companies with a five year track record of consistent profitability will be free to price its issue provided the participation of the promoting companies is not less than 50 per cent of the equity of the new company and the issue price is made applicable to all new investors uniformly.
3. An existing private/closely held company with a three year track record of consistent profitability shall be permitted to freely price the issue.
4. An existing listed company can raise fresh capital by freely pricing further issue.

ORGANISATIONAL

DEVELOPMENT

&

HUMAN RESOURCES

DEVELOPMENT

GUIDELINES FOR ANSWERING ASSOCIATE EXAMINATION - FEBRUARY 1999

ORGANISATIONAL DEVELOPMENT & HRD

SECTION I

Q 1. Answer any ten question from those give below.

State whether the following are true or false and give reasons for your answer in not more than two lines.

a) Scientific Management approach is the foundation of today's concept of Human Resource Management.

b) The purpose of policy is to provide rules and regulations that the employees have to adhere to.

c) Customer focus is not one of the passing fads. It is a permanent feature of the future.

d) There are no impediments to womens' carrier in the organisations.

e) Span of control is the same as span of management.

f) Successful people have high tolerance for ambiguity.

g) TQM is a part of Benchmarking Process.

h) Potential of an individual for higher level jobs can be judged on the basis of the performance appraisal.

i) Role and Position are one and the same concept.

j) The Positive aspect of Information Technology is that more number of people can be utilised to think about a problem.

k) Job analysis is critical for HRD systems.

l) The desirable size of the group is 7 to 9 members.

m) Training plan is a summary of all training needs identified.

n) Organisations have to take responsibility of individual's career by providing opportunities.

o) Organisations have to change their ways of doing things because everybody is changing.

Q 1 a **Scientific Management approach is the foundation of today's concept of Human Resource Management.**

Ans 1 a False. The concept of present HRM is qualitatively different from the assumptions made by the Scientific Management.

Q 1 b **The purpose of policy is to provide rules and regulations that the employees have to adhere to.**

Ans 1 b False. The purpose of policy is to provide a broad framework/guideline that give direction to the decision making by the employees.

Q 1 c **Customer focus is not one of the passing fads. It is a permanent feature of the future.**

Ans 1 c True. Customer focus has in an built concept of interdependence and as such will continue in future marked by globalisation.

Q 1 d **There are no impediments to womens' carrier in the organisations.**

Ans 1 d False. Even though most of the countries have accepted the equality for women in employment, the cultural bias is expected to reflect in the behavioural patterns in the organisation thus causing impediments.

Q 1 e **Span of control is the same as span of management.**

Ans 1 e False. Span of control relates to the number of people that can be supervised while span of management relates to the levels of management in an organisation.

Q 1 f **Successful people have high tolerance for ambiguity.**

Ans 1 f True. Since ambiguity does not create stress of anxiety in such individual, they are able to deal with new, uncertain situations effectively.

Q 1 g **TQM is a part of Benchmarking Process.**

Ans 1 g False. Benchmarking is a process to create awareness about the changes required whereas TQM aims at ensuring the quality of product by aligning people, systems and process.

Q 1 h **Potential of an individual for higher level jobs can be judged on the basis of the performance appraisal.**

Ans 1 h False. Performance appraisal given information about what individual does today, if an individual performs well at one level, it may not mean that he would do so at higher levels.

Q 1 i **Role and Position are one and the same concept.**

Ans 1 i False. Role and position are related but not the same thing. Position is relational while role is mutual. Position is hierarchical, role is interdependence interdependent.

Q 1 j **The Positive aspect of Information Technology is that more number of people can be utilised to think about a problem.**

Ans 1 j True. In the future, effective use of information will be the key factor for success. The more ways and interpretations, the better and stronger the organisation will be.

Q 1 k **Job analysis is critical for HRD systems.**

Ans 1 k True. Job analysis creates data about required competencies which are essential for almost all HRD systems like recruitments Training, Performance, Appraisal, Placements Career path etc.

Q 1 l **The desirable size of the group is 7 to 9 members.**

Ans 1 l True. Research has indicated that with more than 7-9 interactions between all members do not take place meaningfully.

Q 1 m **Training plan is a summary of all training needs identified.**

Ans 1 m False. Training - plan is what organisation plans to do after considering the priorities among the training needs identified, as such it is not a summary.

Q 1 n **Organisations have to take responsibility of individual's career by providing opportunities.**

Ans 1 n True. Since work forms a major component of an individuals life, their ambitions have to fulfilled in the context of work and therefore, the organisations have to provide opportunities.

Q 1 o **Organisations have to change their ways of doing things because everybody is changing.**

Ans 1 o False. Organisations need to first evaluate the areas of change for their effective performance and then change not because all are doing so.

SECTION II

Q 2. **a)** **Given below in Set I are eight names of individuals who propounded some theory or concepts. You have to match the two sets naming the individual and his theory/**

concept which are given in Set II.

Set I : Maslow, Adams, Alderfere, Carl Rogers, Freud, McClelland, Friedman & others, Herzberg,.

Set II : Equity Theory, Psychoanalytical Theory, Type A - \type B personality, ERG Theory, Need Hierarchy Theory, Self-concept Theory, Achievement - Motivation Theory, Two factor Theory.

Ans 2 a	Maslow	Need Hirerarchy Theory
	Adams	Equity Theory
	Alderfers	ERG Theory
	Carl Rogers	Self Development Theory
	Freud	Psychoanalytical Theory
	McClelland	Achievement - Motivation
	Friedman & Others	Type A - Type B Personality
	Herzberg	Two Factor Theory

(0.25 for each correct matching - Total 2 marks)

Q 2 b What are the objective of labour legislation? Explain in ten sentences.

Ans 2 b Objectives : Labour Legislations

To protect and safeguard the interest & well being of workers

To regulate and improve working conditions

To provide for fixation and payment of minimum wages

To ensure timely payment of wages

To spell out and notify service conditions

To provide for formation of trade unions to promote collective bargaining.

To arrange social security measures

To promote industrial peace by providing machinery for settlement of disputes.

(Minimum any four of these should be mentioned.)

Q 3. **a) State whether true of false**

Quality of work life includes :

i Adequate and fair compensation

ii. Guaranteed Promotions

iii. Role clarity

iv. Growth and Security

v. Protection and respect for employee's rights to privacy, dissent, equity etc.

vi. A clear career path

vii. Good working conditions

viii. Flexitime facility

Ans 3 a Quality of work Life includes :

I Yes

II No

III No

IV Yes

V Yes

VI No

VII Yes

VIII No

Q 3 b What is the definition of Organisational Behaviour?

Ans 3 b Any one of the following definitions

OB is the study and application of knowledge about how people act within organisations.

OB is directly concerned with the understanding prediction and control of human behaviour in organisations.

OB - A field of study that investigates the impact that individuals, groups and structures have on behaviour within organizations for the purpose of applying such knowledge towards improving organisational effectiveness.

Q 4. **a) The term OCTAPACE stands for _____**

b) Why does Human Resources Management need an information system? Explain in ten sentences.

Q 4 a **The term OCTAPACE stands for _____**

Ans 4 a OCTAPACE stands for eight steps towards healthy culture O-Openness, C- Confrontation, T-Trust, A-Authenticity, P-Proactivity, A - Autonomy, C - Collaboration and E - Experimenting (2 marks)

Q 4 b **Why does Human Resources Management need an information system? Explain in ten sentences.**

Ans 4 b Need for HRIS to

Deal with the volume

Analysis of whats happening with respect to the policy and practices

Analysis for trends for policy reviews

Analysis for decision making for HR systems like training, performance and potential identification etc.

Data base for day-today decision making like nomination for training, placements, transfers etc.

Q 5. **a) Fill in the blanks**

i. The three stages of management of change suggested by Schein and others are :

i)...... (ii) ...... (iii).......

ii. The Force Field Theory from Physics is applied to explain _____ to _____.

The two factors discussed are _____ and _____.

b) What are the various barriers to communication and which one of them in your opinion is the most crucial. Explain in ten sentences.

Q 5 a i **The three stage of management of change suggested by Schein and others are :**

Ans 5 a i i) Unfreezing, ii) Moving/changing iii) Refreezing

Q 5 a ii **The Force Field Theory from Physics is applied to explain _____ to _____.**

The two factors discussed are _____ and _____.

Ans 5 a ii Resistance to change

Driving forces and restraining forces.

Q 5 b What are the various barriers to communication and which one of them in your opinion is the most crucial. Explain in ten sentences.

Ans 5 b Barriers to communication.

Badly expressed messages, faulty organisation structure, use of Technical language, Filtering, Unclarified assumptions, Distrust, Distortion, One media, Poor retention etc. (Any four should be mentioned)

Q 6.

a) The Development model of Personality is given by _____. The eight stages are marked by specific mind sets, which are _____

b) State the difference between a grievance, dispute and conflict in 50 words.

Q 6 a The Development model of Personality is given by _____. The eight stages are marked by specific mind sets, which are _____

Ans 6 a The Development model of Personality is given by Erickson's Development Model

The eight stages are marked by specific mind sets, which are:

Stage 1 - Trust Vs. Mistrust

Stage 2 - Autonomy Vs. Share & Doubt

Stage 3 - Initiative Vs. Guilt

Stage 4 - Industry Vs. Inferiority

Stage 5 - Identity Vs. Role Diffusion

Stage 6 - Intimacy Vs. Isolation

Stage 7 - Generativity Vs. Stagnation

Stage 8 - Integrity Vs. Despair

Q 6 b State the difference between a grievance, dispute and conflict in 50 words.

Ans 6 b Grievance : Any real or imagined feeling of injustice, which an employer has, concerning his employment relationship.

Dispute - a definite manifestation of conflict and may be a result of many unsettled grievances.

Conflict - is clashing of point of views - differences in opinions, ideologies

Q 7. **a) Name any four institutions in India which are related to Human Resource Management as a discipline. Mention their main activity.**

b) Describe the stages of policy making and state which one in your opinion is the most important and why? Explain in 50 words.

Q 7 a Name any four institutions in India which are related to Human Resource Management as a discipline. Mention their main activity.

Ans 7 a Any four Institutions like NIPM, HRD Network, Academy of HRD, ISTD, NIPM, IIM, Indian Management Association.

Q 7 b Describe the stages of policy making and state which one in your opinion is the most important and why? Explain in 50 words.

Ans 7 b Four stages are :

Input - Ideas - could come from anywhere. Formation - Top Management activity - discussion. Communication - clarifying the written document if any. Implementation - Procedures to realise the intentions

(Candidate should give reasons for his choice)

Q 8. **a) Choose the correct answer and write in the Answer book.**

The stated objective of IIPM was---

i) to promote the study of Personnel and Industrial problems.

ii) to change the outdated labour laws.

iii) to introduce a degree course in universities.

iv) to make the organisation appoint a mandatory personnel officer.

b) Name four Indian organisations which are known for their HRD approach to people management.

c) Explain in 50 words the interlinkages between the trainer, the topic and methodology in a Training Process.

Q 8 a **The stated objective of IIPM was---**

Ans 8 a i) is the correct answer i.e. to promote the study of Personnel and Industrial problems.

Q 8 b **Name four Indian organisations which are known for their HRD approach to people management.**

Ans 8 b Tisco, Telco, Thermax, Modi Xerox, SBI, SB Patiala, BOB, Godrej, HDFC, BHEL, Madura Coats. Crompton, Cadbury etc. (Any four) (Total 2 marks)

Q 8 c **Explain in 50 words the interlinkages between the trainer, the topic and methodology in a Training Process.**

Ans 8 c Training process is aimed at improving and updating professional knowledge of individuals by developing skills required for the job and cultivating appropriate behaviour and attitude. As such the trainer - his skills, knowledge - about the topic and his capability to utilise the methodology are interlinked. The purpose will not be served if the trainer has no knowledge of the topic or is not confident of using a particular methodology.

SECTION III

Answer the following in 15 sentences each

Q 9.

a) What skills and attributes are expected in the HRM functionary today?

b) Describe the concept of Locus of control

c) Managerial Grid as a concept to study leadership behaviour. Explain.

d) Write short note on any one of the following

i) Career Movements / patterns ii) Career Roles

e) Define Collective Bargaining.

Q 9 a **What skills and attributes are expected in the HRM functionary today?**

Ans 9 a Skills and attributes for HR functionary

Technical - knowledge about performance Appraisal system, Tests and other measurements of behaviour, career planning, counselling process, understanding, organisational culture etc.

Managerial - Organising ability, skill for system development.

Personality - Faith in HRD philosophy, concern for people, approachable, effective team member, imaginative and experimental.

During the war the men (age group 30-45) were taken away for fighting. The organisations had to use the alternative manpower like those older than 46-50 years, women minority groups etc. These individuals could perform after due training indicating the "development" potential of human beings.

Q 9 b Describe the concept of Locus of control

Ans 9 b A concept to understand personal orientation of individuals. How much control is experienced or perceived by individuals over the events occurring around him/her. Explanations for internal and external locus of Control behaviour, consequences of such behaviour.

Q 9 c Managerial Grid as a concept to study leadership behaviour. Explain.

Ans 9 c Leadership with its dual focus - on getting the task done and on maintaining relationship with people doing the task. Concern for Task - Concern for people. Grid allows placing people at different points - effectiveness is related to these positions. The author points 1.1, 1.9, 9.9, 9.1 and 5.5

Q 9 d Write short note on i) Career Movements / patterns ii) Career Roles

Ans 9 d **Career Movements / Patterns -**

Three dimensions - Horizontal, Vertical and Circumferential Different Patterns - Steady, plateau, Linear, Spiral, Transifary etc.

Career Roles - Erickson's Stages } Reference may be

- Levinson's Transitions }

- Daltons & Others - 4 roles

Apprentice, Colleague, Mentor, Sponsor

Performance Appraisal	Potential Appraisal
to assess past / present	to assess future
related to what he / she has done	related to what he/she has to do
capabilities demonstrated	capabilities interpreted
abilities may not be needed for future	abilities definitely needed for future
at times used for reward	to be used for future grooming

Q 9 e **Define Collective Bargaining.**

Ans 9 e Collective Bargaining :

- a joint endeavor as against individual action
- both parties have common interest
- power rests on remaining together
- Bargaining takes place in terms of getting a fair deal for services and conditions of work

Trade Union Act 1926 recognised and formalized this process.

SECTION IV

Answer any three of the following question in 25-30 sentences.

Q 10. **a) What are the emerging challenges for HR functionaries?**

b) Why is Pedagogy not suitable for adults?

c) Management of change is a crucial phase of organisational Development - Elaborate.

d) If you had to choose between `Type A' and 'Type B' personality, whom would you choose and why?

Q 10 a **What are the emerging challenges for HR functionaries?**

Ans 10 a Personnel Management has traditionally remained scheduled from the business concerns of the organisation. The most crucial emerging challenge would be to shift to strategic HRM. This will ensure alignment of HR systems to the live issues of the organisation like moving towards a quality or organisation or a learning organisation. In a way the focus would be developing required mind set for the issue in focus alongwith the systemic changes. Each of these have specific value to be fostered. (The candidate is expected to write example of any one of the orientations like adoption technology, quality ethics to elaborate the challenges).

Q 10 b **Why is Pedagogy not suitable for adults?**

Ans 10 b Pedagogy is an approach wherein the teacher/trainer is in full control of information, solutions, answer and the way learner learns. Adults learning process implies integration of new knowledge, approach or perspective with the existing base. This implies that these two sets need to be consciously thought, deliberated upon and assimilation sought. The process foresees learning as well as unlearning. For this pedagogy has no scope as it is one way and from the platform to another lower than that. Andragogy aims at doing this (explain how).

Q 10 c **Management of change is a crucial phase of organisational Development - Elaborate.**

Ans 10 c Organisation development aims at growth and progress through change that is encompassing structure systems and people. As such it implies - diagnosis based on data, interventions at appropriate levels and units and stabilizing the new perspective. Problem diagnosis is relatively easy but implementation of new strategy or perspective is crucial as it involves change from one position to another. Resistance to change is the main task in OD. Lewin Force field theory and Schein's three stages of change are relevant concepts in highlighting the importance of resistance and effective strategies of change (Both the concepts need to be explained.)

Q 10 d **If you had to choose between `Type A' and 'Type B' personality, whom would you choose and why?**

Ans 10 d Should examine Type A and Type B personality - where are the consequence of Type A behaviour and Type B behaviour - what are the limitations? Why would he choose one over the other - If choosing A the focus should be on achieving task if choosing B it is on creating conducive and non-threatening environment. Ideally speaking no extreme is desirable - some where in between but could be slightly on either side (candidate must give his reasons).

ELECTRONIC BANKING & INFORMATION TECHNOLOGY IN BANKING

GUIDELINES FOR ANSWERING ASSOCIATE EXAMINATION - FEBRUARY 1999

ELECTRONIC BANKING AND INFORMATION TECHNOLOGY IN BANKS

SECTION I

Q 1. **a) Define**

- **i) MICR Cheque**
- **ii) LAN**
- **iii) Fibre Optics**
- **iv) VSAT**
- **v) Multiplexing**

Q 1 a i MICR Cheque :

Ans 1a i The MICR (Magnetic Ink Character Recognition) cheque is the cheque encoded with the ink containing magnetisable particles using specialized character shapes. The MICR technology is the successful example of character recognition for cheque sorting in clearing houses.

Q 1 a ii LAN :

Ans a ii LAN (Local Area Network) is the network of computers that links computers and peripherals within a localized area say within a building. Usually there is a central computer (server) providing and controlling all the services of the network sought by the user nodes. The communication media is privately owned by the user.

Q 1 a iii Fibre Optics :

Ans 1a iii The invent of fibre optics has been a technological breakthrough in the communication technology. It is a highly reliable communication media providing high quality (low bit error rate) transmission of signals at a very high speed. The transmission of data is through very thin glass with a beam of light.

Q 1 a iv VSAT :

Ans 1 a iv VSAT (Very Small Aperture Terminal) is satellite based communication technology. VSATs provide communication channels of high quality and can be installed and operated in widely dispersed locations irrespective of the distance and terrain. These are easy to install and provide easy centralized control and monitoring of remote sites from the earth station (Central hub).

Q 1 a v Multiplexing

Ans 1 a v Multiplexing is the technique to enable more than one signal to be sent simultaneously over one physical channel. It combines inputs from two sources and transmits the combined data stream over a single high-speed channel.

b) Fill in the blanks

(i) Four Divisions of COBOL program are Identification, Environment, Data and Procedure.

ii) Four important principles of flow-charting are each flow chart should have two terminate symbols leveled as start and stop, only standard symbols should be used, simple decisions like yes/no should be used and direction should be drawn from top to bottom.

iii) Window is Graphical User Interface and Windows 95, Windows 98 are Operating Systems

iv) DOS is Single-User OS and UNIX is multi-user OS.

v) dBase is written in C programming language.

c) State with reasons, true of false

i) Expert Systems are most suited for structured decisions

ii) A feasible solution may not satisfy all the constraints

iii) Probability distribution is necessary when values of variables are uncertain

iv) X.25 is widely used protocol for wide area networks

v) The EFT can be considered as sub part of EDI

Q 1 c i Expert Systems are most suited for structured decisions

Ans 1c i False : A structured decision is always made using predefined procedures or rules. Decisions, which require creativity and intuition, are unstructured decisions. The expert systems are developed by using the domain knowledge and wisdom of experts in variety of situations.

Therefore, expert system are more suited for unstructured decisions.

Q 1 c ii **A feasible solution may not satisfy all the constraints**

Ans c ii False. A solution is considered feasible only if it satisfies all the constraints. However, any feasible solution may not be the best or the optimal solution although it satisfies all the constraints.

Q 1 c iii **Probability distribution is necessary when values of variables are uncertain**

Ans c iii True. In case of deterministic values of a variable, probability distributions are not required as nothing is left to the chance. In case of uncertainty the chances or the probability is worked out with the help of probability distributions to determine the chance of a variable achieving a particular value or a range of values.

Q 1 c iv **X.25 is widely used protocol for wide area networks**

Ans c iv True. A protocol is a set of rules governing the format and meaning of the messages that are exchanged between the computers. X.25 is a packet switched protocol allows high-speed links between two end points. This is one of the best-known and widely used protocols and commonly used to connect computers to packet switched public data networks. The CCITT, which makes the technical recommendations about data communication services, has recommended X.25 standard interface between a computer and a packet-switched computer network.

Q 1 c v **The EFT can be considered as sub part of EDI**

Ans c v True. The Electronic Data Interchange (EDI) is the electronic transfer of business information in standard format in machine pocessable form. The Electronic Funds Transfer (EFT) is used for exchanging structured fund transfer telecommunication messages over a computer network. EFT like SWIFT is a standarized message transfer system used for funds transfer.

SECTION II

Q 2. **Pick up a correct answer and explain briefly why?**

a) **Strategic information is needed by <u>Top</u> management**

i) Middle **ii) Top** **iii) Operational**

b) **The banking system is a <u>Open</u> system**

i) Open **ii) Closed**

c) Financial application can be represented by <u>Mathematical</u> models

i) Mathematical ii) Pictorial iii) Physical

d) <u>Exceptional</u> reports may be used to ensure the security

i) Exceptional ii) Periodic iii) Demand

e) Media used in LAN is <u>Co-axial Cable</u>

i) Radio Link ii) Co-axial Cable iii) Telephone line

Q 2 a Strategic information is need by _______ management

Ans 2 a The answer is top.

Explanation : The top management is required to take crucial decisions keeping in view the interdependent objectives/goals of the organization. Top management needs information which can be used for the strategic decision making to achieve the objectives. The importance of strategic information is increasing day by day in the ever-increasing competition.

Q 2 b The banking system is a _____ system

Ans 2 b The answer is open.

Explanation : An open system is the system that interacts and operates with other systems. Banking is the lifeline of trade, commerce and any type of economic activities. It is the vehicle of economic growth. The banking system therefore operates with any other system. Hence it is an open system.

Q 2 c Financial application can be represented by _____ models

Ans 2 c The answer is Mathematical.

Explanation : A physical model is a scaled replica of actual system being studied. For example, an architect makes a prototype of a building to be constructed. Similarly, the pictorial model is used to represent the different objects or concepts symbolically or graphically. For example, an organizational chart shows the structure, relationships and authority within an organization. Thus these two models can't adequately represent financial applications. On the other hand, a mathematical model represents a real system or a problem using mathematical relationships. It therefore can adequately represent financial applications.

Q 2 d _____ reports may be used to ensure the security

Ans 2 d The answer is Exceptional

Explanation : The exception reports in a computerized environment are generated to identify the deviations and exceptional transactions. These reports are scrutinized to find out the genuineness of the transactions in order to prevent both bonafide errors and malicious attempts to commit fraud.

Q 2 e Media used in LAN is _____

Ans 2 e The answer is Co-axial cable.

Explanation : In LAN the communication media used is wired and privately owned as the distance covered is small and the network is generally located within a building. The radio link and telephone line are used in wide area networks (WAN). These communication media are provided by the public network system like Telephone Company, etc.

Q 3. Define in about 5/7 lines following terms

a) TCP/IP

b) WWW

c) SWIFT

d) EDI

e) ATM

Q 3 a TCP/IP :

Ans 3 a The TCP/IP (Transmission Control Protocol / Internet Protocol) helps in connecting and communicating between different networks on the Internet. Each computer on the Internet needs TCP/IP. It divides long messages into packets. Each packet is marked with sequence number with address of recipient along with some error control information. The packets are then sent over the network, where it is the job of IP to transport the packets to the destination. IP provides the addressing information necessary to get the data to the right Internet computer. Each host connected to the Internet has unique address called in IP address.

Q 3 b WWW :

Ans 3 b The WWW refers to the World Wide Web. It offers a simple and consistent interface to the vast resources of the Internet. By using the Web, one can access much of what the Internet has to offer. The Web has enhanced the use of Internet infrastructure. Web also helps the user to jump from one page to the other on Internet. The amazing thing is, with only a few simple commands or mouse clicks, one can jump his way around the Internet.

Q 3 c **SWIFT :**

Ans 3 c SWIFT stands for Society for Worldwide Inter-bank Financial Telecommunication. It is an international computerized telecommunication network dedicated to International banking system. It is basically a messaging network which is used to exchange structured messages within a correspondent banks and connecting banks for financial settlements. Its headquarters is at La Hlpe, Belgium. It was set up in 1973 and went operational in 1977. India became the 74th member of SWIFT in December 1991. At present it operates in more than 100 countries with over 4000 member banks transmitting more than two million financial messages per day. Each bank is given a unique address code by SWIFT. The messages have to conform to the structured formats and certain standards laid down by the SWIFT. It is a highly secured system using encryption technology

Q 3 d **EDI**

Anc 3 d The EDI i.e. electronic data interchange is the inter-orzanisational exchange of business documentation in a structured, machine-processable form. It is the interchange of standard formatted data between the computer application systems of the business partners with minimal manual intervention. Implementation of EDI can help to cut costs by reducing unnecessary inventory and spreeding up orders, automatically ensuring stock-levels, cutting data entry and reducing errors. Its operates by interchanging agreed messages between the partners and can take place over private or public telecommunication network.

Q 3 e **ATM :**

Ans 3 e It refers to automated teller machine. The automated teller machine is primarily used as cash dispenser. It is located on or off the bank's premises to dispense the cash round the clock. Customers can also use ATMs for depositing cash, cheque, obtaining balance, obtaining statement of last few transactions, requesting for cheque books, etc. The machine is accessed through an ATM card. The card contains a magnetic strip hiding the customers ID. The customer has to use his personal identification number (PIN) for the purpose of security. ATM is also referred to as Asynchronous Transfer Mode. This technology uses data transmission, which can be considered as a special type of packet switching technology.

SECTION III

Q 4. Write short notes on following terms

i) Cyber Banking

ii) Committee for proposing legislation on Electronic Funds Transfer and other Electronic Payments (Shere Committee)

iii) Computer Security in Banking Operations / Transactions

Q 4 i Cyber Banking

Ans 4 i Cyber Banking means the banking in cyberspace. Generally people use the term cyberspace for the internet. Cyber banking allows the customer to do banking from anywhere at anytime in a simple, flexible, and instant way. Advanced cyber banking tools and techniques provide security in the form of advanced encryption systems which ensure safety of client's name, address, credit card and transaction details. Cyber banking involves credit cards, smart cards electronic cheques, electronic cash etc., use of telecommunication networks, various communication protocols and security techniques.

Many banks have started Internet banking in India recently. These banks however restrict their operations only to the transfer of money from one account to the other of the same customer because of security reasons. The electronic commerce or e-commerce is also packing up in a big way. E-commerce also uses Internet infrastructure for transmission of business information like placement and confirmation of business orders, etc. It may also require payment through electronic means. Business on the Internet has been the cheapest and fastest way and provides global coverage with increasing number of users. The Internet itself provides various services to carry out business.

Increasing volume of home PCs accessing the Internet helps the customers to do shopping, ordering the goods, making payments, etc. by sitting at home. Home banking using the Internet infrastructure or any other infrastructure is also picking up. The major issue in cyber banking relates to the security of the transactions. The encryption software and the firewall technology ensure secure on-line banking over Internet. A customer can open an account, transfer the funds, pay for the goods and services and access the on-line banking services from anywhere in the world.

Q 4 ii Committee for proposing legislation on Electronic Funds Transfer and other Electronic Payments (Shere Committee)

Ans 4 ii The advent of electronic banking has made a sea change in the nature of banker-customer relations and perception of customer service in the banking business. The Indian banking sector is on the threshold of a computer revolution. Payment system is one area where electronic technology can bring about several salutary innovations. Realising the need for giving greater impetus and priority to the adoption of technological innovations in payment system, the Governor of the Reserve Bank has constituted a committee headed by Shri W. S. Saraf, Executive Director, Reserve Bank in June 1994 to look into, among other things, technological issues relating to payment system and to make recommendations for widening the use of modern technology in the banking industry. The committee recommended the need for providing legal support to the electronic mode of funds transfer. It was in this background that a Committee for Proposing Legislation on Electronic Funds Transfer and Other Electronic Payments was constituted by the Governor Reserve Bank of India on August 1, 1995 under the chairpersonship of Smt. K. S. Shere, Principal, Legal Adviser, Reserve Bank of India

The committee looked into the definition and the scope of electronic fund transfer, determining the responsibilities and liabilities of participants arising out of contractual obligations; defining the trigger events that determine the finality and irrevocability of the transfer of funds at different stages; operational security; determination of liability in the event of operational failure at any state; definition of frauds in electronic environment; admissibility of electronic media for the purpose of evidence; preservation period of electronic media; cheque truncation, etc.

The committee made recommendations pertaining to the short-term and long-term measures. The committee drafted the (i) RBI (EFT) Regulations, 1996 (ii) Model Customer Agreement, (iii) Amendment to RBI Act, (iv) Amendment to Bankers Book Evidence Act. etc.

Q 4 iii Computer Security in Banking Operations / Transactions

Ans 4 iii Data stored on computer systems is generally accessed through programmes. In case of financial systems like banks, data available on the system represents funds. If the data on systems is altered, the fund position gets altered; it may lead to a fraud. By a computer fraud, we refer to a fraud committed by altering data on computers or over networks.

In the normal course financial transactions, genuine credits and debits have to be done on balances which are restored as data on computers. These data alterations have to be done by authorised persons as per a pre-determined procedure. If unauthorised persons have access to the data on the computer systems, then they will be in a position to change the data to their advantage. It can happen if access control procedures are not in place. Both physical and logical access control measures assume significance. It should be ensured that input, processes and output controls are taken care of.

Most of the multi-user operating systems provide password security. A user is identified by user identification and is given access to specified data / programme resources only through a valid password. It restricts unauthorised access. Besides, additional security at application level can also be provided in such a way that access is restricted to only authorised personnel.

With the data flowing over networks, it is necessary to ensure that data is not tampered enroute to its destination. This is generally taken care of with networks security measures like data encryption with the help of keys. In the remote banking environment the authenticity of the user is also to be established before allowing him to access the system. There should be well-laid security policy. The rights of each functionary to different databases should be restricted keeping in view the role and the function of the employees.

Q 5. A Bank manager has to decide about money lending of Rs. 1,00,000/- to one of the three persons Mr. A, Mr. b and Mrs c for 5 years. The manager considers two states of nature :

i) Loan amount will be repayed with probability of 0.8

ii) Loan amount will not be repayed with probability of 0.2.

The borrowers Mr. A, Mr. B and Mrs. C are ready to pay flat interest rates of 16%, 14% and 15% respectively. Upon screening the borrowers' proposals, the manager thinks that he could recover at least 70%, 100% and 80% of the total loan amount from the borrowers A, B and C respectively, on their inability to repay the loan amount. Using decision table or decision tree to whom the manager should lend the money?

Ans 5 In decision tables or decision trees the data is arranged in the standard tabular format or using diagrams that helps in systematic analysis of the problem. General decision table or decision tree consists of four elements.

a. Alternative course of action -- independent variables

b. States of nature - independent, uncontrollable variables.

c. Probabilities of states of nature -- independent, uncontrollable variables

d Expected results / payoffs (dependent variables)

The alternative course of actions represent the set of values (alternatives) a particular decision variable takes. Out of which one is selected as the best alternative. The problem has been solved using both decision table and decision tree.

Decision Table

States of nature	P=0.8	P=0.2
Alternatives	Amount will be repaid	Amount will not be repaid
Mr. A	Rs. 1,80,000.00	Rs. 70,000.00
Mr. B	Rs. 1,70,000.00	Rs. 1,00,000.00
Mrs. C	Rs. 1,75,000.00	Rs. 80,000.00

Assumptions : The interest paid by A, B and C during 5 years has been worked out on simple basis i.e. the time value of money has been ignored. If time value of money is to be taken into account, either compound interest has to be worked out or net present value of future receipts have to be taken which may make the calculations complicated and require discount tables. This is not the intention of this question. The simple interest has been worked out as follows :

Interest paid by Mr. A = 100000 x. 16x5 = Rs. 80000

Interest paid by Mr. B = 100000 x. 14x5 = Rs. 70000

Interest paid by Mrs. c = 100000x. 15x5 = Rs. 75000

The expected money value (EMV) for all the three alternatives can be worked out as follows :

EMV (A) = 0.8 x 180000 + 0.2 x 70000 = Rs. 158000.00

EMV (B) = 0.8 x 170000 + 0.2 x 100000 = Rs. 156000.00

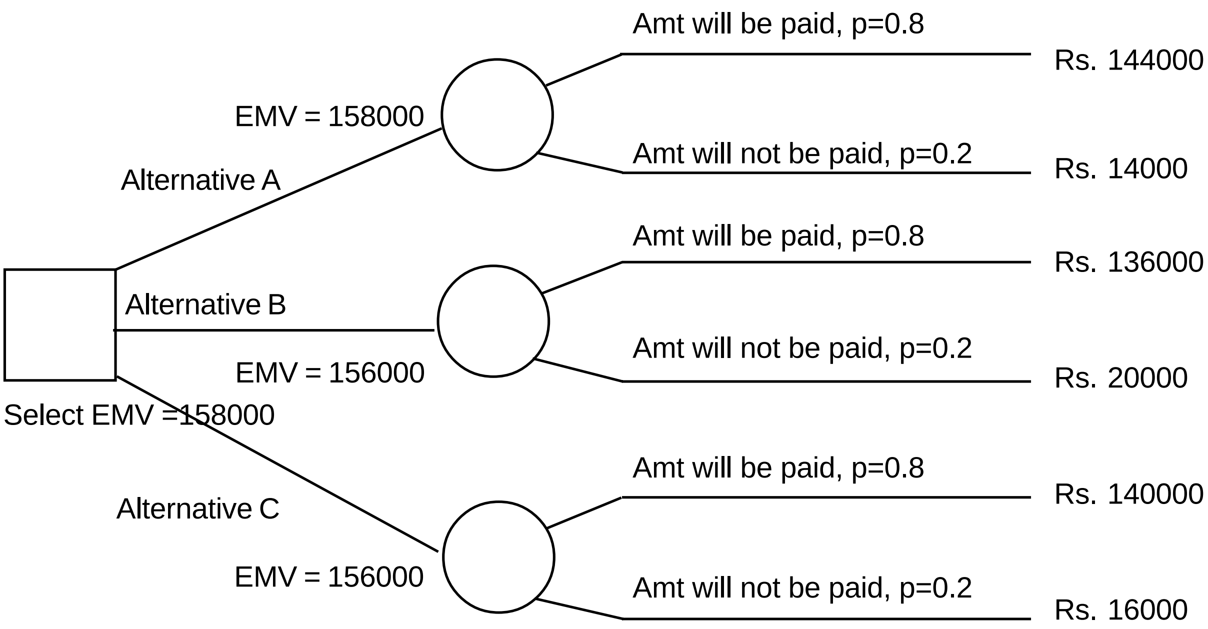
EMV (C) = 0.8 x 175000 + 0.2 x 80000 = Rs. 156000.00

Therefore, the alternative A is most favourable to the bank i.e. the manager should lend the money to Mr. A.

Decision Tree :

The above analysis can also be presented in the form of decision tree as follows

Pay Offs



Answer Select Alternative A with highest EMV of Rs. 158000.00

SECTION IV

Q 6. Describe in details the security arrangements that should be observed by the following types of branches :

a) The branch working with 5 AMPMs (Advanced Ledger Posting MacMachines)

- **i) Two for Savings bank accounts**
- **ii) Two for OD/CA/CC**
- **iii) One for Cash Book / GL**
- **There is no spare machine for all back**
- **SW is developed by outside vendor.**

- **HW vendor does not have representative office in town of branch**

- **Branch is headed by Sr. Manager with business of Rs. 60 lakhs (Deposits & Advances)**

Ans 6 a In a standalone environment like use of ALMPs, the machines are dedicated to single or a few functions using small number of application programmes. All the data and records are also maintained in the form of hard copies. In such environment more of the physical security is required than the logical security.

Physical Security of Hardware :

i) Fastening of machine to table

ii) Putting the machine in a protected cabinet with proper lock and key at the end of the day.

iii) Protection of Hard-disk and other magnetic media to be ensured.

iv) Assigning an individual official to a machine and making him, responsibile for its security.

Security of Programmes and Data

i) Employ password

ii) Change password frequently

iii) Use hidden files and secret file names and file level security

iv) Security through application program as the OS hardly provides any security in stand-alone environment

v) Security for generation and preservation of various statements

vi) Input control, checking input with the vouchers

vii) Regular back-ups. Off-site storage of back-ups

viii) Machines should work as standby to each the other, as there is no spare machine to fall back. For example : the machines used for savings bank accounts may work as fall back machines to each other and the machine used for OD/CA/CC may be used as fall back to each other. One of these machines may be used as standby for Cash Book / GL and other back office jobs.

ix) There should be close coordination with the software vendor to ensure that the software works properly.

x) As the hardware vendor does not have any representative office in the town, the hardware maintenance may be assigned to any local vendor, if available. However, the branch should be in a position to resume the work manually at any stage due hardware or software failure as all the data and statements are available in hard copy form.

Q 6 b **The branch is fully computerised (TBM/TAB)**

- **SW is running on LAN (Novell Netware OS)**
- **SW is developed in-house**
- **There are in all 13 nodes (1 for DBA (Data Base Admn.) and 1 for Branch Manager)**
- **There is a FALL BACK (SFT machine for server)**
- **Branch is headed by AGM with business of Rs. 120 Cr. (Deposits & Advances)**

Ans 6 b In a totally computerised branch running on LAN system more than the physical security, the logical security in needed for the access control. Any employee can log in to the machine from any terminal. The user ID and the password are generally used for the access controls. However, the Novel Netware provides lot of security features which the system administrator can implement to restrict the permission to any application, file or any particular activity. There can be application level security to restrict the access to any particular activity. It has always been desirable to have separate system administrator (SA) and data base administrator (DBA). It is evident from the question that there is a separate DBA. It is presumed that the Branch Manager is performing the job of SA

In a TBM/TBA branch the back-up and recovery procedures have to be implemented more rigorously as it becomes extremely difficult to revert to the manual procedure in case of any disaster. The disaster management procedures should be property documented and periodically tested. There is Fall Back SFT Server which almost ensures the continuity of the business due to hardware failure. Audit trails, exception reports and various controls are implemented to detect the frauds at any stage. The branch is not having connectivity with any other branch or office therefore, the high-level encryption etc. is not needed.

All other safeguards as listed in connection with the ALPM environment relating to Hardware, Software and Data security should also be implemented.

Q 6 c **The Branch is fully computerised with an ATM**

- **SW is running on UNIX (V-4.1) and ORACLE (7.0)**
- **SW is developed by vendor.**

- **Branch is having NIC-NET and also SWIFT connectivity with Zonal office and Head Office respectively for Electronic Banking.**
- **Branch is headed by DY GM with business of Rs. 700 Crs. (Deposits and Advances)**

Ans 6 c In addition to the Total Branch Automation, the branch has wide area networked connectivity with the Zonal and Head Offices. In addition to that the branch has ATM also. In the WAN environment, in addition to the Confidentiality, Integrity and Availability of data/system, authenticity of customer/user assumes a great significance. The physical security can hardly protect the system when it is having WAN connectivity. In addition to the security measures enumerated in (a) (b) above the following measures are suggested.

For ATM

(a) User ID and Password to be used by the customer

(b) The password of the customer should be stored in the encrypted form on the machines.

(c) Proxy server should be linked to the ATM users to protect the data on the main server.

For NIC-NET and SWIFT connectivity

a) High level encryption of message / information is needed to ensure the data integrity.

b) Digital signature to identify the user may be implemented. In case the branch is connected to other branches of the bank or any other branch of other bank through INFINET, the certification from some central authority may also be needed.

c) The NIC-Net is a network mainly used by different government departments/agencies and have connectivity at district level. This network is not a secured network and used for data transfer. For financial messages this network should be used with high level of encryption.

d) SWIFT is a word-wide Inter Bank communication system used for transmitting financial messages. It is highly secured network which uses sophisticated encryption and authentication procedures. The only additional precaution has to be taken is to restrict the use of SWIFT terminal by only authorised user.

The UNIX (V-4.1) and ORACLE (7.0) provide adequate security features at OS and application levels respectively.

MARKETING

OF BANKING

SERVICES

GUIDELINES FOR ANSWERING ASSOCIATE EXAMINATION - FEBRUARY 1999

MARKETING OF BANKING SERVICES

SECTION I

Q 1. a Fill in the blanks

- **i) Benchmarking means**
- **ii) Deposits in Bank are ---- funds**
- **iii) L/C & B.G. are called as ____ facilities.**
- **iv) Break Even Analysis can be used in Bank marketing for**
- **v) In product life cycle, ----- stage comes after saturation stage.**
- **vi) Market Research means**

b) Expand the following

- **i) ATM**
- **ii) MIS**

c) Define

- **i) Marketing Concept**
- **ii) Marketing Plan**

d) Differentiate between needs and wants, in two lines.

e) Name two committees connected with pricing of Bank's products.

f) Mention two main distribution channels in bank marketing.

g) Marketing can be successful even without communication/s. Is it rue or false.

h) Personal selling is ___ method of communication

i) Direct ii) Indirect

Q 1. a **Fill in the blanks**

i) Benchmarking means standard to measure performance to decide fulfilment of expectations.

ii) Deposits in Bank are source of funds

iii) L/C & B.G. are called as Non Fund facilities.

iv) Break Even Analysis can be used in Bank marketing for deciding pricing of a new product.

v) In product life cycle, Decline stage comes after saturation stage.

vi) Market Research means research about market - size, composition and its structure.

Q 1 b **Expand the following i) ATM ii) MIS**

Ans 1 b i) ATM : Automated Teller Machine

ii) MIS : Market Information System

Q 1 c **Define : i) Marketing Concept, ii) Marketing Plan**

Ans 1 c i) Any Definition - e.g. Phillip Kotler's

ii) Marketing plan is a document which formulates a plan for marketing products and services.

Q 1 d **Differentiate between needs and wants, in two lines.**

Ans 1d A human need is a state of felt deprivation of some basic satisfaction like food, clothing, shelter wants are desires for specific satisfiers of needs are few & wants are many.

Q 1 e **Name two committees connected with pricing of Bank's products.**

Ans 1 e T. K. Sinha, Sukhomaya Chakraborty.

Q 1 f **Mention two main distribution channels in bank marketing.**

Ans 1 f Branch Network, Specialised Branches

Q 1 g **Marketing can be successful even without communication/s. Is it rue or false.**

Ans 1 g False

Q 1 h **Personal selling is ___ method of communication i) Direct ii) Indirect**

Ans 1 h Direct

SECTION II

Q 2. Answer each in ten sentences

a) Describe five new instruments which can be handled by the banks besides routine or traditional banking instruments.

b) Explain the concept of transfer pricing in banks & its relevance on pricing/profit.

c) What is market segmentation? Why is it important in Bank's advertising?

d) Briefly explain the concept of marketing mix through a chart.

e) Briefly illustrate important steps in selling process in Bank Marketing.

Q 2 a Describe five new instruments which can be handled by the banks besides routine or traditional banking instruments.

Ans 2 a In the growing competition faced by all the banks from various types of banks due to changes in money market and its effect on demand and supply which affects bank's deposits and advances, it has become necessary to design, develop new instruments which would attract the customers by satisfying their identified need. The product should be evolved after studying customers needs and probable demand - existing and / or probable due to the same.

To give as idea two such products / instruments are described in the following paragraphs :

In the context of products of Banks in recent days Bank Marketing it is essential to take a look at the following products which attract the middle class customers and also are profitable to the bank

a) Consumer Loans

b) Credit Cards

Due to the restrictions of loanable funds and the less demand for lonable funds by industry the profits of banks were affected during the period when stock market and industrial scenario was slack. Merely mobilising deposits does not mean sound marketing policy. It becomes all the more necessary to market the loans as well to improve profitability. Similarly, taking into account the customer's 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 (consumers' demand and supply of bank's lonable 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 lapped segment becomes 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:

1. 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

ii. **Salient Features**

- It can be availed by individuals who are 18 years of age (As minors are not entitled).
- It is offered for worthwhile purchase or approved purpose to purchase an article, furniture. TV/Video, air-conditioner or a vehicle-2 wheeler or 4 wheeler.
- The amount cen be minimum Rs. 5,000/- to maximum oRs. 5.00 lacs
- The purpose can be besides, purchase of consumer durable goods, to persue higher education or for holiday or meeting wedding expenses etc.
- 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 instalmens (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 repayment 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.
- Such instruments enable banks to market their services either by channelising their loanable funds or adding more deposits or giving more float funds & ensuring more profit for the bank.

Q 2 b Explain the concept of transfer pricing in banks & its relevance on pricing/profit.

Ans. 2 b The concept of Transfer Pricing : In the changing & complex banking scenario-today-where there is pressure on mobilising deposits & also lack of demand for a bank's loanable funds, the banks have to necessarily look for the methods & techniques to improve their profitability to ensure sound capital base & reserves. Transfer pricing is one such effective method. Let us take a look at it as a concept & machanism through a carestudy.

Transfer Pricing concept and Mechanism : Simply speaking if we take profit as excess of income over expenditure, the same has to be thought in branch level system where some branches will be predominantly deposit centre and some branches will be predominantly advance centres where deposit centres will have mostly interest payable and show losses. The advances branches will have large demand are all profits by way of interest on advances but these will not be deposits available as loanable funds.

This means in one branch there will be high supply (deposits) and high interest payable and demand or interest receivable whereas as in other branch there will be high demand and his (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 further supplier and certain interest is payable to them and high advances branches have to pay certain interest to such supplying branches.

CASE STUDY I

Let us assume a Unit bank (i.e. a bank without any branches). Assuming that there is no liquidity crises we will presume that

(i) The bank has deposits of Rs. 100

and advances of Rs. 100

(ii) The average rate of interest paid on deposit is 5%

and average charged on advance is 15%

(iii) The service charge i.e. expenses on processing deposits and also on advances i.e. say 1% each. Therefore, profit will be :

P = income - expenditure = 15-5-2 = Rs. 8/-

Now if this unit bank converts into 2 branches - one exclusively for deposits and the other for advances, the position will be that

- Deposit branch incurs loss of Rs. 6

- Advances branch would make a profit of Rs. 14/-

Therefore, resultant profit for the bank will still be Rs. 8/-

as P = P1+P2 = (-6) + (14) = Rs. 8/-

At this stage super imposing will come i.e. the advances branch with superimposition of this rate, say 10% the profit of deposit and advances branch will be

Deposit branch = (-6) + (10) = Rs. 4/- (P1)

Advances branch = (14) - (10) = Rs. 4/- (P2)

i.e. the income has been distributed rationally.

The next profit booked by both these branches is indeed their contribution to overall performance. Therefore, total profit (P) = P1 + P2

and a transfer price rate has been superimposed

P = (P1+P1) + (P2+P2)

where P1 + P2 = 0

or

n S Pi = 0 i.e. P = (P1+P1) + (P2+P2) + ...(Pn +Pn) i = 1

Profit being the difference between Income & Expenditure, this technique enables to have an insight into the casting & determine adjust the level of business - Deposit & Advance in bank's branches to decide pricing & in effect the profitability.

Q 2 c What is market segmentation? Why is it important in Bank's advertising?

Ans. 2 c Market Segmentation : Market Segmentation is the process of dividing a company's total market into smaller groups or segments for the purpose of :

(i) Locating target markets

(ii) Identifying the needs of the target markets

(iii) Designing products to fill those needs

(iv) Promoting products specifically to those target markets.

Marketer are a variety of methods to segment their markets & identify behavioural groups. The most common bases for segmenting markets are : -

(i) Geographic

(ii) Demographic

(iii) Psychographic

(iv) Behaviourictic

Application of segmentation to banking :-

1) The most commonly applied application in Banking in the category of deposits is by demographic variables. Therefore target segments which a bank wants to pursue may be defined by :

Age/Income/Occupation/Education

2) For example, a typical definition for a target segment for deposit customers could be :

* Individuals - within a city/locality)
* Age group - 20 to 55 years
* Income - Rs. 100,000 p.a. +
* Occupation - Salaried individuals
* Education - Graduates

3) Very often target segments could be defined by profession :

* Doctors

* Chartered Accountants
* Lawyers
* Consultants

4) Other organisations & non-profit entities to whom banks market :

* Trusts
* Associations, Societies
* Schools, Colleges
* Small Establishments - Like shops

5) Since location is a great influencer in Retail Banking - "Locality mapping" is undertaken. Very often localities have a skew of ethnic / community groups like Gujarathis, Sindhis, Catholics, Tamilians - this forms a basis also for target segmenting.

6) In Retail Banking - Segmentation is done at various levels so that it actually provides proper guidance to the marketing staff :

* Demographic
* Geographic Mapping
* Community clusters
* Listing of entities

7) For corporate lending the target segment of companies could be defined by the following variables.

* Location
* Sales turnover
* Industry category
* Number of employees

Benefit of market Segmentation :

The seller who is alert to the needs of different market segments may gain in three ways

First, he is in a better position to spot and compare marketing opportunites. He can examine the needs of each segment against the current pomperitive offerings, and determine the extent of current satisfaction. Segments from low levels of satisfaction from current offerings may represent excellent marketing opportunites.

Second, the seller can use his knowledge of the marketing response differences of the various market segments to guide the allocation of his total marketing budget. The ultimate basis for meaningful segmentation are differences in customer response to different marketing tools. These response differences become the basis for deciding on the allocation of company market funds to different customers.

Third, the seller can make finer adjustments of his product and marketing appeals. Instead of one marketing program aimed to draw in all potential buyers (the'shotgun' approach), the seller can create separate marketing programs aimed to meet the needs of different buyers (the 'rifle' approach).

It can thus be clear that market segmentation market it easier for banks to identify focussed target market for its specific products in advt. to ensure better saleability acceptability in the market.

Q 2 d **Briefly explain the concept of marketing mix through a chart.**

Ans. 2 d Marketing mix : 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 Border, while quoting from an article of James Culliton, 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 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 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 persue its marketing objectives in the target market.

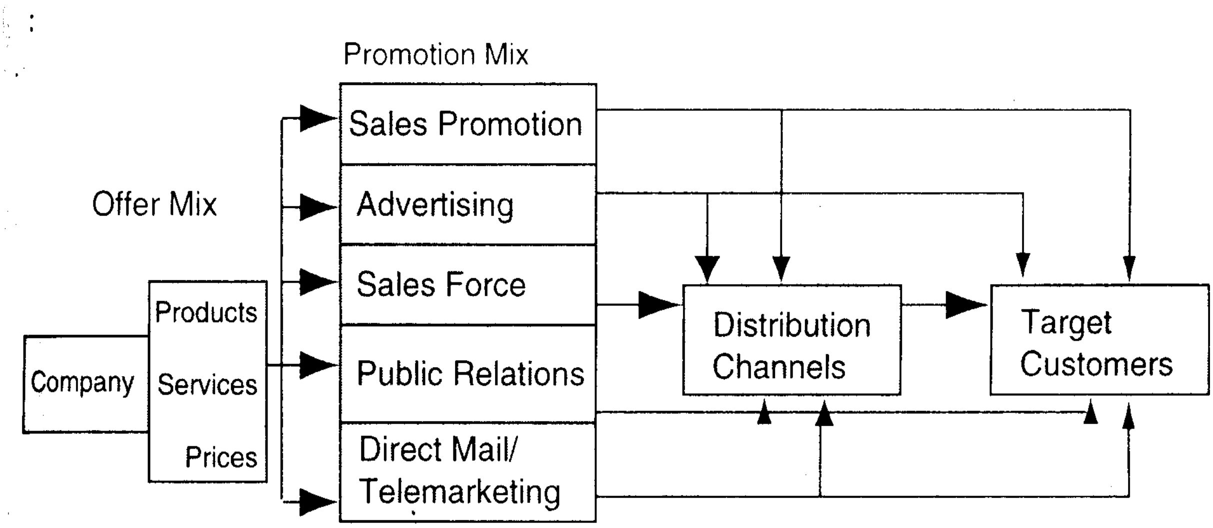
There are literally dozens of marketing mix tools. McCarthy popularized a four - factor classification of these tools called the four Ps : product, price, place (i.e. distribution) and promotion.

The particular marketing variables under each P are shown charts below

Charts A

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

Chart B



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.

Q 2 e Briefly illustrate important steps in selling process in Bank Marketing.

Ans. 2 e **Selling Process in Bank Marketing :**

A management orientation that 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 - its products.

From the above definition, the implicit 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 task then is to organise an effective sales force.

Peter Drucke' 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 then 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 possibly forget 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.

The marketing concept rests on four main pillars, namely

i. target mark,

ii. customer needs.

iii. integrated marketing,a nd

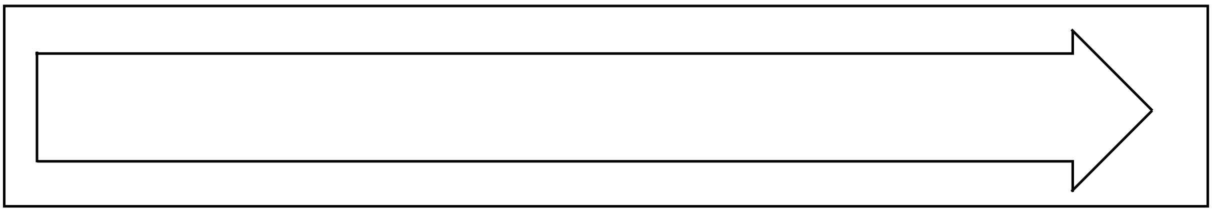
iv. profitability

These are shown in the following figure where they are contrasted with a selling orientation. The seling concept takes on 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 on outside-in perspective. It starts with a well-defined market, focuses on customer needs, integrates all the activities that will affect customers, and products profits by creating customer satisfaction.

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,

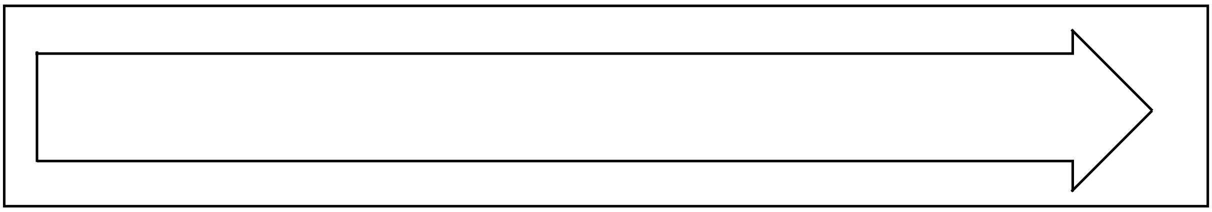
Figure : Selling and Marketing Concepts in Bank Marketing Contrasted

A) SELLING CONCEPT



Starting Point	Focus	Means	Ends
Bak/Branch Branch	Products Deposits advances	Selling & Promoting	Profits through Business

B) THE MARKETING CONCEPT



Starting Point	Focus	Means	Ends
Target Market	Customer Needs	Integrated Marketing	Profits through Customer Satisfaction

will need to adopt the 'strategic marketing concept' which he defines thus:

The strategic marketing concept is defined as

* the corporation's mission to seek a sustainable competitive advantage over competitors by meeting consumer needs.

Thus, when we focus are attention on what Bankers are basically concerned with service, it has many different characteristics which make bank marketing a little more demanding. It is therefore, that the selling process in Bank marketing - whether at corporate level or it branches has to be understood properly as a part & parcel of overall marketing process & business strategies are formulates accordingly.

SECTION III

Q 3. Answer in 10-15 sentences

a) Suggest suitable bank organisation structure for large corporate clients. Define the concept of venture teams.

b) What do you understand by 'Pricing Concept' in banking? What are the implications of higher cost and higher profit on selling a product. Illustrate your answer with suitable graphs.

c) Define product analysis and Explain the important steps in new product development. Illustrate any two new products in Indian Banks.

d) Mention the impact of atleast three banking regulations prevalent in India on bank marketing strategies.

Q 3 a Suggest suitable bank organisation structure for large corporate clients. Define the concept of venture teams.

Ans. 3 a Bank organisation structure for

Large corporate clients :

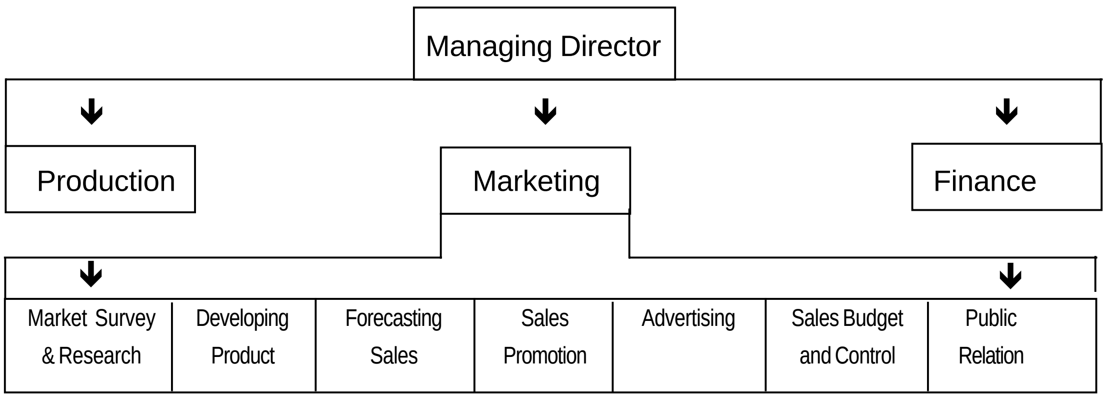
BANK ORGANISATION FOR LARGE CORPORATE CLIENTS

In fact there can hardly be any model organisation structure which will satisfactorily meet the requirements of all types of business.

The organisation structure depends on different factors like:

- size of a bank
- its branch network and geographical distribution
- the customers it serves
- people culture
- expansion plan
- selected market segments etc.

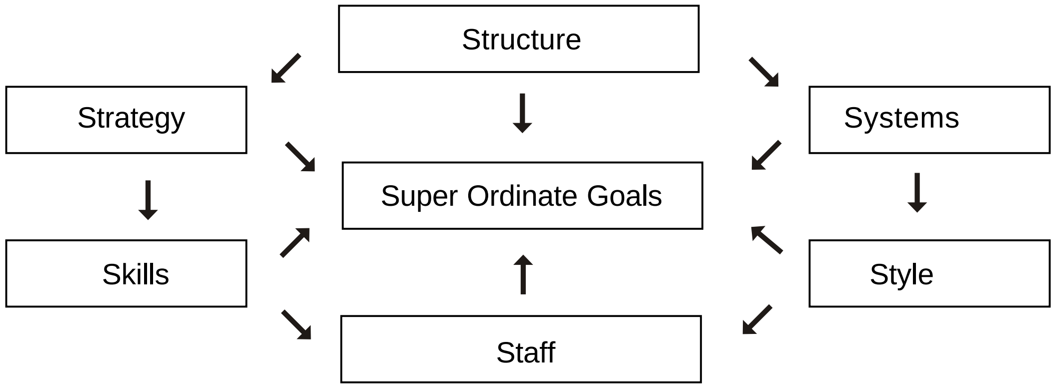
The marketing function in a firm or company is usually tackled through following Structure :



A well structured organisation for marketing is important to decide the success of marketing effort of any organisation. The concept of organisation has 5 main elements viz.

1. Putting together 4 'M's of Management (Men,Money,Material and Method) to achieve the planned goal
2. Proper Division/Distribution of work
3. Clearly defining each department's role and responsibility
4. Proper delegation of authority
5. Maintaining structural relationship

A new view of organisation depicts a '7-S' model as follows:



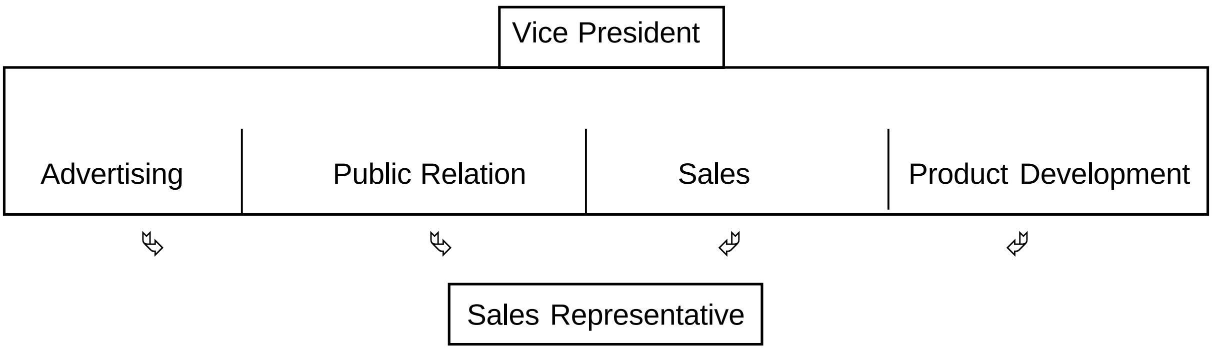
The 7-S are Superordanate goals, Structure, Strategy, Systems, Style, Staff and Skills.

Peter Drucker suggested 3 types of works to devise a proper organisation structure i.e.

1. Top management
2. Operating
3. Innovating work

In the context of a bank for catering of corporate clients needs, the all three works must integrate fully and properly.

In a typical bank organisation following can be structure of marketing division/department:



Any new organisation, as seen above, develops structure to manage production, finance and marketing function. The structure are modified and become complex with changing objectives and functions of the firm.

Venture Teams:-

Setting the organisational structure.

In deciding the Organisational structure, the most important thing to be borne in mind is that it should be functional effectively. Any chart on paper, howsoever attractive, may not be useful unless it can be functionally useful. It must be current, in tune with organisation's goals/objectives and allowing responsibility and authority to the people concerned.

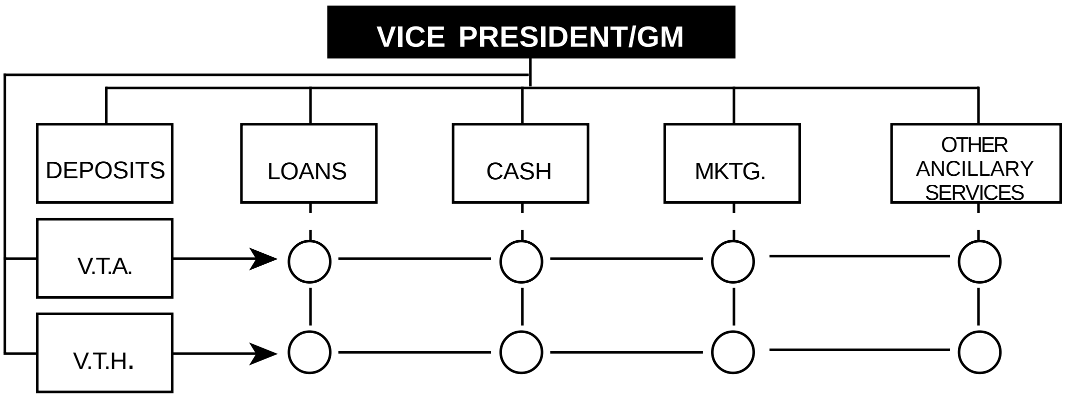
Three basic types of organisational structure are

- Line
- Line and staff
- Line and functional staff

In line organisation direct lines of control and responsibilities start with top management and come down to depths through line executives/managers and in turn to grassroots employees.

Line and staff organisations structure is similar to line type but here the need of a specialists is recognised - who advise to line managers without directly getting involved in management process.

In line and functional organisation. The functional staff is given authority, responsibility and access to top management for smooth functioning which is useful in specialised function like marketing.



V.T. = Venture Terms

The 'Venture Team' as shown above is application of the 'matrix approach' which can be useful to introduce/launch new products or service.

Such a venture team is drawn from the bank's existing personnel from various departments as per need arising to introduce product in the market. The team in that events is separated from the main organisation like a taskforce which is given flexible delegation to carry out the specific mission and it reports to the highest authority of the composite departments.

This structure is usable by banks in entering to the needs of large corporate clients as it gives flexibility, integration of functions and delegation for quick decision and facilitates easy achieving of targets.

Q 3 b **What do you understand by 'Pricing Concept' in banking? What are the implications of higher cost and higher profit on selling a product. Illustrate your answer with suitable graphs.**

Ans. 3 b **Pricing concept in Banking :**

(i) The Pricing Concept :

No discussion on marketing mix 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.

Pricing is equivalent to 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 organisations.

Pricing affects :

1. Sales Volume
2. Profit Margin
3. Rate of Return on Investment

4. Product Position

5. Image of the Organisation

Pricing is the key strategy through which the other marketing strategies have to pass in order to result into profit or revenue like :

RESULT

Other Marketing Strategies	-	Price Strategy	-	Revenue

See the relationship of pricing with profitability in a manufacturing concern. We can see the following break-up :

Direct Expenditure	Direct Material Direct Labour Direct Expenses	Prime Cost
Indirect Expenditure	Work Expenditure or Factory Expenditure	Factory Cost
Indirect Expenses	Administration Expenses Selling Expenses	Cost of Production Cost of sales
Margin	Selling Price	Selling Price

Price simply read can be described as 'cost plus profit'. Therefore, proper analysis of cost and proper decision regarding profit level have direct impact on pricing decisions/strategy.

Normally direct expenses, which vary wiz volume of production/sales, are variable cost and indirect expenses are fixed cost.

It is desirable to study the pricing systems. There are 4 main cost related pricing systems which are :

1. Standard cost pricing
2. Cost-plus pricing
3. Break even analysis
4. Managerial pricing

In the discussion on Pricing in Banking, it is essential to know the typical pricing objectives - important of 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 it is indicator of acceptability of price.
3. Competition - To face competition, prices can be lowered to maintain sales or in the absence of it prices can be raised 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.

Ans. 3. ii Pricing methods/strategies : We have seen that as described by Winkler there are 3 types of pricing methods -

a. Cost related
b. Market related
c. Competition related

As we have briefly seen earlier there are four major cost related pricing methods -

1. Standard - cost pricing
2. Cost plus profit
3. Break even analysis
4. Marginal pricing

1. Standard Cost pricing :

This is based on the cost standards developed by management accounting systems.

In this the (standard) variable cost is calculated by adding the total variable cost of production (cost of material, direct labour and cost of component) dividing by the number of units produced.

The following steps are important -

a. calculate the standard variable cost/unit

b. calculate the fixed cost/unit

c. decide the required profit per unit

d. add a+b+c to give provisional rate

e. Analyse market price for competitive product

f. Adjust provisional price to account for market price level.

COST-PLUS-PROFIT PRICING

Means to all a standard mark upto the total cost of product

E.g. Suppose a retailer pays to a manufacturer Rs. 100/- per unit of product and marks upto sell it at Rs. 150/- per unit, there is Rs. 50/- (50%) mark-up which is the retailers margin. If the retailers cost of storage and selling rate Rs. 40/- then the profit margin will be mark-up cost retailer cost (50-40) = Rs 10/- or 10%.

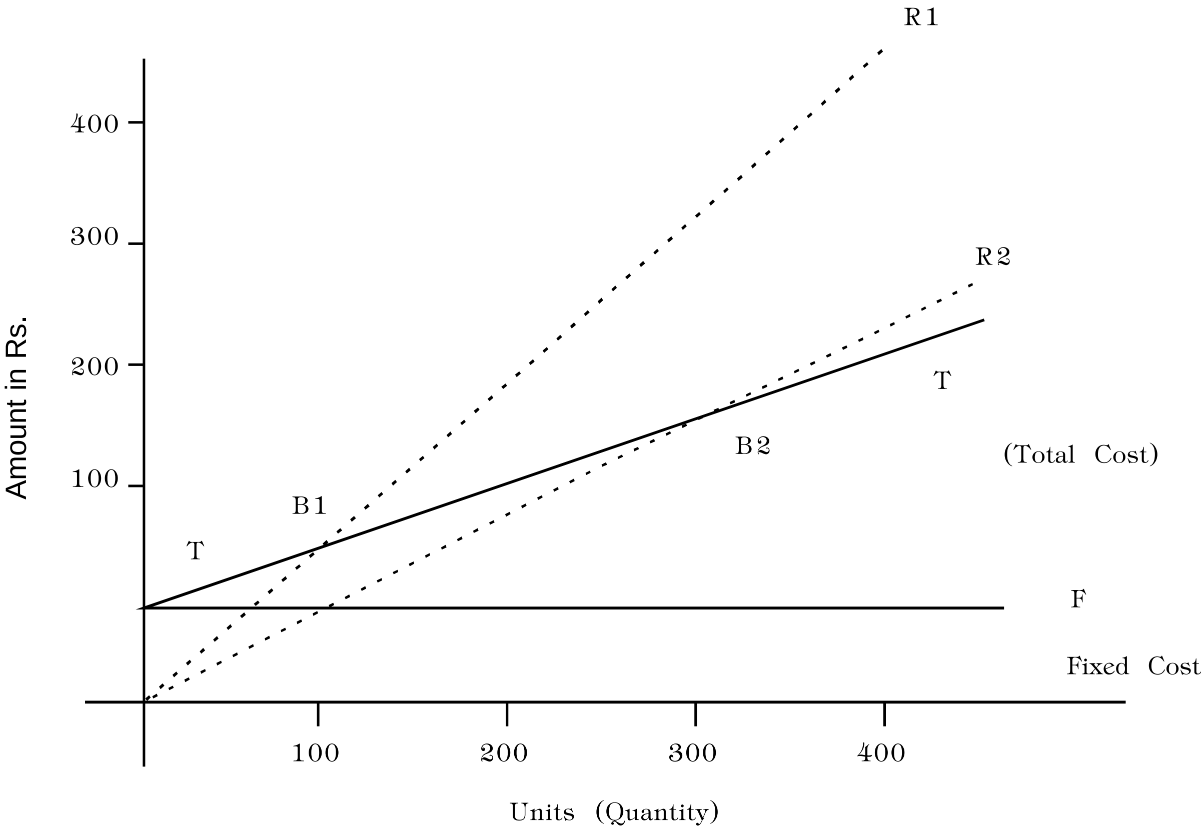
BREAK-EVEN ANALYSIS

This method uses the break evern chart to develop a system of profit pricing target where the organisation can determine the price which will produce the required level of profit.

Although it is profit related a proper analysis and decision regarding fixed cost and variable cost are important in this method.

It, thus takes into account the total price (revenue) as well as the demand.

Let us see the following figure to know the mechanism better :



Steps required -

1. Calculate fixed cost (curve F)

2. Calculate variable cost per unit.

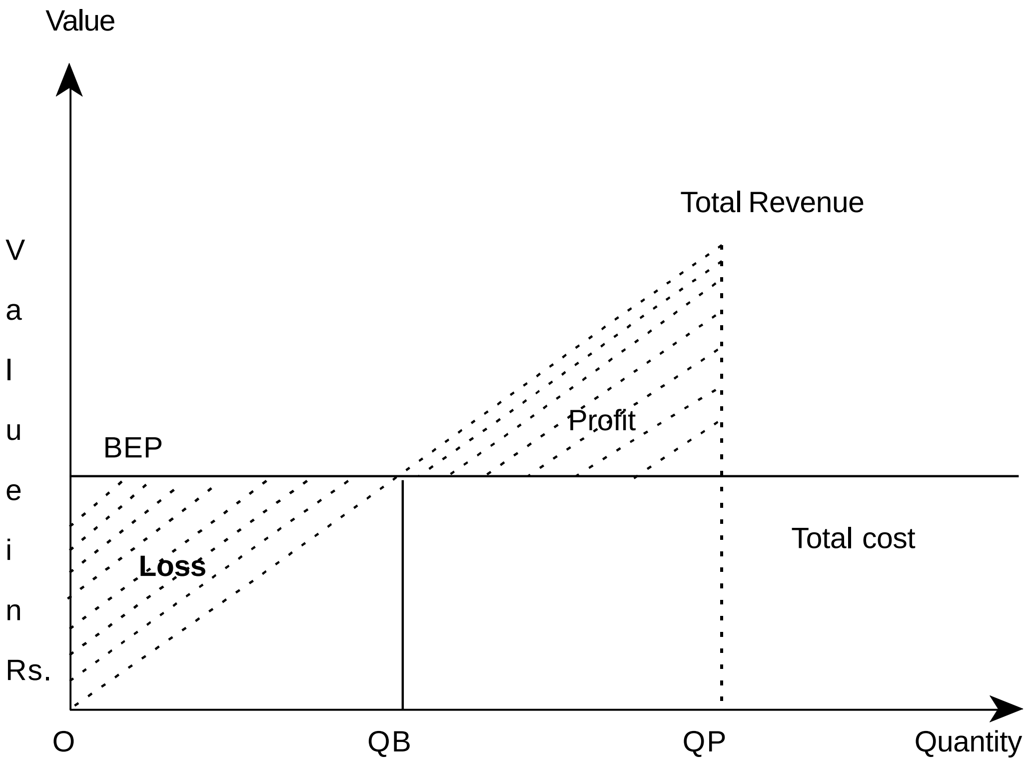
3. Add variable cost to F to arrive at total cost T.

4. Product total revenue curve based on the decided price per unit sold.

   In the example R1 and R2 are two levels of price per unit sold.

5. Break even point is where total revenue curve intersects with total cost curve at B1, B2.

BEP = Total cost = Total revenue i.e. Break even point is where total cost equal total revenue. We can extend the break even analysis to see the relationship of price with profit or loss as follows :



If we combine total cost line with total revenue line we get the graph as shown at "C". The point where two line intersect is the break even point and OB represents the break even quantity i.e., the point at which the total costs are equal to the total revenue i.e. neither profit nor loss. In case less than this quantity (number of units) is produced it will be loss and more than this (QB) if produced and sold, it will be profit.

Ans. 3 iii **Pricing concept in Banking :**

Mr. J.J. Ward in his book on Export Marketing Management has mentioned some of the marketing objectives vis-a-vis their pricing implications which can be tabulated as below :

Marketing Area	**Marketing Objective**	**Pricing Implication**
Product	Improved Quality Acceptances	Higher cost = price rise or lower profit
Advertising & Promotion	Stronger Support	Increased Advtg. budget = price increase or lower profit.
Distribution	Additional Selling Points	Probably Higher Distribution cost = margin increase
Consumers/Users	Greater Acceptance	Increased Advtg/publicity effort i.e. higher distribution cost = higher price or lesser profit.

As we focus our attention to marketing of banking services and further on the pricing aspects, these are 2 major costs which have to be considered and they are :

a . Interest cost

b. Servicing cost

If we analyse the profitability statement of any bank it shows following broad classification :

Interest Cost	-	67
Admn, (staff) cost	-	27
Other (non-int) cost	-	6
		100

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 force did not affect to any considerable extent.

Pricing policy and 'strategies, however, is equally relevant in banking due to the fact that if 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.

Q 3 c Define product analysis and Explain the important steps in new product development. Illustrate any two new products in Indian Banks.

Ans. 3 c Product Analysis & product Development : Product mix being an important concept in bank marketing, product mix analysis is imperative to decide on continuance of existing products or adding new products. This decision will be of course, based on market research w.r.t. the

- Potential Demand
- Gap Analysis
- SWOT Analysis for the bank.

This analysis has to throw enough light on bank's position w.r.t. its strengths, weaknesses, opportunities and threats in the existing and future market vis-a-vis the customers' present and future needs. The need to add new products or remove obsolete-non-profitable products can come to surface after such an in-depth analysis which has to be done periodically by every bank.

Product analysis as a strategy can be better illustrated by the following Grid developed by Prof. Pradeep Kumar in his book on marketing management.

Product Strategy	**Market Strategies**		
	No market change	Improved market	New Market
No Product Change	Design simplification Greater integration	Branding Change Change in Package	New Uses New Users
Product Change	Product Line Simplification New Models	Product Customerisation	Market Extension
New Product	Replacement of old product	Diversification	Product Diversification

An in-depth analysis based on these strategies can make clear the need to continue, innovate, withdraw old product or to launch a new product in the market.

NEW PRODUCT DEVELOPMENT

The new product can be developed in new market or existing market. New product can also be launched in improved market on 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 product and also ensures profits.

New product development starts with the maturity or decline of an existing product or due to lack of demand or due to obsolescence of a product. Stiff competition compels a bank to think of new ideas for survival or success in a given market. Based on changing customer wants and needs the bank's market research department generates new ideas.

Such ideas are subjected to discussion and examination by expert bankers; economists experienced field staff and marketing experts within a bank to validate the applicability of such ideas to lead to new and saleable product.

Normally such ideas for new products pass through following stages :

IDEA

↓

POTENTIAL FOR NEW PRODUCT

↓

SELECTING A NEW PRODUCT FROM NUMBER OF OPTIONS

↓

DETERMINE ACCEPTABILITY BY BANK

↓

DETERMINE ACCEPTABILITY BY CUSTOMERS

↓

DETERMINE THE PRICE

↓

DETERMINE ADVERTISING POSITION

↓

DECIDE AS MOST EFFECTIVE METHOD OF PROMOTION

↓

PROPERLY TIMED LAUNCHING OF NEW PRODUCT

New Product Development by Bank : 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-60s, seventy-five commercial banks had set up such credit plans. However, risk of recovery and lack of quick profits led 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 a buzzword and 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.

Developing Deposit Scheme : Any product or service developed by a bank 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 Customers are :

- Financial Security
- Quick Service
- Convenience
- Attractive Yield
- Low Cost Loans
- Personalised Service
- Advice/Counselling
- Easy Access
- Simple Procedure
- Attractive Package
- Friendly Approach
- Variety of Products

This list is only illustrative.

The product conceptualisation and development has to bear these needs in mind.

A banker may group these needs into following segments to plan to develop new Deposit schemes to its customers needs :

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 presonalised service at convenient location.

Q 3 d Mention the impact of atleast three banking regulations prevalent in India on bank marketing strategies.

Ans 3. d Banking Regulation & their impact on Bank marketing strategies :

(A) Banking Regulation :

Banks are normally subject to three types of regulation :

i. ***Structural regulation :*** There are limits to the activities they may pursue.

ii. ***Prudential regulation :*** There are constraints with regard to their own internal finance, principally in relation to capital adequacy, liquidity and solvency;

iii. ***Investor protection :*** There are regulations designed to protect their clients from fraud and dubious practices.

In India Reserve Bank of India exercises control over the activities of banks by virtue of the powers vested in it under the Banking Regulation Act, 1949 and the Reserve Bank of India Act, 1934.

Under selective credit control, RBI can determine policy in relation to advances, to be followed by banks generally or by any bank in particular. RBI's directives may cover issues like the purpose of advances, margins to be maintained, rate of interest and any other terms and conditions.

Apart from the selective credit control directives, the measures that have impact on the volume of bank credit, are the operations through the following instruments :

i. The Bank Rate

ii. Open Market Operations

iii. Variable Cash Reserve Requirements

i. The Bank Rate

Whenever the Reserve Bank wants to reduce the level of credit, the bank rate is raised and when credit is to be expanded, bank rate is reduced. This is because, by changing the bank rate, RBI seeks to influence the cost of bank credit.

ii. Open Market Operations

The Reserve Bank can influence the reserves of commercial banks, i.e. the cash base of commercial banks by buying or selling Government Securities in the open market. If the RBI buys Government Securities in the market from commercial banks, there is transfer of cash from the Reserve Bank to the commercial banks and this increases the cash base of the commercial banks enabling them to expand credit and conversely if the Reserve Bank sells Government Securities to Commercial banks, the funds position with them get affected in a manner that would restrict credit expansion.

iii. Variable Cash Reserve Requirements :

Cash Reserve Ratio is a tool being used by which Reserve Bank to control the funds availability in the market. Variation in the Statutory liquidity ratio also is another tool at the disposal of Reserve Bank.

(B) Impact of Banking Regulation on Bank Marketing :

The impact on the business decisions of the banks has been multi-fold. The cost of funds mobilisation had shot up considerably in the market, and hence many banks with fewer number of branches in rural and semi-urban areas raise short term deposit rates substantially to tide over the asset liability mismatch and also to avoid defaulting on the statutory pre-emptions. The asset liability management of banks come under strain in situations of high volatility in the money market and foreign exchange market, particularly when the deregulated business decisions of banks do not necessarily fall in line with the moves of the regulatory authorities.

Banking Regulations & the related development in the market have a direct bearing on the business strategies of the banks. This also greatly emphasizes the need to have market oriented strategic planning in Banks.

SECTION IV

Q 4. What is marketing planning with reference to marketing of banking services? Differentiate between marketing plan and marketing planning process.

Ans. 4. **Marketing plan & marketing**

Planning Process :

A Marketing plan is a documents which formulates a plan for marketing products &/or services. The overall marketing plan can be made up of a no. of smaller marketing plans for individual products or areas. The Bank's marketing plan sets out its marketing objective & suggests strategies to achieve them.

'Marketing Planning' is a process which involves application of marketing resources to achieve marketing objectives. It is used to segment markets, identify market position. Forecast market size & play a viable market share within each market segment.

'Meaning & Importance of marketing planning in marketing of Banking Service :'

Any company's management has many important roles. It sets objectives, and develops plans, policies, procedures, strategies and tactics. It organises and co-ordinates, directs and controls, motivates and communicates. Planning is only one of its roles but it is an important one : the company's corporate or business plan runs the business.

The marketing plan is one part, albeit an important part, of this plan. The marketing planning process therefore needs to be carried out as part of the overall planning and budgeting process of a Bank.

There are a number of different approaches that a Bank can adopt in planning for the future. In traditional planning, the plans can be differentiated according to the time-scales they cover, i.e. :

* long-term plans
* medium-term plans
* short-term plans

There is no universal definition of the length of time covered by these types of plans. Long-and medium-term plans are often defined as 'strategic' plans because they consider the longer-term strategies for the business, and short-term plans are often defined as 'corporate' or business plans because they are plans that 'run' the business on a day-to-day basis. The use of these plans depends on the type of business the markets that it serves and the need for future planning of products and expansion.

Long-term planning aims to assess future economic and business trends for many years ahead. It enables a Bank to determine strategies that will sustain growth and meet corporate objectives in the long-term. Long-term planning in these cases may cover periods of up to ten or twenty years. Most Banks do not, however, have such long product development times and in these companies long-term planning looks no further ahead than five or seven years.

Medium-term planning is more practical and normally covers a period of two to five years (with three years being the most common). This is a more practical exercise because the planners are nearer to the present. Fewer assumptions need to be made and the plan is more likely to reflect what will actually happen. The medium-term plan, but will include the major decisions necessary in the shorter term. These decisions will include such things as the introduction of new products, capital investment requirements, and the availability and utilisation of personnel and resources.

Short-term planning (and budgeting) normally cover a one-year period and produces the company 'corporate' or 'business' plan with its associated budgets. This is a plan that covers the immediate future and details what the company intends to do over a twelve-month period (tied in to the Bank financial year). Short-term plans are produced in much more detail than other types of plans. They may also be revised within the year if necessary.

Difference between marketing plan & the marketing planning of process.

'Promotion' and 'Place' are concerned with reaching your potential customers in the first place and 'Products' and 'Price' will allow you to satisfy the customer's requirements.

The 'marketing mix' is often known as the four Ps'. They are four controllable variables which allow a company to come up with a policy which is profitable and satisfies its customers. We shall be discussing the seven Ps as applicable to service marketing, in the next unit.

Markets usually consist of a number of submarkets with different customer requirements. A company must create an appropriate marketing mix for each of its sub-markets. An example, the car sales market consists of fleet markets, the company car market, and the private car market-each with its own requirements.

Each element of the marketing mix is a continuing opportunity to the marketing organisation it must be considered separately and in relation to the other elements of the marketing mix. A mix which is satisfactory at one moment in time may need to be revised because :

- Products or services will become absolute or will be improved
- New products or services will be introduced
- Prices may be reduced by the competition and this may reduce margins
- Promotion may not be as effective as that of the competition.
- The place of sale or method of distribution may become less satisfactory as alternatives arise or the business changes.

Controlling the marketing mix is the key to successful marketing and this is the essence of marketing planning.

Q 5. Describe in detail various behavioural models for analysing buyer behaviour with specific reference to banking.

Ans. 5. Behavioural models for analysing Buyer Behaviour W.r.t. Banking :

Since Psychology of customer & Buyer behaviour form the basis of successful Bank marketing study of behaviour models is very important in analysing Buyer Behaviour with specific reference to Banking :-

BEHAVIOURAL MODELS FOR ANALYZING BUYERS

Five different models of the buyer;s "black box" are detailed along with their respective marketing applications.

a. The Marshallian model, stressing economic motivations

b. The Pavlovian model, learning

c. The Freudian model, psycho-analytical motivations

d. The Veblenian model, psycho-social factors and

e. The Hobbesian model, organizational factors.

These models represent radically different conceptions of the mainspring of human behaviour.

The Marshallina 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 economics 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 Bentham 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 assumptions 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 **modern utility theory : economic man is bent on maximizing 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 a box of "Ship" and "Shakti" matches, he may apply econimic 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 suggest useful behavioural hypothese such as :

1. The lower the price of the product, the higher the sales.
2. The 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.
3. The higher the real income, the higher the sales of this product, provided it is not an "inferior" product.

4. The higher the promotional expenditures, the higher the sales.

The validity of these hypotheses does not rest on whether all individuals act as economic calculating machines in making their purchasing decisions.

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 a 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 Marshallan model ignores the fundamental question of how product and brand preferences are formed. It represents a useful frame of reference for analyzing only one small corner of the buyer's mind the "black box".

The Pavlovian Learning Model

This has its origins in the experiments that a Russian psychologist named Pavlov conducted on dogs. Pavlov rang a bell each time before feeding a dog. Soon he was able to induce the dog 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 are derived socially - such as cooperation, fear, acquisitiveness.

Cue - a dirve 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 dirve in a child. His response will depend upon this cue and other cues, such as the time of day, the availability of other thirst quenchers, and the cues intensity.

Response - the response is the organism's reactions to 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.

Reinforcement - If the experience is rewarding, a particular response is reinforced; 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 reinforced, 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 to location, timing, service standards, facilities, etc.

Marketing applications of the Paviovian model

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

An example would be in the problem of introducing a new brand in a highly competitive market. The company's goal is to extinguish existing brand habits and form new habits among consumers for its brand. But the company must first get customers to try its brand; and it has to decide between using weak cues and strong cues.

Light introductory advertising is a weak cue compared with dirstributing free samples. Strong cues, although costing more, may be necessary in markets characterized 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.

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. It "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 product.

The 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 indentified. For chocolates, it may be hunger,; for cars, it may be status; for safety belts, fear. The marketing and advertising practitioners must search his cue box - words, colours, 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 realizes his separateness from the rest of the world and yet his dependence on its. 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 centre for finding outlets for his drives. And 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 are not obvious to the casual observer nor deeply understood by the individual himself. If asked why he purchased an expensive sports car, he may reply that he liked its speed and shape. At a deeper level he may have purchased the car to impress others, or to feel bound again. At a still deeper level, he may be purchasing the sports car to achieve substitute gratification for unsatisfied sexual striving.

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 a bar of soap from a square to a round shape may be more important in tis sexual than its functional connotatiions. A cake mix that is advertised as involving practically no labour may alienate housewives because the easy life may evoke a sense of guilt.

Motivational research has proved some interesting and bizarre hypothesis about what may be in the buyer's mind regarding certain purchases. Thus it can be suggested at one time or another that :

* Many a businessman don't fly because of a fear of posthumous guilt - if he crashed, his wife would think of him as stupid for not taking a train.

* Men want their cigars to be odoriferous, in order to prove that they are masculine.

* Consumers prefer vegetable oil because animal fats stimulates a sense of sin.

Unfortunately the usual survey techniques - direct observation and interviewing - can be used to establish the representativeness of more superficial characteristics - age and family size, for example - but are not feasible for establishing the frequency of the mental states which are presumed to be deeply “buried” within each individual.

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 of hopes, dreams and fears can often be as effective in stimulating purchase as more rationally-directed appeals.

The Veblenian Social - Psychological 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 saw 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 groupings to which his life is bound. **(His wants are greatly moulded by his present group memberships and his aspired group memberships).**

Veblen’s best know example of this is in his description of **(the leisure class)**. His hypothesis is 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 clothers, 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 of the class immediately above it. And important segments of the affluent class practice conspicuous underconsumption. 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 airconditioners before their neighbours did.

Marketing application of the Veblenian Model

The various streams of thought crystallized into the modern social sciences of sociology, cultural anthropology, and social psychology. Basic to them is the view that man's attitudes 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.

Q 6. Describe the concept of product life cycle and illustrate products strategies using the concept for managing marketing of banking products.

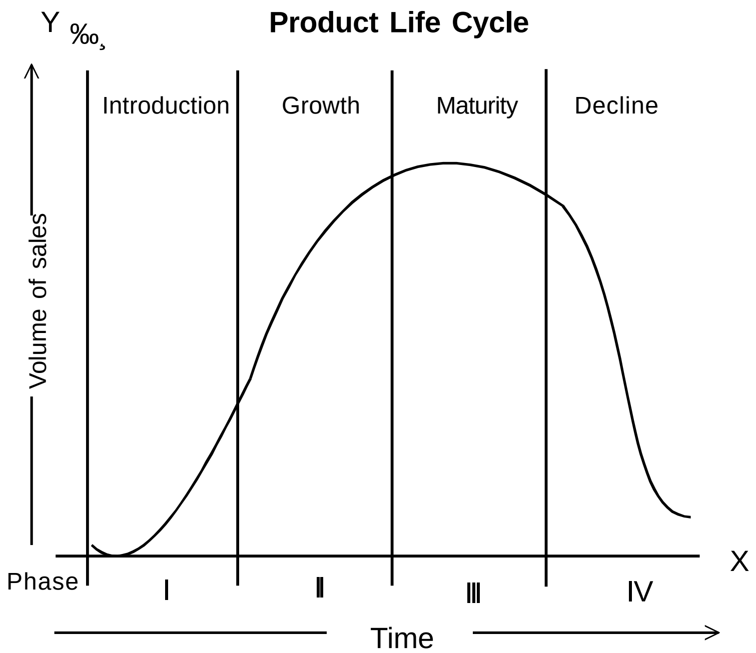
Ans. 6 Concept of Product Life Cycle & product strategies for marketing of Banking Products :-

As the product volume (sales) and sales revenue follows a typical pattern, the concept of product life cycle has been on the important concepts in marketing which must be properly understood.

As each product passes thorugh certain typical but definite stages in its life-span, we will look up into the important stages :

i.	Introduction	ii.	Growth
iii.	Maturity	iv.	Saturation
v.	Decline	vi.	Obsolescence

It must be borne clearly in mind that the growth of decline depends not on product alone but the market in which it is launched.



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 viewpoint 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 stage in the product life cycle is characterised by low sales and most of 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.

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 acceptances of the product is the key factor at this stage.

Maturity Stage :

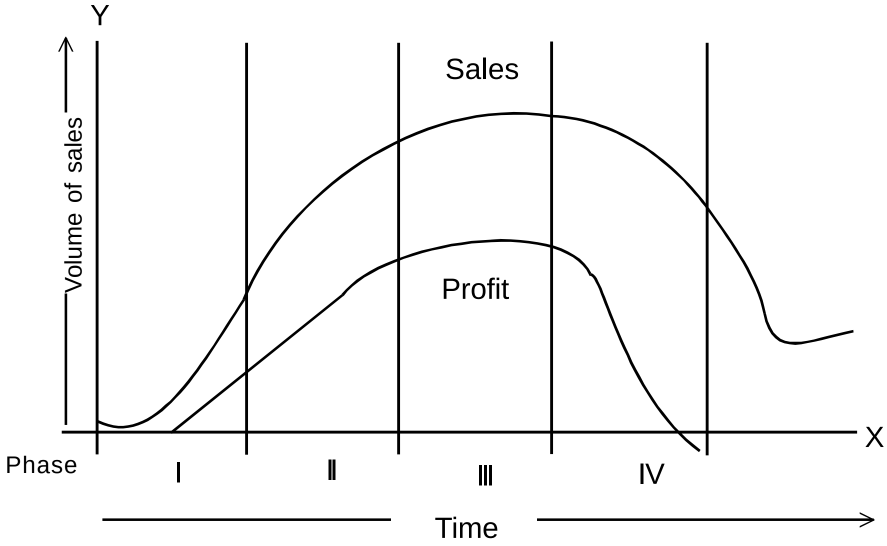
Having continued at the growth stage, the product then enters into the maturity stage. The most notable indicator of this phase can be the initial stability and then slowdown in volume of sales/ profit.

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 stabilise the growth 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 a downward shift/drift in sales or reduction in profit may start. Except in case of new or diversified products in banking industry such sudden decline cases are not many. We will see the application in the foregoing paragraphs w.r.t. decline, death or obsolescence of bank products.

The following figure will illustrate volume and profit relationship in the life cycle of a product :



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 data and quarterly business figures compiled by the planning divisions can indicate the demand and supply position of various products as inter se composition (vis-a-vis budgetted pattern) and as a per cent 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.

Product life cycle governs the strategic marketing planning at different levels.

Using Product Life Cycle to Manage Marketing Banking Products

The introductory stage of the product’s life cycle is characterised by low or negligible sales and negligible or no profit. When any new account or product which is designed to suit to a particular segment of customer is launched after research by R & 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 ‘O’ 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 w.r.t. the design, pricing and need to launch new or innovative products/services to ensure customer’s interest and loyalty to their bank accounts.

Observing and monitoring the product life cycle it becomes easier to decide and implement the product development strategy.

Generally, these are 4 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 show through the following figure :

	Existing Market	New Market
Existing Products ®	Market Penetration A	Market Development B
New Products ®	Product Development C	Diversification D

OR

Q. 6 Describe the meaning of corporate clients and how would you market various banking products to one such corporate client as a marketing strategy.

Ans. Corporate Clients :Nationalised banks have been and are being governed by Government Policies spelt out for them under priority sector lending, they have social obligations to fulfil, the deposit rates have so far been controlled by the Reserve Bank of India and I.B.A. and the products have lot of common factors. The rates of interest on deposit and advances being not very flexible the bank have to plan within the band (spread) and manage expenses and administrative cost etc. with in limited range.

The inflation, money supply, lack of demand for funds and changing pattern of deposits has been affecting bank's fund management function and budgets to considerable extent. The composition of deposits and advances has been showing wide variations which affects the profitability. The banks have, therefore, started to concentrate on innovative ways to limit the cost and increase profits to strengthen their capital base, meet the salary and other cost and simultaneously meeting the social obligations.

It can be said that future banking in India will be governed by rules of business quoted by Jack Welch, CEO to General Electric in 1981 and they are :

a. Control you destiny or someone else will.

b. Change before you have to

c. If you don't have a competitive advantage, do not compete.

The banks normally decide whether their generic strategies will be

i. Customer driven or

ii. Competitor driven

this strategy has to stress up from :

- climate
- customer
- competition
- culture

Banks have become aware of competition in the market and trying to be competent by identifying the core competencies, niche markets and trying to do their business with more awareness about proper mix of deposits and advances, cost of transaction and non-interest income to maintain if not improve the profits.

MEANING OF CORPORATE CLIENTS

Traditionally the banks have been catering to the financial needs of the following broad categories of customer :

a. Household

b. Agricultural

c. Industrial

d. Government

If we take a look at the performance budget of any bank we find the following classification of customers either as Depositors or Borrowers :

Aggregate Deposits

	Past	Present	Future		Past	Present	Future
i. Current Deposits				i. Priority Sector - SSI - Transport - Prof. & Def. employed			
ii. Savings Deposits				ii. Exports			
iii. Term Deposits				iii. Residual - Wholesale - Industry - Others			
TOTAL				TOTAL			

As the composition of these categories affect the profitability of a bank, its business and marketing strategy has to take into account the past trend in each category, present levels and future levels as a composition of 100 (in %). This depends on the total market and share of each category, inter-se, showed by various banks in the command area of the given bank.

In deciding and devising the promotional strategies and marketing mix, the banks usually decide upon proper segmentation of customers while devising the annual performance budget like :

Individual customers - household

Corporate customers *

Small businessmen customers

Rural Customers (farmers, agriculturalists, etc.)

The small businessman can include service activities like retail shop, retail business, repairs activities.

* Corporate Customer : is a segment which includes non-household customers i.e. manufacturer, traders, transport operation, service organisations, exporters, etc.

For the purpose of marketing strategy the corporate customers again are viewed from two angles :

a. Priority Sector

b. Non-priority Sector

as the former one being under social obligation criteria is covered under concessional interest rate whereas the latter one can be covered under commercial and have separate classification under business (profit) planning exercise.

Special Category w.r.t. Marketing of Banking Products :

We have already seen in the earlier paras as to the concept of Corporate Clients. In the market segmentation exercise, this segment plays an important role as the major chunk of loanable funds is utilised by this segment of corporate clients. If we analyse the credit portfolio of any bank, it can be seen that the borrowings to this sector constitute a large per cent share of the total credits granted.

The corporate borrowers are classified further in terms of their credit needs viz, loan, overdraft, cash credit, bills purchased, bills discounted, mortgage loans, etc. The credit needs are met with through working capital finance (for current assets) or through term loan (for fixed assets).

Product/Service - A survey of the banking services utilised by the corporate clients indicates that they avail the following types of facilities/services :

1. Term Loans for Fixed Assets
2. Working Capital for Current Assets
3. Remittance Facility
4. Letter of Credit - Inland or Foreign
5. Bank Guarantees
6. Fixed (Time) Deposits
7. Lines of Credit
8. Investment Guidance Cell
9. Merchant Banking Services
10. Foreign Exchange Service

1. Term Loan for Fixed Assets :

To cater to the needs of corporate clients regarding their expansion/diversification of activities and also for financing the fixed assets like plant and machinery or land and building (as a part of the project) bank finance by way of term loans.

Term loans can be short term, medium term and long term loans with a repayment spanning from 1 year to 7 years. Based on the need of the project and stipulating a margin of about 25% as the clients own contribution, banks finance up to 75% of the asset value as term loans. The repayment instalments are decided depending upon the cash flow and generating/servicing capacity of the customer. Due to shift in deposit mix banks normally don't encourage very long term loans but do consider short term and medium term loans. These are secured against charging the fixed assets for e.g. which the loan is granted.

2. Working Capital for Current Assets :

The funds required for day-to-day operations by a corporate client are known as working capital and banks readily consider finance/limits for such type of banking need.

There are two concepts of working capital - Net and Gross. Net working capital is the difference between the current assets and current liabilities whereas gross working capital means the total of all current assets. The net working capital indicates the amount received from long term sources to finance the part of working capital build up. The gross working capital represents the amount required for the corporate client's day-to-day operations.

The requirements of Working Capital of corporate client depends on the level of sale projections which decides the build up of required inventory in the form of raw material, semi-finished goods, finished good and receivables, if any. In fact the operating cycle prevalent in an industry determines the required level of working capital finance by a corporate client. The operating cycle is the time taken to complete the production process staring from cash to resultant cash proceeds from the sales.