Marketing Financial Products

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Preface

"The potential of the Indian market is attracting many new entrants and this is likely to continue over the next five years."

- Alpesh Shah, director, The Boston Consulting Group (BCG), commenting on the total financial assets managed by funds in India.[1]

"Change and growth are throwing up new opportunities and challenges for the Indian financial services sector. … This (period of sustained growth) will be driven by continued urban consumer demand, expansion into rural markets, corporate investment in India and overseas, and leveraging of core competencies in international markets."

- K V Kamath, managing director and CEO of ICICI Bank, in the Businessworld BW Banking Special 2006.

Organizations, both existing players and potential entrants, are looking to aggressively compete in the growing banking, financial services, and insurance (BFSI) sector in India. Consequently, there is a lot of action on the marketing front, as evidenced by the following list of selected news items from a leading business newspaper. The list is indicative of the relevance and use of almost the entire spectrum of marketing aspects in marketing financial products in the Indian market.

"Business intelligence tools catching up with the insurance sector"

"Bharti Retail likely to offer telecom, insurance services"

"Insurance companies to bid jointly for Air-India cover: PSUs form consortium, private players may follow suit"

"ING Vysya Bank to support SMEs"

"UTI Mutual rolls out gold Exchange Traded Fund (ETF)"

"State Bank spares educational, home loan borrowers from hike"

"Vodafone, Citigroup eye GSM (mobile) money transfer"

"ICICI Prudential eyes 100% growth in premium"

"Financial services companies are partnering B-schools to design industry-specific courses"

"Banks build on kinder home loan recovery process"

"RBI raises doubts on microcredit: Asks banks to adhere to customer identification"

"Law on insurance FDI soon"

"UK mulls 'financial inclusion' fund for developing world"

"NPAs of banks under control: Finance Minister"

Need for this Book

There are very few books that provide a balanced coverage on marketing financial products, either in the international context or in the Indian context. There are some books which focus on a specific financial product or service – such as banking services or mutual funds, and then briefly discuss the associated marketing challenges.

[1] Quoted in a news item in the Business Standard, dated December 21, 2006.

There are others that are oriented toward the marketing of services (or products) in general, with just one or two chapters dedicated to marketing financial products. This lacuna is more pronounced in the context of the Indian business environment of the 21^{st} century. This book aims to fill this gap by first addressing the conceptual issues relevant to marketing financial products, and then giving special coverage to each of the major categories of financial products and services in the Indian scenario.

Organization of the Book

The book is organized into three parts: we start with a macro-level picture of marketing financial products, then drill down into the details of different financial products, and finally return to the macro-view in terms of trends (in India) and international perspectives.

Part I: In the first part, *Marketing Financial Products: The Big Picture*, we begin with an introduction to marketing financial products; this sets the context for the remaining chapters in the book. In the second chapter, we discuss consumer behavior, marketing strategy, marketing research, segmentation, targeting, positioning – especially organizational positioning, and the customer service imperative in the BFSI sector. In Chapter 3, we focus on two important determinants of success -- product management and customer relationship management (CRM), from the perspective of a financial product marketer.

Part II: In the second part, *Marketing Financial Products: A Closer Look*, we take an in-depth look at the marketing aspects for each product category and/or customer segment. Chapters 4, 5, and 6 focus on corporate banking, retail banking, and credit cards respectively. Chapter 7 focuses on non-life insurance and Chapter 8 on life insurance. Marketers in other product categories cannot afford to ignore the competition from small savings and retirement planning products for a share of the consumer spending on financial products. In Chapter 9, we dwell on small savings and retirement planning. Chapter 10 discusses the products and marketing mix for mutual funds, along with the emerging trend of mutual banking. Chapter 11 is dedicated to the marketing of fee-based services -- both corporate and retail services.

Part III: The last part of the book, *Trends and International Perspectives*, consists of two chapters. Chapter 12 discusses the trends in India, in banking and insurance marketing. Chapter 13 takes a look at the global scenario in financial products marketing, with specific reference to the markets in the United States, the United Kingdom, and China.

Using this Book

A. Courseware for academic use:

As a part of courseware, this book can be used as a basic text for an elective course on marketing financial products and services, in a post-graduate program in management, commerce, or business administration. For a focused one-year program or certificate program on the BFSI sector or on a specific segment of the BFSI sector, this book can be used in the final term.

Pre-requisites: An understanding of marketing management is a mandatory pre-requisite. An introduction to services marketing is a desired pre-requisite, especially an appreciation of the characteristics that distinguish a service from a product, consumer behavior in services, services marketing strategy, elements of the services marketing mix – including people, process, and physical evidence, and service quality. If required, the faculty may devote a few sessions in the session plan to first address the essentials of services marketing, before taking up financial products marketing.

B. Professional reference for practitioners:

- If you are a middle-level/senior manager in the BFSI sector, this book provides you with practical insights on the experiences of various financial product marketers.
- If you are an executive engaged in sales/operations jobs in this sector, this book would be a useful reference to prepare yourself for upward career progression into middle management.
- If you are a marketing professional from other product-based/service-based industries and wish to move laterally into the BFSI sector, this book would be a handy guide to understand the characteristics of financial products and their implications for marketing strategies and tactics.

If your focus is on…	**…read the following chapters**
Corporate marketing of financial products	1, 2, 3, 4, 6, 7, 8, 9, 11, 12, and 13
Retail marketing of banking products (including credit cards)	1, 2, 3, 5, 6, 11, 12, and 13.
Retail marketing of insurance products	1, 2, 3, 7, 8, 9, 12, and 13.
Marketing of mutual funds	1, 2, 3, 9, 10, 13.

Your Feedback

During the course of preparing this book, we have witnessed many changes in the Indian BFSI sector. The detariffing of general insurance products is a case in point. We understand that any book that addresses a dynamic discipline (marketing) in an evolving industry (the BFSI sector) in an emerging economy (India) always has the scope to be updated and upgraded.

We invite feedback on this book from academicians, students, and practitioners concerned with the marketing of financial products. Specifically, we would like to understand your experiences in terms of relating the book's contents to the changing business environment, and applying what you have learnt to real-life situations. We will be happy to receive suggestions on how the book can be improved in future editions. Please send your comments to icmr@icfai.org.

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Part I

Marketing Financial Products – The Big Picture

Photo: Janusz Kaliszczak

Chapter 1

Marketing Financial Products – An Introduction

In this chapter, we will discuss:

- Financial Products in the Services Spectrum
- The Business Environment of the BFSI Sector
- Marketing Financial Products
- Transformation in Marketing Practices

Liberalization, privatization, and globalization have changed the face of the Indian economy. The standard of living has increased; consumer confidence and propensity to spend have increased; competition has led to an increased number of choices for the consumers; organizations are consciously trying to nurture external relationships with consumers, suppliers, and partners; they are also trying to nurture internal relationships with employees.

The services sector has been the main beneficiary of globalization. This sector has grown at an unprecedented rate and accounts for more than 50% of India's GDP, as of 2006-07. The services sector comprises many industries such as telecommunication, aviation, tourism, hotels, banking & insurance. Banking, insurance, mutual funds, stock market services, etc, are collectively referred to as the 'Banking, Financial Services, and Insurance (BFSI)' sector, or simply, 'Banking, Finance, and Insurance (BFI)' sector. Along with telecommunication and aviation, the BFSI sector in India has witnessed a tremendous transformation. This has brought about a significant change in the way financial products and services are marketed.

Financial services come as product offerings and service offerings. For example, a home loan is a product with some associated services. In this book, we use the term 'financial products' to refer to all the product offerings and service offerings in the BFSI sector.

This chapter introduces the core concepts that are relevant for marketing financial products. We begin the chapter with a discussion on the basic characteristics of services in general, and financial products/services in particular. The next section focuses on the environment of the BFSI sector. This is followed by a discussion on the need and significance of the marketing of financial products. Finally, the chapter describes some of the fundamental shifts in the marketing practices adopted by financial product marketers over the past decade.

FINANCIAL PRODUCTS IN THE SERVICES SPECTRUM

Financial products and services share some common characteristics with other services. Financial products also have some special characteristics that distinguish them from other services. A clear understanding of these characteristics -- both similarities and differences -- is useful to understand the existence of financial products in the services spectrum. The marketing approaches and techniques adopted for marketing financial products are influenced by these characteristics. This section focuses on understanding these similarities and differences.

Characteristics of Financial Products

Unlike physical goods, services can neither be physically touched nor tasted. They can only be experienced at the time of delivery. That is, a customer can only feel the delivery of the service. Further, services cannot be stored like physical goods. Consequently, they have to be consumed the instant they are produced. The basic characteristics of services in general are intangibility, inseparability, heterogeneity, and perishability. Two-way communications is another common characteristic applicable to many services, including financial products. In addition to these common characteristics, there are four characteristics that are specific to financial products. They include fiduciary responsibility, transparency of performance, uncertainty of outcome, and poor comparability. Fiduciary responsibility is applicable to all financial products while the remaining three characteristics are product specific, i.e. only certain financial products exhibit these characteristics. Table 1.1 gives an overview of the various characteristics of financial services.

Table 1.1: Characteristics of Financial Products

Characteristic	**Relevance/ Applicability**
Intangibility* A service cannot be physically touched or felt. It can only be experienced.	Applicable to all services, including financial products.
Inseparability* Financial services are produced and consumed at the same time.	
Heterogeneity* There is variability in service delivery from one service encounter to another.	
Perishability* Services are highly perishable in that a service not rendered/utilized is lost forever.	
Two-way communications# Communication between the service provider and the customer is on a continuous basis. This helps both the parties to understand each other in the long run.	Applicable to many services like travel, tourism, banking, hospitality, etc.
Fiduciary responsibility# It is the marketer's responsibility to manage the customers' funds and provide financial advice so that customers achieve their financial goals.	Applicable to financial products only.
Lack of transparency of performance^ There is a difficulty in gauging the performance of certain financial products due to unavailability of information and differing perceptions of customers.	Applicable (on a case-to-case basis) to specific financial product instruments (like investment products)
Uncertainty of outcome ^ The outcome of certain financial products is unpredictable.	
Poor comparability^ Some financial products are difficult to compare due to the uncertainty of outcome and the lack of transparency of performance.	

* Proposed by Valarie Zeithaml

\# Proposed by Sally McKechnie

^ Proposed by Antony Beckett

Adapted from Beckett, Antony. "Strategic and Marketing Implications of Consumer Behavior in Financial Services." *The Service Industries Journal*, *Vol.20 No.3, July 2000, p.191-208.*

Intangibility

Intangibility is the most striking characteristic difference between a physical product and a service. It is from intangibility that the other characteristics of services arise. Due to this characteristic, consumers perceive a higher risk while purchasing a service. For example, a person buying units of a mutual fund scheme has to presume that his/her funds are in safe hands. Thus consumers have to rely on the marketer's reputation, word-of-mouth publicity, and the opinion of reference groups, till they actually experience the benefits of the service (in this case, the return on investments).

Financial product marketers have made use of technology to reduce the intangibility aspect in the form of Automated Teller Machines (ATMs), credit/debit cards, etc, which provide physical evidence to consumers to reduce their risk perception. Marketers of financial products also try to offset the impact of intangibility associated with these products by building up a brand image and reputation, delivering high levels of customer service, providing customized solutions, etc. Exhibit 1.1 describes the service branding initiatives of ICICI Bank.

Exhibit 1.1

Service Branding to Attract Customers

Services marketers can differentiate their products through value-added customer service and service quality. Branding of services also helps to differentiate them from the services of competitors. A good brand image increases the customer's trust in the service and reduces the perceived risks associated with purchase of the service.

ICICI Bank has established itself as a strong brand in the Indian financial industry. The bank's philosophy is to provide services that are better than the expectations of the customers and thereby register a strong brand image in the minds of their customers. The ICICI Bank group has focused on branding across all segments of the financial industry, be it banking, insurance, or mutual funds.

Over the years, ICICI Bank has taken up various brand building exercises to increase brand loyalty among the customers. It ran campaigns in print media to educate the retail consumer. It also ran an 'Umbrella campaign' to convey the values of safety and security to the customers, which further reinforced its brand positioning. ICICI Bank targets its products and services at young customers with a view to establish long-term and profitable relationships. The bank used Amitabh Bachchan, the Hindi film superstar, as its brand ambassador to increase brand awareness among its target customers. It also branded its bond offerings as ICICI Safety Bonds, to communicate the safety aspect.

Adapted from Nath, Prithviraj, and Dharmendra Sanwal. "Services Branding Delivering a Value Proposition." http://www.etstrategicmarketing.com/smJan-Feb2/stra_brandp.htm.

Inseparability

Inseparability refers to the production and consumption of a service at the same place and time. For example, an account holder can withdraw cash from either the ATM or the bank's branches. When cash is withdrawn, service is both created and consumed simultaneously.

The degree of inseparability has an impact on the service delivery. Due to inseparability, the service encounter is crucial for the service provider's success. The human element involved in the service encounter becomes very important. Hence, inseparability also prompts the service provider to train and motivate their customer contact personnel to provide better quality service.

Heterogeneity

According to Zeithaml, Parasuraman, and Berry, "Heterogeneity concerns the potential for high variability in the performance of services. The quality and the essence of service can vary from producer to producer, from customer to customer, from day to day. Heterogeneity in the service output is a particular problem for labor intensive service."[1] Financial services like banking and insurance involve the human element, which leads to differences in service delivery. Though two different service providers may render the same type of service, the quality of service may differ between the two.

Heterogeneity in financial products affects three important aspects of financial services -- service encounter, productivity, and service quality. (Service encounter implies all the contact points between the service provider and the customers). Marketers attempt to reduce heterogeneity by streamlining/automating the service production at all the contact points. For instance, in addition to bank branches, ATMs, Internet banking, and phone banking are some of the contact points between the banks and customers. Automated processes at these points reduce the risk of non-uniformity in the service levels; such procedures also improve productivity and service quality.

Perishability

Unlike goods, services cannot be stored for future consumption. A service, when produced, is also consumed at the same instant. An unconsumed service is lost forever. For example, if a safe deposit locker of a bank is not rented in a particular month/year, then the revenue associated with that safe locker for that month/year is considered to have been lost forever. An insurance agent who undersold during a particular month has lost the chance of marketing an insurance product for that month forever.

Perishability of services has a direct effect on the length of distribution channels of the service providers. Due to the perishable nature of services, financial service providers maintain short distribution channels. The common distribution channels of a bank are branches, ATMs, the Internet, etc, which are short and directly linked to the bank. Similarly, a mutual fund house may appoint agents or franchisees on a commission basis. These agents are directly associated with the mutual fund company and thus, it is a 'one-level' distribution channel. Goods, on the other hand, have long channels where middlemen like C&F agents, distributors, wholesalers, and retailers exist.

Two-way communication

The existence of two-way communications between the service provider and the customer is another common characteristic in many service industries. Two-way communications gain importance when they take place on a continuous basis over long periods of time. The telecom industry, the financial services industry, and the airline industry are some examples where two-way communication takes place. For instance, in the financial services industry, there is two-way communication during the customer's visit to the branches, opening of accounts, purchasing of insurance policies, issue of bank statements, issue of credit card bills, granting of loans, etc. Similarly, telecom, airline, and other industries also are characterized by two-way communications. But two-way communications is not a characteristic in many other service industries where one-off transactions take place. For example, watching a movie in a theater does not involve two-way communication between the production team and the audience.

Fiduciary responsibility

This is a characteristic unique to financial services. It is referred to as that responsibility which a financial marketer has to carry out when overseeing the management of customers' funds. The financial marketer is also responsible for providing accurate financial advice to customers when asked to do so. According to Harrison, "a financial transaction includes a set of promises made by the marketer to the customer. It is responsibility of the marketer to safeguard the customer's funds."[2] For example, a person who takes up a term life insurance plan actually buys a set of promises from the insurance company. The company promises to pay the sum assured to the nominee on the event of the death of the insured person. As a consideration for executing this promise, the company accepts periodic payments from the customer in the form of premiums for a pre-specified duration of time. Thus, the funds so collected from all customers are managed by investing them in other revenue earning products.

As transactions in all financial services are financial in nature, it is important that the customer has trust and confidence on the service provider. But trust and confidence develop over a period of time. As a result, customers depend on the credence qualities (image and reputation) of the service provider to make their first purchase.

Lack of transparency of performance

The performance of certain financial products is difficult to understand or evaluate. For example, the performance of cash management services like cheque clearance, fund transfers, etc, can be easily identified and need not be explained in detail. On the other hand, a product like mutual fund, pension plan, etc., whose performance depends on market forces and is difficult to gauge, needs to be explained in detail to the customer. For example, marketers of life insurance products like money back policies, provide specific details about the effective rate of interest, payment of bonus, sum assured, terms of payment of claims, etc. Such information helps improve the transparency in performance and customers are able to understand the situation in the right sense and gauge the performance of the particular financial product.

Uncertainty of outcome

Financial marketers often work to reduce the uncertainty in their products. By nature, the outcome of certain financial products is difficult to ascertain. For example, there is a high degree of uncertainty regarding the outcome of investment products like mutual funds. Customers also have to keep in mind that the past performance of these investment products does not guarantee their future outcome.

Poor comparability

Some financial products can be easily compared, i.e., customers can compare the benefits of each product vis-à-vis another product of a different financial marketer. For instance, in the case of loan products, all that matters is the interest rate, the duration of repayment, EMI, etc. On the other hand, for products like investment products, it is difficult to make such comparisons. Comparability is easier in financial products when their performance, outcome, and benefits are identifiable. Both performance and outcome for the investment products are difficult to ascertain and hence, such products provide poor comparability, making it tougher for customers to make a purchase decision.

THE BUSINESS ENVIRONMENT OF THE BFSI SECTOR

The business environment can be broadly divided into three categories – the macro environment, the micro environment, and the internal environment. The macro environment is external to the business and includes the broad environment comprising the economy, culture, technology, etc. The marketer has no control over the macro environment as its scope of influence is outside the purview of the marketer. The micro environment is the industry level environment which is also external to the business and the marketer has some ability to control this environment. The micro environment includes all the external stakeholders to the marketer, such as customers, suppliers, competitors, etc. The third environment is the internal environment where a good amount of control can be exercised by the marketer on the organization's objectives, management structure, company image & reputation, etc. A clear understanding of these three environments will provide a basis for the financial product marketer to develop product-related and customer-related marketing strategies.

Macro Environment

As just stated, the macro environment is external to the organization/business/industry and it cannot be controlled by the marketers. It is the macro environment, on the other hand, that controls the business of the marketers. The macro environment consists of those factors that have an influence at the national level on all industries or sectors. Since the factors are external and uncontrollable, marketers can only take precautions to either avoid them (in case of threats) or utilize them (in case of opportunities). The macro environment can be further understood in terms of economic environment, socio-cultural environment, and political & legal environment. Let us take a detailed look at each of these environments.

Economic environment

The economic environment of a country sets the broad climate for any business. It is easy for a business to flourish in a booming economy. The economic environment of a country can be assessed using economic indicators such as the Gross Domestic Product (GDP), National Income, per capita income, and purchase power parity. These economic indicators help the marketers in assessing the economic environment and in making the required projections for their businesses. In the 2000s, the GDP growth rate in India has steadily been above 7.5%. This is an indication of a healthy and buoyant economy. The service sector is growing at a faster pace than industry and agriculture. The service sector contributes more than 50% of the nation's GDP. The Government has shortlisted IT-enabled services, healthcare services, financial services, and education as the major growth drivers of the Indian economy. On the supply side, India is gradually opening up its service sectors to foreign competition, as per the General Agreement on Trade in Services (GATS).

Socio-cultural environment

The socio-cultural environment has changed drastically. Economic reforms, followed by the Information Technology revolution, have paved the way for better career opportunities and greater consumer awareness. A new breed of confident consumers has evolved, with the potential and the propensity to spend; this has induced marketers to try and grab a fair share of that disposable income. To tap this segment, financial marketers have developed various financial products to address the needs of savings, growth, risk management, and retirement products. They have introduced credit cards (which are financial products) that have revolutionized the traditional way of shopping.

With the growing economic clout of women and senior citizens, BFSI marketers are coming out with niche products targeted at these segments. The demand for money transfer services (remittances from abroad, and from cities to towns and villages) has increased significantly due to the migration of youth away from their hometowns in search of employment opportunities. With the growing importance given to higher education and the greater role played by private sector institutions in this domain, educational loans have been identified as a key growth area by some banks. Insurance polices (with a savings component) also urge parents to take policies that will result in a lump sum receipt of money, in time for the higher education of the child. There has been an increase in the number of 'empty nesters'[3] and that, in turn, has led to a renewal in spending. Thus, the changing environment has given financial product marketers ample opportunities to develop new products, target new customer segments, and emphasize benefits that are in sync with the current socio-cultural environment.

BFSI marketers also adapt their promotional campaigns to the cultural context of the markets in which they operate. For example, Indian cricket players are used as brand ambassadors. Television commercials are aired during key sporting events. Home loan festivals are organized during the festival season. Cash-back offers and special prizes are given to stimulate credit card usage for shopping during this season.

Legal environment

The legal environment also has evolved over the years. The BFSI sector is regulated by various bodies at various levels in India. They include the government, the Reserve Bank of India (RBI), the Securities and Exchange Board of India (SEBI), and the Insurance Regulatory & Development Authority (IRDA). Let us briefly discuss some of the organizations that influence the legal environment of the BFSI sector.

The Government of India -- through the ministry of finance -- acts as the supreme controlling authority, which governs all the finance-related aspects of the country at the national and international levels. With the liberalization of the economy, the government permitted private & foreign participation in the financial markets. It also increased the limit on foreign direct investment (FDI) in the BFSI sector in India. This changed the dynamics of financial services industry as a whole. New players brought in new marketing strategies, better products, and increased competition.

Through its annual budget proposals, the Government also controls the tax regime. Income tax exemptions are applicable for investments in certain classes of mutual funds, insurance, and savings products; these exemptions reduce the actual cost incurred by the consumer in procuring financial products that are eligible for income tax exemptions. However, indirect taxes such as service tax have the effect of increasing the actual cost incurred by the consumer, which dampens the demand for these products.

In addition to setting policies that govern the BFSI sector, the Government of India also enacts the legislations necessary for the healthy functioning of this sector. Earlier, it had enacted 'the Recovery of Debts Due to Banks and Financial Institutions Act, 1993'. The objective of the Act was to accelerate the debt recovery process in order to reduce the bad debts (Non-Performing Assets - NPAs) of banks and financial institutions. However, the enforcement of the Act did not lead to the intended objectives. Later, to give special emphasis to the control of NPAs and to enforce the creditor's right of enforcement of security interest, 'The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI), 2002' was enacted. Here, the term 'security interest' means 'right, title, and interest upon property created in favor of any secured creditor including mortgage, charge, hypothecation, and assignment'.

RBI: The RBI controls the banking system in India. It regulates the money flow in the country through its fiscal and monetary policies. It uses various instruments to increase or decrease the money flow and control inflation in the economy. The RBI deregulated the banking industry in the 1990s to increase competition in the sector and provide better value to the customer. Refer to Table 1.2 for the roles and functions of the RBI.

Table 1.2: Roles and Functions of the RBI

Role	**Function**
Monetary Authority	Formulates & implements monetary policy to maintain price stability in the economy and monitors proper flow of funds to the required sectors.
Regulator and Supervisor of Financial System	Devises broad rules for banking operations in the country and monitors those operations to protect depositors' interests and provide cost-effective banking services to the public.
Manager of Foreign Exchange	Manages foreign exchange to facilitate external trade and payment and maintenance of foreign exchange market of India.
Issuer of Currency	Issues currency in the form of notes and coins to facilitate adequate supply of money in public circulation. Exchanges fresh notes and coins for the currency that is not fit for circulation. Destroys notes and coins which are not fit for circulation.
Developmental Role	Undertakes promotional functions to support national objectives.
Banker to the Government	Provides merchant banking services to State and Central Governments.
Banker of all Banks	Maintains banking accounts of all scheduled banks.

Source: www.rbi.org.in.

In 2004, the RBI proposed detailed guidelines on the application of Know Your Customer (KYC) norms and anti-money laundering standards. According to the RBI, "The objective of KYC guidelines is to prevent banks from being used, intentionally or unintentionally, by criminal elements for money laundering activities. KYC procedures also enable banks to know/understand their customers and their financial dealings better, which in turn, help them manage their risks prudently. Banks should frame their KYC policies incorporating the following four key elements:

(i) Customer Acceptance Policy;

(ii) Customer Identification Procedures;

(iii) Monitoring of Transactions; and

(iv) Risk management."[4]

SEBI: SEBI is the regulator of stock exchanges and trading in securities. It sets the broad rules for trading in the stock markets and for raising funds through issue of shares and debentures. SEBI was established through the SEBI Act 1992. Its primary function is to protect the interests of the investors in securities and promote the development and regulation of the securities markets in India. Hence it regulates the entire mutual fund industry apart from regulating the stock markets. It is also empowered to take legal action against the defaulters that come under its purview. For instance, in the Initial Public Offer (IPO) scam that took place in late 2005, SEBI barred many of the depository participants from opening fresh demat accounts. See Exhibit 1.2 for further details.

Exhibit 1.2

The IPO Scam and SEBI's Actions

Every Initial Public Offer (IPO) application for shares required a demat account. A depository participant, with whom a demat account can be opened, has to check and verify every demat application under the "Know Your Client" norms. But some depository participants did not diligently adhere to these norms.

The IPO scam in the primary market was essentially about opening demat accounts on fictitious names, getting the shares of an IPO allocated to these retail accounts through fraudulent means, and selling them in the secondary stock market for windfall profits. Some financiers and depository participants joined hands to enjoy these profits at the cost of non-allocation of shares to deserving retail investors. Between 2003 and 2005, more than 50,000 demat accounts were opened under fictitious names.

These fraudulent proceedings came to light in the wake of Yes Bank's IPO in December 2005. As the legal authority, SEBI began its investigations into this scam and passed an interim order on April 27, 2006. Through this order, it barred 24 financial institutions from opening fresh demat accounts. This list included Karvy Stock Broking, HDFC Bank, IDBI Bank, Motilal Oswal Securities, ING Vysya Bank, and Jhaveri Securities.

Adapted from Gajra, Rajesh. "Scorched Earth Policy." <u>*Outlook Money*</u>*. May 17, 2006.*

IRDA: IRDA is the regulatory authority of the insurance industry in India. It regulates the operations of all the players in the insurance market in India. IRDA's mission is "To protect the interests of the policyholders, to regulate, promote, and ensure orderly growth of the insurance industry and for matters connected therewith or incidental thereto."[5]

In addition to the above institutions, organizations like the Deposit Insurance and Credit Guarantee Corporation (DICGC) and the Export Credit Guarantee Corporation (ECGC) also form a part of the legal environment. DICGC was formed to provide insurance on retail deposits and credit guarantee to banks lending to the priority sector. ECGC provides credit risk insurance coverage to small and medium exporting companies against loss during export of goods and services. It also provides fee-based services like guarantees on behalf of exporters.

Micro Environment

All the external stakeholders of the company come under the micro environment. The micro environment consists of those components that have an influence at the industry level unlike macro environment components that are more at the national level. The micro environment includes suppliers, customers, channel members or marketing intermediaries, competitors, and the society at large. These components are discussed at appropriate junctures in the subsequent chapters. Here, let us briefly discuss competition and society as components of the micro environment.

Competition can be either direct competition or indirect competition. Direct competition occurs when competitors compete with the same product and market strategies. Indirect competition arises from marketers of substitute product or from entirely different product marketers who also vie for the same portion of the disposable income of consumers. For example, Non-Banking Finance Companies (NBFCs) are considered as indirect competitors to banks. This is because, though NBFCs may offer deposit and credit products, they have different rules and regulations and are not considered as banking houses.

Financial marketers have fiduciary responsibility not only toward individual customers but also toward the society at large. Various societal elements like the media, NGOs, consumer groups, etc., are considered as part of society and have an impact on the organization's performance in the market. To build a positive brand image, BFSI organizations are also taking up Corporate Social Responsibility (CSR) initiatives.

Internal Environment

The internal environment is internal to the firm/company. The prime characteristic of this environment is that it can be completely controlled by the marketer to achieve organizational goals. From the perspective of organizations in the BFSI sector, let us understand the internal environment in terms of mission and objectives, management structure, human resources, company image and reputation, and technology.

Mission and objectives

The mission and objectives of marketers determine their very presence in the market and they provide the broad framework for carrying out all the management functions. For instance, the mission statement of SBI Life is: "To emerge as the leading company offering a comprehensive range of life insurance and pension products at competitive prices, ensuring high standards of customer satisfaction and world class operating efficiency, and become a model life insurance company in India in the post liberalization period."

Management structure

Management structure defines how the organization is structured for effectively accomplishing the mission. Flow of authority in the management structure is also important in decision making. For example, SBI adopts decentralized decision making for loan sanctions, while ICICI Bank adopts a centralized decision making structure for such decisions.

Human resources

Human resources play the most important role in the services industries. The service quality and customer service largely depends on the employees (who are also termed as internal customers). A motivated workforce provides better service to the customers and hence marketers should ensure that their employees are motivated all the time. In the wake of increasing competition, many financial marketers have begun to pay attractive salaries to their employees along with other benefits.

Company image and reputation

The image and reputation of the company also play an important role in attracting customers. Consumers generally consider highly reputed companies as the safest. Financial marketers have resorted to spending more on publicity and public relations to improve their public image.

Technology

Technological environment refers to all the technological innovations and breakthroughs adopted and used by the BFSI sector to serve customers better. Technology has played a key role in transforming the financial services sector, especially the banking industry. Since the early 1980s, Indian banks have attempted to automate their back-end processes to reduce excessive reliance on people, which led to heterogeneity of services. This automation is called Total Bank Automation (TBA). Though the idea was conceived in the early 1980s, it became a reality only by the turn of the century, when most of the public sector banks automated their back-end processes. The need for centralized infrastructure was felt in the 1990s with the arrival of the new-generation private sector banks. Further, with the development of technologies to integrate all the databases of individual branches into a single integrated, centralized database, it became possible for marketers to focus on Internet banking, phone banking, and mobile banking.

From TBA, the industry moved to front-end automation, using technologies such as those relating to customer relationship management (CRM). These initiatives have played a major role in improving customer interactions with banks and insurance companies, thereby leading to higher levels of customer satisfaction. The next phase of technological development has brought in the concept of core banking, which has changed the traditional perceptions about banking. Core banking enables a bank to provide banking services round the clock, 365 days a year, and customers have the facility to obtain banking services from any branch.

MARKETING FINANCIAL PRODUCTS

The Indian banking system had many small players at the time of independence. The Government attempted to organize these markets through mergers and consolidations. For instance, the RBI merged weak banks with strong banks and brought down the number of banks from 566 in 1951 to 85 in 1969.[6] Further, it nationalized 20 banks with the aim of providing financial products across the entire country. Till the 1980s, expansion of branches (distribution) was the main thrust of the competitors in the banking industry. On the other hand, insurance and mutual fund sectors were virtual monopolies with customers purchasing whatever limited products were available. The mutual fund market saw the entry of other players in 1987, with banks entering the mutual fund business. The insurance sector was opened up to competition only in the late 1990s. With deregulation, and the entry of private and foreign players, the marketing of financial products gained more importance for the players -- both existing and new -- to differentiate their products and establish a loyal customer base. Competition and the resultant pressure to maintain profitability were prominent among the factors that led to an increase in the marketing efforts. Let us focus our attention on these two factors.

Competition

The public sector banks, the Life Insurance Corporation of India (LIC), the General Insurance Corporation of India (GIC), and the Unit Trust of India (UTI) were the most affected financial product marketers, due to the sudden surge in competition. These government-backed entities had ruled the Indian financial markets before the entry of foreign and private players. The new players had the advantage of using modern technology, and were able to provide superior customer service and service delivery. The use of technology also reduced the cost of operations for these private players. Being new to the market, they adopted aggressive marketing strategies to penetrate the market and build their market share.

Profitability

The revenue for a bank primarily comes from its interest spread. Interest spread is the difference between the total interest earned and total interest paid. As interest income is the major contributor to the total income of most banks, any decrease in the interest spread or drop in business volumes will have a drastic effect on the profitability. Large corporations -- with their growing bargaining power and increased choices for funding in a liberalized era – were able to negotiate better terms (lower interest rates) with their lending institutions. At the same time, the deposit rates were being forced up by the fierce competition from the private sector. These developments forced the players to actively market their asset products (loans and advances) and liability products (deposits), in order to maintain the total interest income. Additionally, they also placed emphasis on marketing their fee-based services, to build up their non-interest income.

In the case of insurance and mutual funds, the private sector competitors (to LIC, GIC, and UTI) initially targeted the high-value customers in the metros, and then started spreading aggressively to the non-metro cities and towns. To retain profitable customers and increase volumes, all the players had to adopt a marketing orientation, and execute marketing strategies in terms of well-defined target segments, new product development, better distribution and partnerships, and promotional mix.

Apart from increasing profits and market shares, marketing efforts lead to greater customer satisfaction, an improvement in reputation, greater brand value, better understanding of the markets, and product innovation. Higher levels of service quality lead to increased customer satisfaction. Brand building measures help increase brand awareness and brand image. This is necessary as many first time customers depend on the reputation and image of the financial marketer to purchase a product. Marketing efforts help the marketer to understand the market better and divide it into discrete segments. Such segmentation helps to understand the needs of the target customers better and to develop new products that suit their needs and requirements.

TRANSFORMATION IN MARKETING PRACTICES

The BFSI sector in India has undergone a sea change in terms of marketing practices. New marketers have entered the Indian financial services markets, new products have been introduced, and new levels of customer service have been achieved -- all this to get a greater share of the customer's disposable income in a profitable manner. The market dynamics have changed drastically with the entry of private and foreign players. Domestic private players have formed joint ventures with international leaders in the BFSI sector. The foreign players have brought with them their tried-and-tested marketing practices from the developed economies. The erstwhile supplier-oriented/regulation-oriented financial services markets have now become customer-centric and competitive. A shift in these marketing practices has been evident in three prime areas -- product customization, technology adoption, and customer service.

Product customization

Product customization has increased with the increase in competition. Before liberalization, customers did not have the option of choosing from a wide variety of products from different marketers. Even in the banking industry where 20 nationalized banks were present by 1980, product innovation and customization were given a backseat. When the private players entered, they focused on product differentiation by introducing new products that were more customized to meet the needs of the customers. See Exhibit 1.3 to understand how Standard Chartered Bank positioned its Manhattan credit card. Products have also been accompanied by new, value-added services to maximize the value experienced by the customer. (Product management is discussed in detail in Chapter 3.)

Exhibit 1.3

Customized Credit Cards from Standard Chartered Bank

Standard Chartered Bank was one of the first foreign banks to begin operations in India. In August 2004, it introduced a customized credit card under the brand name "Manhattan" targeted at the upwardly mobile customer. This included upper middle class people who were young and employed in highly paid jobs.

The Manhattan card broke free from the premise of 'one size fits all'. Under the standard card payment criteria, a single interest rate is charged from credit card customers even if they pay at an early date. Manhattan card provides the customized interest rate to each customer depending on their spending and payment patterns. The interest rate could vary between 1.99% and 2.49% per month. Incidentally, Manhattan was one of the first credit cards in India to be offered free-for-life. That is, the customer need not pay any annual fee for the card.

Adapted from "Standard Chartered woos upwardly mobile with lifestyle credit card." http://www.indiantelevision.com/mam/headlines/y2k4/aug/augmam94.htm.

Technology adoption

Technology was the most visible change with the entry of new players in the financial markets. Foreign banks and the new-generation Indian private banks invested heavily in new technologies, both to provide superior service and to compensate for their limited branch network. The Indian private sector banks followed this up with the opening of many new branches, with any-branch banking enabled by technology. Apart from these, banking transactions have seen a shift toward real time transfer of funds using Real Time Gross Settlement (RTGS) technology. This technology became available in India in 2004 and it has helped banks in transferring funds instantaneously between different branches of a bank and between different branches. Technology-related trends are discussed in Chapter 12.

Another important change was to rely more on Customer Relationship Management (CRM) applications that helped marketers nurture profitable relationships with customers. (CRM concepts and implementation are discussed in detail in Chapter 3.) The use of business intelligence software helps marketers understand the customer and markets better so that they can respond to the market changes with newer products and enhanced service quality.

Customer service and customer value

With more and more marketers embracing CRM as a philosophy, the whole meaning of customer service has changed. Thanks to competition, marketers have come to realize that their survival in the long run depends on the level of customer service and service quality, as perceived by the customers. In Chapter 2, we discuss the customer focus in marketing financial products. The quality of service has also improved with the introduction of ATMs, Internet banking, and phone banking. Now a customer can order a draft or cash over the Internet or on the phone and get it delivered at home. Mobile banking has also picked up to a limited extent. Technologies like RTGS, which have increased the speed at which banking is done in India, have further aided in providing value and satisfaction to the customers.

SUMMARY

Financial products are characterized by two-way communication and fiduciary responsibility, in addition to the standard set of four characteristics of services, that is, intangibility, inseparability, heterogeneity, and perishability. Certain types of financial instruments also have issues with respect to lack of transparency of performance, uncertainty of outcome, and poor comparability.

The macro-environment of the financial products sector can be classified broadly into economic environment, socio-cultural environment, political and legal environment. The sector is regulated by various bodies at various levels in India, including the government, the Reserve Bank of India (RBI), the Securities and Exchange Board of India (SEBI), and the Insurance Regulatory & Development Authority (IRDA). The micro environment includes suppliers, customers, channel members or marketing intermediaries, competitors, and the society at large. The internal environment is within the control of the management; it includes the mission and objectives of the company, management structure, human resources, company image and reputation, and technology.

In the liberalized era, competition between organizations and the resultant pressure to maintain profitability were two of the important factors that led to the marketing orientation. As a result, there was a shift in marketing practices, especially in product customization, technology adoption, and customer service.

End Notes:

[1] Edgett, Scott and Parkinson, Stephen. "Marketing for Service Industries-A Review." Service Industries Journal. Vol. 13 Issue 3, Jul93.

[2] Harrison, Tina. Financial Services Marketing. Essex: Pearson Education, 2000.

[3] Middle-aged or older couples whose children have grown up and "left the nest" to live on their own.

[4] http://www.iba.org.in/rbikycguidlines.asp (Accessed on December 22, 2006)

[5] http://www.irdaindia.org/

[6] Das, Ranjan, and Raveendra, C. "Choosing Strategies that Matter: Lessons for Indian Public Sector Banks." Strategic Marketing. http://www.etstrategicmarketing.com/Smmarch-april04/art1-1-1.html (Accessed on December 22, 2006)

Chapter 2

Customer Focus in Marketing Financial Products

In this chapter, we will discuss:

- Consumer Behavior
- Marketing and Strategy
- The Role of Marketing Research
- Market Segmentation
- Target Market Selection
- Positioning
- The Customer Service Imperative

Before liberalization, banking and other financial services were under the strict control of the government and all the functions were highly regulated. With the gradual deregulation of the markets during the process of liberalization, there was a shift in control from the government to market forces. The pace of this change increased with the growing competition in these markets. As customer satisfaction was an important determinant of profitability in a competitive market, customer-oriented financial products were developed. Marketers studied the buying behavior and the buying patterns of the customers so that this knowledge could be effectively used to identify, attract, and retain customers by offering better products and delivering superior customer service.

In this chapter, we will initially focus on the buying behavior of consumers of financial products. We will then discuss the significance of strategy and marketing at the corporate level, business or strategic business unit (SBU) level, and the functional or operating level. The role of marketing research, segmentation, targeting, and positioning functions will be dealt with in detail, followed by a discussion on the importance of customer service in the marketing of financial products.

CONSUMER BEHAVIOR

Financial services differ from other services and this is reflected in their characteristics (as discussed in Chapter 1). Fiduciary responsibility, transparency of performance, uncertainty of outcome, and poor comparability make them more complex than other services. New product offerings in financial services may possess elements of risk and uncertainty. Besides, there may be a difficulty in assessing and comparing their performance with similar products. Such elements play a crucial role in influencing the consumer's purchase of these products. Apart from understanding the buying behavior of consumers, it is also necessary to deliver effective customer service and maintain healthy customer relations.

In this section, we look at financial products from the customer's perspective, in terms of the factors that influence consumer behavior in purchasing these products. We then move on to discuss a framework of consumer behavior that is applicable to financial products. The framework takes a situational approach to modeling the typical behavioral patterns of consumers in four different types of situations.

Factors Affecting Financial Services Buyer Behavior

Buyer behavior pertaining to any goods or service is a result of a host of factors that have their influence on the buyer. The buying behavior displayed by consumers may differ across market segments and these differences are sometimes subtle. Thus, it is imperative for financial marketers to understand the underlying factors that influence the consumer while he/she is making the buying decision. Marketers need to have an understanding of these factors before developing strategies to market various financial products. The influencing factors are discussed here under the sub-heads -- economic, socio-cultural, personal, and product factors, in addition to the stage of purchase. Let us try to understand the various implications that each of these factors has on the purchase decision of consumers.

Economic factors

Fiscal and monetary policies and interest rates are the most important economic factors that influence buyer behavior. The fiscal[1] and monetary[2] policies formulated by the Reserve Bank of India (RBI) directly affect the operations of banks and other financial institutions, and these in turn, affect consumer choices. Interest rates, which are also influenced by the RBI, have an impact on the consumer's decision to save or borrow. Increased interest rates also result in investments moving out of the equity market and flowing into the debt market. This also influences the mutual fund products.

Money flow into the Indian financial markets increased between 2003 and 2006 due to increased investments by foreign institutional investors and domestic investors. This led to the availability of cheap funds to the banks. As a result, banks became liberal in disbursing credit to both the corporate sector and retail sector at low interest rates. In order to curtail the excess credit in the system, the RBI had to increase the Cash Reserve Ratio[3] (CRR), repo rates[4], and reverse repo rates[5]. CRR and repo rates affect the banks directly by reducing the liquid funds available at their disposal. Banks then have to reduce the giving of credit to customers so as to maintain liquidity. In late 2005, the RBI also increased the interest rates on the loans given to the banks to bring into control the excess cash in the system. An increase in interest rates increases the cost of getting funds for banks, thereby restraining them from borrowing more. Due to this, banks pass on the increased rates to corporate and retail customers, who may have to pay a higher rate of interest than usual. Increased interest rates may cause potential borrowers to postpone or refrain from approaching a bank for a loan/credit.

Socio-cultural factors

Socio-cultural factors encompass demographics, family, community, etc. Demographics include elements like age, sex, income, etc., of consumers in a given market segment. As discussed earlier, the needs of the consumer change at different stages of life. And an increase in income levels may prompt people to invest in financial products that have some level of risk like mutual funds, thus increasing the demand for these products. Family and community also act as major influencing factors. In certain families, the habits of saving and investing are inculcated in the children very early, and are passed on from generation to generation. Cultural roots may also determine the risk taking capacity of the individual, and this has a bearing on buying decisions. For example, many individuals from the 'Marvari' community or from a Gujarati business background may exhibit more of a risk-taking attitude than the average Indian.

Product factors

Apart from these factors, product related factors also have their own impact on the behavior of consumers in the decision-making process. Product factors include product complexity, pricing, image of the company, and reputation. Research has shown that the inclination of consumers to purchase a financial product varies with the variation in product complexity. Financial products which are too complex to understand attract fewer buyers. In India, direct investment in the stock market was not preferred by the common man in the 1990s due to the complexity and high risk involved. But with the rapid growth of the mutual fund industry, the complexity has reduced, leading to increased investment in stocks via the mutual fund route. The pricing of financial products also has a high bearing on the demand. Many Indian consumers are price-sensitive. An increase in the price of the product targeted at a salaried individual in the middle income group may lead to a fall in demand for the product. To manage the price perception, many insurance marketers offer their products with convenient monthly or quarterly premium payments. In addition to product factors, brand image and the reputation of the organization also play a part in the purchase decision.

Complexity of retail financial products: Based on their increasing level of complexity, Kamakura et al[6] classified retail financial products into fundamental products, risk management & cash reserves, growth to offset inflation, and risky assets. Adapting this classification to the Indian context, fundamental products include basic products like savings accounts or deposit accounts, credit cards, loans, etc. Products under risk management & cash reserves include insurance products, pension funds, etc. Government bonds and term deposits are low in liquidity and they yield moderate returns to offset inflation. While these products themselves are relatively risk-free, they do not manage existing risks the way an insurance product would. Risky assets are products that have a probability of giving high returns – such as equity shares, where the customer may either lose or gain on the investment due to market fluctuations.

Brand image of the marketer: Brand equity or the image of a financial firm is a major determinant of the sales of its products. Institutions such as ICICI Bank[7] and HDFC[8] have leveraged on their brand equity to attract new customers for existing as well as new businesses. For example, ICICI Bank entered into life insurance and mutual funds; this was done through a tie-up with Prudential[9] of the UK. Similarly, HDFC entered the insurance business by partnering with Standard[10] of Canada. The reputation of the institutions -- in terms of product portfolio, customer service, and relationship management -- helps attract new customers and retain existing customers.

Personal factors

Individual attitudes and behavioral factors play an important role in influencing financial product purchase decisions. Behavior is described as the actions or reactions that are displayed as a response to external stimuli. Thus, the introduction of new financial products or a promotional campaign for existing or new products may evoke either a positive or a negative attitude toward a financial product. Financial marketers in India have used promotional campaigns for insurance plans, retirement plans, mutual funds, etc., to change the consumer's attitude and behavior regarding investments in such financial products.

The individual's perception of risk also plays an important role in influencing financial product purchase decisions. The greater the perception of risk, the less the chances of his/her purchasing the products, and vice versa. Different consumers may have different perceptions of risk as personal risk bearing capacity and propensity differ from person to person.

Kamakura et al[11] describe financial maturity as the hierarchical movement of consumers from high liquidity-low risk products to high risk-low liquidity products. Thus a customer (who holds only a savings bank account) is considered to be financially immature. If he/she starts investing in complex products like highly risky equity schemes of mutual funds, then he/she is considered to be financially mature.

Stage of purchase

The consumer's behavior is influenced by the stage of the purchase -- before, during, or after. Before the purchase, a consumer may actively seek information or access to experts. Based on the inputs obtained at this stage, the consumer takes a decision during the purchase, which is in line with his/her personal needs and preferences. Post-purchase evaluation of a purchase decision is influenced by the experiences during and after the purchase, and any additional information that is gathered during this stage.

Before the purchase: Before the purchase, the consumer's information search is influenced by internal sources and external sources. Internal sources include the consumer's own knowledge, memory, and experience which he/she uses rationally to arrive at the purchase decision. External sources include personal and non-personal sources. Personal sources are family, friends, and relatives who offer advice and word-of-mouth publicity on various financial products. Non-personal sources include promotional activities of the financial marketers and third party information sources like news and analyses in newspapers, magazines, and television, and from brokers and financial institutions. The information explosion after deregulation of the banking and insurance industries has enabled consumers to learn more about the financial service providers and their product offerings.

During the purchase: To evaluate the alternatives during the purchase, and arrive at a purchase decision, the prices and financial performance of the firms can be compared and ascertained from various sources like company websites, online magazines, and reports. Consumers depend on external sources to reduce the uncertainties associated with financial products. As financial products do not possess as many measurable attributes as physical goods, consumers have very few measurable and comparable attributes on which to base their decision. Thus they may depend on peripheral attributes to arrive at decisions regarding service quality. Such attributes can be the reputation of the firm in relation to customer service and service quality, distribution channels like ATMs and branch network, location factors, physical facilities of the firm which indicate their professionalism, etc.

After the purchase: Post-purchase evaluation is rather difficult for financial products, as consumers on many occasions need to evaluate the financial product before it is actually consumed. This is very evident in the investment products of insurance and mutual funds. These products have a delayed consumption unlike physical products and are said to be unconsumed until their maturity (that is when the real benefits are reaped).

Another common problem that arises in the post-purchase evaluation of financial products is the cognitive dissonance on the part of the consumer. A person buying an insurance product from one marketer may be worried about his/her decision to not choose the products of another competitive marketer. This can happen in the selection of a bank or the selection of a certain mutual fund. The difficulty in post-purchase evaluation may also occur due to lack of information and experience on the products bought that may in turn lead to cognitive dissonance. Customer service, quality of service delivery, and proactive efforts at customer relationship management may influence the post-purchase evaluation. For example, a simple 'Thank You' note and a follow-up call from a bank or insurer may delight a new customer.

Consumer Behavior: A Situational Approach

Customers of financial products in India have begun to show an increasing interest in various financial products offered by marketers to meet their requirements at different stages of their lives. Let us consider the example of a person who has just passed out of college. The immediate agenda of the graduate would be to earn money for food, clothes, etc., by taking up a job or through self-employment. This can be related to the physiological needs specified in Maslow's Needs Hierarchy theory.[12] Next, the individual begins to save small amounts of money in a savings account and through fixed/ recurring deposits. The individual also insures his/her life as well as that of dependents (if any), through the purchase of insurance products. These efforts can be considered as part of satisfying his/her security needs. Next, the individual may avail of personal loans or housing loans to satisfy his/her social and esteem needs. In addition, the individual also invests in investment products like mutual funds to maximize returns along with investing in retirement planning solutions offered by various financial institutions. This case in point illustrates the phenomenon that at different stages of human life, people purchase different financial products.

Similarly, organizations also need different financial products in different situations. During the start-up phase, an organization may need a long-term loan to purchase the required equipment and machinery. After commencing regular operations, it may need working capital loans to fulfill its short-term fund requirements, and fee based services like factoring and forfeiting to maintain liquidity. It insures its machinery and equipment, plant and buildings, etc., and its employees through group insurance schemes. To give greater benefits to employees, it may also provide group pension plans as a retirement solution. When it wants to go public, it can use the services of merchant bankers to raise capital through the issue of shares to the public.

Not only are the requirements different at different stages of life for individual consumers but the kind of needs may also differ for different people. Beckett et al[13] (2000) proposed a framework for analyzing consumer behavior in the purchase of financial products. A matrix with two dimensions -- the level of involvement and consumer confidence (which depends on the perceived uncertainty) -- was used to classify consumers. Table 2.1 describes these two dimensions.

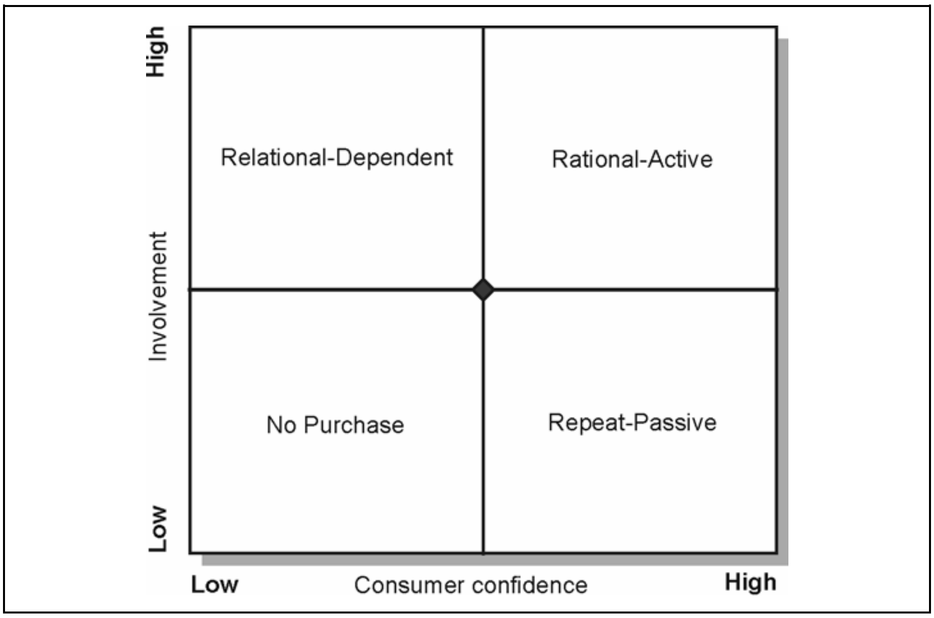
Table 2.1: Dimensions of Beckett's Consumer Behavior Matrix

S. No.	Dimension	Description
1.	Level of involvement	• Involvement is the interest that a consumer displays toward a good or a service. This involvement depends on the needs of the consumers. • Needs can be either physiological or psychological. • Physiological needs have very little to do with financial products. • Psychological needs like safety & security needs, esteem needs, etc. have a major influence on the purchase of financial products.
2.	Consumer confidence	• Consumer confidence about the purchase of a financial product depends on the information available about the product and the cognitive abilities of the decision maker. • Issues related to the transparency of financial instruments and uncertainty of the outcomes may result in poor comparability of various products, thus influencing the consumer's judgment of information availability. • The cognitive ability of individuals is their "ability to collect, process, and make sense of the information available in the choice environment".

Adapted from Beckett, Antony. "Strategic and Marketing Implications of Consumer Behavior in Financial Services." The Service Industries Journal, Vol.20 No.3, July 2000, p.191-208.

Beckett et al placed the consumers on a continuum of high/ low involvement, and high/ low consumer confidence. The matrix (as shown in Figure 2.1) contains four quadrants where each quadrant represents a distinct perspective/behavior of consumers. The four types of consumer buying behavior are: rational-active, repeat passive, no-purchase, and relational-dependent. Let us look into each of the quadrants.

Figure 2.1: Beckett's Consumer Behavior Matrix



Adapted from Beckett, Antony. "Strategic and Marketing Implications of Consumer Behavior in Financial Services." The Service Industries Journal, Vol.20 No.3, July 2000, p.191-208; and Beckett, Antony, Paul Hewer, and Barry Howcroft. "An Exposition of Consumer Behavior in Financial Services Industry." International Journal of Bank Marketing, Vol.18 No.1, 2000, p.15-26.

Rational-Active

Consumers who have high involvement and a clear picture (high levels of confidence due to low perceived uncertainty) about the products they purchase exhibit rational-active buying behavior. They actively search for information on the products and use rational judgment based on this information, in their purchase decisions. Wherever such information is missing or lacking, the consumers seek additional information from information sources like family, friends, financial institutions, etc. To cater to this kind of a consumer, financial marketers make extensive use of advertising and promotions using traditional media vehicles as well as the Internet. The rational-active consumers try to perform active search for information through all possible resources before zeroing in on a particular financial product from a provider. This kind of information search helps them in reducing the perceived risk and uncertainty associated with the financial products. It also enables them to exercise control over the purchase function.

Repeat-Passive

Consumers who have low involvement but are still confident about their purchases exhibit repeat-passive behavior. Low involvement could be due to their disinterest in the product or due to repeat purchases without their active involvement in further information search. The lack of involvement in further information search could be because these consumers are already equipped with adequate information – product-related, market-related, and brand-related. The majority of repeat purchases in financial services is due to this perceived adequacy of information. For instance, an individual who repeatedly invests in a particular mutual fund scheme of an asset management company belongs to this category.

No-Purchase

The next quadrant describes situations where consumers do not make a purchase. Their involvement in the purchase decisions is nil and they are low in confidence toward the financial products that have significant risks associated with them. In this situation, the consumer exhibits a no-purchase behavior. Rather than invest in avenues that have a probability of yielding greater returns, these consumers may prefer to play it safe by (repeatedly) putting their money into bank accounts, where they are more confident about getting assured returns.

The majority of Indian consumers are believed to exhibit such behavior toward investments in the stock market. Financial marketers are therefore directing their marketing efforts toward this potential market segment. Aggressive advertising and promotional offers are the most common tools used to educate this market segment on the fact that financial avenues like mutual funds and insurance products are not as risky as they are thought to be. For instance, a popular television commercial of Franklin Templeton Investments[14] shows a basket full of eggs to drive home the point that diversification of the investment portfolio can help in reducing risk. A print ad of HDFC Mutual Fund[15] highlights its CRISIL[16] certification to communicate to investors that it is safe to invest in its fund schemes. Another print ad of Kotak Mutual Fund[17] addresses the concerns of involvement and uncertainty in a more subtle way. The copy of the ad reads: “If I stay out, I miss out. But if I get in, will I benefit?” Then it goes on to explain the advantages of investing in its mutual funds.

Relational-Dependent

The last quadrant of the matrix represents situations where consumers have high involvement with the product, but they perceive high risk and uncertainty at the same time. Display of high involvement can be due to the urge to satisfy their financial needs, and perceived risk and uncertainty develops due to lack of information to arrive at a purchase decision. As a result, these consumers approach a third party (such as a financial institution or broker) to get expert advice. This relationship with the third party eliminates the active information search associated with the rational-active type and the routine purchase activity associated with repeat-passive type of consumers. Consumers falling in this quadrant can be potential customers who can be retained and converted into a loyal customer base. This is because the consumers themselves approach the financial firms for advice and assistance and this gives financial marketers an opportunity to develop positive relationships and build a loyal customer base.

MARKETING AND STRATEGY

Marketing as a concept has undergone a paradigm shift over the years; the boundary between the marketing function and the organization’s other functions is no longer rigid. For instance, operations executives in banks, apart from their regular activities as part of the internal processes, are also involved in customer service – either directly or indirectly. Customer service and service quality (which we discuss later on in the chapter) are considered as very important aspects in marketing financial products. Financial marketers have also gone to the extent of involving customers in various functions like product development. Such initiatives help marketers build long-term relationships with the customers and strategically orient the firm’s resources in the right direction.

To appreciate the changing role of marketing in this sector, one needs to understand the relationship between marketing and strategy in a business enterprise. According to Webster[18], marketing is practiced at three distinct levels in a firm. These levels are (a) corporate level, (b) business or SBU level, and (c) functional or operating level. Marketing can also be viewed as three distinct dimensions -- marketing as culture, marketing as strategy, and marketing as tactics.

Marketing at the Corporate Level

At the corporate level, the focus is on defining the business, it mission, scope, shape, and structure. The major issue is to position the organization at a suitable place in the value chain. The choice of 'what to buy, what to make, and what to sell' is made based on the core competencies of the organization. The organization also decides on its long-term strategy for growth, such as choice of market and formation of business networks through strategic alliances with its business partners, vendors, technology partners, and even competitors.

At the corporate level, marketing is more of a culture. The top management promotes values and beliefs that provide the direction for the marketing function and encourage the adoption of customer orientation as a culture throughout the enterprise. The role of marketing is to:

(i) assess the market attractiveness by analyzing the marketing structure,

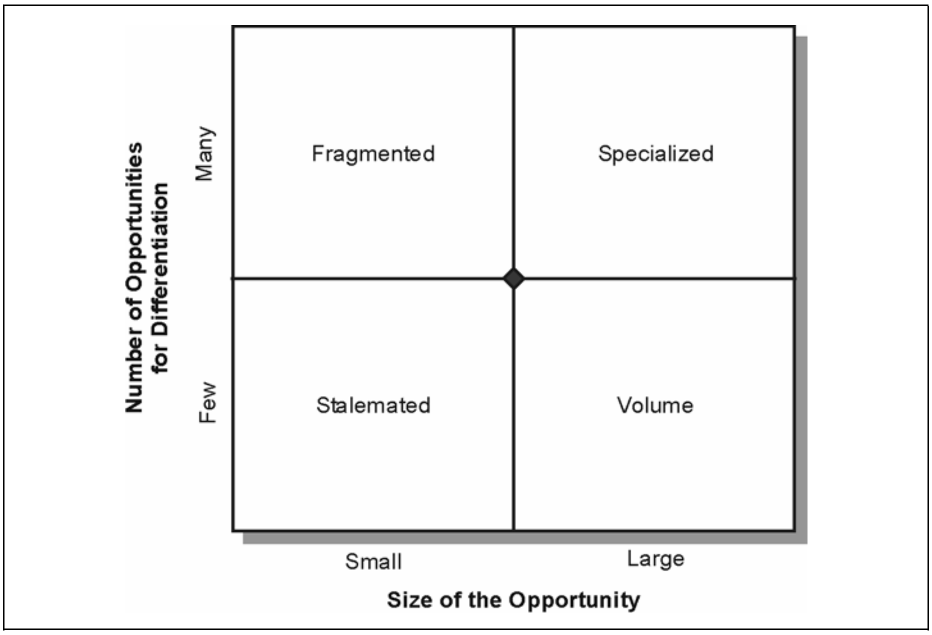
(ii) promote customer orientation by advocating the inclusion of customers' voice in decision making, and

(iii) develop the overall value proposition of the enterprise.

Market structure analysis

The objective of developing a marketing strategy is to gain a competitive advantage in the market. To develop a marketing strategy, the marketer needs to have a thorough knowledge about the market. Marketers analyze the attractiveness of the market in terms of the opportunities it is offering and the threats in terms of competition and other hurdles. Market structure analyses provide insights that help in understanding the market and identifying its segments.

Figure 2.2: Market Structure Developed by BCG



Source: Young, Mark R. "Market Structure Analysis: A Foundation for Developing and Assessing Bank Strategy." International Journal of Bank Marketing, Volume 17 Issue1, 1999, p.20–25.

The Boston Consulting Group (BCG)[19] developed a market structure matrix based on two factors -- the number of opportunities to differentiate products, and the size of these opportunities. Based on these two dimensions, BCG identified four market structures, as depicted in Figure 2.2. The matrix highlights the fact that not all the players in the market are successful in creating a competitive advantage through differentiation.

Fragmented market: This is a market where marketers have many opportunities to differentiate themselves from other players but these opportunities are small. However, profitability is not related to the size of the marketer.

Stalemated market: In this type of market, opportunities for differentiation are fewer and also each opportunity is small. Profitability in this market is not related to the market share of the respective marketers. For instance, current account products offered by a bank have little scope for differentiation. The profitability of the marketer is not a function of the market share in the current account segment, but on how aggressively the bank cross-sells its other products and services to its existing current account holders.

Specialized market: A specialized market has many opportunities and each opportunity for differentiation can yield larger profits. A mutual funds marketer, for instance, can have many differentiated fund schemes, which satisfy the needs of different market segments. Each successful fund could lead to a large number of customers and huge profits.

Volume market: In this type of market, opportunities for differentiation are few but the potential is large for business growth and profitability. In this type of market structure, profitability depends on the size of operations and volume of sales. For example, ICICI Bank ventured into the microfinance market in the early 2000s and by 2005-06, it had 109 microfinance institutions as its partners and catered to 3.2 million low income clients.[20]

Marketing at Business Unit/ SBU Level

At the SBU level, marketing can be viewed both as a culture of customer orientation, and as a strategy for competing in the marketplace. The marketing managers are involved in segmentation, targeting, and positioning decisions, and other strategic decisions such as which marketing functions are to be performed by the firm, which functions are to be performed by strategic partners, and which other functions have to be outsourced. Such functions include marketing research, advertising, sales promotion, telemarketing, managing the direct sales force, direct marketing, and packaging. The marketing managers should also decide on forming business networks by entering into strategic partnerships with selected vendors, channel members, etc.

Marketing at Functional/ Operating Level

At the operating level, the emphasis is on making decisions regarding the marketing mix. As in the case of any service offering, the marketing mix for financial products encompasses the 7Ps -- product, price, place, promotion, people, process, and physical evidence. Marketing is considered as developing tactics for the 7Ps and the distinction from strategy is clearly visible in this level. The role of a marketing manager can be viewed as developing an optimum marketing mix and deciding on the tactics to be used to increase the market share and profitability. Let us look briefly into the generalized functions of the marketing manager in terms of the 7Ps of marketing. In later chapters, we have a detailed discussion of the marketing mix for banking, insurance, mutual funds, fee-based services, and retirement solutions.

Product

Financial products are intangible; they have all the characteristics of services. Every product or service can be divided into four levels -- core level, tangible level, augmented level, and potential level. Marketing managers attempt to increase the tangibility component of the product, thereby making it amenable for presentation in a more marketable form. Financial products are also introduced with various add-on services and frills that augment the core product. Augmentation helps in product differentiation and positioning.

Price

The pricing of financial services depends to some extent on industry regulators like the RBI and the IRDA. With deregulation in the banking sector, the bank marketers have been given the liberty to price their products competitively. With the increased competition in the financial markets, marketing managers have resorted to competitive pricing policies.

Place

The accessibility to financial services has increased manifold due the introduction of breakthrough technologies. Customers can access their bank accounts through ATMs, the Internet, or on the telephone. They can view the status of their insurance policies on the Internet; they can make premium payments by transferring funds electronically from their bank accounts or by using credit cards. They can also open de-mat accounts and trade their mutual fund units through their depository participants. Thus accessibility to financial services is rapidly increasing in India. Marketing managers have to decide on the optimum mix of using the different channels of distribution to increase profitability.

Promotion

The risk associated with financial products and their intangibility make its necessary for marketing managers to use promotional tools to promote their products. The various tools of promotion include advertising, sales promotion, public relations, personal selling, direct marketing, etc.

People

People -- or the employees and agents in the financial services -- play a crucial role in promoting the products and providing customer service. If these internal customers are taken care of by the organization, they take care of the organization by marketing its products to the external customers more effectively and by providing them with superior customer service. External customers who are also involved in the development of new products are termed as co-producers. Marketers who treat their customers as co-producers benefit more from their customer relationships.

Process

The production and consumption of services take place at the same time (inseparability of services). The production process of a service is not as clear as that of a product. In financial markets, processes take place either through personal contact or through non-personal channels. Personal contact involves service encounters that take place between customers and the staff. Non-personal channels include service encounters through ATMs, the Internet, and the telephone. The critical incidents in the service encounters (that are crucial for completing the service delivery) can result in customer satisfaction or dissatisfaction. It is the duty of the marketing managers to ensure that service encounters result in customer satisfaction.

Physical evidence

Physical evidence aims at increasing the element of tangibility of the financial products. Customers perceive a greater risk in financial services due to their intangibility and the fiduciary responsibility of the marketers. Thus increasing physical evidence helps to counter such risks. Monthly banks statements through e-mail or by courier, premium notices and receipts, provide tangibility to the products. Other tangible evidence can be the physical infrastructure, brochures, and annual reports.

THE ROLE OF MARKETING RESEARCH

Marketing research plays a crucial role in formulating marketing strategies. The American Marketing Association defines marketing research as the systematic gathering, recording, and analysis of data concerning problems related to the marketing of goods and services. The main objectives of marketing research are (a) to provide marketing related information (including customers and competition) as inputs for deciding the marketing mix, (b) to help management take effective marketing decisions, (c) to analyze problems like a decline in market share and develop solutions for them, and (d) to provide proactive search so as to identify the possible future problems and opportunities in marketing.

The different duties of a marketing research department in an organization include -- estimating the market potential, undertaking market share analysis and sales analysis, developing demand forecasts, identifying the changing needs of the customers, conducting brand research, conducting research on competitors' market share and their strategies, test marketing new products, conducting product mix and promotion mix studies, media research, customer satisfaction surveys, etc.

The financial services industry in India has changed considerably and the markets have evolved over the years. For instance, in the 1990s, many private banks entered the banking sector. Life Insurance Corporation of India (LIC) was virtually a monopoly in the life insurance market for nearly 40 years till the turn of the century when other nationalized banks like SBI[21] and private sector players such as Reliance and Birla Sun Life[22] entered this market. Similarly, UTI[23] was the sole operator of mutual funds between 1964 and 1987. But this scenario underwent a radical change with of the entry of a number of fund companies such as SBI Mutual Fund[24], Canbank Mutual Fund[25], Reliance Mutual Fund[26], and Franklin Templeton Mutual Fund. Such a surge in the number of players operating in these markets has led to an increase in marketing research activities in the financial services industry. Banks and other financial service providers are increasing their spending on marketing research activities.

Market Analysis

The importance of marketing research and the role it plays in developing marketing strategies has been discussed earlier. Now we move on to understand the basics of market analysis and the need to perform such an analysis. Market analysis is primarily done to understand the dynamics of the financial services market in terms of the market potential, market structure (which was discussed in the previous section), and demand forecasting. Market analysis helps the service provider to develop a quantitative estimate of the total business that a market can provide and also helps in developing forecasts of demand as part of the marketing strategy. It also provides insights into the industry lifecycle and plays a crucial role in identifying the broad market segments and target markets. This, in turn, helps in identifying the needs and preferences of the customers in respective market segments.

Market analysis considers all the historic and potential factors that affect the demand for a product in a market and thereby facilitates the task of forecasting the demand. Market analysis in financial services takes into account an array of factors ranging from broad macro-economic factors like the GDP, per capita income, fiscal and monetary policies, interest rate changes, etc. to other factors like population in each market segment, disposable income of target customers, etc. Refer to Exhibit 2.1 for market performance in 2005 for banking, insurance, and mutual fund sectors in India.

Exhibit 2.1

Performance of Financial Products in India: 2005

Banking

The total number of commercial banks in India as on March 31, 2005, was 289. The aggregate deposits of scheduled commercial banks increased from US$ 331 billion in March 2004 to US$ 374 billion in March 2005. Commercial bank credit in India grew from US$ 185 billion in March 2004 to US$ 242 billion in March 2005. The nationalized banks were the largest contributors to total bank credit at 47.8 per cent as of September 2005. The contribution of foreign banks to total bank credit was at 6.7 percent.

In retail banking, private banks in India outperformed the public sector banks in 2005. ICICI Bank and HDFC Bank witnessed an over 70 percent year-on-year growth in retail loan assets in the second quarter of 2005-06. Another trend was the increase in the average loan size of the home finance companies. ICICI Bank, which was the largest player in the business, had an average loan size of about US$ 13,467 – US$ 15,711; this was an increase of 10-15 percent over 2004. The average loan size of HDFC, the second largest player in the home finance business, increased from US$ 10,773 in 2004 to US$ 13,467 in 2005, an increase of 25 per cent.

Insurance

The insurance sector in India opened up in the mid-1990s to private and foreign players. In 2005, foreign players accounted for nearly 22% in life insurance business and 20% in the non-life insurance segment. The increase in premiums was attracting new entrants to the market. During the financial year 2004-05 alone, the life insurance premium grew by 35 per cent to over US$ 13.5 billion. It is expected that this figure will cross the US$ 33.5 billion mark by 2010. The life insurance market, which was still led by LIC, the leading public sector insurer, witnessed a 38% growth in new policy premiums that stood at US$ 3 billion during April-October 2005. In the general insurance sector, the equivalent amount was US$ 3.3 billion during April-December 2005, a year-on-year growth of 15.4%. Most of this growth was contributed by the private insurers.

Mutual Funds

In this industry, assets under management (AUM) went up 33% to US$ 44 billion in December 2005 as against US$ 33 billion in the corresponding period the previous year. The private sector mutual funds (both Indian and foreign) had AUM of US$ 34 billion. In 2005, more than seven players had assets under management of over $ 2.2 billion with three more nearing the mark.

Adapted from Industry: Financial Services, 08 September 2006. <http://www.ibef.org/industry/financialservices.aspx>

Market potential

Market potential is an estimate that presents information about the expected sales of all the players in the entire market during a given period (say one year). As the financial services market is an emerging market, every financial marketer tries to estimate the market potential independently. This estimate provides a basis for analyzing their market share with respect to the total sales in the market. For example, according to McKinsey & Co., a leading management consultancy, annual revenues in domestic retail banking were expected to more than double from US$6.4 billion in 2005 to US$ 16.5 billion by 2010.[27] As market potential is only an estimate, actual sales may be either more or less than the estimated sales.

Demand forecasting

Demand forecasting refers to the estimation of future demand based on available data. The demand for financial products like banking and insurance products can be estimated using popular forecasting techniques. Demand forecasting helps marketers to develop marketing strategies and prepare marketing plans. These forecasts also act as a standard to compare the actual sales and correct deviations. Demand forecasting can be done using qualitative and quantitative methods. Popular methods of demand forecasting include qualitative methods such as the Delphi method, the survey of buying intentions approach, etc., and quantitative methods such as time series extrapolation, moving averages technique, regression analysis, etc.

Information Needs for Decision Making

Marketing research primarily aims at reducing/eliminating the uncertainties involved in marketing situations. Financial marketers are now increasingly making use of marketing research to solve the problems that arise in areas like new product development, branding, market segmentation, targeting and positioning, sales and distribution, etc. The managers who make crucial decisions require accurate information pertaining to the market, competition, and customers. Marketing research satisfies these information requirements in a systematic and timely manner. Let us now discuss these three types of information in detail.

Customer information

Customer information pertains to information on the needs, preferences, and spending patterns of consumers, information on customer satisfaction, information on customers of competitors, etc. Information on the needs, preferences, and spending patterns of consumers helps in new product development. Information on customer satisfaction helps financial marketers develop customer retention strategies, and information on customers of competitors helps financial marketers understand what makes these customers loyal to their competitors and how they can be induced to switch loyalties. With respect to corporate clients, a financial marketer also needs to be aware of any change in the business approach of the clients and the impact that would have on the marketer's future business relations with them.

Most of the banks in India spend large sums of money on marketing research to get to know their consumers better. For instance, ICICI Bank conducted a survey in association with ACNielsen ORG-MARG[28] in 2004 and found that Indian consumers had become more inclined to paying through credit and debit cards than by cash while shopping and eating out. Another independent survey (see Exhibit 2.2) by ACNielsen revealed that consumers in India were more upbeat and bullish in spending than their counterparts in China, Europe, and the Americas. This was attributed to the vibrant economic growth and growing disposable income in the hands of young educated adults. Such insights about the consumers help the financial marketer to be more successful in attracting them.

Exhibit 2.2

Indians Spend More than their Asian Counterparts

ACNielsen conducts an online global survey on consumer confidence twice a year. The survey measures current consumer confidence levels, spending habits/intentions, and current major concerns across industries throughout the world. In 2005, around 21,000 respondents responded to one such survey; the sample of respondents was drawn from 28 countries from Europe, Asia Pacific, the Americas, etc.

According to the survey, in the first half of 2005, Indians topped the list with 79 %of them being the most upbeat in the world. For the twelve-month period from mid-2005 to mid-2006, Indians (88%) were the most optimistic about their economic development, and 85% of them expected their personal finances to be in good shape.

When it came to disposable income spending patterns, Indians were again on top. In terms of priority, 41% preferred to invest in equities and mutual funds, 34% preferred to spend in out-of-home entertainment, 33% in buying new clothes or going on a vacation, and 30% on home decoration and buying new technology products.

Adapted from "Indians ready for a spending spree as consumers globally pull back in view of uncertain economic conditions." www.acnielsen.co.in.

Market information

Market information includes information about the market in which the financial service provider is operating and/or the information about the service provider's performance in the market. The former deals with information like market potential, demographics of the market, market segments, target markets, etc. Information about market potential is very useful in developing marketing strategy and plans. Information about market segments helps financial marketers identify their target markets.

Market share is the share of sales achieved by the financial marketer relative to the total sales in the market (sales of all the players in the market). Market share provides quantitative measurement of the performance of the financial marketer in the market in a given time period (usually one year). For example, the State Bank of India and its associates accounted for 23.8 percent of the total bank credit in India in 2005.[29]

Competitive intelligence

Competitive intelligence refers to gathering, storing, and analyzing information about competitors in the market. Competitive intelligence is used in decision making and for developing marketing strategies and tactics. The increasing competition in the financial services industry has forced players to learn more about their competitors in the struggle to gain a competitive advantage. The main objective of competitive intelligence is to forecast the steps the competitors will take in the future. The past data about what they have done is useful in analyzing and in decision making for the forecast.

The marketing department is the biggest user of competitive intelligence. Some of the prime areas where competitive intelligence is used are:

- To detect the introduction of new products and the ways in which they will be launched much before the actual launch.
- To identify the marketing strategies of the competitors that may pose a threat to the marketers' sales.
- To detect and identify the competitors' moves with respect to changes in the external environment like government policies, legal issues, etc.

In India, competitive intelligence is new to the financial services industry as this industry is still in the evolving stage. Financial firms either have in-house competitive intelligence departments or outsource this function to marketing research agencies. Competitive intelligence is primarily used by the top management to develop broad strategies, and by the marketing department to develop marketing plans and tactics. Many financial marketers do secondary research by themselves and outsource the primary or field research to research agencies to save on costs as well as to concentrate on their core competencies. Pipal Research, a subsidiary of ICICI OneSource, is a professional research agency that undertakes competitive intelligence assignments for different firms in the financial services industry, apart from other industries like pharmaceuticals and bio-technology.

MARKET SEGMENTATION

Segmentation segregates the entire market into various segments and provides a platform for marketers to target customers in each of those segments. It helps in identifying homogeneous consumer groups. After identifying the segments, financial marketers target a selected segment (or segments) with a marketing mix that is tailored to meet the needs of that segment. (This is in addition to the growing importance of individual targeting, also known as one-to-one marketing, which is discussed in Chapter 3.)

Financial product marketers can divide the consumers into different segments and take advantage of addressing a few target segments. For example, HDFC Standard Life Insurance Company's target segments are the 'middle income' and 'lower middle income' groups. HDFC Bank also targets the same segments. The objective is to synergize cross-selling and relationships among the customer base.

Need for Segmentation

The need for segmentation in the marketing of financial products arises from two crucial factors. First, segmenting a market can provide the inputs required for performing the targeting function. For example, an insurance marketer can promote insurance plans and pension plans to different customer segments. Second, once the market has been segmented, marketers can study the characteristics of the segment so as to identify the target segments and also customize product offerings. This information also helps in identifying potential high value customers or high net-worth individuals. As the cost of acquiring accurate primary data about the consumers in the entire market is very high, segmentation makes it easy for marketers to group much broader classes of potential customers, who can be easily understood and targeted. Let us now discuss the segmentation approaches that financial marketers usually follow.

Segmentation Approaches

Approaches in segmentation refer to the broad outlook of categorizing the markets. Every approach may involve some methods/models to segment the market. Researchers have proposed many methods for segmenting the financial services markets. According to Tina Harrison (1994), all the segmentation methods developed for financial services markets can be categorized into two broad approaches. One is the '*a priori*' approach and the other is the *'post hoc'* approach.

The *a priori* approach uses a basis for segmentation. That is, segmentation is done on the basis of certain criteria like product ownership, product usage, etc. The criteria are largely demographic in nature, such as a person's age, income, and stage in the family life cycle. The *a priori* approach is more popular than the *post hoc* approach as it provides a clear picture about the individual's needs and requirements. For instance, the stage in the family life cycle of an individual is one such important consideration as different stages have different requirements. For example, a nuclear family with toddlers plans to invest in long term financial assets that mature when the children become teenagers. But the problem with segmentation models using the *a priori* approach is that they focus only on the characteristics and do not provide the size or profitability of the segment relative to the entire market.

Models following the *post hoc* approach usually segment a heterogeneous market into different homogeneous segments by analyzing the responses obtained from surveys. Surveys are conducted to identify the tastes, preferences, traits, needs, and wants of the consumers and the market is segmented according to the results obtained. This helps to estimate the size or profitability of the segment relative to the entire market. The segmentation models under the *post hoc* approach of segmentation require sophisticated data analysis. While this approach may help to group consumers into homogeneous clusters based on behavior, the clusters themselves do not provide information on the demographic characteristics of the members.

Segmentation Bases

A basis for segmentation refers to a variable or set of variables on which a market is segmented. Popular segmentation bases include geographic segmentation, demographic segmentation, and socio-cultural segmentation. These comprise segmentation variables such as place, age, stage in family life cycle, social class, etc. Refer to Table 2.2 for an indicative list of different segmentation bases that could be used in India for marketing financial products to retail consumers. (The segmentation bases that are relevant for corporate customers are discussed in Chapter 4 – Corporate Banking.)

Table 2.2: Bases for Segmentation of Retail Consumers

Segmentation Base	Description	Examples
Geographic	Geographical segmentation in terms of area or location	▪ Metros ▪ Rural markets
Demographic	Grouping of consumers according to their age, gender, family size, stage in family life cycle, etc.	▪ Men aged below 30 years ▪ Families with grown-up children
Socio-economic	Segmentation by social classes, and income	▪ Salaried individuals ▪ Self-employed professionals ▪ High Net-worth Individuals (HNI).
Geo-demographic	Segmentation based on geographic and demographic information	▪ Nuclear families in Mumbai ▪ Empty nesters in Kolkata
Psychographic	Segmenting the market based on behavioral aspects like attitudes, perceptions, personality, etc.	▪ Risk averters ▪ Financially mature consumers

Adapted from Harrison, Tina. Financial Services Marketing. Essex: Pearson Education Limited, 2000, p.69-80.

Family life cycle segmentation

Javalgi and Dion[30] recommend using the stage in the family life cycle as a basis for segmentation. Based on the stage in the family life cycle, the consumer preferences vary in terms of product features, financial advisory requirements, pricing, location convenience, and organizational characteristics. According to Javalgi and Dion, there are nine distinct stages in the family life cycle, which can be used to segregate consumers. They are:

- *Bachelor:* Young working individuals who are unmarried and not living with their parents
- *Newly-married couple:* Married couple but with no children yet
- *Full nest I:* Married couple with youngest child under six years of age
- *Full nest II:* Married couple with youngest child six years or above
- *Full nest III:* Older married couple with dependent children
- *Empty nest I:* Older married couple, no children living with them, and head of the family still working
- *Empty nest II:* Older married couple, no children living at home, and head of the family retired
- *Solitary survivor, in labor force:* Single survivor of the family like widow or divorcee, who is still working
- *Solitary survivor, retired:* Single survivor of the family like widow or divorcee, who is retired

Psychographic segmentation

In order to understand the behavioral aspects of the consumers, marketers may also rely on psychographic segmentation. The psychographic approach of segmenting markets stresses more on the attitudes, perceptions, and the overall personality. This approach focuses more on understanding the inner aspects of a person rather than on the outward expressions. Persons with similar behavior and/or personality are identified and grouped to form a segment. The main drawback of using this approach is the confusion that prevails in the process of identifying and segregating the customers based on these variables. Thus, not many marketers use this approach. Exhibit 2.3 describes a tool called Financial ACORN for segmenting markets in the financial services sector in the United Kingdom, based on demographic, lifestyle, attitudinal, and product ownership characteristics.

Benefit segmentation

Another segmentation approach is benefit segmentation. Benefit segmentation focuses on the benefits that customers gain after purchasing various financial products. Assael (1995), Haley (1968), and Kotler (1994) supported this segmentation approach as they felt that consumers always sought benefits while purchasing a financial product. Financial marketers must therefore try to know what benefits the customers were seeking and communicate these benefits while advertising and promoting their products. In addition, knowledge about alternative benefits that customers are looking for is necessary to enable marketers to reposition the existing products and/or develop new products, as required.

Exhibit 2.3

Financial ACORN: A Tool for Market Segmentation in Financial Services

Financial marketers in search of quality customer information have developed computer based analytical tools to help them in segmenting their markets. CACI, a leading provider of marketing solutions and information systems in the UK, has developed a segmentation tool called Financial ACORN that can be used to segment the consumers based on their behavior and family income.

To understand the behavior of consumers, Financial ACORN uses three factors -- financial sophistication (level of investment products held and attitude to planning for the future), attitude to risk (like risk takers and risk averters), and stability (people with long term relationship with the financial marketer).

In Financial ACORN, the four consumer classifications are: financially sophisticated, financially involved, financially moderate, and financially inactive. The financially involved segment included three sub-categories: comfortable investors, better-off borrowers, and prosperous savers. About 31% of Great Britain's population is estimated to belong to this segment.

Adapted from Soper, Suzanne. "The Evolution of Segmentation Methods in Financial Services: What Next?" Journal of Financial Services Marketing. Vol. No.1, 2002, p.67-7; and Harrison, Tina. Financial Services Marketing. Essex: Pearson Education Limited, 2000, p.78.

TARGET MARKET SELECTION

Once a market has been segmented based on certain criteria, the marketer's next action is to select the target segments. The whole process of segmentation is done in order to identify the target markets. Proper targeting is very beneficial for financial marketers. For instance, HDFC has a strong presence in the NRI segment and gets a major chunk of its revenues from this segment. Refer to Exhibit 2.4 for various products targeted at NRIs by the group companies of HDFC.

Exhibit 2.4

Targeting NRIs: The HDFC Way

NRIs are considered as a prime target market by the HDFC group of companies. HDFC, HDFC Bank, and HDFC Standard Life Insurance – all have set NRIs as one of their prime target markets. HDFC Bank has developed asset and liability products exclusively for the NRIs to suit their requirements. It has developed more than 25 products that address the needs of the non-resident Indians worldwide. They include remittances; various types of accounts, deposits, and loans; and advisory services in mutual funds and insurance.

HDFC, the housing finance corporation, as part of its NRI marketing, has developed customized home loan products for this segment. Indians residing in various parts of the world can avail of this product to build their dream homes in India. HDFC has also made it possible for Indians residing in the Middle East to pay in UAE Dirhams, either through cheque or demand draft. In July 2005, HDFC came out with a unique offer called NRI Homeland Offer targeted at NRIs in the Gulf countries. That is the homecoming season for NRIs in these countries and this offer was launched anticipating that buying a home would be a top priority for them. In this way, the Middle East has become an important revenue center for its NRI operations. HDFC has also begun to look for franchisees in countries like the US, the UK, and Canada to tap the NRI customers in those countries.

HDFC Standard Life Insurance also has lined up insurance products that suit the needs of the NRIs; this includes retirement solutions. It has positioned its products in such a way that they give safety and security as well as opportunities to invest in India. It has also simplified the buying procedure for these products.

Compiled from various sources.

In India, most financial marketers have begun to target the SME segment. Earlier, the SME segment was mainly dependent on the public banks for its financial requirements. But competitive pressures, the huge volumes that exist in this segment (despite a high percentage of non-performing assets), etc. are some reasons why private banks are targeting this segment through increased market efforts. Hence, selecting a target market is a very important function of marketing.

Financial marketers adopt different targeting strategies in financial markets. They are undifferentiated marketing, differentiated marketing, and concentrated marketing.

Undifferentiated Marketing

Undifferentiated marketing involves targeting the entire market with a single product offering. This approach is suitable for products like automobiles, telecommunications, consumer electronics, etc. But, it is not widely used in services including financial marketing. Though simple savings accounts and current accounts (which have very little differentiation) can be targeted at the market at large, many other products like educational loans and loans for the SME sector are specifically targeted at these segments using different pricing strategies. Another reason why not many of the financial products use this strategy is the inherent aspect of intangibility and heterogeneity associated with services.

But this targeting strategy was widely prevalent before liberalization and the opening up of the financial sector. For instance, LIC in life insurance and UTI in mutual funds practiced this strategy extensively. Many of LIC's money back policies were not customized to any single segment in the market and were targeted at the mass market for all those who wanted to save money. Similarly, UTI had been marketing a single product called US64 since 1964. This product was also not targeted at any specific segment. In the present day, products are differentiated from market to market. As a result, financial marketers are developing products targeting specific target markets through concentrated strategies.

Differentiated Marketing

In differentiated marketing, the entire market is segmented into many segments and the marketers target two or more segments with customized products. Undifferentiated marketing covers the width of the market, but penetration is not possible with this strategy. Differentiated marketing attempts to cover certain segments of the market as well as penetrate into those segments to achieve in depth coverage. For instance, the Delhi-based Oriental Bank of Commerce (OBC) concentrated only on North India from its inception till the early 2000s.[31] Further, its main focus was on the small and medium business enterprises (SME). It is a strong player in this segment with literally zero non performing assets. Many banks and insurance companies have come up with customized products that suit different segments like high net-worth individuals (HNIs), women, elderly people, young couples, students, etc.

Targeting high net-worth individuals

Many financial marketers have begun to focus on certain high value customers whom they classify as high net-worth individuals (HNIs). The basis for targeting this segment is the economic worthiness of the individuals. Customer grading is a tool to differentiate customers based on their economic worth. Lorrie LiBrizzi defined customer grading as the process of evaluating and defining the customer's worth and assigning a grade or score to individual customers to reflect their worth from the marketer's perspective. Grading helps in identifying the HNIs and targeting the marketing activities around this segment. In India, it was estimated that there were 70,000 HNIs in 2003 who invested around Rs.100 billion in the financial markets.

Also the overall financial wealth of HNIs globally in 2003 was estimated at $31 trillion and this was expected to grow at 6.5% to $42.2 trillion by 2009. Of their investment in financial markets, 34% of the money was invested in equity products, another 27% in income products, and the remaining in alternative investment avenues[32]. The figures indicate that there is a huge potential to be tapped from this market segment.

Indian players are keen on concentrating on this segment. Citibank, for instance, launched its Citigold Wealth Management targeted at HNIs in 2002. This was a set of financial planning tools and wealth management services that supplemented the regular banking products and aimed at wealth maximization of these HNIs. HDFC Bank caters to this segment through its private banking initiative. It offers unique advisory services to this segment in mutual funds, insurance, equities, bonds, risk profiling, and asset allocation. Thus many financial providers in India, be it a bank or insurance company or mutual fund company, have HNIs as one of their target markets and have developed product offerings accordingly.

Concentrated Marketing

Some financial marketers select a single segment of the market and develop a single marketing mix for that segment. By doing so, they achieve deeper penetration into that segment. Further, this strategy helps in creating a niche for the marketer while improving profitability. This strategy is profitable when the marketer faces a shortage of resources and has to develop products using limited resources. One drawback with this strategy is that if the marketer is successful in a segment, it attracts the attention of other players in the market and leads to competition. The marketer then can no longer enjoy the niche benefits of the market and loses the competitive advantage. A typical example of this kind of targeting is of Non-Banking Financial Companies (NBFCs) doing business in auto finance. For instance, Sundaram Finance Limited is a leading player in vehicle finance in South India since the 1950s.

POSITIONING

Ries and Trout, the marketing gurus, argued that positioning is not what is done to the product or service; rather, positioning is what is done to the mind of the consumer. Positioning is the process of implanting the right information about the product or service in the minds of consumers, which stimulates them to purchase that product or service. Marketers attempt to position their products as clearly as possible in the minds of consumers.

In financial marketing, organizational positioning is given more importance than product positioning. Besides, financial products have the elements of intangibility, inseparability, heterogeneity, fiduciary responsibility, etc.; they can also be easily copied by competitors. So, differentiation is often attempted on the basis of the level and quality of customer service. Customer service is projected as a differentiator at the organizational level rather than at the product level. Robinder Singh, Head of Marketing, Personal Financial Services, HSBC India, states that copying a product offering is easy, but delivering quality service associated to the product on a consistent basis is not possible for all. He adds that maintaining consistency itself is a positioning for the organization.[33] In addition to customer service, trust and confidence in the marketer also play an important role in positioning the organization. The levels of trust and confidence in the marketer are determined by the extent to which the marketer carries out the fiduciary responsibility.

Organizational Positioning in Financial Markets

Organizational positioning in financial markets plays an important role in the success of the business. Customers in different market segments relate and compare one marketer with another by identifying the marketers with respect to different attributes. Organizational positioning in financial markets is done through corporate brands. This enables organizations to undertake marketing campaigns to associate themselves with specific attributes that customers look for. Romniuk[34] has identified six different brand positions that can be associated with the different attributes that customers look for in the brand. They are price, relationship or service benefit, security benefit, user type, accessibility benefit, and perceived quality.

Price

Price positioning implies that the organization is actually associating itself with price leadership in terms of favorable interest rates, fees, and other charges. Price positioning is done to attract a huge number of customers and increase business volumes.

Relationship/service benefit

This positioning focuses on the responsiveness of marketers to the needs of their customers and their customer service. It also highlights the aggressiveness of the marketers in building long-term relationships. For an understanding of the positioning strategies that could be adopted by NBFCs in the Indian financial sector, refer to Exhibit 2.5.

Exhibit 2.5

Positioning of NBFCs

According to Ranjan Das and Ravindra, NBFCs incur a higher cost of funds than banks; they focus on niche products and have lean structures and better flexibility. For increasing their profitability, NBFCs can be positioned based on products or services, customer needs, or accessibility.

Positioning based on products and services

NBFCs operate in niche segments with very few products. They can therefore be positioned as specialists in these products. For instance, GE Capital India provides corporate funding involving huge amounts through term loans, hire purchase, leasing, and bill discounting.

Positioning based on customer needs

Due to their relatively small size and product portfolio, NBFCs can serve customers better than banks. With the advent of ATMs, Internet banking, and mobile banking, customer relationships in banks are becoming more impersonal. But far better personal contact exists in NBFCs and this can lead to greater opportunities for them to position themselves on the customer service plank.

Positioning based on access

NBFCs usually follow a concentrated market strategy. They focus on a single market with one or very few products. Due to the high penetration levels in the chosen markets, customers have easy access to the NBFCs. Sundaram Finance Limited and Cholamandalam Finance score high on accessibility in South India and they have a strong presence in the vehicle financing market. This has helped them gain maximum mileage out of the market.

Adapted from Das, Ranjan, and Ravindra C. "Wither NBFCs?" www.estrategicmarketing.com.

Security benefit

Safety and trust are associated with this positioning. Customers may perceive one organization to be more secure than another for guaranteed return of their investment. For example, for lodging funds in the form of deposits, some customers prefer nationalized banks to private banks.

User type

Financial marketers can position the organization based on the user group primarily catered to. One bank may be aggressively focusing on the retail segment while another may focus on the corporate segment. Both the banks position themselves as specialists in their respective segments.

Accessibility benefit

Accessibility indicates the breadth and depth of a marketer's reach. This can be through installations of ATMs at multiple locations or through branches located at convenient places.

Perceived quality

This implies the quality of performance as perceived by the consumers. Quality parameters may include good financial management, investment growth, timely delivery of service, reliability, etc. A mutual fund with a track record of consistently giving good returns on investment would be perceived more positively than another which gives either lower or fluctuating returns.

THE CUSTOMER SERVICE IMPERATIVE

Customer service has become an important aspect of marketing of financial products. Customer service when delivered effectively leads to happy and satisfied customers. And having a loyal customer base reduces the overall service costs drastically and enhances profitability. Most financial marketers include effective customer service as one of their organizational goals. For delivering quality customer service, they design training programs, monitor service encounters, analyze customer feedback, etc.

In this section we discuss the need for customer service; ways of improving customer service; dimensions of service quality that marketers of financial services should understand; and the benefits of providing good customer service.

Need for Customer Service

Customer service and the quality of that service are widely recognized as the key growth drivers in the financial services industry. Every marketer of financial products has to emphasize the quality of customer service that is delivered to the end customer in the whole process of marketing their products. The marketers may reap various benefits from the customer service rendered. They therefore need to consider customer service as an integral component of their marketing efforts.

Consumer awareness

Consumers of financial services are well informed due to the information explosion and information technology. Service levels are an important attribute that they look for in a financial marketer. Customers switch between financial firms due to poor customer service. This is even greater due to the wide range of products offered by different marketers. Marketers need to shift to a proactive customer service and not think that customer service is only about handling complaints.

Business environment

The business environment plays a key role in influencing financial marketers to focus on customer service. With the increasing competition, most financial marketers are trying to become a one-stop shop for a portfolio of financial products. Many banks have entered into the insurance and mutual fund markets through subsidiaries and alliances. They also offer fee-based financial services. For example, private banks like HDFC Bank offer a wide array of products -- asset products, liability products, insurance, investments (mutual funds), fee-based services, etc. Good customer service is a pre-requisite for retaining customers and cross-selling multiple products to them.

Competition in the financial products sector has led to improved customer service. Marketers have begun to realize that those who excel in differentiating themselves from the rest in providing better customer service will have the maximum scope to improve their profitability. The need to improve service levels has led to service delivery through newer channels of distribution. Internet banking and mobile banking are good examples of this development.

Benefits of customer service

There are several benefits associated with implementing customer service as a long-term strategy:

- It primarily differentiates the firm from the competition.
- It improves the brand equity of the firm in the long run.
- It ascertains the reliability factor in the minds of the customer and makes them more loyal.
- It creates more satisfied internal customers as well as external customers.
- It improves the profitability of the firm.
- It creates a loyal pool of customers who can serve as brand carriers.

Ways of Improving Customer Service

Customer service can be improved through service quality, service offerings, and handling of customer complaints. The extent of service quality, design of service offerings, and effective handling of customer complaints has a strong influence on customer service levels of a financial marketer.

Service quality

Service quality is measured as perceived by the customer. Customers assess service quality (though not quantitatively) by comparing what they expect from the service provider with what they actually receive. The various dimensions of service quality are discussed in the next section.

Design of service offerings

The marketer can gain new insights into consumer needs through marketing research, develop new products, and suitably modify the marketing mix so as to provide the maximum customer service. However, the features of service offerings can be easily copied and imitated by competitors. Given the high levels of consumer awareness, financial marketers also need to be cautious in making promises about their service offerings and then be consistent in living up to expectations.

Handling of customer complaints

Finally, marketers can differentiate their customer service from that of the competition through effective handling of customers' complaints and accepting such complaints as potential leads for improving their customer service. This gives the customers an impression of being well treated, leading to improved loyalty and better customer retention.

Employees have a profound influence on customer service, especially when face to face contact occurs. To deliver effective customer service, employees have to be trained and motivated. The main objective of customer service is to achieve customer satisfaction and customer delight and employees are the means to achieve this. Marketers have to consider employees as the face of the organization and the enhancers of brand equity and reputation. They have to take steps to keep the workforce happy by offering them attractive pay packages; helping them grow through promotions and career planning guidance; training them on the trends in delivering customer service and their role in brand building; etc.

Dimensions of Service Quality

Parasuraman et al. (1988) opined that it was service quality that often spelt the difference between a business's success and failure. Their research identified five dimensions of service quality that marketers have to consider while designing and delivering a financial product. They are *tangibles, reliability, responsiveness, assurance,* and *empathy*. *Tangibles* include physical facilities like branches and offices; equipment like ATM machines; appearance of the staff, ambience inside the office which gives a professional look, etc. *Reliability* is the consistent ability to deliver a service as promised. Like in other services, this dimension is considered as the most important of all the five dimensions in marketing of financial products. *Responsiveness* refers to how willingly the employees of the financial firm respond to the customers' needs. *Assurance* is that aspect of customer service where employees of the firm create a feeling of "we are there for you" in the minds of the customers. Finally, *empathy* refers to the caring, sharing, and understanding of the customer's concerns and needs in the process of the service delivery.

In addition to investing time and resources in ensuring service quality, marketers of financial products have been at the forefront in using customer relationship management (CRM) as a strategic marketing tool. See Chapter 3 for a detailed discussion on CRM concepts and implementation in the context of marketing financial products.

SUMMARY

Various factors influence consumer behavior in purchasing financial products. A situational approach can be adopted to understand buyer behavior. Specifically, Beckett's matrix classifies consumers of financial products on the basis of level of involvement and consumer confidence (which depends on the perceived uncertainty).

Marketing has to be viewed from the perspective of three levels in an organization -- corporate level, business unit level, and functional level. Marketing research is an important function that contributes to the marketing of financial products in terms of market structure analysis, market potential, and demand forecasting. To satisfy the requirements of marketers, marketing research provides information on customers, markets, and the competition.

Segmentation models can be broadly categorized into *a priori* and *post hoc* approaches. Various bases of segmentation are applicable for segmenting consumers. Financial marketers generally adopt one of the following targeting strategies -- undifferentiated marketing, differentiated marketing, and concentrated marketing. It should be noted that positioning in financial products marketing differs from that of other products and services in that organizational positioning is given more importance than product level positioning. The corporate brand can be positioned based on various factors such as price, relationship or service benefit, security benefit, user type, accessibility benefit, and perceived quality.

Customer service is an important factor that differentiates the product offerings in the service industry. Service quality can be improved along the dimensions of tangibles, reliability, responsiveness, assurance, and empathy. Financial product marketers need to imbibe in them the philosophy of providing quality customer service in order to increase their profitability. Good customer service and proper handling of customer complaints pave the way for building lasting relationships.

End Notes:

1 As part of the fiscal policy, the government may increase or decrease expenditure, taxes, and borrowing. Through these policy options, the government may attempt to achieve economic objectives such as controlling inflation or stimulating growth, and social objectives such as equitable redistribution of wealth.

2 Monetary policy is a tool used by the central bank (such as the Reserve Bank of India, in India) to influence money supply, interest rates, credit availability, and price stability (or inflation). Depending on the macro-economic situation and requirements, the central bank may want to slow down the economy and dampen inflation, boost economic growth by stimulating investment and consumption, etc.

3 CRR is the percentage of a bank's total deposits that it has to deposit with the RBI. The RBI can increase or decrease the CRR to manage liquidity.

4 This is one of the credit management tools used by the RBI to regulate liquidity (customer spending). This is the rate at which the RBI lends money to the banks.

5 This is another credit management tool where the RBI takes a loan from the banks. The interest rate at which RBI takes the loan is termed as the reverse repo rate; this rate is fixed by the RBI.

6 Harrison, Tina S. "Mapping Customer Segments for Personal Financial Services." International Journal of Bank Marketing. Vol.12 No.8, 1994, p.17-25.

7 ICICI Bank is the largest private sector bank in India and second largest among all banks in India. It had 573 branches and 1900 ATMs in 2005.

8 HDFC Bank was incorporated in August 1994. In 2006, it had 531 branches across 228 cities in India and more than a thousand ATMs.

9 Prudential Plc. is a global financial services provider. It is incorporated in the UK and provides insurance and financial services through its subsidiaries across the world. In India, it operates in partnership with ICICI Bank in insurance and mutual fund areas.

10 Standard Life Insurance Company is the flagship subsidiary of StanCorp Financial Group Inc. Its prime businesses are insurance and asset management solutions.

11 Harrison, Tina S. "Mapping Customer Segments for Personal Financial Services." International Journal of Bank Marketing. Vol.12 No.8, 1994, p.17-25.

12 The Needs Hierarchy theory proposed by Abraham Maslow states that a human being is motivated based on the needs that arise in course of his/her life. The hierarchy of needs include Physiological needs, Safety & Security needs, Social needs, Esteem needs, and Self-actualization needs.

13 Beckett, Antony. "Strategic and Marketing Implications of Consumer Behavior in Financial Services." The Service Industries Journal, Vol.20 No.3, July 2000, p.191-208; and Beckett, Antony, Paul Hewer, and Barry Howcroft. "An Exposition of Consumer Behavior in Financial Services Industry." International Journal of Bank Marketing, Vol.18 No.1, 2000, p.15-26.

[14] Franklin Templeton Investments is a global financial services provider and it had 33 offices in India with assets under management of Rs. 223.6 billion for around 1.7 million investors (as on May 31, 2006).

[15] HDFC Mutual Fund is a subsidiary of HDFC Bank.

[16] Credit Rating and Information Services of India Limited. CRISIL is one of the leading credit rating agencies in India.

[17] Kotak Mahindra Mutual Fund (KMMF) is managed by Kotak Mahindra Asset Management Company Ltd., a wholly owned subsidiary of Kotak Mahindra Bank Ltd. Kotak Mahindra Mutual Fund launched its schemes in December 1998 and it had assets of Rs. 122.5 billion with 427,450 investors in various schemes in 2006.

[18] Webster, Jr., Frederick E. "The Changing Role of Marketing in the Corporation." Journal of Marketing. Vol. 56, Issue 4, October 1992.

[19] The Boston Consulting Group is an international strategy and general management consulting firm whose mission is to help leading corporations create and sustain competitive advantage.

[20] http://www.financialexpress.com/fe_full_story.php?content_id=123689

[21] State Bank of India is the largest bank in India.

[22] A tie-up between the Aditya Vikram Birla Group and Sun Life Financial, Birla Sun Life offers a range of financial services including insurance, mutual funds, and fee-based services.

[23] The Unit Trust of India was incorporated in 1964 under the UTI Act (1963). It was the sole mutual fund company in India till 1987.

[24] SBI Mutual Fund was launched in 1987 and is famous for its 'Magnum' series of products.

[25] Canbank Mutual Fund was launched in 1987 and is famous for its 'Can' series of products.

[26] Reliance Mutual Fund is a group company of the Anil Dhirubhai Ambani Group.

[27] Industry: Financial Services, 08 September, 2006. <http://www.ibef.org/industry/financialservices.aspx >

[28] ACNielsen ORG-MARG is a market research, information, and analysis provider. It provides information through its consultancy services.

[29] Industry: Financial Services, 08 September, 2006. <http://www.ibef.org/industry/financialservices.aspx >

[30] Javalgi, Rajshekhar G., and Paul Dion. "A Life Cycle Segmentation Approach to Marketing Financial Products and Services." The Service Industries Journal. Vol.19, Number 3, July 1999, p.74-96.

[31] After the acquisition of Global Trust Bank (GTB) in 2004, OBC achieved a pan India presence.

[32] "India's churning out 9,000 US$ millionaires pa!" The Economic Times. June 14, 2005, www.ibef.org.

[33] Strategic Marketing Forum, www.estrategicmarketing.com

[34] Romaniuk, Jenni. "Brand Positioning in Financial Services: A Longitudinal Test to Find the Best Brand Position." Journal of Financial Services Marketing. Vol.6 No.2, 2001, p.111-121.

Chapter 3

Product Management and Customer Relationship Management

In this chapter, we will discuss:

- The Product Concept and Product Management
- Importance of CRM in Marketing Financial Products
- CRM and Relationship Marketing
- CRM Concepts
- CRM Implementation and Evaluation

Aviva[1] was a late entrant to the Indian insurance market. The company entered the market in 2002. To catch up with the other big players, it adopted the bancassurance route. Aviva focused on sharing customer information between its departments and locations across the country. It implemented the e-CRM suite from Talisma[2]. This suite helped Aviva analyze the information and understand its customers better. This helped the company to modify its products and services and come out with customized products to suit its existing customers. In the process of implementing the e-CRM suite, Aviva also integrated the sales and marketing teams in an attempt to maximize the value to its customers.

Adapted from Pandey, Tarun. "Aviva uses CRM to insure success." www.expresscomputeronline.com.

There has been a considerable amount of transformation in the financial markets in India over the last decade. Product management and customer relationship management have gained more importance in the marketing of financial products. New features have been added to many existing products; some existing features have been dropped. Many new products have been added to the product line, while some products have been phased out. Such product management decisions help marketers maintain a contemporary product portfolio in response to the changing environment and consumer needs.

Further, financial product marketers have begun to focus on developing and maintaining effective relationships with their customers. The need for customer relationship management (CRM) is felt across all financial product verticals. According to Kathleen Kirallah[3], marketers adopt CRM as a channel independent business strategy in order to ensure that their customer interactions add to the profitability of the organization. Also, marketers are increasingly depending on technology to maintain effective customer relationships.

This chapter begins with a discussion on the product concept and product management. We then discuss the importance of CRM in marketing financial products, the link between CRM and relationship marketing, CRM concepts such as customer knowledge, customer loyalty, and customer switching. Next, the chapter discusses the implementation of CRM, with reference to customer knowledge management, the role of technology in CRM implementation, performance evaluation of CRM programs, and the future of CRM usage in India.

THE PRODUCT CONCEPT AND PRODUCT MANAGEMENT

According to Theodore Levitt, 'a product is a complex cluster of value satisfactions. A customer attaches value to a product in proportion to its perceived ability to help solve his problems or meet his needs'[4] A financial product is essentially intangible, and marketers make use of a combination of price, promises, and people to attract customers. People (sales personnel) offer a financial product/service in the form of promises in exchange for a price. The price varies with the product offering and the associated service levels. For instance, in the case of a simple financial product like a loan, a promise is made to the customer that a certain amount of money will be lent for a price that is charged in the form of interest and applicable fees.

In this section, let us first understand the concept of a financial product. We will then go on to discuss the factors influencing the choice of product strategies, the types of product strategies, and the principles of branding in marketing financial products.

Levels of a Product

Any product is conceived around a set of core benefits, which satisfy the basic needs of the consumers. For instance, the core benefit of a life insurance policy is to insure the life of the policyholder. Products can be broadly divided into four levels -- actual product, expected product, augmented product, and potential product.

Actual product

When marketers focus on packaging the core benefit in the form of a product with a brand name and some basic features, it is known as the actual product. The Jeevan Amulya life insurance plan from LIC of India, the PowerVantage account from HSBC, are examples of actual products. Thus an actual product is a packaged form of the generic product and provides the core benefits under a brand name and packaging. The Magnum Equity Fund from SBI Mutual Fund[5] is another example of an actual product; the core tangible benefit offered is large capital gains rather than a regular steady income.

Expected product

Consumers expect certain minimum features and attributes in the product that they intend to buy or consume. Marketers should identify such requirements and attributes and incorporate them into their products. For instance, in the 1990s, a typical savings bank account was not accompanied by an ATM card. Later, consumers started expecting the convenience of 24-hour banking. Subsequently, they started expecting an ATM-cum-debit card, which they could also use at merchant establishments as a means of payment. In general, marketers try to ensure that the actual product meets at least all the requirements of the expected product.

Augmented product

Given the highly competitive environment in which marketers operate, it would be perilous for them to restrict their product offerings to just the expectations of their customers. Thus, whenever possible, they try to add features to the products that will enhance convenience and comfort as far as customers are concerned. For example, many insurance companies have introduced unit linked insurance plans in which customers can choose the portfolio mix -- equities, debt, or a combination of both. Augmented products are developed to enhance customer value and differentiate the marketer from the competitors. The ultimate objective of developing an augmented product is to delight the customer.

Potential product

A potential product is one where all possible additional benefits or features can be provided with a view to increasing the value offered to the customer. Through potential products, marketers can redefine their product lines and revamp their service offerings. Potential products demand innovation from the marketers. In order to develop such products, marketers should first understand the stated/unstated problems and opportunities of the consumers and generate new ideas to address these issues.

Factors Influencing Product Strategies

There are many factors that influence product strategies for marketing financial products. For instance, a strategy of new product addition to the product line or modification of an existing financial product will be influenced by the environment in which the marketers operate. As discussed in Chapter 1, the environment can be external (macro or micro) or internal. Harrison[6] identified four factors that have the maximum influence on financial marketers when they are deciding on product strategies. They are: customers, competitors, technology, and government & legislations.

Customers

Customers have the greatest influence when financial marketers take decisions on the product mix. Marketers should understand the needs of the customers and develop products that satisfy them. This is not an easy task as customers may not always explicitly communicate their needs to the marketers. In some circumstances, customers may not even know that they need a financial product. The success of the marketer depends on identifying those needs and developing products to satisfy them.

Since needs may differ from one consumer segment to another, financial products can be modified in different ways to cater to different needs. For example, for individuals who get their monthly salaries deposited into the savings account, the product can be enhanced by providing features such as Internet banking, mobile banking, multi-city cheques, etc,.

Competitors

Competitors' product strategies are useful sources of information. They throw light on the competitors' perceptions about the market, which can be compared with the marketer's own perceptions and strategies. Many of the new products developed in financial markets are imitations as it is very easy to copy the idea behind these products. Unlike physical products that usually require an elaborate new product development process, imitation of financial products is easier as the imitator has the advantages of incurring low development costs and taking less time-to-market. However, though competitors may imitate the core benefits of a financial product, the marketer can maintain its differentiation from competitors by modifying the augmented product, as for example, through enhanced customer service.

Technology

Technology has been a great driver of change in the financial services industry. Marketers have successfully used technology as a creator of opportunities for serving the customers in a more effective way. New technologies have brought in new products that have revolutionized the way of life the world over. For instance, internationally accepted credit cards have entirely changed the traveling experience of global travelers, whether it is for business or for pleasure. Internet technology has made possible the concept of online trading in shares.

On many occasions, business needs mandate that the marketers put in place the required technology infrastructure to stay competitive. For example, a wide and well-maintained ATM network is required for a bank to ensure the utility of its ATM cards/ATM-cum-debit cards. It follows that a new product strategy must also be supported by the appropriate setting up of technology infrastructure, including appropriate investments in information technology.

Government and legislations

As discussed in Chapter 1, government policies and the regulatory environment play a crucial role in influencing the market for financial products and the decisions of the players in the market. Though banking in India has been significantly deregulated since the late 1990s, the RBI and the government still exert an influence on the functioning of the Indian banking sector. For example, when the RBI signals a downward trend in interest rates, mutual fund marketers may introduce more equity-based funds. Many banks have introduced 'no frills accounts' in response to the central bank's move toward greater 'financial inclusion', in order to provide banking services to the lower income segment. Relaxation of tariff regulations in general insurance may see the introduction of many new non-life insurance products.

Product Mix Strategies

A marketer may have different products catering to different consumer groups. The product mix of a financial marketer is the entire collection of products that it offers to different customer segments. For example, a typical product mix of a bank could be asset products (loans), liability products (deposits), and fee-based services. Similarly, the product mix of a mutual fund marketer includes equity funds, debt funds, balanced funds, etc. (The types of mutual funds are discussed in Chapter 10). Some of the common strategies that marketers use for managing the product mix are -- product mix expansion, product mix contraction, and product modification.

Product mix expansion

Product mix expansion involves the addition of new products to the existing product mix; this can be achieved by adding new product lines or by increasing the depth of each product line. If a bank decides to sell investment products to its customers in addition to deposits and loans, it means that it is adding a new product line to its product mix. This new product line -- investment products — may, in turn, consist of many products such as mutual funds, pension funds, insurance policies, etc. A bank which starts offering educational loans to students as a new product in addition to its existing loan products like housing loans and vehicle loans is increasing the depth of its loans product line.

Product mix expansion can also be done through trading up and trading down strategies. A marketer 'trades up' by introducing a new variant (of an existing product) with a higher price tag. For example, an insurance marketer may introduce a high-end variant of an existing insurance scheme. This may bring in new customers without its losing customers for existing policies. This may also help to enhance the image of the marketer, which again attracts more customers to its products. On the other hand, a marketer 'trades down' by introducing a low priced variant of an existing product to attract those customers who are interested but cannot afford to buy the existing product. While 'trading down', the marketer may reduce the number of features and benefits associated with the product.

Product mix contraction

Some financial marketers rationalize the number of products in their product mix by either eliminating entire product lines or removing certain products in one of the product lines. Product contraction usually happens when a marketer decides to focus on a narrow product mix and eliminate all loss-making products or product lines. Product contraction also happens when marketers decide to stick to their core competencies and spin off all other businesses that are perceived to be strategically unimportant for the organization's long-term future.

Product modification

Product modification takes place when a product is redesigned, repackaged, or even delivered under a new name. A marketer sees product modification as a means to improve the sales of the product. Usually banks modify and improve their products frequently. For example, to increase the penetration and usage of credit cards, credit card issuers are waiving the annual fees, providing discounts at leading merchant establishments, personalizing cards with the cardholder's photo, etc. Another example of product modification is that of HSBC, which was a late entrant in to the Indian housing finance market. At that time (in the late 1990s), home loans were priced at a fixed interest rate by all the leading players, including HDFC.[7] To gain an advantage over the existing players, HSBC started offering home loans at a floating rate of interest.

Branding in Financial Products

Effective brand differentiation has become an important ingredient for success for financial product marketers. Competition in the form of private and foreign players has increased the need for branding. The concept of branding assumes significance in marketing financial products because of their characteristics of intangibility, heterogeneity, perishability, and inseparability.

As discussed in Chapter 2, customer service and service quality are some of the differentiating factors among financial product offerings. Consequently, greater thrust is laid on branding at the corporate level rather than at the product level. Corporate branding communicates the personality and values of the company, and helps the marketers position those values in the minds of the consumers. Financial product marketers try to establish strong corporate brand images in the minds of the consumers so that they recognize and associate the marketer with that distinct brand image.

In India, the financial products sector is still evolving after the deregulation in the banking and insurance sectors. Many financial institutions have been moving in the direction of establishing themselves as 'one stop shops' or 'financial supermarkets' where all types of financial products are made available under one roof. In such situations, corporate branding helps the marketers to communicate to the customers about how they are different from the competition in providing the products and services.

Branding principles

Farkas and Vishwanath[8] have identified a few principles to be followed by a financial product marketer to build a brand. These principles are described here.

Branding starts with a clear strategy for targeting and positioning: The marketers should have a clear strategy as to which market segments they are catering to and the nature of these market segments (i.e., whether they are high end segments or low end segments or mid-market segments). A clear strategy on these lines allows the marketer to position the brand appropriately with respect to the target market in terms of products, price, service capabilities, and delivery channels.

The brand image must be consistent with the marketing strategy: The brand image of the marketer should be distinct and well received by the target customers. In order to ensure long-term success, the brand image should be consistent with the marketing strategy. For instance, Diners Club credit cards and American Express credit cards are considered as status symbols. These cards are offered only to select customers and corporates and are accepted only in select hotels, restaurants, etc. If the marketer suddenly attempts to increase the volume of usage by offering such a card to consumers across a wide range of income segments, it may ruin the brand image. It also follows that branding is not necessarily about competing on price. For example, Citibank focuses more on nurturing customer relationships and providing superior service rather than on reducing the price of its offerings.

Branding is not about spending lots of money on advertising: Branding is all about providing solutions for the needs and expectations of consumers in the target segments. Advertising only helps to communicate to those target segments and attract them to the brand. Advertising will be successful in building the brand only if the financial product caters to the requirements of the consumer and the entire service experience is consistent with the brand image that is communicated.

Multi-tier branding

According to Sheri Rothman[9], every financial marketer should have a clear definite goal-based strategy in branding, arising from its corporate values and objectives. These goals should be framed based on the marketer's strengths and core competencies. For marketing financial products, branding can be a two- or three-tier strategy. The first tier consists of the master brand or the corporate brand, which conveys the values of the organization. The second tier consists of the banner or core brands. Financial product marketers sometimes develop a third tier of brands, which are also known as sub-core brands. The marketers must remember that the second and third tiers of brands should also convey the same values as the master brand.

For example, SBI is a master brand that conveys the message 'safety for the customers' money'. SBI Mutual Fund is a core brand developed by SBI that operates only in the mutual fund market. The Magnum series of products under the SBI Mutual Fund are sub-core brands, which correspond to the individual products. SBI has successfully used the three-tier branding strategy and its brand communication across all the tiers communicate the safety aspects, which are in tune with the organizational values.

Brand logos and taglines

Brand communication is possible through logos and taglines. A logo with its uniqueness distinguishes the brand from other brands and communicates all the values of the brand to the customers. Thus, marketers need to take utmost care in designing their logos. Shades of red and blue are often used in logos. Blue represents trust, solidity, and conservativeness, while red represents standing out in the crowd. Taglines also help highlight the brand values of the company/product in the market. Refer to Exhibit 3.1 for a few examples of taglines used by financial product marketers.

Exhibit 3.1

Taglines of Some Financial Product Marketers in India

Taglines are considered as an important part of branding. Taglines display the values of the company, their brand image, and their customer-centric approach, as applicable (See table below). They help the marketers to reinforce their existing brand image as well as to build a new brand image. For instance, Bank of Baroda relaunched its brand in 2005 with a new logo and tagline in order to project itself as a modern international bank.

Financial Product Marketer	Tagline
HSBC	The World's Local Bank
ICICI Bank	Hum Hain Na
Andhra Bank	Much More To Do, With You In Focus
Bank of Baroda	India's International Bank
United India Insurance	Right Behind You, Whenever You Want
New India Assurance Company Limited	Born to Lead
LIC	Insuring Lives, Ensuring Smiles
Metropolitan Life Insurance Company (Metlife)	Have You Met Life Today
SBI Mutual Fund	A Partner for Life
HDFC Mutual Fund	Continuing a Tradition of Trust
Franklin Templeton Investments	Gain From Our Perspective

Compiled from various sources

IMPORTANCE OF CRM IN MARKETING FINANCIAL PRODUCTS

Many authors have given different definitions for customer relationship management (CRM). Shaw and Reed[10] (1999) defined CRM as an "interactive approach that achieves an optimum balance between corporate investments and the satisfaction of customer needs to generate maximum profit." Michel[11] (1999) proposed the following definition: "Customer relationship management is to identify, establish, maintain, enhance, and, when necessary, also to terminate relationships with customers and stakeholders, at a profit, so that the objective of both parties are met, and this is done by mutual exchange and fulfillment of promises." From these definitions we understand that CRM is a strategic tool for marketers to acquire customers, retain them, and maintain long-term profitable relationships with them.

Today, CRM is considered as a strategic marketing tool that uses information technology to enhance customer loyalty and increase profitability. Due to the characteristic of intangibility inherent in services, the adoption of CRM can contribute significantly to the success of a services marketer. Within the services sector, the marketers of financial products were one of the earliest to embrace CRM concepts and adopt a strategic approach to develop long-term relationships with customers.

Need for CRM in Marketing Financial Products

In India, the economic boom in the early 2000s led to an increase in income levels of consumers; this increase influenced their spending patterns. With the advent of satellite television and the Internet, consumers have become enlightened in terms of market information. They are aware of the various choices available to them, in terms of competing suppliers and their portfolio of financial products and associated services.

Further, competitive pressures have led marketers to realize the importance of customer retention to survive in the market. As a result, financial product marketers have changed their approach from being product-centric to being customer-centric. They have begun to focus on the importance of understanding the customers and developing long-term relationships with them. The rapid strides in technological development have also enabled the use of CRM to overcome (to some extent) the basic characteristics associated with services – intangibility, perishability, heterogeneity, and inseparability.

Financial product marketers emphasize that adopting CRM is no longer an USP; rather, it is a necessity to survive in the highly competitive market. CRM today is implemented in organizations using technologies like data warehousing and data mining that keep track of customer transactions. The information obtained through customer transactions is very important as an organization, say a bank, may have millions of customers and the information from their transactions is huge. But this information provides insights into customer characteristics and spending patterns, which, in turn, help the marketers to develop strategies for making the customer relationships more profitable in the long run.

Benefits of CRM

CRM helps financial product marketers in many ways. The primary benefit of using CRM is to maximize customer value. Marketers consider CRM as a win-win tool due to its twin advantages. Marketers consider CRM as a tool to segment their customers and identify those segments where marketing efforts are to be maximized. CRM also helps maximize the customer value from a customer relationship, which, in turn, increases the profitability of the organization. That is, marketers use CRM to identify those customers who provide high value and focus on them to maximize this value over the lifecycle of the customer relationship.

In addition to maximizing value, CRM also yields benefits such as long-term profitability, cross-selling of products, and brand building.

Long-term profitability

Not all customer relationships can be expected to become immediately profitable. Relationships nurtured over time create profitable revenue streams. CRM goes a long way in building these relationships and reaping the results from them later through the purchase of different products across the different life stages of an individual. The example discussed in Chapter 2 (of the fresh graduate who starts with a savings account, moves on to various other financial products, and finally invests in retirement planning solutions) is one such situation. If the bank nurtures the relationship by guiding the customer through these various stages, it will benefit both in terms of customer retention and customer profitability. Repeat customers reduce the cost of operations as they are more familiar to the staff who provide the service and consume less time than new customers. Besides, the marketing costs associated with attracting new customers are absent here.

Cross-selling of products

A good relationship with customers allows marketers to cross-sell their products to their existing customers. A long relationship with the customer also enables the marketer to develop customized products that can be cross-sold. For instance, banks can cross-sell an insurance product or a hire purchase product that is tailor-made, in addition to a secured loan that a customer has originally applied for.

Brand building

Customers who have reached higher relationship levels are less susceptible to promotions by competitors. In addition, satisfied customers may act as brand carriers and informally provide word-of-mouth publicity for the marketer. They may also refer potential customers, thus saving time and money for the marketer in terms of developing and implementing special promotional campaigns.

CRM AND RELATIONSHIP MARKETING

The principles of CRM have been derived from relationship marketing. To understand more about customer relationships in the financial services industry, one needs to understand relationship marketing. According to Sally Dibb and Maureen Meadows (2001), relationship marketing has its origins in three different areas -- services marketing, network approach of industrial marketing, and quality management.[12] Relationship marketing is concerned with relationships that can exist between any two stakeholders of a business, such as between manufacturer and supplier, manufacturer and distributor, distributor and retailer, retailer and customer, or manufacturer and customer. Thus, relationship marketing has a much broader scope while CRM is concerned only with those relationships that exist with customers.

Relationship marketing takes a long-term approach rather than a short-term one in building relationships with customers. With the emergence of relationship marketing, the marketing of financial products saw a paradigm shift from transactional relationships to customer-centric relationships.

Two Types of Relationship Marketing

Relationship marketing in an organization can be of two types. The first approach focuses on relationship building with external customers and the second focuses on internal customers (employees).

Relationship building with external customers

At the strategy level, the policies set by the top management determine the level of inclination toward building long-term relationships with the customers. At the execution level, relationship building with external customers broadly depends on customer care and perceived service quality, which, in turn, depend on factors like product portfolio, delivery channels, technology, and the employees of the organization. A wide product portfolio gives customers the freedom to choose from the marketer's product range. Delivery channels make it easier for customers to transact with the marketer. Technology helps bring in new and efficient ways of delivering service to customers. Some employees directly interact with the customers and act as brand builders for the organization, while many others contribute directly or indirectly to the customer's satisfactory relationship with the marketer. Of all these factors, the role of employees is the most important in building customer relationships, as it involves the human touch.

Relationship building with internal customers

Berry (1980) proposed that employees of an organization are its internal customers and that their jobs are the products being consumed. The job satisfaction that arises in the process is taken as customer satisfaction. This will enhance its relationship with its workforce on a long-term basis. The management should take care of their internal customers in order to serve their external customers better. Building relationships with the employees demands management intervention to ensure that the workforce is both motivated and customer-conscious.

To achieve these objectives, the management should be empathetic toward the employees in their career planning and should develop strategies that guide them in building their careers. It should also ensure training and development relating to job requirements to increase the customer consciousness and sales orientation of the workforce. Training and development also lead to better team performance, better employee-job fit, better supervisory control, and avoidance of role conflicts. This results in higher motivation levels in the employee. At the tactical level, rewards and benefits can act as motivators for the employees. Rewards and benefits in terms of recognition, salaries, perks, and other fringe benefits translate into fulfillment of the personal urges of employees.

Levels of Relationship Marketing

The effectiveness of CRM strategies primarily revolves around the levels of relationship the marketer holds with the customers. Customer relationships can be viewed at different levels, from a basic level of interaction to a mature level where marketers and customers work together in a symbiotic manner for their mutual benefit. Kotler (1992) proposed five levels of customer relationship marketing, which throw light on how a relationship between the marketer and the customer evolves and develops into a mutually profitable proposition. The five levels are -- basic, reactive, accountability, proactive, and partnership. The hierarchy is illustrated in Figure 3.1.

Level One: Basic

It is purely a transactional relationship between the marketer and customer. Neither of them shows an interest in developing the relationship. A retail customer opening a savings account with a reputed bank can be considered as an example of this kind of relationship. But this basic transactional relationship can pave the way for a positive long-term relationship with the customer.

Level Two: Reactive

This level is also characterized by a transactional relationship. But the marketer advances a step further and invites the customer to contact the service provider regarding any queries or problems associated with any financial product. This can be considered as the first step toward actual development of a long-term relationship with the customer.

Level Three: Accountability

In this level, the marketer takes the relationship forward by actively enquiring about the performance of the financial product with a view to getting feedback and also providing the necessary after-sales service. Such a step from the marketer provides evidence to the customer that service quality is being maintained and adhered to. This increases the customer's inclination toward the marketer and strengthens the relationship.

Figure 3.1: Five Levels of Relationship Marketing

Adapted from Dibb, Sally, and Maureen Meadows. "The Application of a Relationship Marketing Perspective in Retail Banking." The Services Industry Journal. *Vol. 21 No.1, January 2001, p.169-194.*

Level Four: Proactive

The financial marketer further reinforces the relationship by adopting a proactive approach. In this level, the marketer proactively approaches the customer on a continuing basis in order to understand his/her other needs and develops products accordingly. Such initiatives further strengthen customer confidence in the marketer and elevate the relationship to the next level.

Level Five: Partnership

The marketer-customer relationship reaches maturity at this level. A deep relationship exists between the two parties. At this level, the customer voluntarily provides information and indulges in word-of-mouth publicity for the marketer. The financial product marketer attempts to develop relationships and raise them to the partnership level. This level of relationship is generally seen in business-to-business relationships as in corporate banking (discussed in Chapter 4) or fee-based services (discussed in Chapter 11).

CRM and One-to-One Marketing

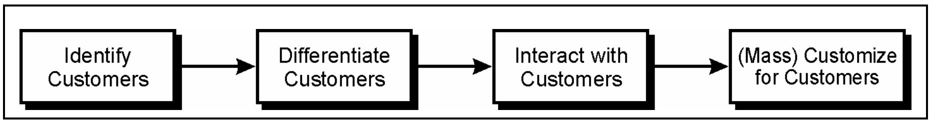
The crux of CRM is to acquire, retain, and maximize the value of the customer base. But it is expensive to acquire new customers as huge sums of money have to be spent on advertising, sales promotions, public relations, personal selling, and direct marketing. Thus, rather than just acquiring new customers, financial marketers aggressively focus on retaining and developing long-term relationships with existing customers -- especially high value customers. The most popular way in which financial marketers try to retain existing customers is by increasing customer loyalty and this they do by adopting one-to-one marketing. One-to-one marketing is an important tool used by marketers who target corporate customers or High Net worth Individuals (HNIs). Apart from customer retention, maximizing customer value is also an objective of one-to-one marketing.

One-to-one marketing is an offshoot of relationship marketing. It essentially involves knowing about each and every possible need of the targeted customers and developing tailor-made solutions for them. In 1993, Rogers and Peppers coined the term one-to-one marketing and defined it as ‘treating each customer separately’. According to them, one-to-one marketing could be achieved at a reasonable cost by the technique of ‘mass customization’, that is, “creating a variety of highly specific products out of pre-existing components, or modules”.

Implementing one-to-one marketing

One-to-one marketing can be implemented in a series of steps. The first step is to identify the target customers based on customer profiling. Technology (in terms of the latest database management tools) helps in profiling customers comprehensively and in identifying the specific requirements of each individual customer. Next, based on the profile, customers are differentiated or segmented on the basis of certain criteria. The criteria vary from marketer to marketer. Next, the marketer interacts with each distinct customer group to understand their current and future needs. The last step is to develop customized products and solutions for each customer group based on this information, in such a manner that each customer feels that his/her individual needs are completely satisfied. This sequence of steps is illustrated in Figure 3.2.

Figure 3.2: One-to-One Marketing - Sequence of Activities



Adapted from Dibb, Sally. “Banks, Customer Relationship Management and Barriers to the Segment of One.” Journal of Financial Services Marketing, Vol.6 No.1, 2001, p.10-23.

Prudential’s[13] direct banking service ‘Egg’ uses CRM to develop and offer tailored services to young professionals and affluent senior citizens in the UK. It offers services like providing an Internet-only bank account for retail customers. Another case in point is that of HSBC. HSBC, as part of its global banking initiative, has targeted high value customers who are also frequent international travelers, with specific products and solutions that cater to their diverse needs. This is an attempt by the bank to carry the relationship with customers into the proactive level of relationship marketing, in terms of Kotler’s framework.

CRM CONCEPTS

With reference to the marketing of financial products, we have discussed the importance of CRM and the overall context of relationship marketing. Let us now understand some of the basic concepts in CRM, such as customer knowledge, customer loyalty and e-loyalty, and customer switching. With a good understanding of these concepts, financial product marketers can use customer knowledge as part of their CRM initiatives to achieve the objectives of increasing customer loyalty and reducing customer switching/defection.

Customer Knowledge

To ensure that they have sustained relationships with customers, marketers need to have comprehensive knowledge about their customers. Customer knowledge includes knowledge about the customer, knowledge to support the customer, and knowledge from the customer. Knowledge about the customers includes the demographic, psychographic, and behavioral components. These components help the marketer understand the customers, categorize them, and target them with appropriate product offerings and promotional campaigns. 'Knowledge to support the customer' refers to the components of knowledge that are useful for the marketer to help the customer have a positive experience with the products or services that the customer has bought. This includes both knowledge about the customer's transactions and interactions with the marketer, and the product-specific knowledge that is required to support the customer. 'Knowledge to support the customer' can also be generated by user communities who interact among themselves, typically using the Internet as a medium of sharing knowledge and experiences. Finally, knowledge from the customers includes feedback, ideas, suggestions, complaints, customer trends, etc. This helps the marketers in the development of new products.

Table 3.1: Types of Customer Knowledge

S. No.	Type of Customer Knowledge	Components of Customer Knowledge
1.	Knowledge about the customer	Processed demographic information
		Knowledge of psychographic characteristics
		Knowledge of behavioral traits
2.	Knowledge to support the customer	Knowledge of products/ services purchased by the customer
		Knowledge of interactions with customer
		Product documentation
		Troubleshooting guides and repair manuals
		Knowledge of interactions between customers (user communities)
3.	Knowledge from the customer	Feedback
		Suggestions and ideas for innovation, especially from lead users/ high-value users/ high-frequency users
		Trends

Adapted from Desouza, Kevin C., and Yukika Awazu. "What Do They Know?" Business Strategy Review. Spring 2005, p.41-45.

Customer Loyalty

Customer loyalty can be of two types -- affirmative loyalty and reluctant loyalty. Affirmative loyalty is characterized by trust, commitment, and a long-term relationship between the customer and the marketer. It develops when the marketer sincerely implements trust building measures and provides superior customer care. On the other hand, reluctant loyalty arises when the customer is pinned down by the marketer despite the urge to switch to competitors. This occurs when marketers set up exit barriers, which ultimately makes it difficult for the customer to leave the marketer without incurring significant switching costs. For example, a high pre-payment penalty for a home loan would cause an existing borrower to reluctantly continue with the existing lending institution, instead of getting the loan refinanced by another institution.

Let us now discuss the factors influencing affirmative loyalty.

Factors influencing affirmative loyalty

Marketers have come to understand that a small increase in affirmative loyalty leads to a big increase in their profits. Thus, they attach high priority to increasing the affirmative loyalty through various measures. According to Reichcheld (1993), in order to manage customer loyalty, four important aspects of the business have to be understood and managed effectively. They are -- customers, product/service offerings, employees, and measurement systems. In addition to these traditional factors outlined by Reichcheld, electronic customer care is now emerging as a powerful tool for increasing the affirmative loyalty of customers.

Focus on the right customers: An organization's *s*uccess depends on those customers who stay with it for a long time. No financial product marketer treats all the customers in the same manner. After segmenting the customers, a particular target segment is identified and preferential treatment is given to those customers who are considered to be profitable.

Product/ service offerings to meet lifetime needs: After identifying the target customers, marketers should understand the needs of these segments and develop product offerings according to their lifetime needs. For instance, the needs of a young unmarried customer change with marriage, and further change when children are born. Thus, the marketers need to provide a portfolio of product offerings which would meet the changing needs of the target customers at different stages of their lifecycle.

Loyalty of employees: As discussed in the section on relationship marketing, employees are the internal customers of an organization. The longer they stay with the company, the more they learn about the company and the more valuable they become in terms of serving the customers. Financial products are service oriented and customers often need personalized advice during the purchase of these products. Employees who have been with the company for a long time know the customers and can serve them better. Thus employee retention has a positive impact on customer loyalty.

Effectiveness of measurement systems: To be successful**,** every loyalty program needs a measurement system. A measurement system helps monitor and control the deviations from the goals of the loyalty program by providing appropriate feedback to the management about the program. To design an effective measurement system, it is important to understand the cause-and-effect relationships that drive long-term profitability rather than focus only on short-term accounting measures. It is important to understand that customer satisfaction scores cannot be taken as a measure of customer loyalty. Customer loyalty can be assessed using metrics such as customer retention rates and/or share of revenue from existing customers.

Electronic customer care: E-loyalty refers to the customer loyalty achieved by a marketer through an electronic communication network. E-loyalty is achieved through the e-CRM initiatives. Salmen and Muir (2003) propose that digital media such as the Internet can be used to increase customer loyalty by providing "digital proximity" instead of "physical proximity" to customers, with an associated reduction in cost and increase in profit. They define e-CRM as "the systematic, active, construction, and maintenance of digital customer relations throughout the complete life cycle of customer relationships."[14] Banks and other financial institutions adopting electronic customer care practices mostly target the young or well-educated consumers who use the Internet extensively.

Customer Switching

For a marketer, customer switching occurs when an existing customer defects and becomes a customer of a competing marketer. Customer switching results in erosion of market share and reduced profits. Marketers search for various alternatives to reduce customer switching rates as the cost of acquiring new customers is much higher than the cost of retaining existing customers.

To reduce customer switching, marketers should first identify the causes for such switching. Keaveney identified eight different reasons relating to service failure on the part of the marketers which cause customers to switch between service providers. Five of these reasons fall within the scope of CRM. They are: (a) core service failures, (b) service encounter failures, (c) price failures, (d) inconvenience, and (e) employee response to service failures. The other three reasons are: (f) attraction by competitors, (g) ethical problems, and (h) involuntary switching. In the following section, we will discuss the reasons which fall within the scope of CRM.

Core service failures

Core service failures include all mistakes and technical problems encountered while rendering the core service. They may range from simple billing errors to big mistakes in terms of reduced service quality or failure to live up to the promises made while selling the service.

Suggested actions: Marketers have to proactively identify such mistakes and errors and correct them as early as possible. When left unattended, a core service failure may have a negative effect not only on the perception of the product but also on the corporate brand image.

Service encounter failures

Service encounters are the personal interactions between the customers and employees of the organization. Service encounter failures arise if the employees are hostile toward the customers and do not give due consideration to the customer's opinion. They also crop up due to technical snags in non-personal service encounters like the Internet, ATMs, interactive voice response system (IVRS) in phone banking, etc.

Suggested actions: Employees are the brand carriers of any service organization and they reflect its image and philosophy. Thus, they need to be properly trained to handle customers. Besides, the management has to treat the employees as their internal customers, understand their needs, and take appropriate measures such as providing for proper career growth for them. Technical problems in non-personal channels should be immediately attended to and rectified to restore the functionality of the channel.

Price failures

Price failures include all the failures relating to price of the products. For financial products, price may include interest rates, fees, charges, surcharges, and penalties. Customers may switch due to increase in existing prices, perceptions of high pricing, unfair pricing practices, or deceptive pricing practices (difference between actual price and quoted price). For example, if the investor (client) in a mutual fund product had not properly understood the concept of annual management fees during the buying process, he/she may switch to another fund on finding out the quantum of the fees and its implications for the effective return on investment.

Suggested actions: As pricing has a major influence on the customer's decision to switch or not to switch, marketers should price competitively and adopt ethical pricing practices to survive in the long run.

Inconvenience

It refers to the trouble customers are put to due to factors such as location of service delivery, hours of operation, and waiting period. Waiting is often a common problem in banks, especially during the mornings and evenings, where customers have to stand in long queues to get a demand draft or make a cash payment. Exhibit 3.2 outlines some of the reasons for customers switching from nationalized banks in India, in the late 1990s.

Exhibit 3.2

Customer Switching from Nationalized Banks in India

The Indian banking scenario was revolutionized by the introduction and aggressive promotion of new products with the support of modern technology. The breed of new private banks like HDFC Bank, ICICI Bank, and UTI Bank, were the first to leverage on this technology advantage in attracting/acquiring more customers. These banks proved to be strong competitors to the nationalized banks. To gain a competitive advantage over the nationalized banks, they used modern service delivery channels such as ATMs and phone banking; this strategy helped them overcome the lack of an extensive branch network. Industry estimates showed that around 12% to 15% of the customers in public sector banks switched to private and foreign banks in the late 1990s. Many of the nationalized banks, which were hampered by their rigid structures and processes and slow adoption of new technologies, could not respond immediately to this phenomenon of customer switching.

Later, some of the nationalized banks -- such as the State Bank of India, Bank of India, Bank of Baroda, Syndicate Bank, etc. -- started restructuring themselves to face the competition from private and foreign banks. They began to invest in technology upgrades, including establishment of ATMs, phone banking, CRM solutions, core banking solutions, etc. They became more competitive by leveraging on their strengths such as huge networks and vast experience. To reduce customer switching, some of these banks followed an area specific plan. As the customer switching rate was high in the metros, the banks laid emphasis on customer retention in these markets. In the smaller cities, they focused both on customer acquisition and retention. In the rural markets, they continued to emphasize on customer acquisition.

Adapted from "Banking in the New Millennium." www.indiainfoline.com/bisc/ari/mill.pdf.

Suggested actions: Marketers can explore other alternatives like alternate channels of delivery, convenient hours of operations, etc. For example, some banks offer 12 hours of regular banking operations on all working days. Extensive use of alternate channels like the Internet and ATMs is another option.

Employee response to service failures

Customer switching also takes place when employees do not treat the customer appropriately when attending to service failures. For instance, employees may either not respond at all to the service failure, or respond rather reluctantly, or put the blame for the service failure on the customer. Whatever be the case, the customer may consider shifting away from the service provider when there is such unresponsive treatment.

Suggested actions: Employees may respond poorly to service failures due to reasons such as lack of training, lack of motivation, lack of job satisfaction, feeling of being overburdened, etc. The management should take up proper employee counseling, understand their needs, and try to solve their problems. Employees may also be motivated through financial & non-financial perks and job rotation.

CRM IMPLEMENTATION AND EVALUATION

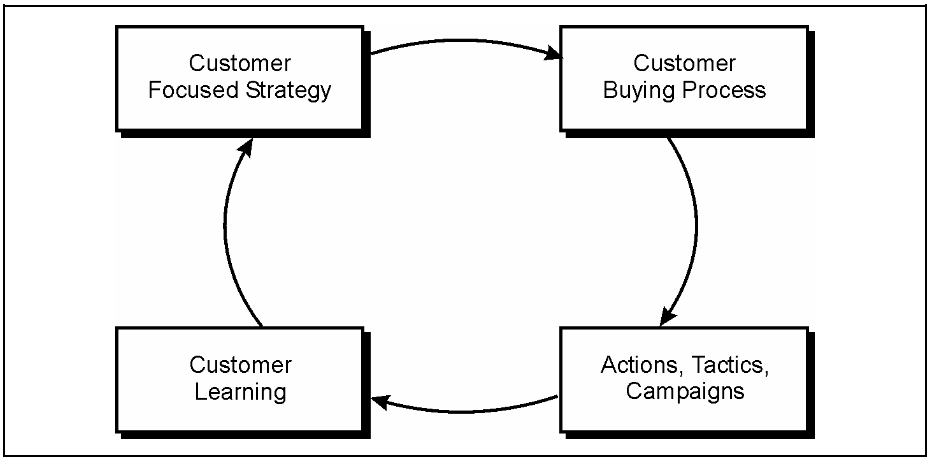
To develop and preserve customer relationships over the long run, financial product marketers need to develop an effective framework toward implementation of CRM initiatives. The first major step in this direction is to acquire and manage customer knowledge. Thus, marketers have to develop a mechanism for managing customer knowledge effectively. CRM is technology intensive; a marketer can choose from multiple technologies available in the market for CRM implementation. The performance of the CRM program has to be monitored and its performance has to be assessed, to see whether it is meeting the organizational objectives. In the near future, the organizational objectives may be more oriented toward operational issues such as customer handling. In the long term, the focus of CRM implementations would be toward the achievement of strategic objectives such as real-time segmentation and co-creating value with customers. In this section, we discuss the process of customer knowledge management, the role of technology in the implementation of CRM, performance measurement of a CRM program, and the future outlook for CRM usage in India.

Customer Knowledge Management

As we saw earlier, customer knowledge includes knowledge about the customer, knowledge to support the customer, and knowledge from the customer. For financial product marketers, customer knowledge is a vital asset that helps them increase their profitability. The main objectives of customer knowledge management are to acquire more profitable customers and retain existing customers in the long term, maximize customer value by increasing customer spending on the company's products, and ensure customer satisfaction.

Employees who interact with customers are an important source of information on customers. But since employees may not have any idea about how to tap that knowledge, the management has to identify ways and means to tap it and use it profitably. Roscoe termed the process of customer knowledge management as 'customer knowledge journey' and identified four steps in this process. The customer knowledge management process is illustrated in Figure 3.3. It has four inter-related steps -- developing a customer-focused strategy; developing the customer buying process; implementing actions, tactics & campaigns; and customer learning.

Figure 3.3: Customer Knowledge Management Process



Adapted from Roscoe, David. "The Customer Knowledge Journey." *Journal of Financial Services Marketing*. *Vol.5 No.4, 2001, p.314-318.*

Develop a customer-focused strategy

Marketers expecting customer loyalty have to adopt a customer-focused strategy. They must orient their products and marketing efforts toward achieving customer satisfaction and delight. Generally, such a strategy promises a host of benefits to the customer in terms of customized products, price, distribution, and satisfactory customer relations.

Develop the customer buying process

The customer buying process refers to the various phases of purchase decision making which a buyer goes through. The marketer should identify all the cues and collect information about customers while they go through these phases. This information is vital to the marketer in that the buying behavior aspects give insights for better positioning of the existing products and for developing new products.

Implement actions, tactics, and campaigns

Knowledge acquired from the first two steps is used in the implementation of suitable actions, tactics, and campaigns. This includes developing a better product, developing and executing customer-centric advertising and promotion campaigns, enhancing customer service levels, etc. All these actions help improve the customer's loyalty and the marketer's profitability.

Customer learning

The most important step in the customer knowledge management process is customer learning. Marketers should learn from their actions and campaigns about consumer behavior and ensure that mistakes or deviations in the actions are taken care of. Learning feeds back to the customer-focused strategy and helps in re-orienting the marketer toward the customer, as required. Thus, customer knowledge management is not a one-time linear process, but a recurring cycle from which marketers keep getting new insights about customers on a regular basis.

Role of Technology in CRM Implementation

Technology is an essential ingredient for effective implementation of CRM. Technology infrastructure, in the form of computer hardware, software, networks, and other facilities, has to be installed for the smooth functioning of the CRM program. CRM solutions are primarily used to (a) aggregate the customer data to create a single, accessible source of information (b) analyze and present the data in a usable form for the marketers to take strategic and operational decisions, and (c) provide tools and information for the front office executives for effectively delivering customer service.

There are two categories of CRM software tools. One is termed as operational CRM and it assists the frontline employees who directly interact with customers in their operations. These operations are mostly transactional in nature and hence, these tools primarily involve collecting customer information. The second type of tools is analytical tools. They help the back office employees and the management in analyzing the customer information collected using operational CRM tools. Analytical tools analyze various transactions over a period of time to identify the needs of the customers. Raw data is converted into useful information from which business intelligence is derived.

Analytical CRM facilitates managerial decision making, such as market targeting, development of customized products and services, etc. For example, Standard Chartered Bank finds its analytical CRM tools very helpful in managing and optimizing the profitability of the products in its retail portfolio. Sedjwick John Joseph, Head, Business Intelligence Unit, Standard Chartered Bank, says, "The solution also enables micro-segmentation. Using analytics and a test-and-learn culture, we know the probability of customers adopting a new product. We now know which card member is more likely to take an auto loan. This has resulted in more focused marketing campaigns and reduced costs, with improved customer satisfaction."[15]

Software applications have evolved over the years and there are many vendors in the market who offer CRM software solutions. Table 3.2 provides a list of CRM software solution vendors in India. Exhibit 3.3 describes the evolution of CRM technologies worldwide and their usage.

Table 3.2: List of CRM Software Vendors in India

Company	Solution(s)
Adapt Software Applications	ADAPTcrm
Business Objects	Business Objects Enterprise Web Intelligence Crystal Reports
Microsoft	Microsoft CRM
Oracle	Oracle CRM
Siebel	Siebel CRM - Sales Force Automation - Marketing Automation "Call Centre and Service - Business Analytics - Hosted CRM
Talisma	Talisma Multi-channel CRM solution

Source: Das Gupta, Soutiman. "The Indian Experience." Network Magazine. May 2005.

Exhibit 3.3

Evolution of CRM Applications

CRM software originated in the early 1980s. The software provided elementary support for customer relationship management practices. The focus of these applications was to automate sales force activities and provide solutions for customer service and support. The aim was to improve customer service through better service delivery.

First round of integration: In the early 1990s, the functions and features of sales force automation (SFA), customer service and support were integrated into a single solution by vendors like Siebel and Aurum. Other vendors like Rubric and MarketFirst offered point solutions (stand alone software) in the mid-1990s for specific marketing functions such as campaign management. These solutions offered marketers the ability to link themselves more closely with the customers. Toward the late 1990s came business analytics and e-customer solutions. Business analytics helped CRM executives in analyzing customer information to arrive at strategic decisions while e-customer solutions addressed the needs of Internet operations and online customer relations.

Second round of integration: A second round of integration of campaign management, marketing functionality, business analytics, and e-customer took place in the late 1990s with vendors like Seibel dominating the CRM market. However, there was a lot of hype around the technology side of the CRM solutions; the people and process elements were usually neglected, though they are vital for the success of a CRM implementation. The dotcom crisis in the early 2000s brought in the much needed change in the mindsets of the CRM vendors. The people-process-technology mix was adopted in the right proportions to enhance the probability of success of a CRM implementation.

Third round of integration: The CRM systems in the 1990s provided information solutions only for the marketing department. But later, enterprise-wide applications that catered to the information needs of the whole organization picked up momentum. Enterprise-wide applications have the capability of providing solutions for the entire organization and its stakeholders like suppliers, distributors, customers, etc. The existing CRM systems that managed huge volumes of data, had to be integrated with the enterprise-wide solutions. This resulted in a third wave of integration.

Adapted from Goldenberg, Barton. "CRM: The Past and the Future." CRM Magazine. www.destinationcrm.com, January 2006.

In addition to the standard CRM systems and enterprise solutions, the other technologies that are used in CRM implementation are data warehousing, data mining, and business intelligence solutions. We will focus on data warehousing and data mining.

Data warehousing and data mining

Data warehousing deals with the efficient storage of historical information. Transactions made at different locations through different channels are normally stored in separate databases. But when a bank or financial institution with a national presence needs to analyze the data to get a complete picture, data warehousing is a useful technology. It integrates all the historical data across different systems at different locations into one single database from which it can be easily retrieved. For instance, the complete data of a customer's transactions/interactions with a bank --

through the ATM, Internet, phone banking, and branches over a period of time -- can be integrated using data warehousing. This helps the bank to study the banking behavior of the customer.

Data mining is used to identify and retrieve useful information from the huge volumes of data present in a data warehouse. The data mining tool recognizes patterns in the available data and provides support for decision making. Data warehousing and data mining technologies help the financial product marketers plan their actions and programs for customer relationship management. George Varghese, Head — Marketing, SAS India, says, "Data mining and data warehousing can help banks identify the right customer for a particular promotion. They also help in cross-sell and up-sell of services to customers."[16]

Performance Evaluation of a CRM Program

CRM implementation in an organization usually involves considerable investments in terms of time, money, and other resources. So, financial product marketers may implement such CRM projects in a phased manner. At the end of the day, CRM implementation should provide both quantitative and qualitative benefits for the marketer. Quantitative benefits include monetary returns on the investment in terms of increased profitability. Qualitative returns can be establishment of long-term relationships with the customers and a reduced burden on the employees while they maintain and enhance such relationships over time.

Marketers need to evaluate the performance of the CRM implementation over time to ascertain its success. Traditionally, many quantitative metrics/indicators of performance have been used for this purpose, such as sales indicators, marketing indicators, and customer service indicators. Sales indicators may include units sold, cross-sell ratio, conversion rates of qualified leads, increased assets under management (AUM), and cost per sale. Marketing indicators may include response rates to specific promotional campaigns, return on investment (ROI), campaign size in terms of targeted prospects/customers, and campaign velocity (frequency of promotional campaigns). Customer service indicators may include average wait time and average duration of call. Table 3.3 provides details on these traditional performance indicators for CRM implementation.

Kathleen Khirallah opines that such traditional indicators help marketers analyze data only in quantitative terms. But these indicators do not provide the scope for analysis of the qualitative aspects of customer interactions and relationships, which may be more important than the quantitative information. Thus, she argues that these quantitative indicators alone are not enough to evaluate the success of the CRM implementation. According to her, these indicators present a snapshot view of the situation while CRM performance can be best understood against a time continuum.

Basket of metrics

TowerGroup, a US-based research and consulting firm focusing on the global financial services industry, has proposed a group of eight metrics for evaluating the success of a CRM implementation. The group of metrics, referred to as a 'basket of metrics', is derived from the popular 'Balanced Scorecard'[17] concept, introduced by Kaplan and Norton. Table 3.3 provides details of these eight metrics that are recommended for evaluating the overall efficacy of a CRM program in a financial institution.

Table 3.3: TowerGroup's Basket of Metrics for CRM Performance Evaluation

Metric	Details
Customer profitability	It determines the level of customer service that is actually applicable to each customer. It depends on the customer's behavior and the extent of resources consumed by him/her. Marketers should give priority to maintaining relationships with customers who are highly profitable from the marketer's perspective.
Customer satisfaction	This metric reflects the type of interactions that customers have with the financial product marketers and the value that they derive from those interactions. It will be higher if the marketer provides appropriate communications to the customer in a focused manner.
Market share	Market share is a relative measure that reflects the market performance of the marketer against the competition. It helps identify the marketer's position in the market and provides the direction to implement further action.
Wallet share	Wallet share indicates the share of the disposable income that a customer spends on the financial products of the marketer, compared to the total disposable income that he/she spends on all financial products. Though this is difficult to measure, it is vital for the marketers to understand the dynamics of customer's disposable income and compare their wallet share with respect to that of the competition.
Cross-sell ratio	This is a very good indicator of CRM success. A higher ratio indicates closer relationships with the customers. However, if the marketer focuses too much on this one metric rather than on the entire basket of metrics, it would be counter-productive.
Response rate	It indicates the responsiveness of the marketer in terms of making 'appropriate' offers to the targeted customer segments.
Relationship duration	In the case of affirmative loyalty, a longer relationship implies more business from the customer. However, relationship duration would be high even in the case of reluctant loyalty -- for example, a dissatisfied customer who is not switching due to high switching costs or lack of initiative. So, financial marketers need to monitor the quality of relationship along with the duration of the relationship.
System availability/ Response time	System availability and response time can influence the customer's perception of the marketer's customer focus and service levels.

Adapted from Khirallah, Kathleen. "Customer Relationship Management: How to Measure Success?" Bank Accounting & Finance. Vol. 13 Issue 4, Summer 2000.

The metrics developed should be measured periodically to measure the success of the CRM program. Kirallah suggests that the optimum time interval for measuring the metrics can be a one month period, at least where the data is available in-house. The CRM performance evaluation may be carried out with the same periodicity for all customer segments; however, the corrective action may be prioritized toward the more profitable segments.

Future Outlook for CRM Usage in India

At the global level, CRM has evolved into a reliable philosophy where process and technology are combined to produce customer-centric practices in the organization. CRM implementation aims at providing accurate customer information for the marketers, which is used for achieving customer satisfaction and customer retention. Though CRM usage in marketing financial products has evolved over the years, it is relatively new in the Indian scenario. The future of CRM can be discussed under two perspectives -- choice of CRM application, and functional usage.

Choice of CRM application

In India, CRM usage began with the deployment of stand-alone software applications. They mainly focused on sales force automation and service delivery; the emphasis was on reducing costs, streamlining processes, eliminating delays in service, and improving overall efficiency. They handled huge volumes of customer information. Later, Enterprise Resource Planning (ERP) solutions (e.g. SAP, Oracle Applications), which addressed the needs of all the departments and functions of the organization in an integrated manner, became increasingly popular in India -- especially with large enterprises. This led to the development of interfaces between ERP applications and CRM applications for seamless transfer of information between the two systems. Going forward, the availability of pre-built interfaces with standard ERP products is expected to be an important criterion for large enterprises when they choose a CRM application. Stand-alone CRM applications will be in demand in the small and medium business enterprises (SME) segment.

Functional usage

For financial product marketers in India, the immediate task is to increase their operational efficiency in terms of customer handling and customer complaints. Swarup Choudhury[18], Director, Field Support Services, IBM, predicts that customers will become more demanding in terms of advocacy, personal security, and control in their relationships with financial marketers. Sharad Bishnoi[19], Assistant Vice-president, Head, Business Process Re-engineering Group, HDFC Bank, points out that with the limited number of basic products in banking, marketers should focus on practices such as service packaging, which are recently being adopted by marketers in India.[20] Service packaging helps in packaging more customized products to suit a customer's needs. A few organizations in this sector are already in the process of becoming financial supermarkets, where all types of financial products are made available.

In the future, CRM solutions should help the marketers work with customers on a real-time basis. Working with customers on a real-time basis would mean re-segmenting the markets based on real-time information. Such developments would help marketers cross-sell more of their products to more of their customers at better prices. This could lead to higher levels of customer satisfaction and increased profitability.

C.K. Prahalad and Venkat Ramaswamy in their book "*The Future of Competition*"[21], proposed that marketers should consider the experiences of customers in the process of product development and service delivery. They stressed the building of an infrastructure for experience-led co-creation of products. Thus, customers will play the role of co-creators of the products and services by more actively involving themselves in the design and development stages. The future of CRM is expected to involve the development of technologies and infrastructure that create a common platform for marketers and customers to come together and work for each other's common good. That is, more importance will be given to the 'knowledge from the customer'.

SUMMARY

Financial product marketers need to manage their product portfolio in response to the changing environment and consumer needs, in addition to managing customer relationships effectively for achieving long-term profitability. The concept of a product can be understood in terms of the following four terms – actual product, expected product, augmented product, and potential product. For a financial product, the product strategy is greatly influenced by customers, competitors, technology, and government & legislation. Depending on these factors, the product mix strategy could be product mix expansion, product mix contraction, and product modification.

Branding in financial services is done more at the corporate level than at the product level. Branding should start with a clear strategy for targeting and positioning. The brand image should be consistent with the marketing strategy. Advertising can be successful in building the brand only if the financial product caters to the requirements of the consumer and the entire service experience is consistent with the brand image that is communicated. In the financial product sector, brands can occur in three tiers -- master brand, core brands, and sub-core brands. When there are multiple tiers, the brands in all the tiers should convey the same organizational values. These values can be communicated through brand logos and taglines.

CRM is a strategic tool for marketers to acquire customers, retain them, and maintain long-term profitable relationships with them. It uses information technology to achieve these objectives. Competitive pressures have led marketers to realize the necessity of customer retention to survive in a deregulated economy. CRM has enabled the shift in approach from being product-centric to being customer-centric. In addition to maximizing customer value, CRM helps marketers to cross-sell products, achieve long-term profitability, and build the brand.

Relationship marketing is concerned with relationships that exist between any two stakeholders of a business. It involves relationship building with both external customers and internal customers. In an organization, relationship marketing can be at one of the following five levels -- basic, reactive, accountability, proactive, and partnership levels. One-to-one marketing essentially involves knowing about each and every possible need of the targeted customers and developing tailor-made solutions for them. To implement one-to-one marketing, the marketer needs to identify the target customers, differentiate them into groups, interact with each customer group, and provide customized products and solutions in a cost-effective manner. This can be done using the technique of mass customization.

Customer knowledge, customer loyalty, and customer switching are three important concepts in CRM. The components of customer knowledge can be classified into three broad categories: knowledge about the customer, knowledge to support the customer, and knowledge from the customer. Customer loyalty can be either affirmative loyalty or reluctant loyalty. The level of affirmative loyalty is influenced not only by traditional factors, such as customers, product offerings, employees, and measurement systems, but also on emerging practices such as electronic customer care. Eight different reasons have been identified for customer switching. They include (a) core service failures, (b) service encounter failures, (c) price failures, (d) inconvenience, (e) employee response to service failures, (f) attraction by competitors, (g) ethical problems, and (h) involuntary switching. The first five reasons in this list can be addressed through the use of CRM techniques.

Implementation of CRM includes customer knowledge management, technology adoption and implementation, and performance measurement. The customer knowledge management process (journey) is a cycle with four inter-related steps –

developing a customer-focused strategy; developing the customer buying process; implementing actions, tactics, campaigns; and customer learning. Technology implementation has become the key to CRM implementation in an organization as huge volumes of customer data can be stored, managed, and retrieved using the latest technologies. CRM software tools can be categorized into operational CRM tools and analytical CRM tools. When the performance measurement of the CRM activities is done using a carefully defined basket of metrics, it helps in managing and controlling the CRM initiatives in the organization. In the future, large enterprises in India are expected to opt for CRM applications which have pre-built interfaces with standard ERP applications, while the small and medium business enterprises may still continue to use stand-alone CRM applications. The usage of CRM in India is expected to evolve from ensuring operational efficiency (in customer handling) to yielding strategic benefits -- through real-time customer segmentation, and co-creation of products with customers.

End Notes:

[1] Aviva Life Insurance is a joint venture between the Indian FMCG major Dabur and UK's largest insurance company Aviva.

[2] Talisma is a US-based provider of Customer Interaction Management (CIM) solutions. In India, it has its regional office at Bangalore.

[3] Khirallah, Kathleen. "Customer Relationship Management: How to Measure Success?" Bank Accounting & Finance. Vol. 13 Issue 4, Summer2000.

[4] Levitt, Theodore. "Marketing success through differentiation – of anything." Harvard Business Review. Vol. 58, January/February 1980, p.83-91.

[5] SBI Mutual Fund is a subsidiary of SBI and was established in 1987 to sell mutual funds.

[6] Harrison, Tina. Financial Services Marketing. Essex: Pearson Education Limited, 2000.

[7] "Strategic Marketing Forum." www.etstrategicmarketing.com/smSep-Oct2/forum.htm.

[8] Farkas, Charles, Vishwanath, Vijay. "The First Step To A Winning Brand Strategy Is Deciding Who You Are." American Banker. Vol. 162 Issue 218, 11/12/97.

[9] Rothman, Sheri. "The Benefits of Branding." Bank Investment Consultant. Vol. 7 Issue 8, August 1999.

[10] Annette Reichold, Lutz Kolbe, Walter Brenner. "Performance Measurement of CRM in Financial Services." Conference paper presented in PMA 2004 Conference, 2004.

[11] Panda, Tapan. "Creating Customer Life Time Value through Effective CRM in Financial Services Industry." Journal of Services Research Vol. 2 Issue 2, Oct2002-Mar2003, p.157-171.

[12] Dibb, Sally, and Maureen Meadows, "The Application of a Relationship Marketing Perspective in Retail Banking." The Services Industry Journal, Vol. 21 No.1, January 2001, p.169-194.

[13] UK-based Prudential Plc. is one of the leading financial services providers in Europe.

[14] Salmen, Sonja M., and Andrew Muir. "Electronic Customer Care: The Innovative Path to E-loyalty." Journal of Financial Services Marketing. Vol. 8 Issue 2, 2003, p.133–144.

[15] Das Gupta, Soutiman. "CRM: Beyond Technology." Network Magazine. May 2005.

[16] Anil Patrick R. "The Tech Factor in Banking." Network Magazine. May 2003.

[17] Introduced by Robert Kaplan and David Norton in 1992, the Balanced Scorecard is an integrated framework for describing strategy through the use of linked performance measures in four, balanced perspectives — Financial, Customer, Internal Process, and Employee Learning and Growth. The Balanced Scorecard acts as a measurement system, strategic management system, and communication tool.

[18] "Indian Banks Defining the Future of Banking." Network Magazine, February 2006.

[19] "Indian Banks Defining the Future of Banking." Network Magazine. February 2006.

[20] "Indian Banks Defining the Future of Banking." Network Magazine, February 2006.

[21] Prahalad, C.K. and Venkat, Ramaswamy. "The Future of Competition: Co-Creating Unique Value with Customers." New Delhi: HBS Press, Penguin Books, 2004.

Part II
Marketing Financial Products – A Closer Look

Chapter 4

Corporate Banking

In this chapter, we will discuss:

- Customers and Relationships in Corporate Banking
- The Product Mix
- New Product Development & Innovation
- Pricing
- Promotion
- Distribution
- The SME Segment

While Indian banks are aggressively pursuing growth in retail banking, they are facing tough competition in the corporate banking business, also known as institutional banking or business banking. To meet their funding requirements, corporates are gradually shifting their focus away from bank loans to other sources such as the primary markets, non-banking financial institutions, and external commercial borrowings[1]. Banks have been forced to make concerted efforts to woo existing corporate customers with newer product offerings and flexible pricing policies. At the same time, corporate bankers are actively targeting the lower end of the market that comprises small and medium business enterprises (SMEs). Corporate bankers are showing an increasing interest in this long neglected SME sector.

We start this chapter with some insights on customers and relationships in corporate banking, the product mix, new product development, and innovation. We then discuss the issues involved in pricing, promotion, and distribution of corporate banking products. Finally, we focus on the importance of the SME segment in the corporate banking business.

CUSTOMERS AND RELATIONSHIPS IN CORPORATE BANKING

It is important for corporate bankers to understand the needs of their customers and manage their relationships with them. Historically, banks have nurtured close relationships with their corporate customers as these customers give them bulk business. Relationship marketing has helped many banks retain their corporate customers, even in a highly competitive market. With advances in technology, newer channels of distribution have emerged which have directly or indirectly helped in strengthening these relationships.

In this section, we first discuss the market segmentation followed in corporate banking and then go on to take a look at the way the relationship between a bank and its corporate customer typically evolves.

Corporate Customers

As mentioned in Chapter 2, in the *a priori* approach to segmentation, the entire market is segmented using different bases of segmentation. Chapter 2 also discussed the different segmentation bases applicable to the retail market for financial products. In corporate banking, the commonly used bases of segmentation are: size (sales volume and/or capital employed) and industry verticals. Based on the sales volume and/or capital employed, corporate customers can be divided into three categories -- large corporations, mid-size companies, and small and medium business enterprises. Traditionally, banks have been giving most of their attention to large corporations and mid-size companies. But this trend has changed now and SMEs have begun to get their due attention. When industry vertical is used as a basis of segmentation, corporate customers are grouped based on their line of business – for e.g., automobiles and auto components, aviation, agri-products, chemicals, and tourism and hospitality.

Corporate bankers use data from the customers and from external sources to choose their borrowers and price their offerings appropriately. They expect a good credit rating from an authorized credit rating agency. For instance, IDBI Bank clearly defines the eligibility criteria for corporate borrowers, for different types of loans. It also specifies the acceptable range of values for different financial ratios, such as the debt equity ratio and the current ratio.

The Bank-Corporate Customer Relationship

Relationship building is one of the critical factors for success in corporate banking. The more longstanding the relationship, the greater is the volume of business that the bank gets from its customer. This usually leads to lower risks, as the banker has in-depth knowledge about the customer's financial situation, and also to greater profitability as the cost of sales is quite low for the incremental revenue.

The relationship between a bank and its corporate customers is similar to the buyer-seller relationships in the industrial marketing scenario, where close and extensive interactions exist between the bank's employees and the customer's key personne[1]. For such relationships to evolve into partnerships, many banks organize their processes around the needs of the customers. Employees are encouraged to be customer-focused, in addition to being knowledgeable about the bank's products and processes. In corporate banking, banks maintain trained staff in the capacity of relationship managers or field officers. These managers are responsible for different corporate customers (also called corporate accounts). Account management helps build confidence in the customers by fostering a sense of trust and commitment, leading to opportunities for generating more business from the account. See Exhibit 4.1 for HSBC's approach to managing relationships with its corporate customers.

Exhibit 4.1

HSBC's Relationships with Corporate Customers

The Hong Kong and Shanghai Banking Corporation (HSBC) entered India in 1959 through the acquisition of the Mumbai-based Mercantile Bank of India. It was named as the 'Best Foreign Commercial Bank' in India by FinanceAsia[2] for four consecutive years, from 2000 to 2004. As of March 31, 2006, HSBC's Indian operations had a net profit of Rs. 5.15 billion.

HSBC's success was primarily the result of its focus on long-term relationship development with large corporates and its leveraging on its global experience to come up with new products and services to suit local corporate requirements. As a result of this focus, HSBC was able to forge long-term relationships with seven of the ten leading Indian companies and eight of the ten largest multinational corporations operating in India.

HSBC uses sector-based client service teams consisting of relationship managers, product specialists, and industry specialists to build relationships with its corporate customers and to develop customized solutions, when required. Every team is supposed to understand the industry/sector thoroughly and the client's Indian operations and global operations. According to HSBC, this approach has been of great use in designing better products and delivering value to the customer.

Adapted from "Hong Kong & Shanghai Banking Corporation Ltd." www.ibef.org/attachdisplay.aspx?cat_id=461&art_id=6814;and http://www.hsbc.co.in/in/cibm/cb.htm

Factors Influencing the Bank-Corporate Customer Relationship

Unlike retail banking customers, corporate customers have sufficient bargaining power and they too have control over the interaction process. According to Zineldin (1995), there are three major components that influence the successful development of long-term relationships between a bank and its corporate customers. They are -- the external environment, the atmosphere of the interaction, and the interaction process. The sub-factors of these components are outlined in Table 4.1.

Table 4.1: Factors Affecting Interactions and Relationships in Corporate Banking

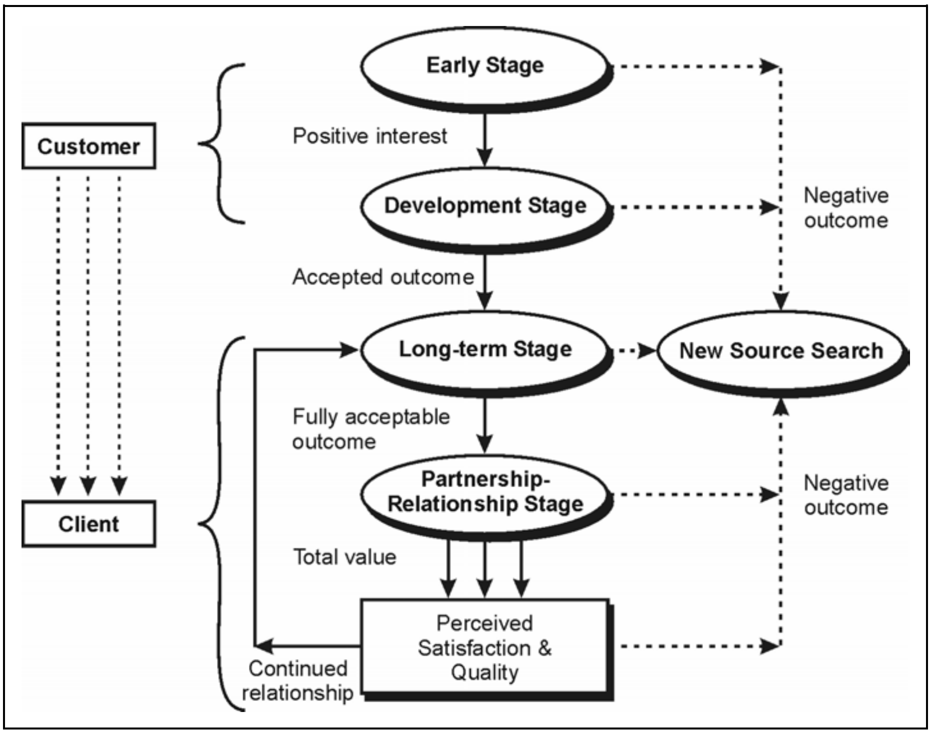
Component	Sub-factors
External Environment	Economic factors, such as: • Competition in the customer's industry • Competition in the banking industry • Interest rate • Inflation • Business cycle Technological factors, such as: • Communication networks • Technology adoption in the banking industry Legal/ political environment, such as: • Political stability • Regulations on business • Policies related to banking
Atmosphere of the Interaction	Power/Dependence (of one party relative to the other party)
	Cooperation/Conflict (between the two parties)
	Trustworthiness (perceived reduction in risk and uncertainty)
Interaction Process	Information exchange Business exchange (e.g. financial transactions) Social exchange between the personnel of the bank and the corporate customer

Adapted from Zineldin, Mosad. "Bank-Company Interactions and Relationships: Some Empirical Evidence." International Journal of Bank Marketing*. Vol. 13 No. 2, 1995, p.30-40.*

The Partnership-Relationship Lifecycle

The evolution of a long-term relationship between a bank and a corporate customer, from the time the relationship starts to the time it develops into a partnership, can be understood in terms of a lifecycle model. This partnership-relationship lifecycle model was proposed by Zineldin in 1995. The partnership-relationship lifecycle consists of four stages -- the early stage; the development stage; the long-term stage; and the final stage or the partnership-relationship stage -- as illustrated in Figure 4.1. At every stage, there can be a positive outcome or a negative outcome. A positive outcome strengthens the relationship and carries it forward while a negative outcome prompts the customer to go in search of a new bank or financial institution for procuring financial products and services. From the third stage onward, the customer is referred to as a client of the marketer. Finally, when the relationship reaches the partnership stage, the bank has in-depth knowledge of the client's business needs; a sense of mutual understanding and confidence has developed between the client and the bank. However, it should be noted that the relationship is dynamic and that the parties involved repeatedly assess the relationship to judge whether it should be maintained.

Figure 4.1: Partnership-Relationship Lifecycle



Adapted from Zineldin, Mosad. "Bank-Corporate Client "Partnership" Relationship: Benefits and Life Cycle." International Journal of Bank Marketing. Vol.14 Issue 3, March 1996, p.14-22.

The early stage

The objective of the marketer in this stage is to build relationships with those corporate customers who have high potential to bring in revenues for the bank. The objective of a business organization, on the other hand, is to select a bank that can offer customized products and services at the optimum price, and provide security for investments. Each party scouts for an appropriate partner with whom to build a relationship, keeping in mind its own set of objectives. In this stage, banks as well as the potential customers are not fully aware of the other party's requirements and capabilities. Thus, they cautiously approach each other and try to explore the possibilities of building a relationship. In the early stage, bank marketers lay emphasis on identifying target market segments to promote their product offerings. The bank attempts to understand the requirements of the corporate customers in the chosen segment(s) and match the product offerings with the requirements.

The development stage

This stage is characterized by transactions between the bank and the customers. Banks try to create a conducive atmosphere for the new customer to carry out transactions. Typically, a corporate customer may be allotted a relationship officer who facilitates all the transactions of the customer with the bank. The marketer measures customer satisfaction with regard to current levels of service delivery. An attempt is also made to identify the customer's current attitudes toward the bank and to take corrective actions to enable further interactions that pave the way for healthy relationships. In this stage, banks not only try to match their product offerings with customer requirements but also attempt to customize their product offerings to meet the customer requirements. In this process, banks may also try to anticipate and address the future requirements of customers.

The long-term stage

In the long-term stage, the relationship is characterized by mutual trust, loyalty, and satisfaction. In this stage, the corporate customer is considered as a corporate client since a long-term relationship has been established. The client exhibits strong loyalty toward the bank and provides a steady flow of business to it. In return, the bank tries to delight the client by offering special privileges and more customized services, which are generally denied to customers in the earlier stages. Marketers attempt to build an enduring relationship with the clients through closer interactions at a professional level.

The partnership-relationship stage

This is the final stage of relationship development between the bank marketer and the corporate client. In this stage, the relationship has blossomed into a partnership where the client is confident about the bank's ability in matters relating to its current and future financial needs. It is confident about conducting the bulk of its business transactions with the same bank. A sense of mutual interdependence develops in this stage. Banks try to ensure that their offerings are unique and differentiated from those of competitors. The relationship grows from just the financial level to the institutional level. Deep and complex individual, social, and financial bonds exist in this stage between the bank and the client. As the bank's employees play a very important role in nurturing these external relationships, the bank should also take care to strengthen its internal relationships with its employees.

Benefits of Partnership Relationship

A partnership relationship develops between the bank and client over a period of time. Corporate bankers should attempt to foster such relationships with their preferred clientele. As discussed here, both the bank as well as the clients benefits from such partnership relationships.

- A partnership relationship develops a sense of mutual interdependence between the bank and the client. This development helps the bank to correctly anticipate the client's future needs. This has been discussed earlier in Exhibit 4.1, in the context of HSBC and its banking interactions with Indian corporates.
- When there is a partnership relationship, the demand for the bank's product offerings is less sensitive to price changes. The client does not independently shop for the best price for each and every product or transaction. This insures the bank from losing business. On the other hand, if the bank-customer relationship has not evolved to the partnership stage, then there is a higher probability of the customer shifting to another bank to get the best possible deal in terms of price.
- For the bank, it is a source of competitive advantage to have clients in the partnership relationship stage. Besides, more products and services can be cross-sold to the same clients. Corporate clients, on the other hand, gain access to more products at favorable terms. HDFC Bank often prices its products based on the relationship with the customers. The more longstanding and trustworthy the relationship, the better the pricing.
- When faced with contingencies, a client, who has a partnership relationship with a bank, is able to leverage on this relationship to get instant credit without losing time in procedural hassles.

THE PRODUCT MIX

Banking products can be broadly categorized into fund-based products and fee-based products. Fund-based products are further classified into asset products and liability products. Asset products are credit products, wherein the bank lends money to its customers. In corporate banking, asset products include financing the purchase of equipment or the construction of a production facility or office buildings, working capital loans, long-term loans, bill discounting facility, etc. Liability products include the various accounts and deposits that a corporate customer maintains with the bank. Table 4.2 lists the various liability products and asset products in corporate banking. (Fee-based products are discussed in detail in Chapter 11. Corporate credit cards are discussed in Chapter 6.)

Table 4.2: Liability and Asset Products in Corporate Banking

<table>
<tr><th>Product Category</th><th>Products</th><th>Details, if any</th></tr>
<tr><td rowspan="4">Liability Products</td><td>Salary accounts</td><td></td></tr>
<tr><td>Current accounts</td><td>Roaming current account
Escrow current account
Customized current account</td></tr>
<tr><td>Fixed deposits</td><td></td></tr>
<tr><td>Payment cards</td><td></td></tr>
<tr><td colspan="3"></td></tr>
<tr><td rowspan="3">Asset Products</td><td>Trade finance</td><td>Export finance
Import finance</td></tr>
<tr><td>Corporate finance</td><td>Working capital finance
Structured products
• Dealer financing
• Vendor financing
• Long-term financing
• Brand financing
• Transporter financing
• Securitization</td></tr>
<tr><td>Project finance and term loans</td><td>Project-specific loans
Long-term loans
Medium-term loans</td></tr>
</table>

Compiled from various sources

Liability Products

Liability products are those products that are a liability to the bank as the bank has to maintain the funds of corporate clients and pay interest on them. Banks utilize these funds in other options for revenue generation. Salary account products, current account products, fixed deposits, and payment cards are the important categories of liability products.

Salary account products

Banks offer salary accounts to employees of organizations. The organization can disburse the salary directly into these accounts; the employees need not be paid in cash. The more the number of salary accounts, the more the volumes of cash that are transacted. Often, banks do not charge anything for these accounts and also waive the minimum balance criteria. Instead, they benefit from their access to the idle funds in such accounts. Salary account products are marketed as corporate banking products to employers, and they create further opportunities for cross-selling retail products like credit cards to the employees.

These accounts also act as savings accounts for the employees. For example, HDFC Bank has a corporate salary account that offers various facilities to the end consumers, that is, the employees. The facilities include net banking, phone banking, mobile banking, and an international debit card which is valid in about 140 countries. These facilities are offered free of cost to the users. The bank also facilitates payment of utility bills through these accounts.

Current account products

A current account basically offers the facility of conducting multiple transactions in a single day. Most companies, institutions, professional agencies, small business enterprises, etc., open a current account with one or more banks. In this product, the bank does not pay any interest on the outstanding balance. The common benefits offered on current accounts include overdraft facility, no restrictions on issue of chequebooks, Internet banking and funds transfer, etc. There are different types of current accounts. They are roaming current account, escrow current account, and customized current account.

Roaming current account: A roaming current account allows the customers to access, operate, and conduct transactions across different branches of the bank across the country. For example, ICICI Bank customers can access their roaming current accounts in as many as 500 branches across the country. This is especially useful for organizations that have geographically distributed operations.

Escrow account: An escrow current account is a current account without the facility of issuing cheques. Organizations open escrow accounts when they enter into contracts with other parties. The funds deposited by the organization are lodged in the safe custody of the bank in order to meet certain contingencies. The escrow account acts as either guarantee or safety against the non-fulfillment of the obligations agreed to by the organization, as part of a contract. The escrow account also serves as a mode of deferred payment in conditions where the total amount is paid to the other party (to the contract) in installments, subject to certain pre-defined criteria being met.

Let us consider the use of the escrow account in a mergers & acquisitions (M&A) situation. Jet Airways[3] intended to acquire Air Sahara[4] for a total financial consideration of Rs. 20 billion; the deal was announced in January 2006. The first part of the payment -- Rs. 5 billion, was paid in advance to the shareholders of Air Sahara. The remaining Rs. 15 billion was to be paid after completing the due diligence exercise to validate the financial soundness of Air Sahara, and after obtaining the necessary regulatory approvals. Jet Airways deposited this amount of Rs. 15 billion in an escrow account with ICICI Bank. Later, when the deal fell through, Jet Airways filed an appeal in the Mumbai High Court to be allowed to withdraw the money from the escrow account. It was allowed to withdraw the amount, after it submitted a bank guarantee for Rs. 15 billion.

Customized current account: A customized current account offers special features and tailor-made services to the corporates that hold such accounts. A normal current account demands a minimum quarterly average balance to be maintained, while a customized current account does not mandate such a clause. The other options offered under this facility are anywhere banking, multi-city cheque facility, pay orders and demand drafts, debit/ATM cards, Internet and phone banking, etc.

Fixed deposits

Banks accept fixed deposits from corporate customers, subject to certain conditions. For example, the minimum amount deposited may be Rs.10,000; the minimum period may be six months; etc. The interest accrued on these deposits is either credited to the organization's current account or credited to the fixed deposit account at the time of maturity.

Payment cards

A payment card is used by corporates to make payments to their business partners. For instance, a business may use these cards to make payments to its supply chain partners like vendors and distributors. Thus, payment cards are operated within a closed group that should be pre-specified by the customer. A payment card helps businesses avoid the problems associated with cash payments.

Asset Products

Asset products, which are the primary revenue earners for many banks, include all types of loans and advances that a bank gives to its customers. The basket of asset products offered to a corporate customer depends on the stage in which the customer's relationship with the bank is. A company with a long-term relationship with a bank may enjoy access to more asset products than a company in the early stage of relationship with the bank. The pricing of the asset products often depends on the stage of relationship.

Asset products can be broadly classified into trade finance, corporate finance, and project finance related products. These products are used by corporate customers based on their needs at different stages of their business -- such as project finance for long-term projects involving significant capital investments, working capital loans to meet the liquidity requirements of ongoing operations, trade finance for meeting import/export requirements, etc.

Trade finance

Trade finance products help corporates finance their export and import needs. These products are broadly classified into export finance products and import finance products. Export finance provides pre-shipment finance (helps in procuring raw materials and equipment) and post-shipment finance (purchase of export bills, advances against exports on consignment basis, etc.). Similarly, import finance products help organizations meet the financial requirements of importing goods and services, such as advances against the product being imported. Export finance and import finance also involve some fee-based services, such as forfeiting, letter of credit, guarantees, etc., which are discussed in detail in Chapter 11: Fee-based Services.

Corporate finance

The products offered by banks under corporate finance can be divided into working capital products and structured products. Working capital products include both fund-based and non-fund based products. Fund-based products include cash credit, short term loans payable on demand, and other working capital loans. Non-fund based products include documentary credit and bank guarantees.

Structured products are those products that are specially designed for some needs that cannot be met through other loan products. Structured financing includes loans given on the performance of certain assets owned by the company or the business partners of the company. Dealer financing, vendor financing, transporter financing, long-term financing, and brand financing are examples of structured products. For instance, a company can get a loan by leveraging on its brand equity. Or it can use a loan to buy a brand from another company. The brand would be mortgaged to the bank, till the loan is repaid. Thus, the brand acts as the security for this type of loan. Also, the dealers and vendors of the company can be granted loans based on their relationships with the company. Securitization[5] is a special type of structured product offering. Thus, structured products reflect the customization and discretion adopted by the banks in meeting the fund requirements of corporates.

Project finance and term loans

Project financing is characterized by large value loans to corporates, where either the whole or a part of the project is financed by a bank or a specialized financial institution. In some cases, a consortium of financial institutions may come together to share the risk when giving such loans. The value of one such loan may be more than Rs. 1 billion. These time-bound projects could be infrastructural or commercial. For instance, the State Bank of India (SBI) provides project finance to both infrastructural projects and commercial projects. Banks also provide long-term loans and medium-term loans to corporates to meet their fund flow requirements.

NEW PRODUCT DEVELOPMENT & INNOVATION

With growing competition, corporate customers' expectations from banks have increased; marketers are under pressure to come out with new products in order to increase revenues as well as to retain existing customers. True innovations in products are not as frequent in the banking industry as in consumer goods. Often, a new product is developed by modifying an existing product. New products may be either existing products bundled together or a standard product customized to meet customer requirements. Many of the securitization products are innovations to meet the specific needs of a customer.

However, financial products can be easily copied. Thus, banks cannot hold on to the uniqueness of the new product for a long time. In addition to new product development, banks also innovate in other areas. In this section, we will first discuss new product development and then discuss other innovations in bank marketing.

New Product Development

Planning for new products usually requires a careful analysis of existing products, combined with market research and profitability analysis. But a survey in the US claims that only one in ten banks follow a scientific approach and research-based methods in the new product development process.[6] To avoid product failures, bankers should possess a proper understanding of their customer needs and how customers adopt new products. In this section, we focus on the different types of new products developed by banks and the new product adoption process of the customer.

Categorization of new products

From a bank marketer's perspective, a new product can fall into different categories. In the first case, an entirely new product is developed, that is, the product has been developed for the first time. This is a rare phenomenon in the banking industry. The launching of the first credit card is such an instance. In the second case, the bank develops a product which already exists in the market. That is, it can make additions and modifications to its product mix. These new products could help the bank address newer target segments and/or provide cross-selling opportunities to generate more revenue from its existing customer base. For example, a bank that has been offering only trade finance, project loans and term loans, may start offering structured products like dealer financing, financing for transportation fleet, etc. In the third scenario, a bank may reposition its existing product portfolio to cater to a different, under-served market segment. Marketers need to educate the customers in the new segment about the benefits of the product. For example, Indian banks are promoting their product portfolio to the SME sector, with the required changes in terms of product features to meet the needs of this segment.

New product adoption

New product adoption can be defined as the customer's ability and willingness to change over to the new product. The new product adoption process starts with the customer's interest in the product, leading to a search for additional information on the product. The customer then evaluates the product by comparing it with existing alternatives and makes a decision on whether or not to purchase it. Let us consider the case of a corporate which wants to relaunch a brand with a new brand image. This may require significant financial investment, in addition to time and effort. The customer may be evaluating different options for financing this investment. At that time, the customer may come to know about a new structured product -- brand financing, where brand image can leveraged for a loan -- offered by the banker. This first stimulates interest in the customer who approaches the banker to get more information about the product. Once the information has been collected, the customer evaluates the product and compares it with the other potential funding sources available for this exercise. The customer may then opt for the brand financing product if it is felt that this structured product will benefit the organization.

Other Innovations in Bank Marketing

Increasing competition through the entry of private players has increased the pace of development of new banking products. In effect, this has increased the choice available to corporates. Even as banks keep developing newer product offerings, they are aware that these innovations may be quickly copied by the competition. So, banks provide customized service along with the product offerings. The competence and responsiveness of the people involved, and the quality and delivery of service are differentiators that competitors may find difficult to copy. Non-product innovations in the banking scenario, whether it is corporate banking or retail banking, can be categorized into four types. They are innovations in operations, media, pricing, and delivery. See Table 4.3 for details.

Table 4.3: Innovations in Bank Marketing

Type of Innovation	Examples
Operations innovation	Digitization of documents Use of CRM software applications
Media innovation	Use of the Internet as a promotional medium
Pricing innovation	Discounted pricing for bundled products, for e.g., equipment financing combined with insurance cover
Delivery innovation	Electronic fund transfer Electronic data interchange Web-based banking

Compiled from various sources

PRICING

The pricing of banking products directly impacts customer retention and customer acquisition, in addition to profitability and long-term viability. Pricing of financial products can be in terms of interest rate for a working capital loan, opening fee for a current account, penalty for not maintaining the required minimum balance in the current account, etc. On each occasion, it is viewed with different perceptions by marketers and customers. Let us first understand the different perceptions on pricing and then discuss the factors influencing pricing in corporate banking.

Marketers perceive pricing as a mechanism used to cover all the costs incurred on rendering a service. This includes production costs, distribution costs, promotion costs, and other operational expenses. Costs can also be categorized into fixed costs and variable costs. Fixed costs involve establishment costs and variable costs involve cost of funds and operational expenses. For marketers, price is an important determinant of profits and long-term survival. Also, pricing is a very useful mechanism which can be used to quickly counter the competitors' offensive strategies. As prices can usually be reduced at short notice whereas changes in product mix strategies, promotional strategies, and distribution strategies take more time to implement. For instance, with growing competition in corporate banking, banks may reduce their interest rates or waive penalties to attract more customers.

On the other hand, customers perceive price as a cost. Cost to the customer represents both explicit costs and hidden costs. For customers, price is also a part of price-value equation. Value in this context represents the worthiness of the product that is assessed (though it is difficult to assess for financial products) based on product attributes and quality of service. Customers always attempt to benefit from their price-quality trade off. Corporate decision makers, especially, consider price as a negotiation variable to maximize the net value to their organization. They command more buying power compared to retail buyers and use this power to negotiate with the banks to reduce prices and achieve better product deals.

Pricing Factors

Having understood the perceptions of marketers and customers on pricing, we now look into the factors that influence the marketer's pricing of financial products. Pricing done without considering any of these factors may lead to underperformance of the product in the market. Primarily, there are four factors that banks consider in pricing their products. They are cost, competition, customers, and constraints. Let us now discuss them in detail.

Cost

Cost involves the fixed costs and variable costs included in developing and delivering the product offering. Fixed costs include establishment costs (buildings, communication networks, investments in software, etc.) For asset products, a very important component of variable costs is the cost of acquiring funds from various sources. In addition, banks also consider the risk involved in lending to a specific corporate customer and factor it in as a part of the cost. To arrive at the final cost, banks adopt techniques like cost-benefit analysis and activity-based costing[7], coupled with customer analysis. Cost plus pricing is one type of pricing strategy that bank marketers adopt to price the various products.

Competition

With respect to competition, corporate bankers can adopt three types of pricing strategies -- price skimming, price penetration, and price parity. Price skimming is adopted when the competition does not have offerings that are comparable to that of the marketer. This may occur when the marketer offers products with added features and high levels of customer service, or when the products are customized to suit to the corporate customer's requirements. Bank marketers often adopt price skimming for high value products like roaming current accounts and customized current accounts.

Penetration pricing is adopted when the bank places very high emphasis on achieving a rapid growth in the market share or on eliminating competition. Here, the banking products are priced below that of the competition. Most corporate loans are priced in this manner, due to competitive pressures and the bargaining power of the corporate clients. On the other hand, price parity is used when the marketer feels that there are fewer options for gaining competitive advantage through product differentiation and that penetration pricing may eat into the profits without a significant increase in market share.

Customers

It is ultimately the customer who pays the price of the products. Thus, banks should assess the bargaining power of the customer and the maximum amount that the customer would be willing to pay for a product. A company with a very good credit rating may bargain for a much lower price, while a start-up company in a high-risk business may be willing to pay a higher price for the same product. A priority sector customer -- such as a small-scale industry or a microfinance institution -- would expect to pay a lower price than a large corporate. Customers may also be ready to pay a higher interest rate for loans that have a longer maturity period.

The price that is a customer is willing to pay depends not only on the attributes of the customer (bargaining power, credit rating, priority sector classification) but also on the perceptions about the marketer and the product offering. A corporate may be willing to pay a premium for products from a bank with good brand equity and a reputation for service quality. Also, customers may be willing to pay more for value-added services, if they believe that the bank is providing value for money.

Constraints

Constraints refer to those factors that affect the pricing of bank products and are normally not within the bank's control. They include RBI stipulations/regulations and government policies. The RBI's regulations especially influence the pricing of banking products. In recent years, the RBI has deregulated the pricing norms on deposits, while it still regulates the pricing of loans and advances. We will discuss this phenomenon in detail, with respect to liability products and asset products.

Pricing of liability products: Till 1992, the RBI was the sole authority for setting prices for both asset and liability products. But in 1992, it partly deregulated the pricing of liability products by restricting its role to setting the maximum rate of interest for these products. In 1997, the RBI withdrew completely from regulating the pricing of fixed and recurring deposits and banks were given full freedom to act on their own accord. (As of December 2006, the RBI still holds the authority in setting the maximum interest rate for savings bank accounts.)

Pricing of asset products: Pricing of asset products in India is based on Benchmark Prime Lending Rate (BPLR). BPLR is the yardstick for setting the interest rates for a bank's asset products. Before deregulation, the RBI used to decide the BPLR. After deregulation, every bank in India has to set its own BPLR and price the asset products based on this rate. BPLR is calculated based on the weighted average cost of funds, average cost of operations (also called operating expenses), and a minimum mark-up as profit margin. This calculated rate is the standard for fixing the prices of all the asset products of the bank.

Bank marketers have the flexibility of setting the prices either below or above the BPLR. This is called interest rate spread. That is, the bank can fix its prices for various asset products within this spread. The interest rate spread varies according to the credit rating of the client and the tenure of the asset product.

Let us consider the case of Bank of Baroda. With effect from May 01, 2006, Bank of Baroda had set its BPLR at 11 percent per annum. Later, this was increased to 11.5 percent per annum, with effect from August 01, 2006. Table 4.4 illustrates the respective interest rate spreads (as of December 2006) for corporate loans given by Bank of Baroda, corresponding to different credit ratings and maturity periods.

Table 4.4: Corporate Lending Rates at Bank of Baroda - December 2006

Credit Rating of the Client	Applicable spread (%) over BPLR		
	Maturity up to 180 days	Maturity of over 180 days and less than 1 year	Maturity of over 1 year
AAA	-0.50	0.00	0.75
AA	0.00	0.50	1.25
A	1.00	1.50	2.25
BBB	1.50	2.00	2.75
BB	2.00	2.50	3.25
B	2.50	3.00	3.75
C	2.50	3.00	3.75
D	2.50	3.00	3.75

Source: www.bankofbaroda.com/int_adv.asp (Last accessed on December 15, 2006)

Banks may revise their BPLR with changes in macro-economic factors such as inflation. For instance, due to the liquidity crunch in the banking system (refer to Exhibit 4.2) since late 2005, ICICI Bank revised its BPLR three times between January and March 2006, and raised it up from 11 percent to 12.75 percent. The increase in BPLR resulted in an increase in the interest rates of corporate loans.

Exhibit 4.2

Liquidity Crunch in the Mid-2000s

The Indian banking system experienced a soft interest rate regime from 2003 to 2005. Interest rates for bank credit decreased drastically and this trend continued until late 2005. This was mainly due to the excess liquidity in the markets and the availability of cheap funds to banks. So banks reduced their lending rates to both corporate and retail borrowers. Lower interest rates prompted more credit disbursement in the financial years 2003-04 and 2004-05. However, banks were unable to mobilize more funds through deposits. This eventually led to the draining off of available funds by mid-2005. Around that time, the RBI began to take measures to stop excess credit disbursements by increasing the interest rates for lending to banks.

Many banks also felt the liquidity crunch, but did not attempt to take measures till the end of 2005. In January 2006, ICICI Bank revised its BPLR upward, from 11 percent to 11.25 percent. Other banks in the private sector followed suit. By March 2006, ICICI Bank had revised its BPLR three times to 12.75 percent. Public sector banks initially maintained status quo but by April 2006, they too began to raise their BPLRs in response to the liquidity crunch. According to MBN Rao, the Chairman of Canara Bank, "The excess liquidity in the system has already been absorbed. The cost of funds is growing and there is an upward bias in lending rates. The loans and advances extended at rates below the prime lending rates will see a 100 basis point rise in interest rates."

The rise in the interest rates had a direct impact on the corporate lending rates, which shot up by at least 100 basis points, that is, by 1 percent. With this hike in the interest rates, the corporate sector began to bear the brunt of this development, as a majority of their borrowings were from public sector banks.

Adapted from BS Banking Bureau. "Corporate Loan Rates Above 10%." www.rediff.com. May 01, 2006.

Sometimes, corporate bankers may deviate from the just mentioned model of pricing loans as BPLR +/- spread (based on the client's credit rating and loan maturity period). This is especially true when the bank has a close partnership-relationship with a client and wishes to give it a favorable pricing, as compared to other customers who have the same credit ratings and similar maturity requirements

PROMOTION

A promotional campaign is a planned series of tactics used to promote products and ensure they are well positioned in the minds of the customers. In general, advertising, sales promotions, public relations, personal selling, and direct marketing are the commonly used tools for promoting products and services. In corporate banking, personal selling is the primary component of the promotional mix. This is due to the importance given to relationship building with the corporate customers. The other components are used on a need basis. In this section, we look at each of these tools of promotion and how corporate bankers make use of them.

Personal Selling

Personal selling is a mode of personal communication where bank marketers use personal selling teams to inform customers about their products in order to persuade them to purchase these products. Personal selling is used more intensively in corporate banking than in retail banking. Corporate banking is characterized by relationship building and hence banks use dedicated personal selling teams/relationship officers to perform personal selling activities. A major advantage of personal selling is that it is an ongoing two-way interaction. Such interactions help the marketer to clearly understand the current needs of the customer, and also to anticipate future needs. The marketer can make use of these insights to tailor the products to the customer's requirement. Such a responsive approach further strengthens the relationship with the client.

Personal selling is not just a component of the promotional mix; it is also a component of the distribution mix through which the bank delivers its services to its corporate customers. The disadvantage of personal selling is that it is the costliest form of promotion. The salaries paid to the sales force and relationship managers, and the expenses incurred per client are huge. This disadvantage is offset by the volume of business generated from the corporate clients, due to repeat sales and cross-selling. In the long run, a relationship with a client can prove to be much more profitable than the costs incurred in the short run on building the relationship. To reduce the overall costs of acquiring new customers, banks may use direct-response advertising or telemarketing to identify high-potential leads.

Advertising

Advertising is defined as any paid, non-personal communication that is aimed at publicizing the product or brand. Marketers use advertising to simultaneously reach out to a large audience. When markets are spread out over vast geographies, or when the customers in the market are scattered, advertising comes in handy as a cost-effective tool to reach out to the masses. The common modes of advertising are newspapers, magazines, journals, etc., under the print media and television, radio, and the Internet under the electronic media.

Corporate bankers use advertising when a new product is launched or a new service is introduced. For example, SBI launched a series of advertisements in 2006, for its corporate Internet banking initiative (For more details, see Exhibit 4.4, later on in this chapter). To highlight the advantages of offering services through Internet banking, SBI released a series of print advertisements. The advertisements used humorous, attention-catching visuals of professionals relaxing in the office in different ways. The visuals were accompanied by the caption: "Suddenly, you have all the time in the world with State Bank Corporate Internet Banking."[8]

Public Relations

According to Pezzullo[9], "public relations (in banking) are a communications intensive activity with special emphasis on the securing of favorable publicity for the bank." Advertising and sales promotions differ from public relations in that they are used to motivate customers to make purchases while public relations is used primarily for disseminating information and building a positive brand image. Public relations focuses on providing publicity to the bank, improving its public image, and overcoming any negative image it may have.

The tools used for public relations include press releases, annual reports, seminars and speeches, cause-related marketing, in-house magazines & newsletters, corporate social responsibility (CSR) initiatives, event sponsorships, etc. For instance, banks use seminars to target specific customer groups. They can sponsor business-related seminars on value added tax (VAT) to merchants and business enterprises, including SMEs. To reach out to corporate customers, banks often sponsor technical conferences. Corporate representatives are invited to be guest speakers, panelists, or delegates. In addition, banks also sponsor/co-sponsor different non-technical events to gain publicity.

CSR initiatives help banks to gain greater visibility among the target segment at a lower cost. In this process, banks are also able to satisfy other stakeholders such as the government and non-governmental organizations. See Exhibit 4.3 to understand HSBC's philosophy of using CSR as an integral part of its business strategy.

Exhibit 4.3

Corporate Social Responsibility (CSR) Initiatives at HSBC

The HSBC Group (HSBC) provides a full range of personal financial services, consumer finance, private banking, commercial banking for small and medium enterprises, corporate & institutional banking, investment banking, and transaction banking to customers across the globe. As of 2005, the group employed about 232,000 employees in 76 countries.

HSBC saw CSR as a way to build on its reputation of being a financial institution that cared for its customers, society, and the environment. As a good reputation is an important element in brand management for a financial institution, CSR was viewed as complementary to the nature of business at the bank. HSBC used the CSR initiatives to enhance its brand image globally. It took up a number of initiatives to address the needs of the poor and the disabled in developing and under-developed countries around the world. This was in line with its positioning of being 'the world's local bank'. Also, by implementing CSR initiatives, HSBC was able to instill a sense of purpose in the day-to-day activities of its employees.

HSBC incorporated CSR initiatives into the strategic plan of the group and made efforts to translate them into action across the organization. The top management set up a CSR Committee that was responsible for implementing the CSR initiatives and reporting the progress directly to the Board. The group also focused on upgrading the reporting system for data that would help track the progress of CSR initiatives.

CSR initiatives in HSBC began as early as in 1992 when it signed the UN Environment Program Statement by Financial Institutions, on Environment and Sustainable Development. It published its first Environmental Policy in 1997, and the Statement of Business Principles and Values in 1998. Later, HSBC started regularly reporting its progress in CSR activities through yearly CSR reports.

Following are some of the CSR initiatives of HSBC.

- It funded schoolbooks, classroom equipment, fees, clothing, etc. to disabled school children in India, Malaysia, and Bangladesh.
- '*Coral infantil HSBC'* was launched in 2002 in Brazil under which 850 children were taken care of by eight charities. The children were given help in staging 15 performances during the year concluding in a grand Christmas show.
- An exhibition of 130 paintings and handicrafts by disadvantaged children was funded by The Hong Kong Bank Foundation in 2003 in Beijing, China.
- The group built up goodwill among the local communities through a partnership with local not-for-profit organizations to implement various community development and environmental management programs

Apart from these initiatives, the company also took steps to optimize energy usage and water consumption in the organization. Besides, it went on to reduce greenhouse gas emissions and waste in all of its business entities. HSBC announced its commitment to go carbon neutral by implementing efficiency improvement measures, trading carbon credits, and tree planting around the world. The listing of HSBC on the Dow Jones Sustainability Index (DJSI) and on the FTSE4 Good Ethical index also helped improve the group's image as being serious in its commitment to walk the talk on CSR issues.

Adapted from Fernando, Rajiv. "Case Study: CSR Initiatives at HSBC: Making Good Business Sense." The Icfai Center for Management Research (www.icmrindia.org), 2005.

Sales Promotion

The aim of using sales promotions targeted at customers is to encourage them to use the product where some incentive is given for buying/using it. . Sales promotions are basically used to attract more customers. Till the early 1990s, banks used to give premiums and gifts to customers as a token of thanks for doing business with them. Since deregulation, banks have had the liberty to differentiate themselves through interest rates and thus the use of premiums and gifts has decreased.

Further, internal promotions are actively undertaken by bank marketers to promote their products. They include incentives and promotions to the employees of the banks. The more products they sell/cross-sell, the more incentives they get. Performance-linked bonuses are also commonly used to motivate employees to achieve targets in corporate banking.

DISTRIBUTION

In India, the dynamics of distribution of banking products has drastically changed since the 1990s. Technology brought in a mini-revolution in the form of electronic funds transfer (EFT) and electronic data interchange (EDI). With the nationwide development of telecommunication infrastructure, ATMs were introduced. And when the Internet came to the forefront of business, it gave a new definition to the concept of distribution in the banking sector.

Process improvements in distribution and service delivery have been enabled by technology developments and applications. Banks welcomed the technology-related changes and vied with each other to implement them first. Different banks are in different stages of implementing integrated banking software applications, known as Core Banking Solutions (CBS).[10] CBS implementation helps in real-time synchronization/integration of the transactions that happen through different modes of distribution. For more details on CBS, refer to Chapter 12.

Any bank that wants to develop multiple distribution channels has to view it from a strategic perspective. Every bank should develop an optimum distribution mix to deliver superior customer service to customers and to ensure operational efficiency and profitability. In corporate banking, branch banking and direct sales force are the primary modes of distribution, supplemented by Internet banking and phone banking. Let us now discuss each of these channels.

Bank Branches and Direct Sales Force

Bank branches are still considered the most important channel of distribution. Due to the personal contact element, branch banking and direct sales force help in shaping customer relationships and converting them into clients of the bank. Corporate bankers have traditionally used branches both for developing relationships and delivering service/advice to the clients. The corporate banking activity of banks is usually intense in branches situated in the vicinity of the corporate/regional headquarters of the client.

Banks generally appoint different teams (usually one team for each industry vertical) where relationship officers take charge of developing relationships with each corporate client. These teams are based at different branches; the team members make frequent visits to client offices to nurture the relationship and develop new business opportunities.

Internet Banking and Phone Banking

Internet banking has an edge over other channels in many ways. This technology driven channel is used to perform basic operations like money transfers, viewing the account balance, etc. See Exhibit 4.4 for details of SBI's corporate Internet banking initiative. The challenge in Internet banking is to prevent security breaches, which can lead to leakage of sensitive data or to financial frauds. Phone banking is another non-personal channel of distribution. Corporate customers use this channel to perform basic operations like enquiries.

Exhibit 4.4

SBI's Corporate Internet Banking

SBI has made use of the Internet banking initiative to offer corporate banking services targeted at specific customer groups. SBI introduced three types of services -- Advantage, Privilege, and Freedom -- that were targeted at small firms and institutions; small and medium business enterprises; and large/very large firms respectively.

Advantage (Khata): Advantage is targeted at small firms, companies, and institutions. Authorized users have the right to access complete information related to the company's account. One can access all the account information from any branch within a set of selected branches over the Internet 24 hours a day.

Privilege (Vyapar): Under this service, corporate customers can use the Internet banking facility to carry out transactions like funds transfer, third party payments, ordering drafts, etc. The service offers businesses the benefit of individual transactions of up to Rs.500,000. It also provides a closed user group with limited access, where authorized employees can also make transactions. This service is mainly targeted at SMEs.

Freedom (Vistaar): Targeted at large and very large corporations who have a wide geographical spread, this facility brings in flexible Internet banking. The management can access information on accounts at multiple branches and make transactions like funds transfer, third party payments, taking drafts, etc. This facility also enables customers of the company to make payments through the Internet. For example, businesses can use this service to collect pending bills from customers. It also acts as a control mechanism for the top management of the company as it has access and control pertaining to the financial information of subsidiaries and divisions. Another benefit offered is online auditing. The auditors of the company are provided the facility of auditing the company's financial position online.

Source: www.onlinesbi.com/corporate.

THE SME SEGMENT

In India, the category of small and medium business enterprises (SMEs) is one of the fastest growing sectors, both in manufacturing and in services. According to classification norms, small- scale industries are those whose capital investment in plant, building, machinery, etc. does not exceed Rs.10 million. The cap is raised to Rs. 50 million in the case of certain sectors such as drugs and pharmaceuticals. Medium enterprises have capital investments ranging from Rs. 10 million to Rs. 100 million.[11] The SME sector is considered as the growth engine of the economy and a prime source of employment in the country. India has around 3 million SMEs operating in various industries and providing employment to about 30 million people. SMEs contribute about 30 percent to the nation's GDP.[12] Marketing to SMEs is no longer considered by corporate bankers as just a social responsibility; it is also an integral part of their business strategy. However, it was the Oriental Bank of Commerce (OBC) that had its focus on this sector even before other banks shifted their focus to it.

Factors Influencing Bank Lending to SMEs

Though SMEs have been a major source of employment and economic output, they were one of the most neglected market segments in terms of bank lending. Banks preferred to lend only to small businesses in certain sectors like bulk drugs, knitwear, auto ancillaries, textiles, etc. and avoided SMEs like gems and jewelry, sea food processing, sport goods, etc. This was despite the fact that the Indian government had classified the small-scale industries sector in the priority lending segment. Earlier, the Deposit Insurance and Credit Guarantee Corporation (DICGC) provided guarantees to the credit given to SSIs. In case of repayment failure by the SSI, DICGC would repay the amount to the bank. However in 1991, certain categories of priority sector advances which are guaranteed by the State/Central Governments, Export Credit Guarantee Corporation (ECGC), etc. were excluded from the scope of DICGC. Further, when modifications were made to the terms and conditions of the credit guarantee scheme in 1995, all the banks opted out of the scheme. Since then, DICGC has not been operating the credit guarantee scheme. The trend in lending by public sector, private sector, and foreign banks to the SME sector from 2002 to 2004 -- in terms of share of Net Bank Credit (NBC) -- is given in Table 4.5.

Table 4.5: Bank Credit to Small Scale Industries: 2002 - 2004

Bank	2002		2003		2004	
	Amount (Rs. billion)	**% Share of NBC**	**Amount (Rs. billion)**	**% Share of NBC**	**Amount (Rs. billion)**	**% Share of NBC**
Public Sector Banks	497.43	12.5	529.88	11.1	582.78	10.4
Indian Private Banks	86.13	13.7	68.57	8.2	78.97	7.1
Foreign Banks	45.61	12.0	38.09	8.7	54.38	10.4
Total	**629.17**	**11.8**	**636.54**	**10.3**	**716.13**	**9.4**

NBC = Net Bank Credit (Amounts indicated reflect the net outstanding amount borrowed by Small Scale Industries, as on March 31 of the respective year)

Source: Bhasin, T.M. "SME Financing – The Next Big Business Opportunity." <u>*IBA Bulletin.*</u> *December 2005, p.7-10.*

The major reasons for Indian banks considering financing to the SME sector as highly risky business are insufficient credit information, inadequate credit appraisal, poor risk management, poor repayment records, limited market power, high share of intangible assets, absence of adequate accounting track records, low market credibility, vulnerability to market fluctuations, and high mortality rate. Non-performing assets (NPAs) in the SME sector are quite high at around 17 percent to 18 percent.[13] Alan Hughes and Cosh in their 1994 study "Financing Small Firms[14]", characterized the SMEs in financial terms as follows:

- They have lower fixed to total asset ratios.
- They have high debt-equity ratios.
- They have a much higher proportion of current liabilities to their total assets.
- They rely heavily on retained profits rather than external funding
- Of the external sources, they rely heavily on banks for credit assistance
- They are financially more risky due to high debt-equity ratios and high failures in repayments.

The Changing Scenario

There has been a marked shift in the bank marketer's approach to SMEs. One of the primary reasons was liberalization. After liberalization, large corporations gained access to various sources of credit, other than banks, to fund their financing needs. Till then, the profitability of a bank depended heavily on the loans given to large corporations. When large corporations reduced their dependence on banks as a source of funds, it resulted in banks shifting their focus toward the SME sector. Many banks have come out with innovative products that suit the needs of this sector. They have also reduced their lending rates by as much as 100 basis points.

In order to help banks to cope with credit rating and other factors that act as obstacles in SME financing, the Government of India has introduced a new policy authorizing the public sector banks to fix their own targets to fund the SME sector, provided they achieved at least 20 percent growth, year on year, in funding the SMEs. The National Small Industries Corporation (NSIC) has also developed a credit rating mechanism for the SME sector. Leading credit rating agencies like CRISIL[15], ICRA[16], Dun and Bradstreet[17], and Onicra[18] have agreed to perform credit rating for this sector through NSIC. Further, the RBI has also come out with guidelines for a one-time settlement of the SSI-related NPAs, subject to certain conditions.

SUMMARY

The marketing of bank products to corporate customers is discussed in the chapter. On the basis of sales volume and/or capital employed, banks may classify corporate customers into three segments – large corporations, mid-size companies, and small and medium business enterprises (SMEs). Corporate customers may also be segmented into industry verticals, such as automobiles, aviation, tourism, etc.

As part of their marketing efforts, banks develop long-term relationships with their corporate customers. Strong relationships help the banks improve profitability and retain customers in a competitive market. The interactions and relationships between the banks and their corporate customers are influenced by three groups of factors – the external environment, the atmosphere of the interactions, and the interaction process. The 'Partnership Relationship Lifecycle Model' describes the evolution of the bank-corporate customer relationship, beginning at an early stage where a 'customer' shows interest in the bank's offerings, and maturing to become a mutually beneficial 'partnership relationship' between the 'client' and the bank.

Banking products are broadly classified into fund-based products and fee-based services. Fund-based products are further sub-divided into asset products and liability products. Liability products include salary accounts, current accounts, fixed deposits, and payment cards. Asset products include various kinds of credit products like trade finance, corporate finance, project finance, and term loans. New product development and innovation are considered vital for a bank's long term sustainability. Banks need to address the changing requirements of their clients through new product development. However, financial products can be easily copied. To maintain differentiation, banks also need to come up with innovations on how they deliver the new product.

The pricing of banking products directly impacts customer retention and customer acquisition, in addition to profitability and long-term viability. For the marketer, price is a mechanism to cover the costs of operations which include production costs, distribution costs, promotion costs, and other operational expenses. The pricing decision is influenced by cost, competition, customers, and other constraints. With the advent of deregulation and the consequent increase in competition, many of the banks have adopted a competitive pricing strategy. RBI has deregulated the pricing mechanism for both asset and liability products. Every bank has to set its own Benchmark Prime Lending Rate (BPLR) to price its asset products. A bank may price its asset products (for a given customer either above or below the BPLR, depending on situational factors such as creditworthiness of the customer, stage of relationship, etc.

Personal selling is the most important component of the promotional mix for corporate banking. As personal selling is a two-way interaction, it also plays an important role in the service delivery. To reduce the overall cost of personal selling, banks may use direct-response advertising or telemarketing to identify high potential customers, who are then approached through the personal selling option. Advertising is used to reach out to a vast audience in a cost-effective manner, as at the time of introducing a new product or service. Public Relations (PR) is used to provide publicity to the bank, to improve its public image, and to overcome a negative image (if any). PR tools include press releases, annual reports, seminars and speeches, cause-related marketing, in-house magazines & newsletters, corporate social responsibility (CSR) initiatives, and event sponsorships. As part of sales promotion, banks give employees incentives to achieve business targets such as volume of new business, extent of cross-selling, etc. Customer promotions (such as gifts) are less important as banks can decide the price (interest rate) for customers on a case-to-case basis.

Corporate banking products are distributed mainly through bank branches and a direct sales force, supplemented by phone and Internet banking. Relationship officers are based at different branches; they make frequent client visits to nurture relationships and to develop new business opportunities. Banks attempt to develop an optimal distribution mix using personal/non-personal modes of delivery, in order to achieve multiple objectives such as superior customer service, operational efficiency, and profitability. Integrated banking software applications – usually referred to as Core Banking Solutions (CBS) -- are vital to the real-time synchronization of the transactions that happen through the different modes of distribution.

The small and medium business enterprises (SME) sector is considered as the growth engine of the Indian economy; it generates employment for nearly 30 million people and contributes around 30 percent to the nation's GDP. However, corporate bankers neglected this segment for a long time due to the high incidence of Non-Performing Assets (NPA) and the lack of proper methods to assess the credit rating of the SMEs. This trend is changing and the SME segment is now one of the focus areas of growth for many banks. This shift has been influenced by the policy initiatives introduced by the Government and the RBI in favor of SMEs. With large enterprises getting access to cheaper funds from other channels, their bargaining power has increased with respect to the banks. This situation has also induced corporate bankers to look at SMEs as an avenue for profitable growth.

End Notes:

[1] External Commercial Borrowings (ECBs)

[2] Finance Asia is a Hong Kong-based finance magazine that sponsors awards for excellence in banking.

[3] Jet Airways is India's largest private airline, as of December 2006. It has both domestic and international operations. It has a fleet of more than 50 aircraft, with 300+ daily flights reaching more than 40 destinations. (Source: Company website).

[4] Air Sahara is a part of the multi-million Sahara India Pariwar. Air Sahara began operations on December 3, 1993. With a fleet of 28 aircraft as of December 2006, Air Sahara connected nearly 30 destinations (including 5 international destinations) with more than 125 daily direct flights. (Source: Company website)

[5] Securitization is the process of gathering a group of debt obligations such as mortgages into a pool, and then dividing that pool into portions that can be sold as securities in the secondary market. (Source:www.investordictionary.com)

[6] Albro, Walt. "Developing New Products." Bank Marketing. Vol. 32, Issue 5, May2000.

[7] Activity based costing is a costing method that measures the cost of a product/service, based on the activities performed to produce the product/service.

[8] Print advertisement in the Business Standard.

[9] Pezzullo, Mary Ann. "Marketing Financial Services." American Bankers Association, 1998.

[10] Core Banking Solutions are provided by many software vendors. Some of the popular vendors and their core banking solutions are -- Infosys: Finacle; Tata Consultancy Services: BANCS; 3i Infotech: Kastle and; i-flex: FLEXCUBE.

[11] Bhasin, T.M. "SME Financing – The Next Big Business Opportunity." IBA Bulletin. December 2005, p.7-10.

[12] Patnaik, Santhosh. "SMEs: Challenges and Opportunities." IBA Bulletin. November 2005, p.17-20.

[13] Bhasin, T.M. "SME Financing – The Next Big Business Opportunity." IBA Bulletin. December 2005, p.7-10.

[14] Patnaik, Santhosh. "SMEs: Challenges and Opportunities." IBA Bulletin. November 2005, p.17-20

[15] CRISIL is India's leading ratings, research, risk, and policy advisory company. CRISIL's majority shareholder is Standard and Poor's, a leading global provider of independent credit ratings, indices, risk evaluation, investment research and data. (Source: http://www.crisil.com/about-crisil/about-crisil.htm)

[16] ICRA Limited (Investment Information and Credit Rating Agency of India Limited), an Associate of Moody's Investors Service, was incorporated in 1991 as an independent company. ICRA is a leading provider of investment information and credit rating services in India. (Source: http://icra.in/profile.aspx)

[17] D&B is a leading provider of business-to-business credit, marketing, purchasing, collection services, and decision-support services in India and worldwide. Their offerings include Risk Management Solutions, Sales and Marketing Solutions, Financial Education Solutions, Export Marketing Solutions, and Data Consultancy Solutions among others.

[18] ONICRA Credit Rating Agency of India Ltd. is the pioneer in providing individual credit rating and reporting services in Indian financial markets. Its services include credit rating, associate rating, employee verification, and SSI/SME rating.

Chapter 5

Retail Banking

In this chapter, we will discuss:

- Retail Banking in India
- Types of Retail Banking Products
- New Product Development (NPD)
- Pricing
- Promotion
- Distribution
- Cross-selling

Today, every third dollar in the open and competitive consumer finance market in India is funded by ICICI Bank. To increase its brand recall among retail consumers, ICICI Bank spent nearly 16 times more on advertising and promotion than the State Bank Group. The bank increased its customer base from a mere 100,000 to 14 million in just five years. In 2004-05, ICICI Bank earned $460 million on revenues of $1.4 billion and $39 billion in assets. However, the bank feels there is still a huge potential to be tapped in the retail sector. "Nobody had played the retail game in a big way," says K.V. Kamath, its chairman and managing director.

Adapted from "Big is Beautiful." www.ibef.org. July 22, 2005.

Retail banking in India has come of age and both the public sector banks and the private sector banks across the country have embraced it as a welcome business opportunity, especially with revenues declining in the corporate banking sector due to the availability of other sources of funds like capital markets and External Commercial Borrowings. In addition, excess liquidity in the banking system led to a soft interest rate regime (low interest rates due to the availability of cheap funds) for over three years from 2003 to 2005, further spurring the growth of retail banking in India. The RBI, in its annual performance report for 2004-05, stated that in that year alone, the retail lending by banks rose 41.2% over 2003-04. Industry analysts like Merrill Lynch expected this growth rate to hover around 35% for the next few years[1]. With such a large market potential, many banks are vying for a share in the retail pie by developing marketing strategies to enhance their market shares and improve profitability.

We start this chapter with a discussion on the characteristics of retail banking and the factors that have led to the rapid growth of this segment in the Indian banking scenario. We then move on to discuss different types of retail banking products and the role of new product development in retail banking. This is followed by a detailed description of the pricing, promotion, and distribution aspects in retail banking. Finally, we focus on cross-selling, a technique that has been adopted by most retail bank marketers to sell their products aggressively to existing customers.

RETAIL BANKING IN INDIA

Retail banking in India was primarily restricted to the nationalized banks and a few private banks, till the economy was liberalized in 1991. The basic characteristic of retail banking is to provide banking services that meet the needs and requirements of various individual/retail consumers. Internationally, with the advent of banking technology (ATMs and credit cards that were introduced in the late 1970s and early 1980s respectively), banks began to lay greater emphasis on the retail segment. The retail banking revolution began in the 1980s in the US and Europe with the advent of credit cards. In India, this revolution began in 1995 with the entry of foreign banks and new generation private banks. The introduction of new technologies made it easier for the banks to provide better services to consumers. Before discussing the characteristics of retail banking, let us first take a look at the paradigm shift that took place (from corporate banking to retail banking) in the banking industry during the ten-year period between 1995 and 2005.

The Paradigm Shift

In India, since independence, corporate banking had been the main source of revenue for nationalized banks. But with the onset of economic reforms, foreign banks entered the Indian banking scenario. To differentiate themselves from the domestic banks, they introduced the latest technologies in providing banking services and thus, retail banking began to grow. HSBC was the first bank in India to introduce the concept of the ATM in 1987[2]. Reforms also revolutionized the stock market functioning; many companies started to come out with Initial Public Offers (IPOs). With newer channels to fund financial needs, the corporate sector slowly reduced its dependence on banks. Also, stringent rules on asset classification, income recognition, and provisioning norms had led to mounting NPAs (Non-Performing Assets) in corporate banking[3]. Further, competition had increased in the corporate banking segment and corporate customers were bargaining for credit at favorable interest rates; this led to a fall in profit margins.

Most of the corporate customers were clients of the nationalized banks and private banks had a smaller share of this business. The post-reform period also witnessed the emergence of a new breed of banks – the new generation private sector banks. Thus, the private banks were forced to target the retail segment in marketing their product offerings to boost their revenues and profits. In this way, retail banking gained prominence. Private banks such as ICICI Bank and HDFC Bank were among the few to expand their branch network aggressively to maintain a pan India presence. New technologies like Electronic Data Interchange (EDI), Electronic Funds Transfer (EFT), and the Internet further helped the banks in leveraging on new channels to market their products to the retail consumer.

Non-Banking Financial Companies (NBFCs), which had been competitors to banks for a long time, were weakened by stringent RBI norms in the late 1990s. With RBI restrictions on raising of deposits, the cost of funds increased significantly for the NBFCs. These developments made it difficult for them to sustain themselves in the competition with banks and some of them converted themselves into scheduled commercial banks. Kotak Mahindra, a prominent NBFC, became Kotak Mahindra Bank; Ashok Leyland Finance was merged with IndusInd Bank, a new private sector bank. However, other large and popular NBFCs chose to continue with status quo while many small NBFCs were eventually wiped out in the competition. See Exhibit 5.1 for a brief note on the impact of RBI regulations on the competitiveness of NBFCs.

Another major change in the early 2000s was the foray of banks into microfinance, as part of their financial inclusion initiatives. People below the poverty line are the most neglected segment in terms of banking services. Nearly one-fourth of the people below the poverty line in the world, live in India. Many Non-Governmental Organizations (NGOs) and financial institutions (like Basix, Spandana, Share Microfin, etc.) have made forays into microfinance for uplifting the lives of the people in this segment. With micro-credit as the major product, accompanied by micro-savings and micro-insurance, these organizations have achieved a certain level of coverage and success in this segment. Having realized that the poor are also bankable, and recognizing the huge potential in this segment, banks have also entered into microfinance. SBI and ICICI Bank are the major players among banks, in terms of volume of assets. As of December 2006, nearly 17 million people were being served under microfinance. Microfinance and financial inclusion are further discussed in Chapter 12.

By international standards, however, there is still much scope for growth in retail banking in India. Retail loans constitute 9 percent of GDP in India in comparison to an average of about 32.5 percent for other Asian economies – Korea (64.8 percent), Taiwan (59 percent), Singapore (46.1 percent), Hong Kong (54.2 percent), China (12.0 percent), Malaysia (47.4 percent), and Thailand (23.3 per cent).[4]

Exhibit 5.1

Competitiveness of NBFCs: Impact of RBI Regulations

The RBI Act was amended in January 1997 to bring in policy changes regarding the regulations on NBFCs. Under the new policy, the RBI got more powers to regulate the functioning of NBFCs where it brought into force certain norms that severely affected their functioning.

Source of Funds

The new policy stated that it was mandatory for any NBFC to get a credit rating before it could accept deposits. This was implemented as a means to provide security to the depositors' money. Depositors in NBFCs were mainly retail consumers who had saved up their hard-earned income. Thus, credit rating would provide information on the NBFC's credit-worthiness and the consumers could then make sound decisions based on this information. NBFCs that accepted deposits from the public were subject to stringent scrutiny.

Further, RBI imposed upper limit restrictions on all types of deposits raised by NBFCs. Many NBFCs offered high interest rates on deposits and attracted huge corpuses of funds. However, without proper liability management, they were unable to pay the promised interest rates. Thus, it was felt that a ceiling on the deposits collected would discourage them from making such promises.

Use of Funds

In December 2006, the RBI introduced a new classification of NBFCs, known as Asset Finance Company (NBFC – AFC, or simply, AFC). According to the RBI, "AFC would be defined as any company which is a financial institution carrying on as its principal business the financing of physical assets supporting productive/economic activity, such as automobiles, tractors, lathe machines, generator sets, earth moving and material handling equipments, moving on own power and general purpose industrial machines. Principal business for this purpose is defined as aggregate of financing real/physical assets supporting economic activity and income arising therefrom is not less than 60% of its total assets and total income respectively." The regulations applicable for an AFC would be, to some extent, different from those applicable for Investment Companies (NBFC – IC) or Loan Companies (NBFC – LC). With the new provisions in place, AFCs may be able to compete better with banks.

Adapted from Talwar, S.P. "Regulatory Framework for Non-Banking Financial Companies." www.rbi.org.in. May 30, 1998; and rbidocs.rbi.org.in/rdocs/notification/PDFs/74536.pdf.

Differences between Retail and Corporate Banking

In this section, we will attempt to understand the characteristics of retail banking in comparison to those of corporate banking (discussed in Chapter 4). As the name implies, retail banking is aimed at retail customers who tend to save smaller amounts of money than corporate customers and to avail of credit to meet requirements like building a house, educating their children, etc. Retail consumers therefore approach a bank for personal needs while corporate customers approach the bank for business-related needs. Following are some of the differences between retail and corporate banking.

Higher interest rates: The difference in interest rates for loans is one of the most prominent differences. Bankers charge the retail customer a higher rate of interest than they do a corporate customer. The loan amount availed of by retail consumers is comparatively smaller than that of corporate customers. Further, corporate customers have more bargaining power than retail consumers due to the large volume of business that they can give. For instance, a personal loan on a credit card may be charged interest rate of 23% or more, while a corporate loan may be charged at around 10%.

The maximum tenure for most retail loans is 5-7 years. However, housing loans may have longer repayment periods of 15 to 20 years. The interest rate charged on housing loans is less if the repayment period is more.

Lower risk of NPAs: Housing loans are the major part of the retail credit. Housing loans are secured by collateral in the form of a house, land, etc. The probability of such loans falling under Non-Performing Assets (NPAs) is very low. Thus, retail credit frees the banks from the NPA burden, unlike in the case of corporate credit where NPAs are relatively high.

Relationships not the sole means of growth: Corporate banking requires closer relationship management than retail banking. Banks need to maintain close relationships with each of their customers. Retail bankers do not need to specifically focus on building close relationships with all customers. For instance, it may not be necessary to maintain partnership relationships with customers who only have a basic savings account with the bank.

Need for publicity: In corporate banking, marketers sell their products to corporate customers largely through relationship building and limited advertising in the mass media. Retail banks promote their products to mass markets through the mass media. So, they are more often in the public eye than corporate banks. Retail banking brings instant recognition to a bank while corporate banking is more of low profile banking.

Sensitivity to pricing: Corporate loans are sensitive to the ups and downs in the economy, while retail loans are, to a large extent, not affected by such changes. When the cost of funds for the banks increases, they feel the pressure on their margins on corporate loans as they are priced low at around 10%. However, in retail loans like personal loans, interest rates hover around 20% or more, which acts as a big cushion.

Volume-based strategy: Though retail products give less business per consumer, the number of these consumers compensates for the costs involved. On the other hand, corporate customers are fewer and give more business per customer.

Freebies for customers: Retail customers are offered a host of freebies like free debit cards and credit cards, free doorstep opening of accounts, free accident insurance covers, etc. in order to persuade them to purchase more products. Such freebies are seldom seen in the case of corporate customers.

Factors Contributing to the Growth in Retail Banking

The retail banking sector has grown tremendously in India. There are many factors that have been contributing to this growth. Some of them like banking reforms, increase in funding options for corporates, etc., have been mentioned in the earlier sections. Let us understand some of the other factors that have fuelled the growth of the retail business in the Indian banking sector.[5]

Economic prosperity: Since 1992, the economy has been growing at a compounded annual growth rate of 6.8%. Economic prosperity has led to an increase in the purchasing power of the consumers.

Changing demographics: Changing demographics has also contributed to the growth of retail banking. As of 2006, nearly 70% of the Indian population is under 35 years of age. The Indian population is, to a large extent, young and young people are generally ready to take risks.

Technological advancements: Technological advancements in the distribution of banking services have revolutionized the way banking is done. They have brought in comforts like phone banking, ATMs, credit/debit cards, and, more recently, any-branch-banking and Internet banking. Also, technology has helped in the automation of back office processes in banks, thereby saving a lot of time for the employees, which they can use to focus on attending to the customers.

Lower NPAs: NPAs and impaired assets[6] are relatively lower in retail banking than in corporate banking and this factor is attracting more players to retail banking. For example, Deutsche Bank, a leading investment banker, entered the retail segment in 2006.

Liquidity in the banking system: Liquidity in the banking system increases with more inflow of funds through deposit mobilization, flow of foreign investments, or due to regulatory relaxation of provisions such as Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR). More liquidity reduces the cost of funds, which in turn, reduces the interest rates. For instance, the decline in interest rates due to excess liquidity in the banking system between early 2003 and late 2005 further fuelled the growth of retail banking.

Competition to Retail Banks

NBFCs typically incur higher costs in procuring funds than banks. RBI regulations also place some restrictions on their operations. However, NBFCs still compete strongly with the banks, in selected market segments. NBFCs like Sundaram Finance, Bajaj Auto Finance, Mahindra & Mahindra Financial Services, Shriram Transport Finance, etc. have a strong presence in non-metros and semi-urban areas. They have also tied up with equipment and asset manufacturers to gain deeper penetration into their respective markets. NBFCs have been very strong in commercial vehicle financing and two-wheeler financing. They compete fiercely with banks in these asset product categories.

The postal department, on the other hand, is a strong competitor to the banks in the liability products category. The banking and savings products offered in post offices across the country are on a par with similar products offered by the banks. Savings bank accounts, recurring deposits, the monthly income scheme, the senior citizen savings scheme, etc. are some of the banking products offered at the post offices. The greatest strength of the postal department in India is its extensive distribution network, as it has over 150,000 branches reaching out to every nook and corner of the country. This vast network has helped it reach out to the remotest hinterlands and to understand the customers better. The postal department has been a favored destination for semi-urban and rural customers looking to save money for their future.

TYPES OF RETAIL BANKING PRODUCTS

Having understood the characteristics of retail banking, we will move on to learn about the different products that are being offered to the retail consumer. The needs of the retail consumers differ with varying demographics – age, income, etc. Bank marketers must bear this in mind while developing products and services. Banks are slowly moving toward becoming ‘one-stop shops’ or financial supermarkets, which cater to all kinds of financial products, ranging from traditional asset and liability products, to complex investment products. Deposits and loans form the traditional products of banks, which most customers are already familiar with. But with the changing demographic and socioeconomic situation (e.g. increase in income levels and changing spending habits), today's consumers have evolved and are ready to invest in products that have higher risk levels. Increased awareness about different investment avenues and their respective rates of return is another factor that has influenced a shift toward various investment products. To cater to these consumer groups, banks have expanded their product portfolio.

In this section, we will briefly discuss the various retail banking products available in the market, as listed in Table 5.1. The subsequent sections of this chapter will focus on asset and liability products. Credit cards are discussed in Chapter 6 and insurance products in Chapter 7 and Chapter 8; pension plans are covered in Chapter 9 while Chapter 10 takes a look at mutual funds. Retail fee-based services, which are offered by banks and/or other financial institutions, are discussed in Chapter 11.

Table 5.1: Products in Retail Banking

Product Category	Generic Products
Liability products	• Savings accounts • No-frills accounts • Current accounts • Fixed deposits/Term deposits • Recurring deposits
Asset products	• Housing loans • Personal loans • Education loans • Gold loans • Loans to senior citizens • Property and mortgage loans • Vehicle loans • Agricultural loans
Credit cards/ Debit cards	• Credit cards • Debit cards
Investment products	• Insurance products • Pension plans • Mutual funds

Compiled from various sources

Liability Products

Liability products are associated with a liability on the bank's side. Customers deposit their savings with the banks, for safekeeping, earning interest, and/or for the ease of carrying out various financial transactions. When a customer deposits his/her savings, an account is opened in his/her name and a pre-decided interest (if applicable) is paid to him/her at pre-decided intervals of time. The typical liability products of a retail bank are savings accounts, current accounts, time deposits, and demand deposits. Time deposits are those deposits which are linked to a maturity period such that the full benefits of those deposits can be experienced only after maturity; premature withdrawal of such deposits attracts a penalty. Fixed deposits and recurring deposits are some of the popular time deposits which will be discussed in this section. Demand deposits are another type of deposits where customers have the privilege of withdrawing their deposit amounts at any time, that is, on demand. Savings banks accounts, no-frills accounts, and current accounts fall under this category.

According to RBI's guidelines with regard to 'Know Your Customer' (KYC) norms, banks have to segregate their customers into different risk categories. The customers have to be classified into low, medium, and high risk categories based on the nature of their business activity, location of the customer, mode of payments, volume of turnover, social and financial status, etc. Banks should not open any anonymous account or an account in any fictitious name. Documentation requirements to open an account change with the risk profile. For instance, salaried employees (whose identities and wealth can be easily identified) are associated with low risk.

In India, all the customer deposit accounts in every bank are insured by the Deposit Insurance and Credit Guarantee Corporation (DICGC). DICGC was formed in 1978 with a view to providing security for the deposits of customers in banks. In case a bank is liquidated, each customer deposit in that bank is repaid up to Rs.100,000. Refer to Exhibit 5.2 for further details on DICGC.

Exhibit 5.2

Deposit Insurance and Credit Guarantee Corporation (DICGC)

The Deposit Insurance Corporation was established on January 1, 1962, by an Act of Parliament. In 1978, it took over the functioning of the Credit Guarantee Corporation of India Limited, a public limited company promoted by the RBI. The former provided insurance for deposits held by the banks, while the latter provided credit guarantee for financial institutions that provided credit to the weaker sections of the society. After integrating these two functions, the new body was renamed as the Deposit Insurance and Credit Guarantee Corporation (DICGC). From 1981, DICGC began extending its credit guarantee to loans provided to small scale industries, which are classified under the priority sector, and from 1989, the guarantee cover was extended to the entire priority sector advances as per the RBI definition of priority sector.

The objective of DICGC in providing deposit insurance is to insure against the loss of all or part of the deposits in all branches of a bank, to a maximum of Rs. 100,000. All commercial banks and cooperative banks operating in India are insured by DICGC for their deposits, where the deposit insurance premiums are to be paid by the banks. DICGC insures different kinds of deposits such as savings bank accounts, current accounts, fixed deposits, and recurring deposits. It does not insure certain types of deposits such as deposits of foreign governments, deposits of central/state governments, deposits of the State Land Development Banks with the State co-operative bank, any amount due on account of and deposit received outside India, and any amount which has been specifically exempted by the corporation with the prior approval of Reserve Bank of India.

Each depositor in a bank is insured upto a maximum of Rs. 100,000, which is inclusive of the principal amount and the interest accrued on the deposit. If a depositor holds any amount in excess of Rs.100,000 in a deposit account, DICGC insures only upto Rs.100,000 and is liable to pay only this amount in case of liquidation or amalgamation or merger of the bank. In case a depositor holds more than one deposit account in different branches of the same bank, then all such accounts are aggregated and a maximum amount of Rs.100,000 is paid. But if a depositor has deposited the amount in different banks, then each deposit account is insured separately.

Adapted from "43rd Annual Report of the Board of Directors, Balance Sheet and Accounts for the year ended 31st March 2005." www.dicgc.org.in; and Frequently Asked Questions, http://www.dicgc.org.in/html/faq.htm#a2

Savings account

A savings account is a financial product that allows a customer of a bank to save small amounts of money with the banks. Customers can either deposit into or withdraw from the account. Withdrawal was traditionally done through cheque books and withdrawal forms (available in the bank). But technological advancements like the ATMs and debit cards have reduced the dependence on branches for withdrawal. ATMs are used for instant cash withdrawals and balance enquiry, while debit cards are used to make cashless transactions while shopping or purchasing. Banks invest the amount deposited in the savings account in various avenues and in turn pay a modest interest to the customer.

Many banks have come up with savings accounts for children like ICICI Bank's "Young Stars" account, Citibank's "Junior Package", HDFC Bank's "Kid's Advantage Account", etc[7]. Exhibit 5.3 provides a brief description of ICICI Bank's Young Stars Account. Also, banks have developed savings accounts that specially cater to women and senior citizens. For women, these accounts come with added features like family insurance; for senior citizens, the banks pay higher interest rates for deposits than the normal savings accounts.

Exhibit 5.3
ICICI Bank's Young Stars Account

Like a few other private sector banks, ICICI Bank also has come out with its own savings bank account aimed at children. Children between 1 year and 18 years of age are eligible to open this account, called the Young Stars Account. The parent or the legal guardian has the authority to open the account. Unlike other banks where opening a child account mandates an existing savings bank account, the Young Stars account does not require any savings bank account with ICICI Bank. However if the parent/guardian already holds a savings bank account with ICICI Bank, it is easy to transfer funds to the Young Star account.

A Young Star account can be opened as a savings bank account or a fixed deposit or a recurring deposit or a flexi-recurring deposit. Thus the parent has the flexibility to choose the type of deposit account to be opened. The features of this account include a free international debit card for children above 7 years of age, free Internet banking with separate login IDs for parent and the child, facility to transfer funds from the parent's account to the Young Star account, and the facility to transfer funds from the Young Star account to a recurring deposit.

From April 2006, ICICI Bank started used world-renowned cartoon characters Tom and Jerry as brand ambassadors for increasing public awareness of the Young Star account and to induce more parents/guardians to open such accounts for children.

Adapted from http://www.icicibank.com/pfsuser/icicibank/depositproducts/kid-e-bank/features.htm; and Madhan, G. "Banking Products for Children…Getting Them to be Fiscal." The Hindu Business Line. October 19, 2003.

No-frills account

A no-frills account is a type of savings banks account with zero-balance or low minimum balance facility. In 2005, the RBI directed banks to provide such accounts as part of a broader agenda of financial inclusion of poor people in the financial system. According to the RBI, banks had earlier been targeting only the well-off classes in the market and the poor classes have been deprived of such services. So it directed all banks to include a no-frills account in their product portfolios. Some public sector banks like Allahabad Bank and UCO Bank have introduced these accounts where they mandate Rs. 5 as the minimum balance. To avail of ATM and cheque book facilities, they charge Rs.250.

Current account

As explained in Chapter 4, a current account helps the customer to perform multiple transactions within a single day. Any individual businessman, professional, or Hindu undivided family can open a retail current account. Though the bank does not pay any interest on the amount deposited in the account, it allows the user to make unlimited transactions in a day. Current accounts also come with cheque book facility, Internet banking, etc. Banks mandate a minimum balance to be maintained by customers, failing which a penalty is charged. Current accounts are also used to pay rents, taxes, utility bills, insurance premiums, etc.

Fixed deposits/ Term deposits

A fixed deposit, also known as a term deposit, is a type of time deposit. It is a way of depositing a fixed amount of money in the bank for a fixed period of time. A bank accepts fixed deposits for pre-specified durations of time and pays the interest on them at pre-decided intervals of time. The amount from the fixed deposit can be withdrawn at the end of the period. Besides this, money can also be withdrawn before maturity; but in such cases the bank pays less interest. Some banks permit partial withdrawal of the deposited amount at ATM machines using ATM cards, without the customer having to go through the time-consuming process of visiting the bank in person for such a withdrawal. Fixed deposits are also linked to safe deposit lockers in many cases; banks insist on the customers opening fixed deposits as a pre-requisite to availing of the safe deposit locker facility. Safe lockers are discussed in detail in Chapter 11.

Recurring deposits

Recurring deposits, another type of time deposit, allows the customer to save small amounts of money with the bank every month. This product is aimed at those people who have high expenditure during the month, yet would like to save money for the future. Banks pay a modest interest for the amount thus saved, quarterly, half yearly, or annually. For example, in June 2006, the rate of interest for recurring deposits with SBI was 6.00%[8] and that of ICICI Bank was 6.25%[9].

Asset Products

An asset is anything that the bank holds in terms of the credit given to the customer. Retail bank assets are domestic in nature. They include housing loans, education loans, professional loans, vehicle loans, property loans/mortgage loans, personal loans, and agricultural loans. The interest rates charged are different for different products. A fixed interest rate is followed for some products while a floating interest rate is followed for others. A fixed interest rate implies that the interest rate usually remains fixed throughout the tenure of the loan, whereas in the case of floating interest, the interest rate varies with changes in the inter-bank rates[10] or other standard benchmark rates like the Benchmark Prime Lending Rate (BPLR). For instance, if the BPLR is 10% and a loan is sanctioned at a floating rate of 2% below the BPLR, then the interest rate changes with the change in the BPLR. If the BPLR increases to 11.5%, then the customer has to pay 9.5% for the loan. This would be reflected in terms of increased EMI (equated monthly installment), if there is no change in the period of repayment. But if the BPLR drops to 9%, the interest rate payable by the customer also drops to 7%, which means a reduced EMI, if there is no change in the same period of repayment. On the other hand, a fixed rate usually remains fixed throughout the tenure of the loan, except in some exceptional conditions like if there is a heavy rise in interest rates in the economy. Thus customers are protected against variations in interest rate in the case of fixed rates, while this is not the case where floating rates are concerned. Let us discuss a few of these asset products.

Housing loans

Housing loans form the majority of the asset portfolio for a retail bank. These loans are given to consumers who need financial assistance in order to construct a house or purchase a house/land. The amount involved is large and may go up to as much as Rs.5 million. Banks consider many factors like the customer's age, income, qualification, number of dependents, assets owned, etc. while deciding on the loan eligibility. The amount sanctioned also depends on the expenditure involved (value of the collateral) and credibility/repaying capacity of the customer. The repayment period is also long term in nature (usually between 5 years and 20 years). Many banks are shifting to floating rates for home loans, as it covers the element of interest rate risk involved in the loan. See Table 5.2 for home loan rates of some standard players in this market, as of December 2006.

Table 5.2: Home Loan Interest Rates of Some Financial Institutions

Institution	Floating Rate (as of December 2006)	Fixed Rate (as of December 2006)
HDFC	9.75	11.00
ICICI Home Finance	9.50	10.75
IDBI Bank	9.50	10.50*
Citibank	9.75	13.50
HSBC	9.75	11.00
SBI	9.25	9.75
Standard rates are for Rs. 1 million for a term of 15 years; the rate may vary between customers, on a case to case basis. (* term of 5 years).		

Source: http://sify.com/finance/loans/

Personal loans

Banks give personal loans to customers to help them meet personal exigencies like marriage, travel, medical, etc. The personal loan amount sanctioned depends on the customer's credibility and repayment ability. The bank decides this based on the customer information like age income, stability in employment, previous repayment track record, etc. Personal loans are given to salaried employees or self employed people. Interest is generally charged at a fixed rate.

Property loans/ Mortgage loans

This is a traditional asset banking product and one of the most common types of loan that the public sector banks have been issuing over a long time. Under these loans, property assets like land, buildings, vehicles, gold, etc., are mortgaged. Banks retain the authority to decide on the amount of loan to be given against the security. Interest rates are fixed based on the prevailing market rates.

Agricultural loans

The scope of agricultural loans is wide in terms of the products offered. Typical products include crop loan, farm equipment loan, loan against warehouse receipts, and term loan. Other products include farm produce marketing loan (to meet the expenses during the sale of the produce), land purchase loan, land development loan, irrigation loans (to meet the costs of digging wells, laying canals, etc.) and loans for processing of agri-foods. Banks also provide loans for horticultural activities, poultry, dairy, rearing of goat and sheep, sericulture, etc. A certain kind of property has to be mortgaged and/or hypothecated in most of these loans, or a suitable third part guarantee should be provided. For instance, land has to be mortgaged for crop loans; crop produce has to be mortgaged for loans against warehouse receipts; and farm equipment has to be hypothecated in a farm equipment loan.

Many banks have brought out loan cards for farmers to facilitate access to funds. These cards can either be credit cards or ATM/debit cards. For instance, SBI offers the Kisan Credit Card through which farmers can have money on credit for crop needs. ICICI Bank offers the Kisan Loan Card to enable farmers to avail of loans through an electronic card which also supports cash withdrawal through ATMs.

Vehicle loans

Banks provide loans for purchase of vehicles – two-wheelers, four-wheelers, and commercial vehicles. Vehicle loans are usually financed up to 85-90% of the total invoice amount. Some banks finance the loans based on the ‘on road’ cost of the vehicle. Repayment is usually made through Equated Monthly Installments (EMI). The repayment tenure for car loans and commercial vehicle loans may range from as low as 6 months to even 7 or 8 years.

Credit/Debit Cards

Credit and debit cards are another set of products offered by banks. They do not fall exactly into either the asset or liability product category.. Credit cards are primarily used for shopping. When a customer shops with a credit card, the invoice amount is paid by the card issuer to the merchant electronically (electronic funds transfer). The credit card holder has to repay the amount to the card issuer either in lumpsum, or through monthly installments with interest. Thus, the credit card allows the consumer to ‘buy now and pay later’.

In contrast, for a debit card holder, when the card is swiped at the merchant’s swiping machine, the invoice amount is debited (deducted) from the card holder’s bank account and is directly credited to the merchant’s account. Hence, a debit card holder does not need to pay any interest to the bank. The debit card is essentially an extension of the ATM card, but it offers convenience in terms of cashless/paperless transactions.

MasterCard and Visa products of credit and debit cards are issued by financial institutions world over. Credit cards are one of the most aggressively marketed products by bank marketers. Credit card marketing has become a common strategy employed by most banks to increase their customer base and profitability. ICICI Bank has become the market leader in the Indian credit card market with 3.5 million cards holders by 2005, followed by Citibank with 2.85 million card holders. In 2002, Citibank was the market leader with 29% market share while ICICI Bank commanded a mere 5%.

The push is evident from the fact that the number of card holders is increasing every year as also the number of consumers using credit cards as the mode of payment in their shopping experiences – be it a case of traditional shopping or internet (online) shopping. A study carried out by ACNielsen India in 2005, has revealed that the most preferred online shopping payment mode of Indians is through credit cards. The use of debit cards and direct bank transfers amount to a very small percentage. The study also reveals that one-third of online credit card users in India use credit cards to book airline tickets on the Internet. Other major online purchases include train tickets, consumer durables like DVD players, video games, clothing/shoe/accessories, and music downloads.

Investment Products

Investment products are a new category of retail banking products, in addition to conventional asset and liability products. They usually include insurance products, mutual funds, and pension funds. Retail bankers have increased their marketing efforts to sell investment products. This is because banks get the additional liquidity (apart from liability products), which they can invest in various financial avenues and pass on the revenues to the customers. This helps the bank in two ways -- it gives extra income, and these products are used as tools to retain customers. When a customer buys an investment product, a relationship is built between him/her and the bank. Retail bankers use this relationship to understand the customer and his/her needs. These products are then tailored to the customer's requirements. On the other hand, customers do benefit from these products by earning additional income from their investments.

Investment products are mostly cross-sold by the banks to their customers. When a customer opens an account in a bank or approaches it for a loan, the bank motivates them to invest in these products while rendering the primary service. Thus, the customer ends up buying these products. We will discuss more about cross-selling in the final section of this chapter.

NEW PRODUCT DEVELOPMENT

We discussed in an earlier chapter that innovation in banking can encompass the following five areas – operations, media, pricing, delivery, and product. While the first four are related to enhancing the service to customers, the last category focuses on developing altogether new products. Customer Knowledge Management (CKM) is an important tool that helps banks in developing new products. Kevin DeSouza and Yukika Awazu (2005) opined that knowledge from the customer is a wealth of information that an organization seeks. This information can be in the form of customer feedback, ideas, suggestions, etc., in addition to customer trends. This information essentially helps the banks to understand their customers better and provides them with helpful insights into what the customer expects from the bank.

Generic New Products

One of the major concerns of online shoppers is security of payment. The increasing instances of cybercrime involving theft of credit card numbers, account information, etc. have led to concerns over the information security on the Internet. To address this concern, HDFC Bank launched the Netsafe virtual card in 2004, in association with Visa International. This product is now accepted as a safe payment mode for online payments. Refer to Exhibit 5.4 for further details on this product.

Some private banks have introduced pre-approved loans as an innovative service to existing accountholders. Here, customers need not go through the usual time-consuming loan approval process. Instead, the banks go through the customer information and do a pre-approval of a loan and sanction a certain loan amount, even before a customer applies for it. The customer can then get the mandatory paperwork done, so that the loan is disbursed without any delay.

Many banks have invested in R&D to understand the behavior and expectations of the customers. For example, Bank of America in the US dedicated a few of its branches in the Atlanta region to carry out experiments that led to new product development. Till then, the bank had mainly grown using the inorganic path, through mergers and acquisitions. In the late 1990s, when the opportunities for further acquisitions had narrowed down, the bank decided to shift to an organic growth path. It realized that in order to grow organically, it had to make a considerable investment in R&D so as to get to know the customer expectations. Thus, in 2000, it dedicated 20 of its branches in the Atlanta region to carry out its R&D activities by adopting a scientific, five-stage process. The stages were: (a) Evaluation of new product ideas; b) Design of plans based on the ideas; (c) Implementation of these plans in the selected branches; (d) Testing for the viability & practicality of the plans implemented; and finally (e) Recommending implementation in the remaining branches across the world. Bank of America, thus, came out with many new products and processes that fuelled its organic growth.

Exhibit 5.4
NetSafe – The Virtual Card

NetSafe is a virtual card developed by HDFC Bank in association with Visa International. This was considered as India's first virtual card to carry out e-commerce transactions. The basic feature of NetSafe is that there is no need to disclose the credit (or ATM-cum-debit) card information while making payments on the Internet. While launching the card in January 2004, Aditya Puri, managing director, HDFC Bank, said, "NetSafe will enable HDFC Bank cardholders realize the full value of their debit and credit cards, even on the Internet. Possibly, this could just be the catalyst that was needed for the much-awaited explosion of e-commerce in India."

HDFC Bank cardholders can create their own virtual card on the Internet, based on their credit or debit card. The virtual card can be created with a pre-defined limit amount and is either valid for a limited period and/or for a single use. When a virtual card is created with a limit amount of Rs.1,000 and is valid for only one day, this amount is debited from the user's credit/debit card. In case the virtual card is not used within the stipulated time, it becomes invalid and the amount is automatically credited back to the underlying credit/debit card. Virtual cards can be used like any normal credit card/debit card for shopping or to make payments online. Users can access the card through a login ID and PIN (Personal Identification Number) number given at the time of registration for the card.

Adapted from "HDFC Bank and VISA Launch India's First Virtual Card for E-commerce." www.domain-b.com. 28 January 2004.

Banking to HNIs and NRIs

Banks segment their customers using different bases that we discussed in Chapter 2. High net-worth individuals (HNI) and non-resident Indians (NRI) are two segments that retail banks address with special focus and attention. Banks adopt preferential strategies to tap these market segments.

A bank may have its own definition as to who an HNI is. For example, HDFC Bank defines an HNI as any person who holds a minimum of Rs. 200,000 as balance in a savings bank account, and/or a minimum of Rs. 500,000 as balance in a current account. Banks usually give preferential treatment to such affluent customers as they give bulk business to the banks. Banks offer a range of advisory services to HNIs to invest their surplus funds in equities, mutual funds, and debt markets, in addition to the bank's own savings products.

There are about 25 million Indian migrants globally who keep the foreign exchange registers ringing. They accounted for remittances worth $24.5 billion in 2006. Kerala is one of the states in India with the highest proportion of NRIs. NRIs in the Silicon Valley are estimated to have a combined wealth of US$ 250 billion.

Many Indian public and private banks are making efforts and developing their own strategies to cater to this highly profitable segment. Some common products, which have been developed by bank marketers for these segments are remittance accounts, NRI deposits, and NRI loans.

Banks usually come out with new remittance products that offer safe and speedy money transfers. Many banks in India offer this facility through various modes of money transfer. One such mode involves a tie-up with a foreign bank. This is a popular mode through which money can be transferred online quickly. For example, ICICI Bank has tie-ups with Wells Fargo Bank in the US, HSBC in Hong Kong, Commercial Bank in Qatar, Me-Bank in United Arab Emirates (UAE), etc. ICICI Bank mandates that the remitter should be an accountholder of ICICI Bank.

IndusInd Bank in March 2006 launched a new product "Fast-Remit" through a tie-up with the Bank of New York. Under this tie-up, NRIs from the US can register themselves with Fast-Remit on the IndusInd Bank's website and remit funds from their local bank accounts. The transaction takes less than 24 hours. The remitter need not have an account with IndusInd Bank.

PRICING

In corporate banking, banks follow discriminatory pricing to a large extent as corporate banking is based on relationship building. That is, banks provide credit to different corporate customers at varying interest rates based on their credit rating, their relationship with the bank, and their bargaining power. However, the bargaining power of a retail customer is comparatively lower than that of the corporate customer. This enables banks to charge the same interest rate for all retail customers, with the exception of segments like HNIs. Though banks assess the creditworthiness of a retail customer, it is taken as an input for deciding whether to sanction a loan, rather than to decide the interest rate to be charged for the retail loan.

The pricing of a bank product is influenced by cost, competition, customers, and constraints (as discussed in Chapter 4). The pricing of retail banking products is influenced by three broad sets of inputs. First, it is important to identify the bank's objectives, such as profit margin and target market share. Market analysis is done to understand the trends in the consumer behavior and competition. Then cost analysis is done to identify all the associated costs (for a product, customer, or activity). These inputs are helpful in determining the probable outcomes of different pricing decisions.

In addition to these factors, pricing decisions are influenced by external factors like policy changes, bank rate fluctuations, etc. Banks also assess the perceived value from the customer's perspective, in terms of service levels provided, range of products offered, distribution and delivery reach, and brand positioning. Once the prices are fixed, banks observe the extent of sensitivity of the customers toward the price level and adjust it accordingly. Let us now discuss the concept of price elasticity of demand, followed by the pricing of asset and liability products. Let us also understand the different types of pricing.

Price Elasticity of Demand

Price elasticity of demand has a major role to play in the pricing of banking products. If the demand for an asset product is elastic, a slight decrease in price increases the demand for the product considerably. If the demand for the product is inelastic, a slight decrease in price may not have a significant impact on the volume of business. In countries like the US and the UK, where the markets for banking products are mature, the demand for these products is relatively inelastic. On the other hand, in India, where banks have been growing at healthy rates, the demand is elastic. For instance, if the interest rate for home loan (an asset product) is reduced by 1%, there would a manifold increase in the demand for these loans. Similarly, if the interest rates of fixed deposits (a liability product) are increased, there would an increase in the demand for them.Let us focus our discussion on understanding the dynamics in pricing of asset and liability products.

Pricing of Liability Products

In the deregulated environment, banks are free to price their liability products. They can also decide on the penalties to be charged for any premature withdrawal of deposits. In late 2005, banks began to face a liquidity crunch in India. This led to an increase in the interest rates of the deposit products. Many of the banks (public as well as private) raised their deposit rates in early 2006. For instance, SBI raised its deposit rates between 25-50 basis points. The average deposit rate (for a deposit with maturity just over one-year), which was 5.00-5.50 percent on January 23, 2004, increased to 5.25-6.25 percent on January 21, 2005.[11] With this move, there was an increase in the total deposits with the banks.

Table 5.3 shows that in 2005-06, the net interest margins for many of the public sector banks suffered while mobilizing their deposits. All the banks raised their deposit rates to mobilize more deposits. This is one of the reasons for the reduced net interest margins in 2005-06 for banks such as Andhra Bank, Corporation Bank, and Oriental Bank of Commerce (OBC).

Table 5.3: Growth Rates and Net Interest Margins of Banks

Bank	Deposit Growth FY06*	Credit Growth FY06*	Net Interest Margin (%)	
			FY06	FY05
Andhra Bank	23.10	25.50	3.30	3.60
UTI Bank	26.00	43.00	2.90	2.90
Union Bank	19.80	32.90	3.00	3.30
Indian Overseas Bank (IOB)	14.20	36.00	4.00	4.00
ICICI Bank	65.00	60.00	2.30	2.20
HDFC Bank	53.50	48.10	4.30	4.00
Dena Bank	13.10	24.30	3.00	3.10
Corporation Bank	20.70	29.20	3.60	3.90
Canara Bank	20.70	31.50	3.60	3.60
Bank of India	19.20	23.30	2.80	2.60
Bank of Baroda	11.40	41.00	3.30	3.40
Oriental Bank of Commerce (OBC)	4.90	29.30	2.80	3.20

* Percentage change year-on-year

Source: "Interesting Times." Business Standard. May 8, 2006.

Pricing of Asset Products

The liquidity crunch in 2005 had its effect on the pricing of asset products also. Most banks raised their prime lending rates in early 2006[12]. With deposit rates being raised, banks began to feel the pressure on their profit margins and their net interest margins began to shrink. In order to maintain their profitability, they raised their lending rates by as much as 100--125 basis points. For its home loans, ICICI Bank raised the floating rate from 8.5% to 9% and the fixed rate from 9.75% to 10.25% in May 2006. SBI also raised its home loan PLR, which it calls SBI Advance Rate (SBAR) from 10.25% to 10.75%, with effect from May 2006. The interest rates for other credit products like personal loans, vehicle loans, etc., also were increased.

Pricing for the HNI and NRI segments

Banks normally adopt a discriminatory pricing policy for high value segments such as HNIs and NRIs. Such customers transact in bulk – bulk deposits and big ticket loans. Thus, in order to retain and expand business in these segments, banks price their products favorably. This is more evident in pricing of loan products. Such customers also possess sufficient bargaining power due to the high value of their transactions.

For example, a high net-worth customer may ask for a loan at a rate of interest that is 2% lower than the normal lending rate. When a bank is confronted with such a situation, it carries out a customer analysis and a cost analysis to arrive at the pricing decision. Customer analysis is done to verify the relationship of the customer with the bank. It includes details such as how many products the customer has purchased or currently holds with the bank, how many of these products are profitable to the bank, and for how long the customer has been associated with the bank. Cost analysis is used to analyze the profit the bank gets by giving the loan at that rate of interest. If the bank feels that it will still get a reasonable profit margin by lending at 2% less than the normal rate, then it can sanction the loan to the customer.

Covert and Overt Pricing

Overt pricing refers to the explicit charges that a bank collects directly from a customer for its product offerings. For example, the bank may charge a quarterly or yearly flat fee for unlimited usage of its ATM networks or phone banking facility or Internet banking facility. Other than a flat fee, banks may also charge a variable fee which varies with the volume and frequency of account operation. Variable fee or charges are used to cover the variable costs of the transactions, which sometimes, the flat fee may not cover. It may also charge penalties for non-maintenance of minimum balances in savings accounts or current accounts. In asset products, a bank can charge penalties for pre-payment of loan, over and above the regular interest rate. That is, if a customer offers to prematurely re-pay his/her loan in part or full, he/she may be charged a penalty for such early repayment.

On the other hand, covert pricing refers to costs which are not explicitly charged to the customers against the product consumed. Thus covert pricing implies that loss in one product is covered by revenues from other products or customers. According to Tina Harrison[13], the costs/loss incurred by the bank in one product may be recovered by either charging another customer a higher price, or charging higher prices on other products, or paying lower dividends to shareholders as a result of lower profits, or increasing the interest margin between the deposit rates and loan rates, or any combination of these.

Retail bankers announce free banking facilities where some products are given free of cost. For instance, to ensure higher credit card sales, retail bankers like ICICI Bank offer lifetime free credit cards. This implies that customers need not pay a yearly fee for the credit card in their entire lifetime. As such, this is a cost for the banks and these kinds of costs are recovered in other products or from other customers. For instance, a bank pays no interest on a current account. In effect, a customer is extending a free loan to the bank.

PROMOTION

Prior to deregulation, most of the public sector banks adopted a product-centric approach; there was little emphasis on promotional techniques such as advertising. There was also little emphasis on conducting marketing research to get to know the needs and preferences of the customers. The situation changed with growing competition after the deregulation of the banking industry. Advertising became an important element of the marketing mix. Private sector players led this change and eventually public sector banks followed suit. For instance, State Bank of India, the largest bank in India, found itself losing its market share slowly to the private players. To arrest this slide, it started advertising on a regular basis.

The retail banking industry as a whole is undergoing a metamorphosis in terms of customer service and a customer-centric approach. In this section, we will first discuss the advertising and the sales promotion techniques used by retail bankers. We will then move on to the importance of branding in retail banking and how successful branding helps in increasing the bank's business. Finally, we will discuss the part played by personal selling, telemarketing, direct mail & direct response advertising, and public relations in the promotion mix.

Advertising

Banks may advertise their product attributes, highlight their customer-centric approach, or focus on their infrastructural capabilities in terms of better reach in the market. Hill and Gandhi (1992) recommended certain guidelines to overcome the obstacles that arise due to the characteristics inherent in services – intangibility, inseparability, heterogeneity, and perishability. The intangibility aspect of retail banking can be downplayed in the advertisements by highlighting the tangible aspects of the products. For example, a bank can talk about its ATM network and. In 2005, one of the outdoor hoardings of SBI read, "Who has the largest network of ATMs in India? Surprisingly SBI." Documentation of the consistency in providing quality service can reduce the problems perceived due to heterogeneity. Emphasizing the reputation of the bank, especially its reputation on the customer service front, could address the problems perceived due to inseparability. Thus, as part of the advertising strategy, retail bank marketers must focus on ways to showcase concrete physical evidence, the reputation, and the documentation of the service delivery.

Some of the popular modes of advertising in retail banking are the print media, electronic media, the Internet, outdoor advertising (such as hoardings), statement inserts, and co-branding. Of these, statement inserts and co-branding are relatively new media vehicles. Statement inserts refer to inserting advertisements of the bank products in monthly account statements, credit card bills, ATM balance statements, etc.

Further, banks use different advertising appeals to convey their message. An advertising appeal is the manner in which a message is developed and expressed in anticipation of a specific customer response. Rational appeal and emotional appeal are the most commonly used advertising appeals to promote retail banking products.

Rational appeal

Rational appeal, also called logical or informational appeal, is used to provide information on product features and their benefits. The information provided in such ads focuses on how the product satisfies the needs of the customers. Rational appeals are further divided into price appeal, quality appeal, features appeal, and competitive advantage appeal. The SBI ad campaign mentioned earlier uses this type of rational appeal This ad informs the target customer that SBI has the largest ATM network in the country, which strongly suggests that a customer can conveniently use this network almost anywhere in India. In the case of other ads using rational appeal, there could be product information that throws light on specific product features and the resulting edge that it derives over similar products from competitors

Emotional appeal

An emotional appeal portrays human feelings so as to evoke a favorable response from the target consumers. These appeals highlight the social or psychological needs that the product aims to satisfy. Marketers choose emotional appeals in instances where they feel that a rational appeal may not be very effective. Emotional appeals are further divided into humor appeal, fear appeal, music appeal, etc. One of the ad campaigns for the Bank of Baroda used the emotional appeal. In it, Indian cricket captain Rahul Dravid says, "*sab kuch badal raha hai ... hamara bank bhi badal raha hai*. (Everything's changing ... our bank is also changing)." ICICI Bank's famous tagline "Hum Hain Naa", implying 'we are there to take care of your needs', also conveys the safety and reliability aspects to the retail consumer.

Competitive pressures have also made banks search for alternative channels that provide greater exposure to the target markets. As banking is a service-oriented industry, word-of-mouth publicity is usually more effective than advertising. Thus, banks have to ensure that their advertising statements match their actual operations.

Sales Promotion

Consumer promotion is used to attract new customers by giving offers and incentives. Sales promotion is also used to motivate existing customers to try new products of the bank. Banks consider this as an effective technique to attract the customers of competitors. The common sales promotions techniques used by most banks are giving premiums, gifts, cash back offers, etc. Premiums are used commonly by many banks in the US and range from simple calculators to Mercedes sports coupes. Gifts, cash back offers, etc., are prevalent in India. Banks also use cuts and discounts in their processing fee to attract customers to many of their products.

In countries like the US and the UK, banks have resorted to using competitions as a sales promotion tool. They promote their products by sponsoring competitions and the prizes for winners. In the US, competitions came into existence as early as 1987. The prize can be a simple surprise gift for opening an account or a full-fledged sponsored competition as part of the marketing communication efforts. In India, the momentum for competitions is yet to pick up. Sales promotion competitions can be addressed at consumers (consumer promotion), employees, or channel partners.

There are many advantages associated with consumer promotion, which mainly include the following:

- Consumer promotion helps in attracting potential customers from the target markets to purchase the products.
- Effective consumer promotion can also attract customers of the competitors who may otherwise stick on with the competitors.

- Brand switching can be restricted to a considerable extent using consumer promotions like offering attractive interest rates for the deposits, etc.
- Consumer promotion also acts as a motivating factor for the loyal customers with the bank.

Branding

Branding has gained prominence in the retail banking scenario, as in the marketing of consumer and industrial products. Banks have become aware of the fact that a brand can be a long-term asset for the bank and as such they have accepted branding of the financial institution (and its products, as applicable) as part of a long-term strategy.

Brand building in retail banking has its own advantages. It helps the bank get widespread recognition and to improve loyalty toward the bank's products. Brand loyalty in turn helps attract and retain customers. A strong brand image, like that of SBI or ICICI Bank, leads to certain competitive advantages. The bank can charge premium prices that customers will not hesitate to pay. Further, once customers purchase a brand, they do not go through the entire decision making process for subsequent purchase of that brand, instead they will rely on their past experience and the performance of the brand. Another advantage of branding banking products is that it decreases the customer acquisition cost, i.e., cost of attracting a customer. A strong brand leads to better customer retention and improved revenues for the bank.

Celebrity endorsements are often used as part of the branding strategy. ICICI Bank was one of the early users of celebrity branding when it roped in Amitabh Bachchan[14] in 2000. The bank also featured the Hindi superstar Shah Rukh Khan[15] as part of its celebrity endorsement strategy for marketing its NRI products. Deutsche Bank, a German bank present in India since 1980 in global investment banking and corporate banking, also made use of celebrity endorsement when it entered into retail banking. To promote its retail banking products, it roped in Sania Mirza, the young tennis star, and Sunil Gavaskar, the cricket legend, as brand ambassadors. Exhibit 5.5 describes the brand re-launch initiative of the Bank of Baroda, in 2005.

Exhibit 5.5
Bank of Baroda's Brand Relaunch: 2005

Bank of Baroda, a reputed public sector bank, has a widespread branch network in India. It also has an international presence, with branches in countries like the UAE, Mauritius, Hong Kong, Singapore, Malaysia, Thailand, Kenya, and other African countries. Despite such a vast presence, the bank earlier suffered from very low brand recall, even in the domestic market. Viewing this as a potential threat to the bank's future business prospects, it started a brand re-launch exercise in 2005. The objective of this campaign was to improve the corporate brand image. The bank engaged Rahul Dravid, captain of the Indian cricket team, as its brand ambassador and launched an advertising campaign. Results began to show by the end of 2005. The bank had regained adequate brand awareness and deposits began to flow in after the ad campaign. For example, in the first 45 days of the Rahul Dravid campaign, the bank successfully enrolled 1.26 million new customers, and mobilized Rs. 6.5 billion of savings bank deposits.

Adapted from: "The Dravid Ad is Making Us Change." The Rediff Interview, www.rediff.com. November 25, 2005.

Personal Selling

Personal selling is a prominent form of promotion at the branch level, where sales personnel of the branch develop contact lists of potential customers and contact them in person to sell the bank's products. Banks may adopt two different personal selling approaches – product-based sales approach and customer-based sales approach. In the first approach, the sales force is trained to sell the products without much prior knowledge about the customers. The sales force makes extensive cold calls and tries to push the products to prospects. The sales personnel do not attempt to understand the needs and requirements of the customers nor do they try to deliver a better product that suits those needs. This approach was the traditional approach to personal selling and is often termed as a quick fix approach. Banks, which either lack a well-focused marketing strategy or a comprehensive sales force, opt for this approach. When personal selling or telemarketing is outsourced to third party agents, banks may often face this problem.

The second approach is a new model of personal selling in the banking industry, according to Brooksbank (1995). This approach emphasizes that the sales force should make efforts to understand the customers' needs and requirements, and that they should match the products to suit those needs. The sales force is trained to identify the customers' financial and psychological needs by interacting with them. In this approach, they sell solutions/benefits as a means to satisfy the needs of the customer. This is a win-win situation where the customer gets the right product and the bank marketer gets the sale. Table 5.4 illustrates the differences between the two approaches.

Table 5.4: Personal Selling Approaches - A Comparison

Product-based sales approach	**Customer-based sales approach**
Focus on closing the sale	Focus on understanding the needs of the customers
I win, you lose approach	Win-win approach
High pressure on sales force to push the products	Emphasis on pushing the product is low
Customers are compelled to say 'Yes' to the product	Customers say 'Yes' to the product if they like it
Product is sold to the customer	Benefit is sold to the customer.

Adapted from Brooksbank, Roger. "The New Model of Personal Selling: Micromarketing." Journal of Personal Selling & Sales Management. *Vol. XV Number 2, Spring 1995, p.61-66.*

Usually personal selling is used to follow up on the advertisement of the products through various media. Customers who have already come across the ads of the product find it easier to understand what the salespeople tell them about the products. Typically, a good salesperson spends more time in listening to the customer than in talking. By doing this, he/she extracts more information from the customer, which makes his/her job easier.

Training and compensation

Training improves the efficiency and effectiveness of the salespeople. They are usually trained to sell specific products to specific target markets. Training of the sales force includes imparting selling skills and covers issues like making presentations, interaction with customers, tackling of customer queries, etc. Training is also imparted in the areas of improving their self-confidence and overall personality development.

Compensation for the sales force can either be in the form of a salary or a commission or both and is based on the nature and type of the product and also on factors like industry norms, company policy, and nature of employment (part-time or full-time employment). Compensation, which includes commission, is used as a motivation tool to achieve more sales.

Telemarketing

Telemarketing is another promotional tool for retail bankers in which product information is given to customers on the telephone/mobile phone and they are persuaded to purchase those products. Typically, credit cards and retail loans are promoted through telemarketing. H. N. Sinor, Chief Executive of Indian Banks' Association, said in February 2005 that 40 to 50 percent of credit cards and up to 25% of the retail loans are sold through telemarketing. Retail bankers derive many advantages by using telemarketing as a promotional tool. One, they get a sizeable chunk of business from telemarketing. Two, as it is usually outsourced to a direct selling agent, the costs involved in infrastructure and salaries are comparatively lower. In this regard, Sinor also said that the sales obtained through this channel are 40 to 50 percent more economical than other sales options. Thus telemarketing has become a useful tool in the hands of the retail bankers which they can exercise to promote their products and record sales.

But from the customer's perspective, it is considered a menace with his/her privacy being invaded. There has been much criticism from customers in India as well as the entire world over the aggressive use of telemarketing. Public interest litigations have also been filed in courts of law in this regard. On the directions of the court, banks have agreed to take steps to develop a "Do Not Call Registry" where any customer who does not want to be disturbed with such calls can register on the bank's websites. But chances are that customers of one bank who register in its registry may get calls from a different financial institution/bank. To tackle such problems, the Indian Banks' Association announced in April 2006 that it would develop a nationwide "Do Not Call Registry" where customers of all financial institutions could register themselves on a single website. This website would cater to all the customers across the nation irrespective of banks.

Direct Mail and Direct-response Advertising

Direct mail is another promotional tool which is used to target specific customer groups through customized presentation of information. As the name implies, product information is mailed to the customer groups in varying formats and styles. The advantage of this promotional tool is that it provides detailed information about the product in an attractive format and gives the customer time to consider the information and react to it. Another advantage is that the timing of releasing the mails can be controlled and if the marketers can anticipate the needs of the customers accurately, they can use direct mail to motivate customers to purchase their products. But the disadvantage associated with this is that many marketers use the same message for all their customers and many customers consider these mails as spam or unsolicited information.

Direct-response advertising provides the solution to this problem. It is a variant of direct mail where a product is first advertised without the full details being given. Interested customers are requested to contact the banks for more information. When such customers do request information, the banks send it to them. . Thus, it surmounts the problem that marketers encounter in using direct mail. This form of promotion is very helpful to the financial marketers and it is believed that financial marketers the world over are the major users of direct-response advertising.

Public Relations

Traditionally, public relations (PR) has been considered as a mere tool to get good publicity and create awareness among the public about existing products or new product releases of the bank. But there has been a 'paradigm shift' (discussed earlier) that has led to the use of more sophisticated tools in PR to improve the image of the banks. Bank marketers use different media to conduct the PR campaign. The range of PR tools used are annual reports, speeches by the top management, seminars, charitable donations, event sponsorships, in-house magazines, press releases, etc. PR as a function in the promotion mix is handled at the corporate level rather than at the operational level.

The main objective of PR is to maintain a consistently positive image in the public and this applies to banks also. The enhancement of this positive image helps the bank gain a competitive advantage in terms of building a positive perception about the bank. ICICI Bank sponsored a stage show in Dubai on March 2006 to create awareness and enhance its image. The show was attended by nearly 1,000 of its private banking customers. [16]. The bank has had a representative office in Dubai since October 2003 and event sponsorship was an attempt to increase awareness and gain instant recognition from the public.

DISTRIBUTION

Banks have the flexibility of choosing from among various distribution channels and thus reducing their distribution costs. Some of these channels are also avenues for promotion of the bank's products and offerings, in addition to making them available to the retail consumer. Thus the line between promotional avenues and distribution channels is slowly getting blurred. The different channels that banks use to distribute their products are bank branches, ATMs, the Internet, phone banking, mobile banking, EFTPOS (Electronic Funds Transfer at Point of Sale), DSAs (Direct Selling Agents), call centers, and distribution network of alliance partners. These channels are outlined in Table 5.5.

Before going into the details of each distribution channel, let us understand the reasons behind the development of these channels. Traditionally, retail banking was done through the branch network. The main reason why a bank chooses to go in for channels other than branches is to reduce the transaction costs and operating overheads, and increase reach. ATMs, Internet banking, phone banking, and mobile banking have revolutionized the channel strategies of banks and brought down operating costs to a fraction of what they used to be with branch banking. In this section we shall discuss seven channels in detail. They are bank branches, ATMs, Internet, mobile and phone banking, EFTPOS, DSA, and call centers (refer to Table 5.5).

Table 5.5: Distribution Channels at a Glance

Distribution Channel	Description
Branches	The traditional distribution channel for banks. They still are considered the most important of all the channels.
ATMs	The ATM channel is the fastest growing channel in India and banks have begun to share each other's ATMs to reduce their costs.
The Internet	It is one of the cheapest channels of distribution in retail banking.

Distribution Channel	Description
Phone Banking and Mobile Banking	Phone and mobile banking provides flexibility, convenience and continuity. The services include checking account balances, cheque status, ordering cheque books, requesting bank statements, etc.
EFTPOS	It enables the customer to carry out cashless transactions at merchant establishments, where the invoice amount of the goods purchased by the customer is debited from the customer's account and transferred to the merchant's account.
DSA	DSAs are the third parties to whom banks outsource selling of asset and liability products.
Call Centers	In-bound call centers act as distribution-cum-service delivery channels, by taking calls on product enquiries, change of address, complaints, etc. Out-bound call centers are used for telemarketing and tele-order booking.
Distribution Network of Alliance Partners	Financial institutions may form strategic alliances at the corporate level, the scope of which would include sharing their respective distribution networks at the operational level.

Compiled from various sources.

Branch Banking

Branch banking is the conventional and traditional way of banking. But with the advent of ATMs and Internet banking, this delivery channel is being sparingly used by customers. However, branch banking, despite the growing usage in other delivery channels, remains the basic banking channel. This is because ATMs, Internet banking, and phone banking are being used by customers for their basic banking transactions. But branches allow customers to have personal interaction with the bank personnel and enhance the value to customers. In addition, customers prefer to get first-hand information on any liability or asset banking product from the bank personnel in person. Naresh Wadhwa, Vice President-West, Cisco Systems (India) says, "It is very interesting to observe that no channel has replaced any of the others. Rather, they are complementing each other. The customer remains one, but over the years, there are multiple channels being developed like ATMs, call centers, online banking, mail/fax, WAP, etc. The interesting trend is that customers are using all the available channels instead of settling for just one."

Transforming the branch

Banks have also begun to use branches as places for developing customer relationships through private banking, giving advice, and cross-selling of insurance and mutual fund products. Banks are leveraging on the personal touch advantage of branch banking to attract and retain more customers. As part of providing advice, cross-selling, and enhancing customer relations, banks are currently transforming their branches. The traditional clutter and chaos are being replaced by an altogether different aesthetic environment. Private banks and foreign banks have spearheaded this change. For instance, ABN AMRO has pepped up the look of its branches with coffee bars. ICICI Bank has borrowed its branch design from the retail industry and customer service handling from the airline industry.

This entire changeover is done to ensure that a customer entering a branch is put at ease and in the right mood, which increases the chances of customer satisfaction and purchase potential. Public sector banks are also in the process of replacing their wired mesh teller counters with cubicles, sofas, soft lighting, and customer friendly staff.

ATM

Before deregulation, a bank was considered highly successful if it had a wide network of branches. After deregulation, to differentiate themselves from public sector banks in terms of customer service, private players embraced technology and introduced ATMs as a cash delivery terminal. Customers could thus avoid standing in long queues at the teller counter. The development became a competitive advantage for the private banks in terms of better service as well as reduced costs. The cost involved in using an ATM is very low as compared to the brick and mortar branch. It is said that it costs close to Rs.50 per transaction per customer in a bank branch while it is only Rs.15 in case of an ATM. This cost advantage led to the growth of ATMs in India. An NCAER[17] study pointed that ATMs in India grew from 1100 in 1999 to 14000 in 2004.[18]

With the wider acceptance of ATMs, the focus shifted from differentiation to wider networks. Banks with a wider network of ATMs began attracting more customers as they offered more convenience and flexibility. Private banks like ICICI Bank, UTI Bank, and HDFC Bank, built their retail business around the deployment of ATM networks. For example, as of 2006, 93% of UTI Bank's cash payments took place through ATMs. The respective figures for HDFC Bank and ICICI Bank were 70% each.[19]

With the ATM becoming a common feature, many banks that could not establish their own networks in remote areas began to share the ATMs of other banks until they had established one of their own. There were other reasons that prompted ATM sharing. The establishment and operation costs of ATMs in India are very high compared to western countries. It takes between 250 and 300 transactions per day for an ATM to break even within one year. But the average number of transactions that took place per day in 2004 was less than 100. Such situations prompted many banks to have shared ATM networks where two or more banks shared their ATMs to bring down the costs.

Even while establishing ATM networks, banks do not own the entire stake. They outsource various operations like networking, cash replenishment, security, reconciliation, etc. This has further brought down the cost of operating the ATMs. In India, SBI had the biggest ATM network with 5,300 ATMs in 2005, followed by ICICI Bank with 1,900, and UTI with 1,650. See Table 5.6 to know the percentage share of ATMs among the various banks in India. Industry analysts are expecting white label ATMs to become prevalent in future. A white label ATM does not have the name of the bank on it and account holders of any bank can use it for cash withdrawals and other functions.

Table 5.6: ATMs Deployed by Major Banks in India (2005)

Bank	Number of ATMs	Percentage Share (%)
SBI	5,300	30
ICICI Bank	1,900	11
UTI Bank	1,650	9
HDFC Bank	1,070	6

Bank	Number of ATMs	Percentage Share (%)
Corporation Bank	800	4
Punjab National Bank	560	3
All other banks	6,720	37
Total	**18,000**	**100**

Source: "ATM Outsourcing: State of Indian Market – A Special Report." http://www.wipro.co.in/ATM%20Outsourcing%20-%20report.pdf. June 2005.

The Internet

This channel of distribution has gained wide acceptance with most of the banks offering this option to customers. But the penetration rate of Internet banking in India is very low due to various factors. They include lack of early adopters, low penetration of personal computers (PC), and lack of confidence in Internet transactions due to increasing cyber crime rate.

But the advantages for the banks in using this channel of distribution are many. The prime advantage is the cost of transaction, which is just Rs. 4 per customer. This is even lower than that of an ATM transaction at Rs. 15. Thus, banks save a lot if they get the bulk of business through the Internet. For this reason, banks have begun to induce retail customers to conduct banking transactions via the Internet. Internet banking helps customers check the account balance, apply for a loan, make payments, and get information. Some banks like HDFC Bank have even introduced virtual cards (discussed earlier) as a replacement for credit cards to facilitate online transactions.

Phone and Mobile Banking

Phone banking has also become one of the popular delivery channels of banking. This channel enables a customer to carry out an array of transactions by just sitting at home or the office and thus provides flexibility, convenience, and continuity. Mobile telephony has become very cheap and seamless connectivity has been achieved to a major extent. This development has led to the proliferation of mobile banking in the country. Mobile banking offers all the facilities that are offered through phone banking with the advantage of wireless connectivity.

The banks provide access through dedicated phone banking numbers where the customer can use various services using a telephone identification numbers (TIN). The variety of services that a customer gets through phone banking include looking up account balance, cheque status enquiry, ordering a cheque book or account statement, loan related queries, opening of fixed deposits by authorizing transfer of funds, payment of utility bills like electricity bills, mobile phone bills, enquiries about interest and exchange rates, and enquiries about other products of the bank.

EFTPOS

Expanded as 'Electronic Funds Transfer at Point of Sale,' EFTPOS is a cashless mechanism for purchasing goods and services at merchant establishments. Debit cards are used for this purpose where the invoice amount of the purchase is debited from the bank account of the customer and credited to the merchant's bank account. As these are cashless and hassle-free transactions, customers are motivated to purchase at such merchant establishments while banks charge a nominal fee from the merchants for the facility. It basically involves a card reading machine where the debit card is swiped to access the customer's account. The amount to be debited is entered through a supporting keypad. This channel has become popular with the increase in consumer spending and proliferation of debit card holders in India.

Direct Selling Agents (DSA)

This channel of product promotion-cum-distribution is also relatively new to retail banking in India. Most of the private and foreign banks outsource the personal selling and direct marketing functions to a third party, referred to as direct selling agent (DSA). The DSA conducts the marketing of financial products on behalf of the bank. Banks mainly outsource selling of typical liability and asset products like personal loans, home loans, savings accounts, current accounts, and credit cards.

The DSAs employ field staff who approach the customers as well as non-customers of the bank to generate sales. Information about the existing customers of the bank is provided to the DSA from the bank's central database. Information about non-customers is collected through various other sources such as purchase of customer information from utility providers like mobile operators, etc. Cold calling is a major approach followed to gain access to the potential customers. This is mostly done through telemarketing and personal selling, which are their main avenues of generating sales.

The use of the DSAs as an alternate distribution channel has come under severe criticism due to various reasons. The field staff is usually not well equipped with information on the various products offered by the bank. They may also not spend time on understanding the customer's needs. This leads to an improper match between the needs and the products sold, resulting in the staff performing poorly at times of personal contact with the potential customers. Another disadvantage of cold calling is that sometimes, different DSAs of the same bank may keep calling a customer asking him/her to purchase their products. This may eventually backfire with the customer becoming averse to that particular bank. Besides, fearing an invasion of their privacy, customers are also apprehensive that DSAs may compromise on the confidentiality of sensitive information such as income details and credit records.

Banks are now in the process of addressing these issues. The Banking Code and Standards Board of India (BCSBI) has brought out a banking code that covers the operations of the DSAs and the extent of information sharing between banks and DSAs. It has recommended that banks should not use sensitive customer information to cross-sell their products.

Call Centers

For many banking requirements, customers prefer interactions with the bank staff, rather than using the Interactive Voice Response System (IVRS). In the process, the bank's staff has to spend more time on answering customer queries rather than attending to their core duties. To handle such queries in a centralized manner, banks have established in-bound call centers. Such call centers have evolved into distribution-cum-delivery channels of the banks. The in-bound customer calls of the bank, which include product enquiry, customer complaints handling, etc., are handled by these call centers. Out-bound call centers are involved in telemarketing.

Banks may establish their own call centers or outsource this responsibility to a third party. Outsourcing of call center operations has become very popular as it is more viable for the banks in terms of saving on costs incurred on infrastructure and staff, as well as allowing the banks to focus on core banking operations. Banks in the US and Europe were the pioneers in establishing call centers in India to serve their customers. India is a preferred destination for the setting up and operation of low cost call centers because of the availability of English speaking personnel who come at a substantially low cost.

Despite the advantages, call centers have also been criticized as they have led to a reduction in the customer-bank interface. Further, the length of time it takes to get routine enquiries answered and the level of duty-consciousness of the staff of the call centers have also been often questioned. The infamous theft of sensitive customer information by a call center employee in India, which was eventually sold to a reporter of Sun Magazine (UK), came to light in June 2005. This and other such incidents have cast doubts on the ethics and efficacy of call centers as distribution channels. As a response to such incidents, banks have come out with stricter codes of conduct for call centers and their employees.

Distribution Network of Alliance Partners

As discussed in Chapter 2, corporate strategy decisions include decisions on strategic alliances for collaboration with other organizations, including competitors. The strategic alliance between Corporation Bank, Indian Bank, and the Oriental Bank of Commerce is expected to include sharing of banking infrastructure such as branch network and ATM network, training infrastructure, and even people, in order to deliver superior customer service at lower cost.[20] Thus, it is expected that competitive pricing among these banks will be replaced by collaborative sharing of resources, leading to greater profitability.

CROSS-SELLING

Cross-selling has become a buzzword today in the retail banking industry. Banks have understood the associated benefits of cross-selling and look at it as a tool to retain customers and improve sales. Banking experts consider it as a viable marketing strategy to expand their retail segments. Cross-selling refers to selling additional products of the bank to the existing customers. For example, a customer who holds a savings bank account is motivated by the personnel to purchase a personal loan, a credit card, an insurance policy, or a mutual fund scheme. The bank uses its entire portfolio to match the requirements of the customer and sell the product that best suits those requirements. This approach not only enables the customer get a product that solves his/her problems, but also helps the bank get an additional sale from an existing customer.

Need for Cross-selling

Banks use different strategies to increase market share, sustain consistent growth rates, and enhance profitability in an increasingly competitive business environment. Some banks venture into new markets while others put in efforts to further penetrate into existing markets. Cross-selling belongs to the second category and it increases the bank's revenues through existing customers. It is very effective in reducing the cost of sales, especially in selling additional products to the existing customers; it is believed to cost around five times more to sell the same products to new customers. As a result, this cost difference reflects on the bank's profitability and makes a big difference in a competitive marketing environment.

Cross-selling involves building relationships with the customers. Relationship marketing, which was discussed in Chapters 2 and 3, is applied in cross-selling of retail products also. Building relationships with the customers provides more insights into customer needs. The interactions that take place in the process of relationship building provide the scope and impetus to develop tailor-made products. These products can then be cross-sold to existing customers.

The cross-selling process also brings in new referrals from existing customers. This makes it easier for the bank to search for and acquire new customers. See Table 5.7 for the benefits of cross-selling, both from the bank's perspective and from the customer's perspective.

Table 5.7: Benefits of Cross-selling

Benefits to Banks	**Remarks**
Reduction in the total cost of acquiring new customers	A significant part of the revenue growth can be achieved by cross-selling to existing customers. For a given volume of total business, the bank needs to acquire a fewer number of new customers. So the total cost of acquiring new customer would be lower.
Improved customer retention	Cross-selling usually comes with better pricing offers for customers, as the bank passes on some of its savings. This increases the switching cost for customers. Even if they switch over to a competitor bank for some of the products, they may continue the relationship with the first bank for the other products.
Insights that help offer better suited and more customized products	With a clear understanding of the customer profile and the customer's requirements at that point of time, banks are able to offer products that meet these requirements and deliver greater value to the customers.
Enhanced 'Per Customer Lifetime Profitability'	Cross-selling helps banks to assess profitability in terms of customer lifetime for a portfolio of products, rather than at an individual product level or for a shorter time span. This helps in taking decisions that are beneficial to the organization, in terms of attracting and retaining customers who have a higher potential for 'per customer lifetime profitability'.
Benefits to Customers	**Remarks**
Reduced prices	When loyal customers buy new products from their regular bank, the bank may reward their loyalty with a better price. Banks can afford to do so as they do not incur acquisition costs on these customers. Also, in the case of asset products, they have a better understanding of the profile and creditworthiness of the customer, and are able to estimate the probability of default with greater accuracy.
Faster and easier processing	Existing customers gain in terms of simplified processes, reduced documentation, and reduced time required, when they go in for new products with a bank with which they already have a relationship.
Customized products	Banks have a clear understanding of the profiles of existing customers. They also have a vast amount of historical data that helps them to statistically predict the products that would suit the requirements of different profiles of customers at different stages of their lives.

Adapted from Dasgupta, Bireshwar. "Cross Selling in Banks: The Imminent Marketing Revolution." Professional Banker. March 2006, p.33-40; and Singh, Rajendra. "Cross Selling: Innovative Marketing Approach." Professional Banker. March 2006, p.27-32.

ICICI Bank was one of the first private sector banks to aggressively implement the cross-selling strategy in the Indian retail banking scenario. See Exhibit 5.6 to understand the impact of ICICI Bank's cross-selling strategy.

Exhibit 5.6
ICICI Bank's Cross-selling Strategy

ICICI Bank started to implement a cross-selling strategy in 2000, when Chanda Kochar (Kochar) took over as Executive Managing Director of the retail banking division. In 2000, many of the industry analysts were of the view that cross-selling was something new to the Indian customer and had apprehensions about its success in the Indian retail banking. They felt that the Indian retail customer might not be willing to be exposed to more than a single loan at any point of time.

But the management of ICICI Bank believed that a cross-selling strategy would help in increasing ICICI Bank's revenues and in improving customer satisfaction. According to Kochar, "Through cross-selling we will achieve three targets: One, we achieve customer satisfaction as the customer has a one-stop shop for his products. Two, it creates customer stickiness as a number of his needs are satisfied and three, it gives us efficiency in operations as marketing the product to different customers is more expensive."

The bank's retail operations started in 1999 and it was very aggressive in terms of market share expansion. As part of the bank's expansion strategy in the retail sector, Kochar focused on cross-selling, in addition to adding new products to the bank's retail portfolio, As on March 31, 2005, ICICI Bank had become the second largest bank in India with a total asset size of about US$ 38.5 billion and profit after tax of US$ 461 million.

Adapted from "No.1 In Two Years In All PFS Products - Says ICICI's Senior GM." www.indiainfoline.com. July 5. 2000.

Issues in Cross-selling

Despite the benefits mentioned earlier, there are some obstacles that hinder the successful cross-selling of products. A major obstacle is the mindset of the executives in a bank. When there is a collective opinion that business development is the task of the marketing personnel and that it is their job to go to the field and acquire new customers, executives from other departments fail to actively consider the potential for new business that can be generated from existing customers. This can be addressed by various measures such as:

- ensuring greater interaction between the marketing function and other operations at the branch level;
- modifying the criteria for performance appraisal to include cross-selling targets;
- creating a team of dedicated personnel to centrally analyze data, identify opportunities for cross-selling, follow-up on such opportunities; etc.

Cross-selling initiatives run the risk of causing customer dissatisfaction if the wrong products are recommended to the customers. This issue can be addressed by giving the required training to the executives, and by having sophisticated systems to predict what products can be successfully cross-sold to which customer profile. If there is excessive cross-selling, and especially if it is done through the telemarketing channel, it may be viewed by customers as harassment and as an intrusion into their privacy. Banks should have monitoring systems in place to prevent or reduce such instances.

SUMMARY

Liberalization, economic growth, changing demographics, and technological advancements have fueled the growth of retail banking in India. The product range in retail banking includes four broad categories: liability products, asset products, credit cards/debit cards, and investment products. Liability products include savings accounts, no-frills accounts, current accounts, fixed deposit/term deposits, and recurring deposits. Asset products include all kinds of retail loans, such as housing loans, personal loans, education loans, gold loans, loans to senior citizens, property and mortgage loans, vehicle loans, and agricultural loans. The investment products include investments in mutual funds, insurance policies, and pension plans. These are discussed in subsequent chapters.

As the bargaining power of a retail customer is less than that of a corporate customer, banks tend to charge the same price/interest rate for all retail customers, with the exception of high-value segments (HNIs and NRIs). Banks set the price for liability products, without the interference of the RBI. Asset products are priced based on the prime lending rates set by banks for each asset category. Overt pricing and covert pricing are the two different approaches to pricing.

The promotion of retail banking products is done through various avenues of promotion, such as advertising, sales promotion, personal selling, brand building, public relations, telemarketing, direct sales, and direct-response advertising. The common distribution channels in retail banking are branches, ATMs, the Internet, phone banking, and mobile banking, EFTPOS, direct selling agents (DSAs), call centers, and distribution network of alliance partners. There are some overlaps between the promotional avenues and distribution channels. For example, telemarketing and personal selling may be outsourced to DSAs.

Cross-selling helps the banks to increase their sales by selling different products to existing clients. It helps improve customer retention, reduce the cost of customer acquisition, and enhance customer lifetime profitability. Cross-selling also helps the customers in terms of reduced prices, faster and easier processing, and customized products. However, excessive cross-selling would be viewed by the customer as harassment.

End Notes:

1 "Big is Beautiful." www.ibef.org. July 22, 2005.

2 "Hong Kong & Shanghai Banking Corporation Ltd." www.ibef.org/attachdisplay.aspx?cat_id=461&art_id=6814.

3 Sodhi, P.S. "Retail Banking in the New Flavour." IBA Bulletin. December 2004, p.18-23.

4 Chakravarthy, Manas. "Happy Days Are Here Again." Businessworld. December 4, 2006, p.44.

5 Adapted from the keynote address of Gopinath, Shyamala at the IBA — Banking Frontiers International Conference on "Retail Banking Directions: Opportunities & Challenges" on May 28, 2005, in Mumbai. www.rbi.org.in.

6 An asset with a market value that is less than its book value.

7 Madhan, G. "Banking Products for Children…Getting them to be Fiscal." The Hindu Business Line. October 19, 2003.

8 www.statebankofindia.com

9 www.icicibank.com

10 Interbank rate is the rate that banks charge each other. The interbank rate is applicable to the short-term interbank market and applies to very large loans borrowed for anywhere from one day to five years.

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[11] "Economic Survey 2004-2005." http:/indiabudget.nic.in.

[12] "ICICI Hikes Home Loan Rate." Business Standard. May 6, 2006.

[13] Harrison, Tina. Financial Services Marketing. Pearson Education Limited, 2000.

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[18] Rai, Archana. "The Plastic Revolution." Outlook Money. March 31, 2005.

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Chapter 6

Credit Cards

In this chapter, we will discuss:

- Branding
- Pricing
- Promotional Mix
- Distribution
- The Current Scenario

The popularity of credit cards has increased tremendously over the past few years in India. Credit cards facilitate cashless transactions and allow the user to pay for purchases in installments over a specified period of time. For credit card issuers, this is a low margin, high volume business. To be viable, they must issue a very large number of credit cards and also have high volumes of regular transactions on the cards. In India, credit card marketers are competing to catch the attention of Indian consumers and make them adopt the credit card as an instrument of spending. Each marketer has a specific strategy based on the target market. There are also specific credit cards for the corporate as well as retail clients.

The inventor of the first bank issued credit card was John Biggins of the Flatbush National Bank of Brooklyn in New York. In 1946, Biggins started the 'Charge-It' program between bank customers and local merchants. As part of this program, merchants could deposit the sales slips at the bank and the bank would bill the customer who had used the card. Later, in the year 1950, Diners Club introduced the Diners Club credit card. These cards were essentially charge cards. The Diners Club cardholders could have food at specified restaurants without having to pay the bill; instead, Diners Club would pay the bill on behalf of the customer. Diners Club would then recover the dues from the customer within the specified period. American Express first issued its credit card in 1958. In the latter half of 1958, Bank of America issued its BankAmericard (now known as Visa).

Table 6.1 lists out the card name, the brand, and the type of card for the different categories of payment cards available in India.

In this chapter, we will first discuss branding in the credit card industry, followed by pricing, promotion, and distribution. This will be followed by a description of the current scenario in credit card marketing in India.

BRANDING

Branding is the process of creating an identity, image, or reputation for a product or service in the market. Organizations often invest huge amounts of money on branding. In the financial services industry, branding has become as important as the other aspects of marketing like the reach of the product, product quality, and customer relationship management. This is also true for the card industry, especially credit cards. We will look into three aspects of branding: branding strategies, co-branding, and brand measurement.

Branding Strategies

Financial marketers can follow several branding strategies to manage their brands. In general, most organizations begin with a single product and become multi-product organizations over time. Most organizations adopt a corporate or product or mixed branding strategy. In most cases, the product has the name of the organization, which marketers refer to as corporate branding. As new products are added, marketers have the option to continue with the corporate branding strategy. If the marketer chooses different names for each new product (without the organization's name) it is known as a 'house-of-brands' or product branding strategy. If an organization uses corporate names for some of its products and individual names for others, the organization uses a mixed branding strategy. In general, the type of branding strategy can be inferred by examining all the brand names of an organization's products.

Credit card marketers pay great attention to branding. One of the strategies that are commonly used in branding financial products, especially credit cards, is co-branding. This is discussed in the next section.

Table 6.1: Categories of Payment Cards in India*

Category	Card Name	Brand	Type of Card
Credit Cards	Bank Of Baroda Bharat Premium	Visa Card	Domestic Card
	Bank Of Baroda Exclusive	Master Card	Domestic Card
	Bank Of Baroda Global	Visa Card	International Card
	Bank Of Baroda Gold	Visa Card	Domestic Card
	Bank Of Baroda Own	BOB Card	Domestic Card
	Citibank NA CRY	Visa Card	Domestic Card
	Citibank NA Gold/Preferred	Master Card	International Card
	Citibank NA Gold/Preferred	Visa Card	International Card
	Citibank NA Indian Oil	Master Card	Domestic Card
	Citibank NA Jet Airways	Master Card	International Card
	Citibank NA MTV	Master Card	International Card
	Citibank NA Maruti	Visa Card	International Card
	Citibank NA Silver/Classic	Master Card	International Card
	Citibank NA WWF	Visa Card	Domestic Card
	Citibank NA Women	Visa Card	Domestic Card
	Citibank NA eCard	Master Card	International Card
	ICICI Bank Solid Gold	Visa Card	International Card
	ICICI Bank True Blue	Visa Card	Domestic Card
	SBI Cards Classic	Visa Card	Domestic Card
	SBI Cards Doctor	Visa Card	International Card
	SBI Cards Gold	Visa Card	International Card
	SBI Cards International	Visa Card	International Card
	SBI Cards Mumbai Card	Visa Card	International Card
Charge Cards	American Express Gold	Amex Card	International Card
	American Express Green	Amex Card	International Card
	Bank Of India Indiacard	Master Card	Domestic Card
	Bank Of India Taj Premium	Master Card	Domestic Card
	Canara Bank Cancard	Master Card	Domestic Card
	Canara Bank Cancard	Visa Card	Domestic Card
	Citibank NA Diner`s Club	Diner`s Card	Domestic Card
Debit Cards	Bank of Punjab ebank	Master Card	International Card
	Centurion Bank Gold Vantage 24	Master Card	International Card
	Centurion Bank Silver Vantage 24	Master Card	International Card
	HDFC Bank Debit	Visa Card	International Card
	ICICI Bank Ncash	Visa Card	International Card
	Standard Chartered Bank aXcessPlus	Visa Card	International Card

** The list is not exhaustive.*

Compiled from various sources

Co-branding

Co-branding is also known as dual branding or co-partnering. It is a process by which an existing brand (product or service) partners with another well established brand, for mutual benefit. Co-branding has emerged as an effective marketing tool for credit cards due to its ability to reach a wider audience. Co-branding began to be used worldwide in credit card marketing in the early 1990s. Most banks tie up with another service provider to provide a co-branded credit card. For example, Diners Club & British Airways (BA) together offer the Diners Club International British Airways Card, a credit card where the card owner becomes a member of British Airways' Executive Club - a premier frequent flyer program.

The card holder will earn BA Miles when they fly with British Airways or its partners.

Some banks have gone even further with co-branding. They have launched co-branded credit cards suited to the Internet transactions of customers. For instance, Citibank has formed an alliance with Indiainfoline (a prominent web portal on business, investment, and finance) to introduce the first co-branded credit card for the Internet. With this card, the customer is given the option to decide on the credit limit on the card, based on personal preferences. In addition, the credit card covers some of the risks like information theft associated with making purchases (with the card) over the Internet. Table 6.2 gives a list of some of the co-branded credit cards available in India along with the issuing bank.

Table 6.2: Co-branded Credit Cards in India

Issuing bank	Partner	Name of the Co-branded card
HDFC Bank	Idea Cellular (part of the Aditya Birla Group)	HDFC Idea Silver card HDFC Idea Gold card
ICICI Bank	Kingfisher Airlines	ICICI Bank Kingfisher Airlines Credit Card
SBI Bank	Indian Railways Vishal Group	SBI Railways Card SBI Vishal Megamart Card
ABN Amro Bank	Barista Coffee Chain	ABN Amro Barista Credit Card
Citibank	Jet Airways	Citibank Jet Airways Gold Card

Compiled from various sources.

Significance of co-branding

Co-branding of credit cards has become popular due to the host of advantages that it offers. There are many reasons why credit card marketers use co-branding as a branding strategy. It enhances brand reputation through synergies, influences the potential customer at a psychological level, and also helps increase brand awareness.

Enhances the brand reputation through synergies: In co-branding, the synergies derived from combining two corporate brands help make the product more appealing to the customer. This is because a brand's reach is greater when it is paired with another well-known brand, rather than when it is marketed individually. Many credit card marketers in India have made use of co-branding to gain this advantage. For instance, Bank of Baroda (BOB) and Bharat Petroleum Corporation Limited (BPCL) issue a co-branded credit card called the Bharat BOBCARD. With this card, customers can buy BPCL's products namely petrol, diesel, lubricants, etc., for which they are given points that can later be exchanged for gifts. BOB is able to increase its customer base while the card helps BPCL increase its sales.

Influences the potential customer at a psychological level: Co-branded credit cards tend to create greater psychological comfort in the minds of prospective customers. This positive psychological impression is high if there are several partnering brands or if the partnering companies have a good market image and presence. Besides, co-branded credit cards tend to offer greater benefits that create a stronger preference among consumers for co-branded credit cards than regular credit cards. To reap this benefit, nationalized banks like the State Bank of India have also launched a range of co-branded cards targeted at different customer segments. Exhibit 6.1 describes the co-branding efforts of SBI, where it offers a host of credit cards with tie-ups with companies in sectors like consumer goods, automobiles, and retail.

Exhibit 6.1

Co-branded Credit Cards from SBI

The State Bank of India (SBI) offers the SBI credit cards in partnership with many different organizations. It has introduced the 'LG card' in association with LG Electronics. The LG-SBI Card is India's first co-branded credit card for the consumer appliances industry. Some of the benefits offered are -- Exclusive discounts and access to periodic special schemes & promotions from LGEIL & SBI Card, 'Flexi pay', where customers can convert their retail purchases into an easy installment payment plan at low rate of interest, balance transfer facility at 0% interest for 75 days, etc.

SBI has another co-branded credit card in association with Hero Honda. The 'Hero Honda' card offers a personal accident insurance cover of Rs. 100,000. This insurance cover is doubled if a life is lost in an accident on a Hero Honda two-wheeler. SBI has also tried to influence customers by tapping into their philanthropic interests. It has introduced a credit card co-branded with four prominent NGOs viz., National Association of the Blind, SOS Villages of India, Cancer Patients Aid Association, and the World Wildlife Federation. This credit card enables the cardholders to contribute to social causes. Whenever a transaction is made with this card, a small amount goes to the specific trust as contribution.

Adapted from "SBI Card Now 2 Million Strong and Going," *http://www.indiantelevision.com/release/y2k6/jan/janrel13.htm,* January 6, 2006, *and http://www.sbicard.com/sbi/creditcards.jsp?CID=3&Lid=1&Ctype=CC*

Co-branding increases brand awareness: The co-branding process helps in increasing consumer awareness of the partner brands. This helps the partnering company to gain the attention of those customers who were previously unaware of its brand.

Other advantages of co-branding are: it helps in bringing in new customers; it lowers the costs of operations, space, and personnel; and the credit card marketer can benefit from the existing corporate image of the partnering organization.

Brand Measurement

It is not enough if marketers select the kind of branding strategy they will use; implementation and continuous tracking of branding programs are equally essential. Generally, marketers tend to lay emphasis on tracking marketing activities; they do not give much importance to measuring brand value. One of the reasons for this is the difficulty in measuring brand value. This is also true for credit card marketers. Hence, it is necessary for credit card marketers to set measurement standards to assess the brand value of their credit cards among the consumers. For instance, a credit card marketer must identify whether there is a gap between the expected brand value and the actual brand value of a credit card. The development of suitable metrics and their consistent tracking will lead to credit cards that are suitably modified on a regular basis to meet customer preferences.

Besides, the biggest task for any financial products marketer is to identify, educate, motivate, acquire, and retain the right customers. The nature of financial products and services makes this task more difficult for marketers. Therefore, marketers need to keep in mind key brand metrics and identify specific focus areas to ensure that the branding program is effective.

Key brand metrics

There are several brand metrics (important measurable parameters for the effectiveness of a financial product) that can be considered in the branding of financial products. Three such metrics, based on their importance are customer experience, customer retention, and customer loyalty.

Customer experience: The experience that the customer is able to get through the use of the financial product (in this case, the credit card) or service is a metric that is considered extremely important.

Customer retention: Brands are generally able to retain customers based on their image and quality. Any credit card brand, however well-placed, should continuously focus on retaining the customer. Customers who have moved away from the brand show very little interest in returning to the same brand.

Customer loyalty: The behavior of all the customers toward a brand is not uniform. Among such a wide group, it is important to give priority to loyal customers and provide them with extra services in order to reward their loyalty. Loyal customers deserve greater attention from the marketers. Credit card marketers keep this in mind and give special reward points to customers with high usage.

Keeping track of customer experience will help ensure better retention and greater customer loyalty toward the credit card marketer.

Focus areas for effectiveness in branding

Marketers need to focus on certain areas to significantly improve the overall effectiveness of their branding programs. The order of importance of these areas may vary slightly for different financial service providers, based upon their competencies. Some of the areas are -- better internal buy-in and communication between the shareholders, more precise data on customer opinion, information on experience and information needs, information on competitive forces, information on consistency in brand implementation and brand messaging, fair understanding of customer touch points[1], sound analytics, and good understanding of the customer relationship lifecycle. Some of these focus areas related to the customer have been described in Chapter 3 (Product Management and Customer Relationship Management) while some have been discussed briefly later in this chapter, in the section on CRM in credit card marketing. A focus on these areas will improve brand image and draw the customer closer to the credit card marketer.

PRICING

Price determines to a great extent the saleability of a product or service. The price of a product or service can make or mar its chances of success in the market. Substantial changes in the dynamics of credit card pricing have occurred over the past decade. The relatively straightforward pricing model of a single annual percentage rate (APR), an annual fee, and a small penalty fee has been replaced by a model with a complex set of APRs, new and increased fee structures, and sophisticated finance charge computation techniques. As a result of these changes in pricing structure, consumers pay substantially different prices based on individual behavior.

The adoption of new pricing structures has increased credit costs for some consumers and decreased it for others. Low-risk borrowers, who avoid new and increased fees by on-time repayments, have been benefited by lower credit costs than was possible several years ago. Higher risk borrowers, who may not have previously qualified for unsecured credit, can now obtain credit cards by paying a risk premium.

Factors Influencing Pricing decisions

When pricing a credit card, various factors need to be taken into consideration. These include consumer price awareness, perceived price value, pricing opportunities, risk profile of the customer, previous history of managing credit, and the probability of defaulting. Some of the factors affecting pricing decisions are discussed here.

Consumer price awareness

The knowledge that consumers possess about the price of any product or service is called consumer price awareness. Price awareness varies for financial and non-financial services. The 'price-quality' interaction is an important factor in setting the price of credit cards. For instance, the price of financial services is often difficult to assess because of the complexity of these services. Similarly, if there is not much information available on the quality of a product, the price of the product has a significant effect on customer perceptions about its quality. The effect of the 'price-quality' factor is greater when the difficulty in assessing quality is greater. A higher price leads the customer to assume that the product or service is of a higher quality.

Perceived price value

The pricing of credit cards follows a different approach from the competition-driven pricing approach used for many products and services. Credit card marketers can leverage on the perceived price value of their product. Perceived price value is the price that the consumer assumes for a financial product in the absence of accurate price information. It is possible that the perceived value of a credit card is higher than the price of competing cards. A marketer can opt to pursue the objective of profit maximization through higher pricing, when the consumer awareness of the price about a particular financial product is low and perceived price value is high.

Pricing Issues

The increased competition for new customers and the adoption of new technologies by the credit card industry have resulted in a decrease in the price of the credit cards. Besides, by offering features like the transfer of the outstanding due from one card to another and the elimination of annual fees, credit card issuers have made it easier for the customer to switch from one card issuer to another. In addition, higher levels of consumer awareness about the Annual Percentage Rates (APR) along with ease in applying for new cards, and mandatory requirements to keep the customers informed on the credit costs, have meant that issuers have to take considerable care in pricing their credit cards.

Risk-based pricing

Due to the absence of adequate data on credit records, risk based pricing was not followed in India till the end of 2004. Credit records provide details on the demographics, risk profiles, credit repayment histories, etc., of borrowers and credit card users. For a specific financial product, risk varies depending on the individual applicant and the customer segment profiles. Risk-based pricing has become more common with the increased availability of customer data and a greater number of tools like behavioral scorecards to assess risk profiles. The implementation of a risk-based pricing strategy is largely dependent on the customer profile that the issuing bank handles.

Use of APRs

The annual percentage rate (APR) is the interest rate that a consumer has to pay in the event of the credit balance being carried over, a cash advance being taken, or transfer of a balance from another card being done. The APR states the interest rate as a yearly rate. Some credit card marketers have a 'fixed interest rate', that is, the APR does not change frequently. Other credit card marketers charge a 'variable rate' where the APR changes from time to time. The APR is usually tied to other factors like the prime lending rate (PLR) fixed by the Reserve Bank of India (RBI). Credit card marketers use different APRs depending on their product offerings. Some of the APRs are mentioned in Table 6.3.

Table 6.3: APRs Used by Credit Card Marketers

Type	Description
Multiple APRs	A single credit card may have several APRs, one for purchases, another for cash advances, and yet another for balance transfers. The APRs for cash advances and balance transfers often are higher than the APR for purchases.
Tiered APRs	Different rates are applied to different levels of the outstanding balance. For example, 16% on balances of Rs. 1000 – Rs. 5,000 and 17% on balances above Rs. 5,000.
Penalty APR	The APR may increase if there is a delay in making payments. For example, if the payment arrives more than ten days late two times within a six-month period, the penalty rate will apply.
Introductory APR	A different rate will apply after the introductory rate expires.
Delayed APR	A different rate will apply in the future. For example, a marketer may advertise that there is no interest till next May. Then the appropriate APR may come into effect after May.

Compiled from various sources

Fees

Fees are another important aspect associated with credit card pricing. Most credit card marketers use fees as a promotional tool. For instance, many marketers waive the annual fee for a fixed period (one to two years) to attract customers. Like APRs, fees are also a means by which marketers earn revenues, though at a lower level. Let us look into some of the kinds of fees charged by credit card marketers at large.

Annual fee: The annual fee is payable in advance, at the start of every year. The annual fee is included in the first billing statement received by the card member. The fee could be as low as Rs 400 (for a Cancard) or could go as high as Rs 1,500 (for an HSBC Gold Card).

Joining fee: This is the fee that is to be paid to the credit card issuer when a customer's application for a credit card is accepted. The fee depends on the bank and the type of card applied for. Typically joining fees vary between Rs 100 and Rs 1,000.

Cash advance fee: This is charged when a customer uses the card for a cash advance. It may be a flat fee or a percentage of the cash advance.

Balance-transfer fee: This is charged when a customer transfers a balance from another credit card.

Late-payment fee: This is charged when the payment is received after the due date.

Over-the-credit-limit fee: This is charged when a customer uses the card over the credit limit specified by the bank.

Credit-limit-increase fee: This is charged when a customer asks for an increase in the credit limit, subject to approval.

Guidelines for Pricing

In March 2005, the Indian Banks' Association released a 'Fair Practices Code' for credit card operations by various banks. Some of the guidelines that the code states with respect to interest rates and other charges are as follows:

- The credit card marketers should ensure that there is no delay in dispatching bills and that the customer has at least ten days for payment before the interest starts getting charged.
- The APR charged and the annual fee should be stated clearly. The credit card marketers should quote the APRs separately for retail purchase and for cash advance. The method of calculation of APR should be given with a couple of examples for the customer to understand them properly.
- Late payment charges, the number of days after which late payment charges will be levied and the method of calculating such charges should be prominently indicated. The manner in which the outstanding unpaid amount will be included for calculation of interest should also be clearly and specifically shown in all monthly statements. Even where the minimum amount indicated to keep the card valid has been paid, it should be indicated boldly that interest will be charged on the amount due after the due date of payment.
- The marketer must not levy any charge that was not explicitly indicated to the credit card holder by the marketer at the time of issue of the card after getting the customer's consent.
- The terms and conditions for payment of credit card dues including the minimum payment due should be stipulated.
- If the marketer wishes to make any change in charges (other than interest), it may be made only after advance notice of at least one month has been given.

PROMOTIONAL MIX

The promotional mix components viz., advertising, sales promotion, personal selling, and public relations are given due importance in the credit card industry. Advertising efforts generally help to create a brand presence for a new entrant and reinforce the brand image for an established credit card marketer. Some credit card marketers do not focus much on promotional offers while others rely extensively on sales promotions. Personal selling of credit cards may be done by direct sales force or through other means. Public relations exercises are also used by some credit card marketers to capture the attention of the customers in large numbers. These four aspects — advertising, sales promotion, personal selling, and public relations -- are discussed in greater detail here.

Credit Card Advertising

Advertising is a communication process that requires a thorough understanding of various disciplines ranging from consumer research to direct marketing. The advertising effort should concentrate on putting across the right product to the right customer at the right time. This will enable marketers to achieve concrete and measurable results. Another point to be remembered is return on investment. An advertising strategy should be aimed at the target market and lead to a higher return on investment.

Advertising is an essential component of the promotional mix of financial product marketers. Credit card marketers in India make use of advertising (print & television) to appeal to customers. Let us look into some of the components of advertising.

Advertising objectives

Advertisements are used to fulfill specific marketing goals and the advertising objectives should be framed accordingly. For example, one of the basic advertising objectives of a credit card marketer could be to highlight the essential or distinguishing features of that particular credit card. In this case, the salient features of the card usually form the core content of the advertisements. Credit card marketers generally use advertisements supplemented with direct mail, to provide the stimulus needed to evoke a response.

Advertising appeals

An appeal can be defined as the manner in which an advertising message is developed and expressed, to derive a particular consumer response or to influence decision making. The appeal of an advertisement is decided by a number of factors like the objective of the advertisement, the product, the creative brief, and the time frame. Advertising appeals can be broadly divided into rational/logical appeals and emotional appeals. The rational appeal is also called the logical or informational appeal. This type concentrates on product features, the benefits to be derived from the product, and so on. Advertisements using a rational appeal are informative and their stress is on how the product will satisfy consumer needs. They provoke viewers to think further and then make a buying decision. Rational or logical appeals include details of price, quality, features, competitive advantage, and favorable costs. Emotional appeal uses human feelings like warmth, affection, humor, or fear to evoke a favorable response in the viewer. Advertisements with emotional appeal emphasize the social or psychological needs that a product can satisfy. This type of appeal can be used to advertise any product category, whether it is high-involvement or low-involvement. The various types of emotional appeals are humor, fear, sex, and music appeal. See Table 6.4 for a brief on types of appeals.

Credit card marketers generally use feature appeals when advertising, either in print or on television.

Based on the content of the advertisements, they could be classified as advertisements with soft value and advertisements with hard value.

Advertisements with soft value: Such credit card advertisements do not mention credit rates or annual fees. For instance, an advertisement for Citibank credit cards emphasizes the fact that its photo cards have a photograph of the cardholder, in order to dispel the fear of possible theft and misuse of the card. The advertisement reads: ‘If someone steals your credit card, they’d better look just like you.’ Generally, marketers of credit cards with a large user base adopt soft value advertisements.

Table 6.4: Advertising Appeals

Category	Types of Appeal	Description
Rational appeal	**Price appeal**	Advertisements of this type communicate the price of the product. This appeal is mainly used by the manufacturer to communicate special offer prices, price cuts, sales, or new price points. The appeal is very effective in times of recession, when customers become price sensitive.
	Quality appeal	Here, the ad copy emphasizes the quality of the product. Products using this appeal should ideally be known for their good quality.
	Feature appeal	This form of appeal is commonly used by services, or by technical and high-involvement products. These advertisements describe the product features in detail and are informative. The ad is structured so that it creates a favorable attitude toward the product.
Emotional appeal	**Humor appeal**	Humor in an advertisement is indicated by the presence of jokes, understatement, goof-ups, etc. An advertisement is humorous if it prompts heightened arousal, smiles, and laughter among the audience.
	Fear appeal	Fear appeal advertising is a type of 'psychoactive' ad, which is capable of arousing fear. Fear appeal is very effective in depicting products designed for safety and products for health.
	Music appeal	Some advertisements use popular music or compose special music for the purpose. The music should be selected in such a way that it goes well with the overall theme of the advertisement.

Compiled from various sources.

Advertisements with hard value: Unlike the soft value approach, the hard value advertising approach focuses on the direct benefits of the card. This includes the card rates, waiver of annual fees, reduction in phone and other bills that can be obtained with the use of the card, rebates, grace periods, etc. For example, one of the campaigns by Discover had the tagline "If you are using some other card, you are probably paying the price". The focus here was mainly on the 1% rebate offered and the absence of an annual fee.

In addition to feature appeals, many marketers have made use of the emotional appeal to attract customers. MasterCard uses the emotional appeal with its baseline 'There are some things that money can't buy. For everything else there's MasterCard'. One of the print ads shows a couple on a date having dinner. The headline reads – "Your first dinner together: Rs 3,400 (MasterCard). The second dinner date: Rs. 4,100 (MasterCard). Your third dinner together: Rs.5,250 (MasterCard). 'Yes': priceless."

Advertising media

The non-personal communication channels used for advertising credit cards are generally the print media and television. Print ads are used at a lower level than television ads. This is because print ads are restricted to feature appeals. Emotional appeals are conveyed more by television ads than print ads as TV ads have the advantage of visual and sound effects. As a result, credit card issuers tend to spend huge amounts on television commercials. For instance, Visa launched a multi-million dollar campaign involving Hollywood celebrities in 2003. In the series of ads, the year 2005 saw the 'birds' campaign involving the Hollywood actor Richard Gere. This was aired across all the major English and Hindi television channels in India.

With increasing competition and near identical offerings, financial marketers need to devise ways to differentiate themselves from others. This is especially true in the case of credit card marketers. Exhibit 6.2 describes some of HDFC Bank's campaigns.

Exhibit 6.2

No Flash, Just Solid Delivery

HDFC Bank has used a 360 degree approach in the form of television, radio, print, and outdoor advertising for its credit cards. 'We understand your world' was the baseline created for the entire range of products of HDFC Bank. Although HDFC Bank offers a wide array of financial products, it found that many consumers were not fully aware of them. For instance, many savings account holders of the bank were not aware that HDFC Bank also provided credit cards. All this led to the creation of a new campaign with the theme "Don't wait".

The campaign focused on the young working segment in the age group 24-30 years. The ads highlighted the rewards programs, low interest rates, comprehensive insurance coverage, travel benefits, and balance transfer facilities. One of the ads had an emotional element attached. It showed how a person manages to impress and propose to a girl using the HDFC Credit card. The man is trained by his sister and brother-in-law to propose to the girl. But he fumbles and cannot utter the words that he has rehearsed when he actually meets her. In an attempt to reassure the girl of his seriousness and financial stability he then flaunts his HDFC Bank credit card. The ad conveyed that one need not wait to make a decision.

HDFC Bank had a different advertising campaign for its HDFC Bank International Silver Credit card. This particular campaign had the tagline 'The card for wherever you go'. One of its print ads had a series of playing cards on one side and the 'International Silver Credit card' on the other. The subhead read 'Trump card,' indicating the credit card. The body copy read: -- "The HDFC Bank International Silver Credit Card. Diminishing Interest Rate. Comprehensive Insurance Coverage. Attractive Rewards Program. Travel Benefits. Balance Transfer. From a bank that offers a complete range of products and services. A bank trusted by more than 1.9 million customers across 70 cities. To apply, log on to www.hdfcbank.com or call 6420484."

Adapted from "Brand Watch: How Different from Competitors? - A Sneak Peek at the New HDFC Bank Ad Campaign," Hetal Adesara, http://www.indiantelevision.com/mam/special/y2k4/hdfc.htm

Sales Promotion

Sales promotion is an important marketing communications tool for credit card marketers in India. Making a purchase on credit is still not as popular in India as in the developed countries. Consequently, credit card marketers have a more difficult time persuading customers about the need for a credit card, and subsequently using the instrument for more purchases. Therefore, to attract first-time users, sales promotions are the ideal tool. Features or characteristics that differentiate the card from others, when accompanied by an irresistible promotional offer, make it more appealing. Some of the different methods of promotion are introductory offers, cash back schemes, rewards programs, cause-related marketing, word-of-mouth, and direct mail techniques. Some of these methods have been discussed in more detail here.

Introductory offers

Introductory offers are one of the best ways to attract prospective credit card users. They are also useful in making existing users switch to a new card issuer. For instance, in April 2001, Visa came out with a promotional offer where the credit card was supported by 14 principal bank members. The promotional offer was targeted at first time subscribers of the Visa Credit or the Visa Electron card. The first prize was a trip for two to the finals of the Sharjah one-day cricket series, with more prizes like gift vouchers from Titan and Crossroads (a bookstore chain). It required the submission of an entry form. This offer was open only to first time customers.

Cash back schemes

This is a very effective mode of promotion primarily used by credit card marketers to target dormant customers or customers who have very low frequency of usage. In this method of promotion, the card user gets a discount on purchases made through the credit card. The marketer stipulates a minimum purchase limit and in some cases makes the offer exclusive to the purchase of a particular good or service. Another objective of such a promotional offer is to habituate customers to making purchases using credit cards. It is assumed that there is a high probability that customers will continue using the credit card even after the end of the cash back scheme period. ICICI Bank, for example, offered a flat cash discount of 5% on any purchase made using its credit card in July 2005. To take advantage of the offer, all that the ICICI Bank credit card holder had to do was make a single purchase of more than Rs. 2,000/- or total purchases of Rs. 10,000/- within the period of offer.

Rewards program

The rewards program is a kind of loyalty program. Based on how frequently the credit card is used, the customer is entitled to certain reward points on every transaction. Accumulation of reward points would make the customer eligible for certain benefits or gifts. For example, ABN AMRO Bank offers reward points to its Freedom Credit Card customers that can be exchanged for exclusive gifts. One reward point is given for every Rs. 50 spent through the card. The reward points can be exchanged for exclusive gifts that include card renewal fees and gift vouchers.

Cause-related marketing

Although many people are interested in actively participating in social causes, many of them do not either find the time or are not in a position to contribute directly. Some credit card marketers have identified such philanthropic interests of the individuals and have developed products to cater to this segment of people. For example, Citibank introduced the CRY-Citibank Affinity credit card on November 14, 1998, coinciding with Children's Day. An affinity card is a form of credit card for people with similar (or) common interests. For every transaction made through this card, a certain percentage of money would be contributed by the bank to Child Rights & You (CRY), a welfare organization for children. This card thus indirectly gave the user an opportunity to help under-privileged children.

Personal Selling

Personal selling is a set of activities directed at the attainment of marketing goals by establishing and maintaining direct buyer-seller relationships through personal communication. In other words, personal selling can be defined as a process of using personal communication to inform and persuade customers to purchase products or services that suit his/her needs. Personal selling is quite different from other promotional tools like advertising and sales promotion. Unlike other elements of a promotional mix which are targeted at the mass market that may not include potential customers, personal selling is targeted at potential customers and allows two-way communication.

Credit card marketers make use of alternative means to sell their card products. The direct sales force is the most preferred. This is followed by the direct selling agents (DSAs). Other means of personal selling are through direct mail and call centers.

Direct sales force

Credit card marketers depend on their sales force to identify prospects and convince them to opt for their card products. Banks generally hire a large number of sales personnel for marketing credit cards. The sales personnel are trained to convince the customer about the benefits of the credit card. Credit card selling is more of consultative selling than aggressive hard selling. It is generally done on a one-to-one basis. Sometimes, credit cards may be developed for specific customer groups, especially corporate groups. As part of corporate marketing, a group of employees are addressed together through a sales presentation by sales personnel and persuaded to opt for the product.

Direct mail

This involves direct communication from the credit card marketer to the customer through mail. Marketers need to consider two important factors when developing the content for direct mail, viz., the element of interest and the process time. Element of interest refers to the content's potential to hold the interest of the customer. The time required to comprehend the content in the desired manner is the process time. Therefore, the direct mail content must be crisp, and persuasive. In addition to good content, marketers use other means to catch the attention of prospects. For instance, the marketer may send a plastic replica of the credit card by mail to a prospective customer to generate curiosity.

However, distribution through direct mail has its own disadvantages, especially with the new laws imposing restrictions on unsolicited mail and telephone calls. In India, most banks need to offer the customers the facility of registering with the do-not-call-registry (DNCR). This facility enables customers to restrict unsolicited promotional mail and offers from the bank for any of its products.

Direct selling agents

Most of the top players in the credit card industry make effective use of direct selling agents (DSAs). DSAs have become a major mode of personal selling because most banks have outsourced the selling function to these private agencies. Personal selling and direct marketing efforts are carried out by designated agents called direct selling agents. The approaches adopted by the DSAs include telemarketing and personal selling. DSAs are usually provided with the database of the existing customers, to help them promote new products. The DSAs are also responsible for identifying and winning new customers. They use cold calling to approach customers and generate leads.

The Indian Banks' Association (IBA) has formulated a code of conduct for DSAs. When banks outsource the various credit card operations, they have to be extremely careful that the appointment of such service providers does not compromise the quality of their customer service and the bank's ability to manage credit liquidity and operational risk. In the choice of the service provider, the banks have to be guided by the need to ensure confidentiality of the customer's records, respect customer privacy, and adhere to fair practices in debt collection. Further, the bank should ensure that the DSAs engaged by them for marketing their credit card products scrupulously adhere to the bank's own code of conduct for credit card operations, which should be displayed on the bank's website and be available easily to any credit card holder.

The bank should have a system of random checks to ensure that its agents handle with care and caution their responsibilities like hours for calling, privacy of customer information, conveying the correct terms and conditions of the product on offer, etc.

Call centers

Many credit card marketers rely on call centers to market their credit card products. Since call centers can deal with customers in a more professional manner, the perception of better customer service is stronger. Call centers are provided with the requisite database that contains prospective customer information, and personnel from the center interact with the customers and sell them the products. Since call center staff are trained on communication and etiquette, they can yield better results. Firstsource Solutions Ltd (earlier ICICI Onesource) is one such BPO. It sells banking products including credit cards for many banks.

Public Relations

Credit card marketers also undertake public relations (PR) efforts to promote their card products. This is done on a constant basis to reinforce a positive image for the card. Press releases are one of the tools of public relations. They can focus on special offers designed to evoke some kind of response from the readers/viewers. The offer could be a gift, a free coupon, or concessions on purchase of products or services using the credit card. The marketer has to ensure that the press release reaches the entire target population and generates sufficient curiosity.

As part of their PR campaigns, credit card marketers sponsor cultural and sports events. This is especially true of private banks, which aggressively market credit cards in India. ICICI Bank is one of them. The bank has been using PR as an effective tool in its promotional mix. Exhibit 6.3 describes one such PR effort of ICICI Bank.

RBI Regulations on Credit Card Promotions

The Reserve Bank of India has taken steps to ensure that customers are clear about the various facets of credit card usage. To reduce unethical promotional practices, the bank has issued certain guidelines under the head 'Most Important Terms and Conditions (MITC).' It states that all details on fees and charges, drawal limits, billing details, disclosure, termination, etc., must be printed clearly in font 12 in the promotional material. The details to be mentioned are:

Exhibit 6.3

Public Relations at ICICI Bank

In October 2004, ICICI Bank, India's largest private bank and the leader in the credit card market, launched an affinity credit card with HelpAge India. The card was launched as part of its social responsibility initiative. The press release about the launch explained how the affinity card would benefit the aged. When a card-holder made a purchase with the card, it would indirectly help an old person find a suitable old-age home. To support the PR campaign, HelpAge also organized an inter-generational walkathon at the Jawaharlal Nehru stadium in New Delhi. About 3,000 students from 35 schools across Delhi, along with their grandparents took part in the launch event of the credit card. In the press releases, ICICI Bank also mentioned the asset value of the company as of that year, broad specification of its services, the customer base that it catered to, and the distribution network. It provided the contact details and options like SMS, URL address, phone numbers, etc., for getting in touch with the bank to learn more about its services.

Adapted from "PR Insight: The 'Direct Response' PR Campaign," http://www.cues.org/pls/cuesp/!cues1.main?complex_id_in=3069489.3071923.3072746.11249144.page

- *Fees and charges*: Joining fees for the primary card holder and for the add-on card holder, annual membership fees for primary and add-on card holders, cash advance fee, service charges levied for certain transactions, interest free (grace) period, finance charges for both revolving credit and cash advances, overdue interest charges — to be given on monthly and annual basis, and charges in case of default.
- *Drawal limits:* Credit limit, available credit limit, and cash withdrawal limit.
- *Billing:* Billing statements — periodicity and mode of sending, minimum amount payable, method of payment, billing disputes resolution, contact particulars of 24-hour call centers of card issuer, grievances redress escalation — contact particulars of officers to be contacted, etc.
- *Default:* Recovery procedure in case of default, recovery of dues in case of death/ permanent incapacitation of cardholder, available insurance cover for cardholder, and date of activation of policy.
- *Termination/revocation of card membership:* Procedure for surrender of card by cardholder — due notice.
- *Loss/theft/misuse of card:* Procedure to be followed in case of loss/theft/misuse of card — mode of intimation to card issuer, and liability of cardholder.
- *Disclosure:* Type of information relating to cardholders to be disclosed with and without their approval.

The RBI has stipulated that these aspects have to be disclosed to the customer. The fees and charges have to be mentioned when marketing the card. When a customer fills in the application, it is necessary to inform him or her about the fees and charges, termination/revocation of card membership clauses, and type of information relating to him/her that can be disclosed with and without his/her approval. The welcome kit sent to the customer must contain details of all the aspects just mentioned. The monthly bill must also contain information on fees and charges, drawal limits, and billing related information. In addition, any change in the terms and conditions must be communicated to the customer on an ongoing basis.

DISTRIBUTION

The distribution strategy essentially focuses on decision making with regard to the number of channels, channel integration, and communications to be used. Generally, most marketers adopt multiple channels of distribution, i.e., they use two or more distribution channels. Credit card marketers resort to this kind of strategy as it provides greater market reach and more ways to provide information to customers, both of which have a positive influence on sales. Credit card marketers primarily rely on their branch network for the distribution of their cards. In addition, they use Internet applications, direct mail, and telemarketing.

Branch network

All marketers of financial products and services try to ensure that they have a good network of branches. Branches are points of direct contact between the service provider and the customer. Earlier, credit card marketers relied solely on the branch networks that they built over a period of time. With the advent of technology, banks focused on streamlining back-end processes to focus more on customer service. Branches have also become more comfortable venues from the point of view of the customer. Physical evidence at the branch, in the form of working personnel, information boards, the presence of other satisfied customers, etc., helps the customer in his or her decision making. On the other hand, technology has brought in other channels like the Internet.

Table 6.5 describes some of the other distribution channels used by credit card marketers.

Table 6.5: Other Channels of Distribution

Internet	The Internet has become a favorite alternative for most credit card marketers. Cost savings is one of the primary advantages. According to Jud Linville, president of the Consumer Card Services Group, American Express Co., "Cardholders who are acquired online are 179% more profitable than those acquired through direct mail. The profitability is driven by two factors. The cost to acquire them is 92% less; but most important — they generate 79% higher spending."[2]
Direct Selling Agents (DSAs)	In India, foreign banks and private sector banks use the direct selling agent (DSA) network to market credit cards more than the public sector banks. DSAs are used to increase the reach of the banks to potential customers. Outsourcing the distribution function to DSAs also enables banks to reduce operational costs.
Merchant Establishments	In 2005, there were more than 190,000 merchants in 150 cities and towns across India who accepted payments through cards as compared to 70 thousand merchants in 1999-2000. ICICI Bank has the largest number of merchant establishments, followed by HDFC Bank. The entry of local terminal manufacturers now in the market has increased the number of terminals available, leading to greater distribution. In March 2006, ICICI Bank had 100,000 terminals followed by HDFC Bank with 60,000 terminals. Bank of Baroda was the leader among nationalized bank, with 29,000 terminals[3].

Compiled from various sources

THE CURRENT SCENARIO

Credit cards have been in India for well over two decades. The credit card segment has registered an impressive growth rate since 2000 and was around 40 per cent in 2005[4]. The credit card subscriber base itself has grown at a phenomenal rate of 30-35 percent a year over the last few years. The rapid growth in the subscriber base can be attributed to the aggressive issuance of credit cards by the top five players in the industry. ICICI Bank has become the number one surpassing established multinational banks like Citibank and Standard Chartered. The credit card segment in India is estimated at $4 billion and is expected to grow at the rate of 35% per year.[5] Citibank was the leading credit card issuer in India, in the 1990s. SBI Card, a joint venture between GE Money and State Bank of India (SBI) achieved the two million customer base in January 2006 within a span of eight years. As of December 2006, ICICI Bank is the leading credit card marketer in India followed closely by Citibank (See Table 6.6 for the top six credit card marketers and their customer base in March 2005).

The following sections discuss some of the trends and issues in the credit card segment in India.

Table 6.6: Credit Card Holders in India Per Bank – March 2005

Name of the Bank	Number of Cards (in million)
ICICI Bank	3.67
Citibank	2.70
State Bank of India	1.98
StanChart	1.90
HDFC Bank	1.26
HSBC	0.90

Source: http://www.ventureinfotek.com/pdf/PaymentCardIndustry Survey 2005.pdf

Credit Card Usage

Of the Indian population, 14 percent possess credit cards but total transactions through credit cards account for only 1 percent of personal consumption expenditure, which indicates a tremendous opportunity for growth in this segment.[6] With increasing competition, more customers and greater acceptance of credit card usage, certain issues and trends have come to the fore. In India, banks on an average spend Rs. 20,000 per year to acquire a credit card customer. This is almost half of the average international spending, which is US$900 (around Rs. 40,000/- per year). Credit card marketers in India face two tasks: First, to increase the frequency of the credit card usage/spending, and second, to get more retail and other businesses to accept credit card payment. The number of merchant establishments can be increased if the marketers increase the tie-ups with the retailing sector.

Increasing usage

Marketers in India have a long way to go as far as increasing credit card usage is concerned. This can be ascertained by the fact that nearly 72 percent of credit card holders in India use the credit card less than twice a month. The comparable international figure for infrequent usage is less than 15 percent. In developed countries, 31 percent of the credit card holders use their credit card more than 10 times a month.[7] Credit card spending is primarily dependent on promotional offers and the interest rates set by marketers. Now marketers are trying to devise different strategies to make customers use their cards. Many companies have tried to achieve this by attracting customers with good promotional offers.

We have already discussed the importance of co-branded credit cards, especially in terms of increasing brand awareness and usage. Banks have gone a step further and launched the white label credit card that also involves a tie-up with a partner. In contrast to the co-branded credit card, the white label card does not have the issuer's logo. Tata Sons and State Bank of India's (SBI) subsidiary, SBI Cards, launched the first white label credit card in India in early 2006. The Tata credit card has the Tata brand on the face of the card while SBI Cards is the issuer and also bears the credit risk. But its logo does not feature on the face of the card. The white-label credit card is the country's first card offering a large-scale, multi-brand loyalty program, called the Tata Privilege Program. Tata credit card holders can avail of benefits from Tata Group companies like Tata Motors, Titan, Tanishq, Voltas, Tata AIG, Westside, Star India Bazaar, Tata Indicom, and VSNL. ICICI Bank also plans to launch a white-label credit card in association with Loyalty Services and Research Ltd (LSRL), a company formed by a group of venture capitalists.

Another means to increase usage is to offer facilities to make purchases. For instance, ICICI Bank provides an EMI (Equated Monthly Installment) option for the purchase of Microsoft Xbox 360 products from designated Microsoft dealers. ICICI Bank credit card holders can now make an initial payment of Rs. 899 and pay Rs. 3,270 as EMI for six months to get the Xbox 360 Core console, which costs approximately Rs 23,990 (maximum retail price excluding taxes).

Technology

As a product, the credit card continues to evolve. The current form includes a magnetic strip on a plastic card. The newer versions being developed are credit cards enabled with microchips, called Smart Cards. Smart Cards keep track of the accumulated reward points and also guard against frauds. These Smart Cards offer marketers two kinds of advantages. They help them to easily keep a record of the reward points accumulated by the credit card holder and also enable a higher level of scrutiny and check for authentication to prevent fraud. Marketers in India also need to incorporate these changes to conform to the 'European MasterCard Visa' (EMV)[8] standard for secure transactions at the point-of-sale. EMV migration is one of the greatest challenges that banks will have to face in the coming years. Although it is well down the road in the UK, it has yet to be implemented on a full scale in Asia.

Credit Cards for Corporate Use

Companies find it easier to meet and manage the official expenses of employees with the help of customized corporate cards. Corporate credit cards are tailored to the needs of corporate customers and they help companies manage their employees' travel and entertainment expenses. For example, American Express focuses on credit card marketing to the corporate sector. American Express issues Amex cards, which are tailored to the needs of corporate customers. In India, the Amex card is billed in two ways -- either as an INR billed or as a US dollar billed card. With the INR billed type, payments made anywhere in the world are converted to Indian Rupees.

Fraudulent Practices

Credit card fraud is on the rise in India. Any sort of unlawful handling of a credit card account by a person for whom the account was not proposed amounts to credit card fraud. To curtail this kind of fraud, and assure the consumer about the security of the card, the credit card issuer has to incorporate certain risk management methods. Credit card fraud assumes different forms. Table 6.7 shows some of the most prevalent credit card frauds.

Table 6.7: Credit Card Frauds

Application fraud	This takes two forms viz., familiar and unfamiliar. In the first kind, a close relative or friend gets the personal details of the cardholder and uses the card. In the latter, an unknown or unrelated person gets hold of the card details with the help of Internet search portals and databases.
Lost and stolen cards	These are the most common cases of fraud. Once in possession of the credit card, the criminal gets direct access to the account of the victim.
Non-receipt (mail intercept)	In this type, the perpetrator of the fraud intercepts the card in the victim's mail. However, most credit cards have card activation programs which require the customer to call and authenticate the card in order to gain confirmation from the bank to initiate purchasing with the credit card.
Counterfeit cards	These are fake cards created by criminals. It is possible to create such cards if the criminal possesses valid credit card numbers. The information is then encoded on to the magnetic strip of a blank card. The Internet provides information on how to create counterfeit cards, which adds to this menace.
Account takeover	In this case, the criminal first obtains adequate information so as to represent the target person in the card issuing bank. The individual first requests a change in address on the account. He/she later calls to report the theft or loss of the credit card. As a result, a new card is issued but now the owner of the new credit card account is the imposter.

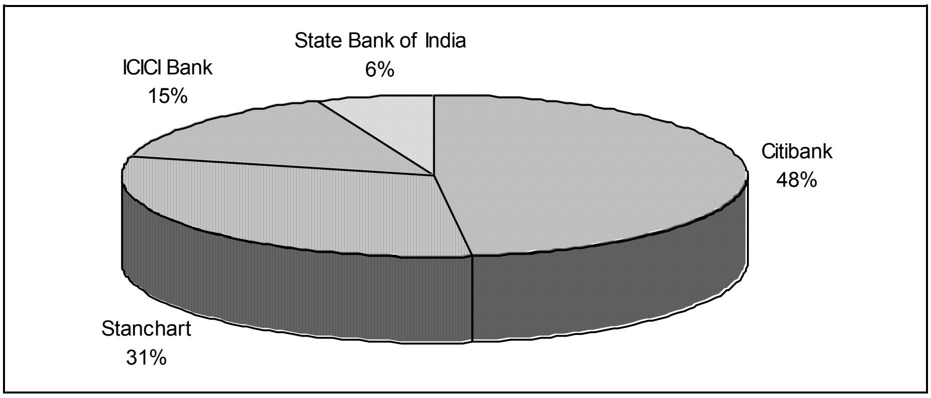
Adapted from Burns, Peter; and Stanley, Anne. "Fraud Management in the Credit Card Industry." www.phil.frb.org, April 2002.

Privacy Issues and Soft Targeting

In India, credit card marketers by and large deploy the 'push strategy' where the prospective customer is contacted through a customer database via e-mail, telephone, personal contacts, mailers, etc. In their efforts to attract and increase the number of customers, marketers tend to ignore the comfort levels of the prospective customer. They intrude into the personal space and time of the customer, thereby raising the issue of individual privacy. The Indian government has made provisions to safeguard the individual's privacy through a 'Right to Privacy' law. As a result, marketers need to first confirm whether a customer is willing to receive product related information before proceeding further with their sales-related communications.

Aggressive marketing, especially by DSAs, has resulted in a loss of image for the card issuer. This is due to persistent phone calls and receipt of unsolicited promotional mail. The RBI has made provisions to stop this through a code of conduct for DSAs (discussed earlier) and other regulations. The number of credit card related complaints is also on the rise. These complaints include wrong billing and additional fee demands by marketers. This has resulted in a loss of customers and absence of payments from existing customers. Figure 6.1 gives a break-up of the share of some of the leading banks in complaints related to credit cards, as of December 2005.

Figure 6.1: Major Banks and Credit Card-related Complaints - 2005



Adapted from "Beware, Card Users!"
http://www.domain-b.com/investments/general/2006/20060125_users.html

CRM in Credit Card Marketing

Customer management is the key to success for credit card marketers. There are primarily two reasons for this: first, the pace at which the financial services industry as a whole is embracing modern technology, and second, the increasing competition due to the entry of new players and the increasing focus on new product development. Every player in the financial services industry is eyeing a major share in the market. This has led to the evolution of processes (like CRM) by which the service providers can retain existing customers and also acquire new ones. CRM involves the ability to measure the customer's intentions well in advance and launch products and services even before an explicit demand is made. For CRM to be successful, an integrated system that includes people, process, technology, and data have to be put in place. For the credit card marketer, good customer service and better customer retention are the two major challenges. These two challenges are discussed here.

Customer service challenge

Service delivery is a key differentiator in the credit card market. Credit card marketers try to improve satisfaction on various service parameters and improve their service delivery standards.

Training: Studies have shown that the contact between the employees and the customers is the key determinant in customer satisfaction levels and is often the most important factor that customers look into (even more than price) before switching to a competitor. Hence, marketers must ensure that their personnel are adequately trained. The communication from the marketer to the customer should be clear and well reasoned. The representatives handling customer calls and queries should be capable of providing clear and logical explanations to customer queries.

Billing and payment: Errors in billing are another important cause of customer dissatisfaction. The customers get annoyed by faulty billing and expect quick remedial action from the credit card issuer.

Customer retention

Customer retention is another challenge for a credit card marketer where service delivery standards determine the fate of the marketer. Customer retention is the ability of the marketer to retain existing customers despite attempts by competitors to make them switch. Retention of customers is a key performance indicator for service providers. Studies have shown that it has the power to increase profits. The formulation of the customer retention strategy involves four steps. These are market structure definition, segmentation, recognizing service needs, and providing segmented service.

Market structure definition: The first task is to have a clear definition of the market structure. This requires a holistic approach on the part of the credit card marketer.

Segmentation: The customer base should be segmented properly and it should be based on parameters such as age, gender, etc.

Recognizing service needs: The needs of the segmented customer population have to be thoroughly analyzed as service needs vary from segment to segment.

Segmented service strategy: Finally, suitable strategies have to be evolved. These strategies should be segment-specific.

SUMMARY

Credit cards, charge cards, and debit cards facilitate cashless transactions. The credit card business is a low margin, high volume business. Branding is of immense significance in the credit card industry. Different types of branding strategies are used of which co-branding is the most commonly used approach. Co-branding involves the alliance of two brands for mutual benefit. Effective branding requires an understanding of brand metrics and the focus areas for effectiveness.

The pricing of credit cards is a difficult task. The primary factors influencing pricing are the consumer price awareness and the price-quality cue. Annual percentage rates (APR) and fees are two important components in pricing. Risk-based pricing is a commonly followed pricing method where the pricing of credit cards is based on an assessment of the risk profile of the customer. The major components of pricing are the annual percentage rate (APR) and the different types of fees that are charged by credit card marketers.

Credit card marketers make use of all the elements of the promotional mix. The advertising campaigns are created with certain advertising objectives. The advertisements can have different types of appeals. The focus of the content also segregates ads into ads with soft value and ads with hard value. Promotional offers are the most prevalent approach to sales promotion. A thorough study of the market and the competitors is needed for devising an effective sales promotion strategy. Sales promotion techniques include introductory offers, cash back schemes, rewards programs, and cause-related marketing.

Another element of the promotional mix is personal selling. Credit card marketers use direct sales personnel, direct selling agents, direct mail, and the Internet as personal selling tools. Credit card marketers also use public relations (PR) efforts as part of their promotional mix. The Reserve Bank of India has issued guidelines to curb unethical promotional practices.

The kind and number of distribution channels, the sales force, and strengthening of the branch network are to be given emphasis as part of the channel decisions. The sales and distribution channels are common for most marketers. Bank branches are the predominant means of distribution. In addition, the advent of technology has led to the use of call centers, the Internet, and creation of terminals at merchant establishments.

The various trends and issues in the credit card industry in India include -- ways to increase credit card usage by retail consumers and corporate customers, importance of CRM, technology in marketing, issues related to credit card fraud, aggressive selling, and privacy related issues.

End Notes:

[1] Touchpoint Mapping™ improves customer experiences and relationships through Touch point Optimization.

[2] AMEX acquisition effort shifts to the net." CardLine. 2006, Vol. 6 Issue 30, p34.

[3] http://www.ventureinfotek.com/pdf/Payment%20Card%20Industry%20Survey%20-%202005.pdf

[4] http://www.ventureinfotek.com/pdf/Payment%20Card%20Industry%20Survey%20-%202005.pdf

[5] "Card now 2 million strong and growing." http://www.indiantelevision.com/release/y2k6/jan/janrel13.htm,SBI

[6] 'Credit Cards will soon become mass products.' http://www.ventureinfotek.com/pdf/July-August86.pdf

[7] Atul K Sawant. 'Credit Cards - Emerging Trends and Concepts.' Bank Quest. October-December 2005.

[8] The EMV standard was developed by Europay, MasterCard, and Visa following the introduction of increasing numbers of chip card programs. EMV specifications ensure there is interoperability between chip cards and terminals around the world, regardless of the manufacturer, the financial institution, or where the card is used.

Chapter 7

Non-life Insurance

In this chapter, we will discuss:

- Product Range in Non-life Insurance
- Product Planning and Development
- Pricing of Non-life Insurance Products
- Promotional Mix
- Distribution
- The Current Scenario

According to historians, insurance was first used in Sumeria and Babylonia (present day Iraq) around 3000 BC. Sumerian merchants are believed to have contributed to a common fund which was used to compensate for the losses incurred by members of the merchant community (Bandits and pirates who frequented the trade routes were the cause of most of these losses). Around 1800 BC, the Babylonian King Hammurabi introduced laws that governed risk transfer activities. Around 1200 BC, merchants of Phoenicia (present day Lebanon), used a form of insurance called 'bottomry'. The ancient civilizations of Greece and Rome are also believed to have used a form of insurance. There is evidence that between the 5^{th} and 15^{th} centuries in England and Italy, 'guilds' compensated workers and their families in the event of illness or death. Modern insurance began in the late 17th century with the practice of underwriting. Insurance in the current form deals with and manages different kinds of financial risks.

Insurance may be broadly classified into life and non-life insurance. Non-life insurance is referred to as Property & Casualty insurance in the west. In India, there were only four non-life or general insurers till the year 2000, all of them were in the public sector. This changed when the insurance sector was opened up to private players in 2000. As of December 2006, there were 14 players in the non-life sector, the latest entrant being Star Health and Allied Insurance. Banks have also entered the non-life insurance sector. Allahabad Bank, Karnataka Bank, Indian Overseas Bank, Dabur Investment Corporation, and Sompo Japan Insurance Inc. have tied up to form a non-life insurance company. Similarly, Bank of Maharashtra has tied up with the Shriram Group and South Africa's Sanlam Group.[1]

In this chapter, we will first discuss the product range in the non-life insurance sector. We will then focus on the marketing mix decisions of non-life insurance marketers, including product planning and development, pricing structures, promotional mix, and distribution.

PRODUCT RANGE IN NON-LIFE INSURANCE

A non-life insurance contract is different from a life insurance contract. A life insurance contract is a long-term contract, while a non-life insurance contract is a one-year contract that may be renewed. The risk, namely 'death', is certain in life insurance. The only uncertainty is as to when it will take place. In non-life insurance, on the other hand, the insured event may or may not take place. Besides, it is difficult to determine the economic value of life, whereas the financial value of any asset to be insured under a non-life insurance policy can be determined.

Most non-life insurers offer cover for a range of material risks. The different non-life/general insurance products include the following classes: property insurance, motor insurance, liability insurance, pecuniary insurance, personal accident insurance, and health insurance. In terms of the customers, insurance products may be classified into retail products, that is, products purchased by individuals, and corporate products, that is, products purchased by organizations.

Retail Products in Non-life Insurance

These policies are mainly targeted at individual/household customers. Some of the most common retail non-life insurance products cover risks associated with motor vehicles, home, medical conditions, accident, travel, baggage, transit, postal value, pet, liability, and fidelity guarantee. Some of these products are discussed here.

Motor vehicle insurance

All types of personal and commercial vehicles such as two-wheelers, three-wheelers, four-wheelers, passenger buses, and trucks are covered under the motor vehicle insurance. Vehicle insurance offers the policyholder cover against every conceivable risk related to the vehicle – theft, damage, death of driver and passengers, and damage caused by the vehicle to another person or property. In India, third party liability[2] coverage is mandatory. Motor vehicle insurance may also cover the loss due to theft or own damage, and cover for occupants of the vehicle. Earthquake coverage is usually inbuilt in this insurance scheme.

For instance, Tata AIG General Insurance Company Ltd. (Tata AIG) offers AutoSecure that provides a comprehensive insurance cover for cars. In addition to third party liability, AutoSecure also has certain add-ons like personal accident coverage offered against an extra premium. Other features include tie-ups with reputed garages to ensure faster claims processing and quick repairs. Also, drivers who follow safety rules are rewarded under the safety bonus program with a reduction in premium on renewal of the policy if no claim has been made in the previous year.

Personal accident insurance

Personal accident insurance is one of the most commonly marketed non-life insurance products in India. The personal accident policy covers the policyholder for one or more contingencies like temporary total disability, permanent partial disability, permanent total disability, or death. The premium does not vary with age as in life insurance but depends on the sum assured, the extent of cover, and the profession of the policyholder. In the event of such contingencies, a personal accident policy will provide for the payment of a lump sum, which may either be the full sum assured or a percentage of it. For example, Tata AIG has launched a personal accident policy 'Shanti' wherein the coverage amount may go up to Rs 10 million[3]. Personal accident insurance does not cover death due to natural causes, war, civil disorders like riots, suicide, pregnancy, intentional self-injury, sickness or disease, injury sustained under the influence of drugs or alcohol, etc.

Health insurance

A health insurance policy is different from a personal accident policy. While a personal accident policy provides cover in the event of an accident, a health insurance policy reimburses hospitalization expenses for illness or accidental injury during the policy period. For example, the Mediclaim policy offered by the United India Insurance Company Ltd. covers expenses incurred by the insured for hospitalization for illness/diseases or injury sustained. These include hospital charges (room, boarding, and Operation Theater); fees for surgeon, anesthetist, nursing specialist, diagnostic test charges; cost of medicines, oxygen, etc.; and the cost of appliances like pacemaker, artificial limbs, etc. The premium rate is usually decided based on the age of the insured person and the sum insured.

Householder's insurance

A householder's insurance policy, also known as the householder's package policy, provides insurance for buildings and possessions. In addition to insuring the policyholder against loss/ damage to the house and its contents including jewelry and domestic appliances, it may also cover third party liability, and the loss of baggage during travel within India. This policy covers risks associated with natural calamities like floods, earthquakes, and cyclones; and incidents such as riots, strikes, burglaries, and acts of terror; leading to damage to the house or its contents. Earthquake coverage is inbuilt in the householder's insurance scheme. A standard householder's insurance policy generally covers ten sections -- Fire & Allied Perils, Burglary & House breaking including larceny and theft, All Risks (Jewelry & Valuables), Plate Glass, Breakdown of Domestic Appliances, T.V. Set including Video Cassette Player/Video Cassette Recorder (All risks), Pedal Cycles (All Risks), Baggage Insurance, Personal Accident and Public Liability. A discount or reduction in the premium is given to the customer based on the number of sections opted for.

Miscellaneous non-life insurance policies for retail consumers

For individuals, there are a host of other non-life insurance products such as travel insurance, baggage insurance, transit insurance, and pet insurance. Table 7.1 lists these policies with a brief description.

Table 7.1: Types of Miscellaneous Non-life Insurance Products: Retail

Non-life Insurance Product	Description
Baggage insurance	The policy provides for cover against loss or damage to accompanied personal baggage due to fire, riot and strike, terrorist activity, or theft or accident during the course of the journey including stoppages en route anywhere in India. Ex: the Suhana Safar policy of United India Insurance Co Ltd.
Travel insurance	The policy provides cover for risks one may be exposed to during an overseas trip. Generally, it covers death, personal accident, medical expenses, repatriation, loss of checked baggage, loss of passport, third party liability, etc. Ex: Gold and Silver travel insurance plan of ICICI Lombard.
Transit insurance	The policy covers loss of or damage to household assets when shifting house due to fire, theft, pilferage, water, etc.
Pet insurance	The policy covers pet owners against the death of their pet due to natural causes or accident. The pet must be between 2 months and 8 years. Ex: Dog insurance policy of Allianz Bajaj General Insurance.

Compiled from various sources

Corporate Products in Non-life Insurance

Organizations opt for non-life insurance policies to protect their property and their employees (in some cases as part of the employee benefits program through group accident policies). Some of the common non-life insurance policies are group health insurance, cargo insurance and hull insurance, industrial insurance, social insurance, etc.

Group health insurance

Non-life insurance companies offer group health insurance and group accident insurance policies. These policies are for specific groups and the premium is comparatively lower than that of the corresponding policies for individuals (retail). The discounts on premium are based on the size of the group. Tata AIG, for example, offers group policies such as voluntary accident guard, group multi-guard, and group personal accident. The voluntary accident guard is a group accident insurance policy suitable for employees of a firm and the premium is collected in the form of salary deductions. The policy covers individual employees and their family members.

Cargo insurance and hull insurance

Cargo insurance and hull insurance are often referred to as marine insurance. Cargo insurance is one of the oldest non-life insurance products and covers risks associated with transportation of goods through rail, road, sea, post, or air. It can be broadly classified into two types – import/export cargo and inland cargo.

Export or import cargo: This policy provides insurance for cargo transported by ships. Cargo insurance may be offered with multiple options. For example, consider the marine import policy offered by ICICI Lombard. The coverage of this policy is categorized into three types -- A, B, and C. Under the A and B types of policy, earthquake risk is also covered along with risks that may occur during transit, storage, and while the goods are being transported from warehouse to warehouse (of both the seller and the buyer). If the policy subscribed is of the C type, then the policy holder has to pay an extra premium to get the earthquake cover. The insurance rate is determined based on factors like the scope of cover, nature of cargo, past claims experience, and mode of payment convenience. On payment of additional premium, the risk cover can extend to war, strikes, riots, etc.

Inland cargo: Inland cargo insurance covers the risks associated with inland transit of export/import cargo. The inland transit may be through rail, road, air, government and private postal services, etc. For instance, Reliance General Insurance Company Ltd[4] offers inland cargo insurance with two variations, A and B. All types of physical losses including those caused by earthquakes are covered under policy A. Policy B is a more restricted cover and does not include risk cover due to earthquake.

Hull insurance: The policy covers loss/damage to the property insured due to a fire or an explosion, stranding, sinking in sea; overturning, derailment (of land conveyance); collision; etc. This insurance is applicable to loss or damage to ships, tankers, bulk carriers, smaller vessels, fishing boats, and sailing vessels.

Industrial insurance

An industrial insurance policy insures the movable and/or immovable property of organizations against losses that arise due to accidents. There are various types of industrial insurance policies to cover property losses. They include industrial all risk policy, boiler and pressure plant insurance, contractors' plant and machinery policy, and machinery breakdown policy.

The industrial all risk policy offered by United India Insurance Co Ltd. covers all the risks (other than petrochemical risks) having a minimum sum insured of Rs. 1 billion. The contractors' plant and machinery policy provides risk coverage for engineering related tasks in both the construction and manufacturing sectors. For instance, the Contractors All Risk Insurance policy offered by the Oriental Insurance Company covers loss or damage with regard to the contract works, construction plant and equipment, and damage either to the property or individual during the execution of civil engineering projects. This policy is more suited to civil engineers, architects, contractors, etc.

Fire insurance

This is another common policy offered by most general insurers. There are different types of fire insurance policies such as fire insurance for dwellings and contents, standard fire and special peril policy, and fire loss of profit policy.

Fire insurance for dwellings and contents: Unlike the householder's policy, this is not a package policy. This policy covers institutions, offices, shops, etc., against fire, lightning, explosion/implosion. If required, earthquake cover has to be taken as an add-on on payment of extra premium. For example, ICICI Lombard offers a policy that covers the risks due to fire, lightning, overflowing of water tanks, missile testing, etc. The premium is determined based on the type of construction and the occupancy of the building.

Standard fire and special peril policy: Buildings, machinery, and massive industrial complexes are covered under this policy, which provides coverage for as many as twelve risks. Earthquakes are not one of the twelve risks covered. It is an add-on cover, for which the customer needs to pay extra premium. For instance, Bajaj Allianz offers a policy to cover against any damage to the business premises of the insured that will interrupt business.

Fire loss of profit policy: This policy can be taken only if a Standard Fire and Special Perils Policy exists for the risk. The risk covered includes loss of net profit due to the stoppage of business as a result of an insured peril, standing charges which continue to accrue in spite of stoppage of business, and additional expenditure incurred by the insured to maintain normal business activity during the period in which the normal business is affected. The indemnity period commences with the date of damage and lasts till such a time as the business is restored to its pre- damaged level or the period stipulated in the policy, whichever is earlier. This policy insures the earnings of the business lost during the indemnity period.

Miscellaneous non-life insurance products for corporate customers

A range of insurance products comes under this category. Many companies offer insurance policies like shopkeeper's policy, fidelity insurance, jewelers' block policy, and liability insurance. A brief description of these products follows.

Shopkeeper's policy: This policy covers against all possible risks incurred by a shopkeeper. For instance, New India Assurance Company Ltd. offers a policy to shopkeepers whose shop (and its content) value does not exceed Rs. 1 million.

Fidelity insurance: Fidelity insurance covers against financial losses caused by acts of infidelity (omission and commission) of the insured's employees. The various acts of infidelity are forgery, embezzlement, larceny, misappropriation, and default. One variant of this insurance is the banker's blanket insurance that provides protection against losses incurred by the banks due to employee infidelity. The coverage of losses varies from insurer to insurer. For instance, the 'Bankers Indemnity policy' offered by IFFCO Tokio General Insurance covers losses caused due to employee fraud, misappropriation of funds, infidelity by agents, robbery in transit, etc.

Jeweler's block insurance: All jewelers and jewelry establishments are eligible for this product. The 'Jeweler's Block Insurance' offered by the National Insurance Company provides risk cover against currency loss, property on the premises and during distribution, transit through post or air freight, etc.

Liability insurance: It covers losses incurred due to omissions and errors of the insured. It includes a public liability cover (individual actions leading to a material loss to others) and a professional liability cover (work-related mishaps leading to a loss to clients). The officers, directors, and other individuals holding senior positions are responsible for certain functions and activities within the organization. These individuals can opt for public liability cover policies meant for such professionals. Such policies are offered by various general insurers like the National Insurance Company, the Oriental Insurance Company, the United India Insurance Company, and the New India Assurance Company. For instance, the 'Directors and Officers liability insurance' offered by the National Insurance Company essentially provides cover against liability to shareholders, customers, suppliers, creditors, employees, and other third parties. After the amendments to the Companies Act, such a policy has been made mandatory for the top managers (directors, CEOs) of companies. The Professional Indemnity Insurance policy for doctors, provided by the National Insurance Company Ltd., covers any errors or omissions committed by a registered medical practitioner while rendering medical services. It provides the doctor cover against financial loss due to any kind of bodily injury or death caused or alleged to have been caused to the patient out of professional negligence.

In addition to the products just mentioned, there are a host of other non-life insurance products like cattle insurance, poultry insurance, aquaculture insurance, and the farmer's package. Exhibit 7.1 outlines a couple of niche products in non-life insurance.

Exhibit 7.1
Niche Products in Non-life Insurance

Non-life insurers are launching new policies that cater to specific customer segments. These policies are developed keeping in mind each segment's unique needs. For example, ICICI Lombard has a weather insurance policy for farmers. Similarly, many general insurers in the US and the UK have entered the domain of intellectual property and have launched patent insurance policies.

Weather insurance: ICICI Lombard's weather insurance product for farmers was developed in alliance with the World Bank, ICICI Bank, and BASIX -- a Hyderabad-based microfinance institution. It is targeted at farmers, especially those below the poverty line. The premium varies from farmer to farmer and depends on the geographical location of the farm and the risks associated with it. For ensuring the authenticity of the weather information, ICICI Lombard has tied up with the Indian Meteorological Department.

Patent insurance: Patent insurance is useful for developers of new technology, new products, new designs, etc. The crucial factor here is newness. The premium is generally determined on the basis of the nature of the product to be covered. In general, the premiums fall in the range of 2 to 5 percent of the total insured amount. For a patent insurance cover of say US$ 1 million, the minimum premium to be paid would be in the range of US$ 25,000. Patent insurance is often sought by pharmaceutical companies.

Sources: Srinivasa Raghavan, TCA "Changing Face of Indian Insurance Market." http://www.insure2bsecure.com/insure/NewsArticles/articles/changing_face_of_indian_insuranc.asp;"Teflon Coating on Armour?", http://www.domain-b.com/finance/insurance/2006/20060415_insurers.html; "Patent Insurance: An Inside View." http://www.domain-b.com/finance/insurance/2006/20060415_inside.html; and "Who Should Obtain Patent Insurance?" http://www.domain-b.com/finance/insurance/2006/20060415_obtain.html.

PRODUCT PLANNING AND DEVELOPMENT

The insurance sector, like the fast moving consumer goods (FMCG) segment, requires a high level of product innovation. The more successful players in this sector launch new products on a continuous basis. New product development is a tough task for any organization and needs concerted efforts. Before the opening up of the insurance business, non-life insurance companies in India launched new products only for reasons such as poor performance of their existing products or because of political compulsions. Now, with the deregulation of the sector and increasing competition, most private players are looking at new product development as a strategic imperative. They see it as a way to reach new customer segments and fulfill their needs better than the competitors.

New Product Development

Successful product development needs both a well-developed and clearly defined internal process and a receptive external environment. The latter requires a customer who is receptive to new ideas. In addition, for successful new product development, it is advisable to form a group of cross-functional experts with a variety of experience and from various hierarchical levels. They should focus on learning about the unmet needs of the consumers and then develop suitable products. For instance, the American International Group Inc. (AIG) has a separate corporate product development group within the organization that focuses solely on developing financial products for the corporate segment. The company also solicits opinions on new products and requirements from existing and potential customers through its portal, www.aigproduct.com. This information is then passed on to the product development group.

A useful product development strategy could be to meet the demand in areas that are currently not being served. The general insurance companies in India have focused more on the manufacturing sector. However, with the services sector contributing a major share of the GDP, products catering to this sector will offer immense opportunities for business growth.

Customization

The number of players in the general insurance segment has increased and due to the resulting competition, the insurers have been forced to make changes in their products. While insurers continue to offer products in the broad categories of home insurance, medical insurance, auto insurance, and overseas travel insurance, they also try to differentiate their offering from those of their competitors by customizing the product to suit the customer. For example, earlier, the overseas travel insurance policy was the same for everyone going abroad. But now insurance marketers are offering travel insurance policies customized to customer groups like students, tourists, and business travelers. ICICI Lombard General Insurance Company, for instance, offers different overseas travel insurance policies. It has a plan for leisure and business travelers – ICICI Lombard Overseas Travel plan (Platinum, Gold, Silver, Bronze, Family, Multi-trip plans), and another plan for students – ICICI Lombard Student Overseas Insurance Plan (Gold, Silver, Bronze, Plus plans).

However, there is no great difference among the products offered by different companies. By and large, the companies have similar types of products; often the differentiation comes in through the riders. Riders are the extras or the add-on features that are provided with the basic cover; an extra premium is charged for each rider.

PRICING OF NON-LIFE INSURANCE PRODUCTS

The pricing of insurance products is quite different from that of tangible products. In the case of tangible products, the cost of inputs is available, which makes it easier to arrive at a price. Insurance products, on the other hand, are priced according to the risk that the insurer assumes. Based on the risk assumed, the premium charged varies. However, assessing and quantifying the risk is a difficult task and can only be handled by experts in the field of actuarial sciences.

Life Insurance vs. Non-life Insurance

The pricing of life insurance products is simpler than that of non-life insurance products. The pricing of life insurance and non-life insurance products can be differentiated on the basis of rating mechanism, constancy, correctness, and the factors considered for pricing. Table 7.2 gives an overview of the differences between the pricing of life and non-life insurance products.

Table 7.2: Differences between the Pricing of Life and Non-life Insurance Products

Basis	**Life Insurance**	**Non- life Insurance**
Rating mechanism	Deciding on the extent of risks is simple. The use of age and gender is more rational and easy to understand. It varies only for the group life insurance policies.	The risk rating process is complicated. It makes use of several rating systems for different kinds of exposure to commercial risks.
Constancy	The rates do not change frequently as mortality by and large remains unchanged. Overhead costs also do not experience significant changes from one year to another.	Rates experience continuous changes owing to the kind of operating environment and also the varying claim experiences.
Correctness	Rating in life insurance is more accurate. This is due to the relative constancy in mortality, expenditures, and investment income. Also the adverse events are certain to occur. Claims are known in advance to the insurer.	The rates are not as accurate as in life insurance policies. This is because losses are circumstantial, which are uncertain. Only the maximum amount is specified but not the loss payment amount.
Pricing factors	In life insurance, the main factors used for determining the premium rates are mortality, expenses, and rate of interest.	The factors considered when pricing general insurance products are claims cost, business acquisition cost, management expenses, margin for fluctuations in claims experience, and a reasonable profit.

Adapted from P K Gupta, "Pricing of Insurance Products: Actuarial to Managerial." Management Accountant, ICWAI, February 2004.

Factors Affecting the Pricing of Non-life Products

Factors that must be considered in insurance product pricing are risk costs, insurer overheads, marketing and distribution costs, claims handling costs, and profit margin. In addition, some important factors that non-life insurance marketers consider are product definitions (including add-ons), portfolio performance, packaging, investment return, and reinsurance costs. Pricing is also loosely linked to inflation, valuation levels, economic cycles, and changing weather patterns.

These factors affecting the pricing structure are broadly categorized into portfolio level, case level, and other factors.

Portfolio level factors

The portfolio level factors include a combination of costs which affect the price of the non-life insurance product. These include costs like average claims expenditure, reinsurance costs, acquisition costs, servicing costs, contribution to profit (profit margin), and cost of value additions offered, if any, to the customer. Two of these costs are discussed here.

Claims expenditure: Claims settlement by the insurer is a major activity and it involves huge costs based on the nature of the claim made. Claims expenditure involves costs such as burning costs[5], exposure costs[6], and payback costs[7].

Reinsurance costs: Reinsurance is a means by which insurance companies transfer the whole or part of the risk of losses arising from their issued policies to other insurance companies or to reinsurance companies. The General Insurance Corporation of India (GIC) is the national reinsurer in India and provides insurance cover in the form of assuring continuity after a loss and providing guarantees for non-life insurance companies.

Case level factors

Pricing insurance products at the case level or the individual level is a more specific approach. In this category, the insurance company essentially looks into the differentiation of the risk potential of the policyholder. The risk level of the policyholder is compared to the normal standard risk potential to check if it falls above or below the set standard. The price of the premium is then fixed accordingly.

Other factors

Apart from portfolio factors and case level factors, there are other factors that influence the pricing decisions of the insurers. Some of these factors are investment practices followed by the insurer, inflation rate, exchange rate, cash flow underwriting, and pay out patterns.

Pricing Objectives

The underwriting and the actuarial departments are responsible for the determination of the insurance product prices. Insurance marketers do not necessarily follow the prices set by the actuaries and the underwriters. This is because the prices set by them are based on statistical calculations rather than on competition or other factors. The marketers tend to cut down on these prices to attract customers. Pricing for non-life insurance products in India was highly regulated till December 2006. The Tariff Advisory Committee (TAC) set up by the Insurance Regulatory and Development Authority (IRDA) was the regulating authority. It regulated the rates, advantages, terms and conditions offered by the insurance marketers with regard to fire, marine, motor, engineering and workmen (group). These rates were known as statutory rates.

All other non-life insurance products came under non-tariff products, where the pricing is not regulated. The last section of this chapter focuses on the changing scenario with the IRDA detariffing certain general insurance products.

Every insurance marketer has different pricing objectives based on which the actual price is set. The factors are adequacy, reasonableness, fairness, consistency, and flexibility.

Adequacy

The premium should be able to generate sufficient income to provide for claims expenditure, administrative expenses, and the cost of capital (interest payment to creditors and dividend distribution to shareholders). Besides, the profits should be sizable enough to fund continuing growth and expansion of the insurance firm.

Reasonableness

The rates should not be so high that they result in abnormal gains for the insurance companies. A 'reasonable' price is the price justified considering the free market condition that the company is operating in.

Fairness

The pricing should ensure that there is no unfair discrimination among consumers. The premium rates must be different across heterogeneous groups and the same for homogeneous groups.

Consistency and flexibility

The rating system followed should be easy to understand with little scope for confusion. There should not be frequent changes in the rates. At the same time, the rates should be flexible enough to be revised at short notice to minimize losses.

PROMOTIONAL MIX

Most consumers in India perceive insurance primarily as a tax-saving instrument. Only a small portion of the population looks at non-life insurance policies as an instrument that actually shields the policyholder during emergencies. So insurance marketers need to first educate the consumers of the potential benefits of insurance policies. Insurance marketers develop general or specific advertisements to attain a particular level of consumer awareness for a product. The general approach focuses on the entire market whereas the specific approach targets a particular customer segment.

The promotional mix in the Indian non-life insurance industry is primarily centered on advertising. Personal selling and direct marketing are discussed as part of the distribution strategy. Sales promotions and public relations are not used to a great extent. Sales promotions are the least preferred option in the promotional mix for non-life insurance products. The IRDA has imposed restrictions on offers including rebates on commission/brokerage given by the agents/brokers to the customers.

Advertising

Advertising is critical to the success of the insurance product. It is one of the effective ways of communicating information to prospective policyholders. The non-life insurance marketers have to ensure that their advertising campaigns comply with the advertising norms set by the IRDA. The advertisements need to be unique in their approach so as to create an interest in the customers. Creation of interest is important as there is a general disinclination among businesses in India to purchase non-life policies. In this section, we will focus on the effectiveness of non-life insurance advertising, various advertising appeals, and the responsibilities of advertisers and consumers.

Effectiveness of advertisements

Advertisements for insurance products, just as for any other product, have to generate curiosity or interest. However, creating interesting advertisements for non-life insurance products is more challenging because, as mentioned earlier, end-consumers are not too keen on knowing about insurance products. Therefore, insurance ads should avoid clichéd messages and come up with exciting and innovative messages.

The advertisements should be such that they stimulate 'responsive behavior' amongst the customers. The reader or viewer of an advertisement should take notice and respond to an advertisement. This should be the prime objective of non-life insurance marketers. Most insurance marketers have begun to take the services of reputed ad agencies to develop their ad campaigns. Insurance advertising also has become as technical and creative as advertising for FMCG or consumer durables. Exhibit 7.2 describes the innovative advertising approach adopted by Esurance, a reputed US-based auto insurer.

Exhibit 7.2
Erin Esurance: Animated Special Agent for Advertising

In 2004, Esurance, the leading US auto insurer, created an animated female character and called her Erin Esurance™. Erin was projected as the company's spokeswoman and special agent. She had pink hair and was smartly dressed. The company developed a special web page 'Erin's World' on the company website. The description stated, "I'm Erin Esurance™, a secret agent. My mission: to help you crack the auto insurance code. Luckily, saving time & money is no secret at Esurance. My deep cover is insurance agent. It's a pretty good cover, & I'm licensed! Surprisingly, insurance is more interesting than you'd think. Find out all about my life & times in my secret diary. Check out my latest efforts to save consumers with fast, easy auto insurance on Erin Cam & my audio files. Or, unlock the secret to saving time and money on your auto insurance. Get your quote today."

The entire creative effort to create Erin Esurance was done in-house. Within a short span of two years, the animated agent became one of the most popular characters in the US. As of March 31, 2006, Esurance was one of the fastest growing auto insurance companies in America, based on year-on-year premium growth.

Source: "Secret to Success", Best's Review, p.14, March 2006; and <www.esurance.com/home/ErinsWorld.asp>

Advertising appeals

Non-life insurance marketers follow different types of advertising appeal. Two of the most common advertising approaches used by them are the fear-based and humor-based approaches. These are discussed here.

Fear-based advertising: Most of the traditional non-life advertising focused on the fear factor. The advertisements attempted to convey the message that customers need not be afraid of unforeseen future risks if they purchased the insurance policies. For example, New India Assurance Co. Ltd made use of this appeal in one of its ads. The ad showed an old woman stepping out of a shop having made her purchases. Three goons follow her with the intention of robbing her. Just as they close in on her, a call, 'Mom,' makes them all stop and turn around. A man still standing at the shop, calls out to the woman, 'Mom, wait.' As the son walks in, the rogues quickly turn away and try to appear busy. The ad ends with the voice-over: "Where you go often depends on what you have with you. New India Assurance, assurance of the leader."

Humor-based advertising: With the launch of new insurance products and increasing awareness of insurance products, insurance marketers have started to use other appeals in their advertisements. Instead of instilling fear in the customer, these ads are filled with humor. Such ads attempt to suggest that non-life insurance products will help the customer's life get better and more joyous. . The basic objective is to make the customer happy about buying an insurance product.

For example, a campaign by Cholamandalam General Insurance Co Ltd. makes good use of this form of advertising. In one of the ads aired by the company, a man stops in his tracks on seeing an acquaintance and asks him with feigned concern, "Anand saab, kaam se Rampur gaye aur vahan appendix operation?" (Went to Rampur on work but had an appendix operation?) Looking totally amused at the question, 'Anand saab' in turn asks, "To?" (So?). The 'concerned' friend continues, "Itana kharcha? Loot gaye boss!" (Such expenditure? You have been robbed, boss!). An unruffled Anand responds, "Sab manage kar liya Chabilalji." (I managed everything, Mr. Chabilal). Stunned by this response, 'Chabilalji' inquires, "Konsa insurance bola?" (Which insurance did you say). Anand replies, 'Chola'. The ad ends with the voice-over "Chola health insurance se paye cash free hospitalisation. Adhiktam shehron main, adhiktam bimariyon...ke liye. To jo bhi hoga Chola manage karega." (Get cash free hospitalization with Chola health insurance ……in most cities ……for most illnesses. Whatever happens, Chola will manage the situation.)

Responsibilities of advertisers and consumers

Insurance marketers must ensure that they communicate responsibly. The information disclosure through the advertisements should be clear and must not conceal any vital information. The IRDA works to protect the interests of the consumer through the 'Insurance Advertising and Disclosure Act' of 2000. The Act requires that insurance marketers adhere to the code of conduct in the disclosure of information. According to the Act, 'insurance advertisement' means and includes any communication directly or indirectly related to a policy and intended to result in the eventual sale to or solicitation of a policy from the members of the public. It also includes all forms of printed and published materials or any material using the print and or electronic medium for public communication such as newspapers, magazines, and sales talks; billboards, hoardings, panels; radio, television, website, e-mail, portals; representations by intermediaries; leaflets; descriptive literature/circulars; sales aids flyers; illustrations form letters; telephone solicitations; business cards; videos; faxes; or any other communication with a prospect or a policyholder that urges him/her to purchase, renew, increase, retain, or modify a policy of insurance.

The Act also states that an 'unfair or misleading advertisement' will mean and include any advertisement: that fails to clearly identify the product as insurance; makes claims beyond the ability of the policy to deliver or beyond the reasonable expectation of performance; describes benefits that do not match the policy provisions; uses words or phrases in a way which hides or minimizes the costs of the hazard insured against or the risks inherent in the policy; omits to disclose or discloses insufficiently, important exclusions, limitations, and conditions of the contract; gives information in a misleading way; illustrates future benefits on assumptions which are not realistic nor realizable in the light of the insurer's current performance; where the benefits are not guaranteed, does not explicitly say so as prominently as the benefits are stated or says so in a manner or form that it could remain unnoticed; implies a group or other relationship like sponsorship, affiliation or approval, that does not exist; or makes unfair or incomplete comparisons with products which are not comparable or disparages competitors.

In addition to regulations directed at insurance marketers, IRDA expects the consumers to be responsible for checking for the completeness of the advertisements. The consumer is responsible for verifying the genuineness of the insurance marketer's claims, clarifying the kind of 'riders' and 'exclusions' forming part of the policy, and checking on post-sales service that includes claims settlement, and has to be wary of complicated language distorting the facts.

DISTRIBUTION

It is estimated that insurance marketers spend anywhere between one-third to half of their marketing budget on distribution. The performance of the sales department depends to a large extent on the channel chosen. Considering their importance, marketers, therefore, pay a lot of attention on designing an effective and integrated distribution system. Insurance marketers use multiple distribution channels to reach their target customers.

Designing a Distribution System

Insurance marketers attempt to design a distribution service system that will yield optimal results. An optimal design should consider the kind of products, the customer segments, kind of channels, and technological, financial, and human resources. Products should be given due emphasis. The marketers have to be selective in the kind of non-life products that must be marketed to consumers. This is possible by getting a clear picture of the customer segments and the kind of channels. The channels chosen should help in making the products more easily available to the targeted customer segments. A good amount of thinking is required with respect to the allocation and usage of the technological, financial, and human resources.

Distribution Channels

Insurance companies have traditionally used agents, agencies, and brokers as the modes of indirect distribution. But now, there is a host of alternate distribution channels like call centers, the Internet, NGOs, banks, etc., that ease the entire process of distribution and allow an increasing availability of their products. As a result of this proliferation of channels, it makes sense for the marketers to carefully pick the right kind of distribution channel that suits the overall marketing strategy of the product.

Direct mail and direct sales force

A database of prospective customers is created and the marketing personnel directly correspond with the customer about the product through post or by e-mail. The direct sales force consists of employees of the company who have been formally trained in various aspects of selling. The direct sales force is monitored by branch managers or area managers. The sales agents are responsible for the relationship between the insurer and the insured, right from identifying the prospect to closing the deal.

Insurance agents, brokers, and agencies

Any individual is eligible to be an agent for an insurance company. These agents are required to pass certain qualifying exams as required by the IRDA. Different companies have their own selection criteria for appointing agents. On selection, these agents are trained on the salient features of policies, and on how to sell the policies to the prospects identified by them. The remuneration is in the form of commissions offered by the company. Brokers are intermediaries who negotiate directly with the customers. They are also free to fix the premium of the policy after understanding the risk profile of the customer.

Agencies, on the other hand, act as representatives of the insurance companies, especially the bigger insurance companies. The agencies have their own sales force. The disadvantage with using agents/agencies is that the marketer has no direct control over their sales activities and selling approach to customers.

Modern channels of distribution

These are different from the traditional channels and a majority of them are technology-based. Call centers, worksite marketing, the Internet, etc. are some of the modern channels of distribution. Table 7.3 gives an overview of the various alternate distribution channels used by modern-day insurance marketers.

Table 7.3: Modern Channels of Distribution

Channel	Description
Call Centers	They can be an in-house department of the insurance company or an outsourced agency. The company provides the database of the prospects and the call center professionals make outbound sales calls with the objective of attracting and sometimes selling insurance products.
Tie-ups	This is another form of distribution. An example is a tie-up between auto manufacturers and non-life insurance players. Authorized car dealers offer free vehicle insurance cover of a company to customers purchasing a new two-wheeler/car. For example, Maruti Udyog Ltd (MUL) has a sales program called Maruti Insurance. Under this program, insurance services are provided to its customers purchasing the various car models through tie-ups. MUL has tie-ups with insurance companies like Bajaj Allianz, New India Assurance, National Insurance Company Ltd., and Royal Sundaram.[8]
	Some insurance marketers have tie-ups with large travel agencies like Thomas Cook, Sita World Travels, etc. Insurance products like baggage and overseas travel insurance are sold through these partners. For example, Tata AIG has a tie-up with Thomas Cook who is the corporate agent that sells its overseas travel insurance plans.
	In an effort to penetrate further into rural markets and increase their outreach, insurance companies have started to tie up with non-governmental organizations (NGO) and village panchayats.
Worksite Marketing	This involves the sale of insurance policies to employees. The insurance marketer has an arrangement with a corporate whereby they sell non-life products by conducting presentations and seminars within/outside the company premises. A certain amount of pre-decided premium is deducted from the salaries of the employees opting for a

	particular non-life product. For example, Tata AIG General Insurance uses this distribution channel to sell its general insurance policies.[9]
Chit fund firms/ Trade financing companies	Like banks, chit fund companies are fast becoming a dependable channel for insurance products. For example, the Shriram Group has set up 'Shriassurance', a marketing initiative of the company, to leverage on non-life products by bundling or combining them with other Shriram products.
Bancassurance	This is one of the more recent forms of distribution in India. This mode of distribution is more prevalent in life insurance marketing than in non-life marketing. For example, New India Assurance Co has a tie-up with State Bank of India. SBI distributes the general insurance policies of New India through SBI's extensive branch network.

Adapted from Krishanan, V, "The Road Less Travelled", IRDA Journal , Vol.2 Issue No.7, June 2004;and Avi Giloni, Sridhar Seshadri and Pasuparti V Kamesam, "Service System Design for the Personal and Casualty Insurance Industry", Production and Operations Management, Vol.12 Issue No.3, 1993;and "ING Vysya, Royal Sundaram in a Strategic Distribution Partnership." http://www.domain-b.com/finance/insurance/royal_sundaram%20_alliance_insurance /20031105 _partnership.htm.

THE CURRENT SCENARIO

Till the year 2000, the Indian non-life insurance market was dominated by General Insurance Corporation (GIC) and its four subsidiaries. The establishment of the IRDA and industry deregulation led to the entry of private players in the insurance market. The Indian non-life insurance market has grown considerably over the years. In 2004, it accounted for 2.5 percent of the total Asia-Pacific non-life insurance market (the Asia-Pacific market includes Australia, Japan, China, India, South Korea, and Taiwan) and was valued at US$ 4.3 billion (INR 195 billion). The Indian non-life insurance market is poised to achieve significant growth in the coming years. It is estimated that the Indian non-life insurance segment will be a US$ 7.2 billion market by the end of 2009[10].

Japan has the largest non-life insurance market in the Asia-Pacific region with 59.70 percent, followed by China with 10.20 percent[11]. The key players in the Indian non-life insurance segment are Oriental Insurance Company and Export Credit Guarantee Corporation (ECGC) in the public sector, and IFFCO Tokio, Bajaj Allianz, and Tata AIG in the private sector.

Joint Ventures

The entry of private players has brought about a sea change in the number and variety of insurance products developed and marketed. The foreign companies include Tokio Marine[12], New York Life[13], Aviva[14], Allianz[15], Lombard General[16], AIG[17], and Standard Life[18]. Table 7.4 gives an overview of the joint ventures in the Indian non-life insurance business.

Table 7.4: Joint Ventures - Non-life Insurance Companies

Name of Joint Venture	Partners	Remarks
IFFCO Tokio General Insurance Co. Ltd. (ITGI)	IFFCO (Indian Farmers Fertilisers Co-operative Ltd.) and Tokio Marine and Fire Insurance Company Ltd., Japan	Tokio Marine comes with more than 120 years of experience in the general insurance business. It is also the largest and oldest general insurance company of Japan.
Tata AIG General Insurance Company	Tata Sons and American International Group Inc.	AIG is a reputed US-based insurance and financial services company. It has a presence in more than 130 countries worldwide.
ICICI Lombard	ICICI Bank Ltd. and Lombard Canada Ltd.	Lombard Canada is one of the oldest property and casualty companies in Canada.
Bajaj Allianz General Insurance	Bajaj Auto Ltd. and Allianz AG, Germany	The Germany-based Allianz group has been in the insurance and asset management business for over 110 years. It is one of the fastest growing insurance and financial companies in the world.
Royal Sundaram Alliance Insurance Company Ltd.	Sundaram Finance Ltd. and Royal & SunAlliance Plc., UK	Having begun operations in 1710, Royal & SunAlliance is one of the oldest and most reputed insurance companies in the world. It is present in more than 130 countries and has around 20 million customers.
HDFC Chubb General Insurance Company Ltd.	HDFC and Chubb Corporation	Chubb Corp. was founded in New York in 1882. It is one of the world's largest insurance companies with operations in 32 countries.

Adapted from http://insuremagic.com; http://www.hdfcchubb.com/aboutUs_hdfcChubb.asp

The joint ventures with foreign partners have been more successful in India than in other Asian markets. These joint ventures were able to garner considerably high market shares both in the life and non-life insurance market. In the Indian non-life insurance market, the market share of foreign partner joint ventures was 20 percent, while their share in other Asian markets was between 5 and 10 percent[19].

Detariffing

Detariffing in the non-life insurance market will bring about a sea change in the way insurers price and manage their products. Cross-subsidization may be on its way out and certain insurance products like health insurance may witness a significant increase in the premiums charged. The IRDA has laid the groundwork for detariffing non-life insurance from January 2007, except in third party liability insurance for motor vehicles. The controls on premiums on insurance covers for motor vehicle, fire, and engineering were lifted on January 1, 2007. This could lead to a drastic fall in premiums charged due to the cut-throat competition. In the initial phase, the IRDA has asked general insurance companies not to lower the premium beyond the recommended limits – a maximum reduction of 10 percent on motor own damage covers and a maximum reduction of 20 percent for premiums of fire and engineering insurance.

On the flip side, the premiums for group health insurance may increase significantly, the reason being that group health insurance policies were earlier priced based on the risk profile of the overall insurance portfolio of the corporate taking the policy. This led to cross-subsidization. But in the detariffed regime, all products will be priced individually. The corporate consumers will have to reassess the covers being offered to their employees to optimize the cost benefit. In addition, group health policies will be underwritten keeping in mind the specific risk of the corporate client.

SUMMARY

The common non-life insurance products targeted at individual (retail) customers are motor vehicle insurance, personal accident insurance, health insurance, and householder's insurance. Other retail products include baggage insurance, travel insurance, transit insurance, and pet insurance. The common non-life insurance products targeted at corporate (organizational) customers are group health insurance, cargo insurance and hull insurance, industrial insurance, and fire insurance. Other non-life insurance products include the shopkeeper's policy, fidelity insurance, jeweler's block insurance, liability insurance, cattle insurance, poultry insurance, aquaculture insurance, farmer's package, weather insurance, and patent insurance.

With the deregulation of the sector and increasing competition, most private players are looking at new product development as a strategic imperative. Successful product development needs both a well-developed and clearly defined internal process and a receptive external environment. The private players have attempted to customize their offerings in order to attract customers. The basic product is made more suitable by adding riders. Riders are the extensions or the add-ons provided on a particular product for which the customer pays extra premium.

In life insurance, the main factors used for determining the premium rates are mortality, expenses, and rate of interest. The factors considered when pricing non-life insurance products are claims cost, business acquisition cost, management expenses, margin for fluctuations in claims experience, and a reasonable profit. The factors affecting the pricing structure are broadly divided into portfolio level, case level, and other factors. The objectives that must be kept in mind when pricing insurance products are adequacy, reasonableness, fairness, and consistency & flexibility.

The promotional mix in the non-life insurance industry is primarily centered on advertising. Two of the most common advertising appeals used by non-life insurance marketers are fear and humor. IRDA has taken steps to protect the interests of the consumer through the 'Insurance Advertising and Disclosure Act' of 2000. The Act requires that insurance marketers adhere to the code of conduct in the disclosure of information.

Non-life insurance marketers use multiple distribution channels to reach their target customers. The traditional channels include direct mail and direct sales force, insurance agents, brokers, and agencies. The contemporary channels of distribution include call centers; tie-ups with corporate agents, NGOs, automobile distributors, etc.; worksite marketing; and bancassurance.

The foreign players have been more successful in joint ventures in India, as compared to their experience in other Asian markets. Till December 2006, IRDA stipulated the limits of fixing premiums for various non-life insurance products. Detariffing has been implemented from January 2007 (except in third party liability cover for motor vehicles), with significant implications for the use of pricing strategy as an important component of the overall marketing strategy.

End Notes:

[1] "Detariffing, New Players, FDI Made Headlines in Insurance." Business Standard. December 30, 2006.

[2] This covers the liability of the policyholder to compensate any person up to a pre-specified amount for bodily injuries and property damage caused by the policyholder's vehicle.

[3] "Tata AIG Launches New Personal Accident Policy." Financial Express. January 28, 2002.

[4] Reliance General Insurance Limited, a venture of the Reliance group, is one of the first general insurance companies in India to get a license from the IRDA. Some of the products that it offers are the office package policy, personal accident policy, shopkeeper's package policy, and householder's package policy.

[5] Burning cost is the ratio of the reinsurance losses incurred to the ceding company's subject premium. It is also known as pure loss cost.

[6] The exposure rating is usually used as a rating method when there is excess of loss reinsurance. Under this method, the rate is determined based on the exposure inherent to the business to be covered and not on the basis of the loss demonstrated by the business in the past.

[7] Payback is a method of underwriting. In this type, the price is set by the underwriter based on the judgment as to how many times the loss event might occur in the future. Let us assume that the underwriter is of the opinion that the loss event would occur only once in five years. Then the price would be set such that it is equivalent to the coverage limit divided by five and the insurance contract would have a 'five year payback'.

[8] Source : http://www.marutiudyog.com/bp/insurance.asp?ch=2&ct=8&sc=2#MF1

[9] Source: "Tata AIG-MarkStrat Project Brief." <http://www.iiml.ac.in/prism/pdf _events /TATA-AIG%20General%20Insurance%20Ver1%201.pdf >

[10] "Non-Life Insurance in India: Industry Profile." www.datamonitor.com November 2005

[11] "Non-Life Insurance in India: Industry Profile." www.datamonitor.com November 2005

[12] Tokio Marine, a Japan-based general insurer, operates in India through IFFCO-TOKIO General Insurance Company.

[13] New York Life, a US-based life insurance company, operates in India through Max New York Life

[14] Aviva is a Dutch general insurance company.

[15] The Germany-based Allianz group is in the business of insurance and risk management for more than 110 years.

[16] Lombard General operates in India through a joint venture (with ICICI Bank) called ICICI Lombard General Insurance Company.

[17] AIG, a US-based general insurer, operates in India through a joint venture with Tata Sons Ltd. called Tata AIG General Insurance Company.

[18] Standard Life operates in India through a joint venture (with HDFC) called HDFC Standard Life.

[19] "Non-life Insurance in India – Industry Profile." www.datmonitor.com. November 2005.

Chapter 8

Life Insurance

In this chapter, we will discuss:

- Introduction to Life Insurance
- New Product Development and Branding of Life Insurance Products
- Pricing of Life Insurance Products
- Promotional Mix in Life Insurance Marketing
- Distribution Channels for Life Insurance Products

"Life is a pendulum between tears and joy". And when the tears are accompanied by financial difficulty, most people feel the need for a financial support system. In such situations, insurance cover against risks can prove to be of immense help.

The chapter begins with an introduction to the concept of life insurance and the various life insurance products, followed by the new product development and branding of life insurance products. The pricing and promotion of life insurance products are discussed subsequently. The chapter concludes with the distribution aspects of life insurance products.

INTRODUCTION TO LIFE INSURANCE

The life insurance segment in India was dominated by the Life Insurance Corporation of India (LIC) till the end of the twentieth century. Post 2000, with the setting up of the Insurance Regulatory & Development Authority (IRDA) and the entry of private players, there was a significant increase in competition. As of 2006, there are more than a dozen players in the life insurance segment in India. Many foreign players, who identified the huge potential of the Indian life insurance market, made an entry into the market by forming joint ventures with Indian companies. Business volumes in the life insurance sector are usually assessed on the basis of the premium collected. Table 8.1 lists some of the life insurance companies and the gross premium collected by them in 2004.

Table 8.1: Life Insurance Companies and Premiums Collected - 2004

Insurance Company	Premium Collected (Rs. Million)
LIC	631,676.0
ICICI Prudential	9,892.8
Birla Sunlife	5,375.4
HDFC Standard Life	2,977.6
Tata AIG	2,535.3
SBI Life	2,256.7
Allianz Bajaj	2,208.0
Max New York Life	2,152.5
OM Kotak	1,507.2
ING Vysya	885.1

Source: International Insurance Fact Book 2005, www.internationalinsurance.org .

LIC is still the undisputed leader in the life insurance segment and its closest rival is ICICI Prudential. However, private and foreign players have been more proactive than LIC in developing a range of insurance products and marketing programs to increase market share. Competition has also forced the insurance marketers to differentiate themselves through customized products. In this section, we will focus on the differences between life and non-life insurance products. This is followed by a description of the types of life insurance products offered by marketers in India.

Differences between Life and Non-Life Insurance Products

In India, life insurance has been growing much faster than non-life insurance. This has been associated with a huge difference in ad spends. In 1999, 62% of the total ad spends for insurance were for life insurance while 38% was for non-life products. In 2002, only 12% of the total ad spend for insurance was for non-life and 88% was for life insurance products[1]. Some of the basic differences between life and non-life insurance products can be discussed under the heads objective of insurance, premium amount, policy period, and role of agents.

Objective of insurance

Life insurance products cover the risk to individual life whereas general insurance provides a cover for property and casualty. The former deals with providing financial protection against unforeseen incidents in the life of an individual; the latter focuses on protection of personal and organizational property under various heads – fire, motor, aviation, engineering, agriculture, marine, credit risk, liability, etc. Life insurance, pensions, and annuities come under the life insurance category.

Premium amount and policy period

The premiums for life insurance products are high when compared to non-life insurance. Also, the annual premium decided on at the time of signing the insurance contract generally remains unchanged for the policy period in life insurance. (There could be minor differences in the yearly premium outflow, if a policyholder chooses to change the frequency of payment, say, from annual to monthly, during the premium payment period.) The life insurance contract is usually for a fixed period that is much more than one year; this period is mutually agreed upon by the customer and the insurer. On the other hand, non-life insurance contracts are typically for a period of one year. So the premiums and the extent of insurance coverage for general insurance products can be revised every year.

Role of agents

Agents play a dominant role in selling life insurance products when compared to non-life products where their importance is very low. Besides, life insurance and its related products entail the need for relationships to be maintained over a period of time with the customer.

Types of Life Insurance Products

The life insurance segment has a wide range of products catering to individuals and groups of individuals. Life insurance products are basically classified into two types. Products that target individuals can be classified as retail insurance products or individual life policies; products that target groups are termed corporate products or group insurance policies. Let us look at each of these products.

Individual products in life insurance

Retail insurance products offer risk protection to individuals. They are classified mainly on the basis of the objective of the policy, period of the policy, and returns (if any). Some of the individual insurance products commonly offered by insurance marketers are term policy, whole-life policy, endowment policy, money-back policy, unit-linked products, and annuities and pension plans.

Term policy: This is one of the most common life insurance products. This policy provides a risk cover to the individual against death during the policy term. The entire amount for which the policy cover is available is called the sum assured. In the event of death of the insured person during the term, the nominee receives the sum assured.

There are no survival benefits, that is, if the insured person survives the policy term, there are no benefits at the end of the term. The target segments for this policy are people in their twenties and thirties. This policy can be renewed at the end of the specified term, but the premiums generally increase on renewal. The term offered by insurance marketers generally ranges from a minimum of five years to a maximum of 35 years.

Insurance marketers tend to market the term policy as a loan collateral for borrowers who take loans for large amounts. For instance, if an individual has taken a loan of Rs. 2 million over a 20 year repayment period, a term insurance policy acts as a risk cover and ensures automatic repayment of the loan amount, in case of death of the borrower. For example, LIC offers Amulya Jeevan and Anmol Jeevan, two pure term insurance plans. The premium can be paid either at a time as a lump sum or on a regular basis.

Whole life insurance: The whole life insurance policy provides a comprehensive insurance cover for life without any limitation of time period. The premium is fixed and it is paid for a longer period (till the age of eighty or for a period of thirty five years, whichever is later -- in the case of LIC), after which the sum assured is paid to the policyholder. The sum assured with the appropriate bonus is payable to the beneficiary (nominee) if the individual dies during the term. Besides, the policyholder has the option of receiving the sum assured and the bonuses accrued at the end of the maturity period or of continuing the cover without paying any additional premium. This policy is generally taken to create a corpus for the heirs of the insured individual.

The downside of a typical whole life insurance policy is that it does not take into account the financial limitations that a policyholder may face in the later stages of life and its impact on the payment of premium. Some of the private insurance marketers have developed whole life products with shorter premium payment terms to attract customers. For instance, Tata AIG offers whole life insurance for premium payment periods such as 15, 20, or 25 years. In the case of the Tata AIG Mahalife Gold whole life insurance policy, the premium has to be paid for a period of 15 years. The policy offers a guaranteed lifetime payment of 5% of the sum assured on an annual basis from the tenth anniversary of the policy.

Endowment policy: This is the most popular policy in the life insurance segment. Under this policy, the nominee of the policyholder gets the total sum assured and the accumulated cash value of accrued bonuses, in the event of the sudden death of the policyholder during the term of the policy. In case the policyholder survives the term, he/she is paid the sum assured and an additional amount, based on the return on investments of the insurance company. This policy is generally offered for fixed periods and ranges from five to thirty years with some sort of flexibility in choosing the number of years as the payment period. Endowment policies are often marketed as insurance policies that have a significant savings component.

Apart from the basic product, insurers also offer high value endowment policies. For example, HDFC's endowment assurance policy has various types of plans. They include double sum assured (DSA), accidental death benefit (ADB), waiver of premium (WOP), and critical illness (CI). The premiums can be paid under three options, viz., quarterly, half-yearly, and annual, and vary depending on the type of plan chosen.

Money back policy: A money back policy is similar to the endowment policy in principle. This policy provides the policyholder with both protection and the benefit of a regular cash inflow. It is a variant of a savings plan and helps to manage planned expenses. This policy is tailored to provide returns that coincide with special occasions in an individual's life like higher education of a child once he/she reaches 18 years of age. The policyholder has to pay a fixed amount of premium every year during the term of the policy. In case of the sudden death of the policyholder, the nominee is eligible for the sum assured and any additional amount in the form of bonus.

Irrespective of whether the policyholder survives the term or dies before the maturity of the policy, a portion of the sum assured is paid at regular intervals and the remaining amount, if any, as a lump sum after a predetermined period. For instance, in a money back plan offered by LIC, for a policy duration of 25 years, 15% of the sum assured is payable equally at the end of 5^{th}, 10^{th}, 15^{th}, and 20^{th} years of the policy term. The remaining 40% of the sum assured with the accrued bonus is paid at the end of the 25^{th} year of the policy term.

Annuities and pension: This type of insurance policy is marketed to those individuals who wish to have a constant source of income even after retirement. Under this plan, a fixed amount of premium is paid for a specified period. After the policy matures, the policyholder is entitled to an immediate cash payment of up to 25% of the sum assured. The rest of the sum assured can be invested in an investment fund that will pay a certain sum at regular intervals. The frequency of payment of the premium is at the discretion of the individual (annual, half-yearly, quarterly, or monthly) and can be for a fixed period. (Pension and retirement products are discussed in detail in Chapter 9 — Small Savings and Retirement Planning).

Unit-linked products: These are also called market-linked products. These products are similar to the other life insurance products in terms of the premium payment and different from them in terms of the variability of returns. The premium amount paid is invested by the insurance company in stocks, futures, etc., as in a mutual fund product. The individual has the option of having the premium paid invested in equity, debt, or both. The allocation of money in the various investment categories is solely at the discretion of the policyholder who can opt out of an investment category at his/her personal discretion. For example, Max New York Life offers the 'Life Maker unit linked investment plan.' It has the benefits of flexible investment options, guaranteed free units as loyalty bonus, and attractive tax benefits. Many insurance marketers offer riders that give the customer the flexibility to customize the product as per his/her needs. The add-on riders may be in the form of 'personal accident benefit rider', 'critical illness rider', etc.

Insurance products can also be divided into single premium and non-single premium policies depending on how the premium is paid. See Exhibit 8.1 for further details.

Exhibit 8.1

Single Premium & Non-single Premium Policies

The premium can be paid by the policyholder in one lump sum payment or in small amounts on a monthly, quarterly, half-yearly, or annual basis.

Non-single premium policies: Most life insurance policies fall under this category. The payment of the premium is periodical and the periodicity could be monthly, quarterly, half-yearly, or annual. The choice of intervals of payments is left to the discretion of the policyholder. Premiums paid annually generally tend to be fractionally lower than the total premium paid in a year when the premium payment is on a monthly, quarterly, or half-yearly basis.

Single premium policies: Policies where the premium is paid in one initial lump sum, that is, only once at the beginning, are called single premium policies. After the maturity period, the sum assured and other additional benefits are paid as in the case of non-single premium policies. This policy is suitable when an individual receives a lump sum as a bonus, gift, or as part of inheritance, etc. For instance, the 'Single premium bond' of Birla Sun Life is a unit-linked investment-cum-insurance plan available for 5 years or 10 years. The policyholder has a choice of investing in a secure fund, balanced fund, or an equity fund. It offers returns depending on the performance of the capital markets. The principal amount is guaranteed under the plan. In addition, this plan not only aims to maximize the investment return but also provides a life insurance cover, in case of the sudden death of the policyholder.

Source: Single Premium Bond,
http://www.birlasunlife.com/insurancenet/insurance_plan/individual_life/Single_Premium_Bond2.asp

Group products in life insurance

When life insurance is offered to a group of individuals, it is referred to as a group product or group scheme. Group products are generally taken by large organizations – companies, associations, societies, etc. The advantage of a group scheme is that it helps the client organizations provide insurance to all the employees at a time without any discrimination. Also the group benefits can be availed of at lower costs. Some of the group products that are common in life insurance are: group term life insurance, group gratuity plan, group insurance in lieu of Employee's Deposit Linked Insurance Scheme (EDLI), group superannuation scheme, group leave encashment scheme, and group savings linked insurance scheme. A few of these schemes are discussed in this section.

Group term insurance: The policy provides life insurance protection for a group of employees. It is administered on a group basis and the costs are low. For instance, LIC's group term insurance policy covers the group members for death; there is no survival benefit at the end of the term. The customer organization has to renew the policy every year. At the time of renewal, LIC computes the premium based on the size of the group and the age distribution among the group members.

Group gratuity plan: Gratuity is a statutory benefit payable by the employers under the Payment of Gratuity Act, 1972. The employers have the option of making alternative arrangements if they plan to provide higher gratuity. For instance, the group gratuity plan provided by Birla Sun Life insurance company is a unit-based fund with market-linked returns. It has an option for the employer to select from six investment funds. When the returns on the funds become higher, the contribution by the employer toward the fund decreases.

Group insurance in lieu of EDLI: All employers to whom the Employee's Provident Fund and Miscellaneous Provision Act, 1952, applies, have a statutory liability to subscribe to the Employee's Deposit Linked Insurance Scheme, 1976, to provide for the benefit of life insurance to all their employees. However, under Sec. 17(2A) of the act, employers may be exempted from contributing to this scheme if they have provided for better insurance benefits through alternative schemes. LIC's 'group insurance scheme in lieu of EDLI' has been accepted as one such better alternative. Under this scheme, each employee is covered for a sum falling in the range of Rs.5,000/- to Rs.200,000/-, depending on the current level of salary and years of service.

In addition, to the individual and group insurance schemes already mentioned, the Government of India (GoI) offers insurance cover through the vast network of post offices across the country. These insurance products can be broadly categorized into postal life insurance (PLI) for government employees, and rural postal life insurance (RPLI) for the weaker sections of society.

Postal Life Insurance (PLI): Postal life insurance was introduced in 1984. It seeks to provide life cover to employees of the state and central government departments and the defense services.[2] The postal life insurance products comprise Santosh, Suraksha, Suvidha, Sumangal, and Yugal Suraksha. Some of the common benefits associated with these products are 100% security for the sum assured, income tax rebate on premiums and maturity amount, low premiums, and the facility to apply for a loan against the policy. In addition, policies that lapse due to non-payment of premiums can be renewed.

Rural Postal Life Insurance (RPLI): The rural postal life insurance scheme was introduced in the year 1995 with the objective of providing insurance to the rural and the weaker sections of the society. The premium charged under this scheme is extremely low. The various policies under RPLI include the Gram Santosh, Gram Suraksha, Gram Suvidha, Gram Sumangal, and Gram Priya. Gram Priya is an endowment policy with a ten-year term. Under this scheme, survival benefits are paid to the nominees in the event of death of the policyholder. In the event of the occurrence of natural calamities like flood, drought, earthquake etc., no interest is charged for non-payment of the due premium for a period of up to one year.

NEW PRODUCT DEVELOPMENT AND BRANDING OF LIFE INSURANCE PRODUCTS

The ability to develop and manage a portfolio of insurance products plays a crucial role in the success of insurance marketers. This has become more so with competition increasing after the deregulation of the insurance sector and the entry of private domestic and foreign players. Though the products are in general designed keeping in mind the needs of the customer, existing insurance products have to be periodically revamped or phased out and new products developed in accordance with the changing needs of the customer.

A strong company image and a sufficiently high level of awareness about its products tend to have a positive impact on the selling of insurance products in terms of reducing the extent of information search required to be done by consumers during their decision making process. The most common form of branding is umbrella/corporate branding. Product branding has not yet attained a significant position in the insurance industry

New Product Development (NPD)

The new product development process consists of a series of steps. They are idea generation, idea screening, concept development and testing, business analysis, marketing mix development, test marketing, and commercial launch. To some extent, the NPD process in the insurance sector is similar to that in other sectors like FMCG and consumer durables. Let us look at each step of the NPD process.

Sources of information for idea generation

One good idea could provide enough impetus for the development of a new product. How to tap ideas is the major concern of any insurance company willing to develop new products. Idea generation is possible through internal as well as external sources.

Internal sources: Internal sources include the direct sales force, the product development team, or other employees of the organization. The sales force is a valuable source of ideas as they are in direct contact with the customer. Their discussions with customers will help them give a fairly accurate picture of customer expectations. The product development team is primarily involved in the constant study of the acceptance levels of different insurance products and the purchase behavior of consumers across the market. As a result, they can easily contribute well-researched ideas. For instance, GE Insurance Solutions (GEIS), based in the US, has adopted an innovative way of generating ideas. Idea generation has become a continuous effort for GE employees through regular brainstorming sessions and participation in creative games. Ideas generated are stored in the 'idea repository'. This helps GEIS ensure that there is a constant flow of ideas for product development. The company has a collection of around 200 ideas[3] in the idea repository that are regularly reviewed as and when the need arises.

External sources: Customers are the most important external source of ideas. The customers' views on existing products serve as a good input in getting to know the true potential of a similar product. Many insurance companies do not tap into this valuable resource and so end up developing products that are not in line with the interests of the customers. Exploration of the customer's needs and interests gives a proper direction to conceptualizing the right kind of product. Also, the indirect distribution channel members ranging from agents, agencies, brokers, competitors, market research agencies, etc., are an important source of information and ideas. For instance, brokers with their vast knowledge of the products have a deep insight into the customer needs.

Idea Screening to Product Launch

If getting the right idea is the first issue, the next and tougher task is to convert the idea into a successful product launch. The idea passes through a series of stages: idea screening, concept development and testing, business analysis, marketing mix development, test marketing, and commercial launch. Idea screening helps to check the feasibility of the idea and to decide if it can achieve the set business objectives. The idea is given the shape of a new product in the concept development stage. The features of the product are also decided. In the business analysis stage, the potential of the product is assessed based on the product's strengths and competitive market forces. The marketing mix development stage takes into consideration the branding, pricing, product features and strengths, and promotional and distributional aspects, in addition to any service-related aspect such as people, process, or physical evidence. The final stage is a pilot study where the concept or the product is actually tested in the real market. Based on the feedback, the required changes are incorporated and the product is then officially launched in the market.

Insurance marketers generally adopt different processes to ensure that the idea generated is screened through various stages before a product that meets customer requirements is launched. In general, the product development time in the insurance sector depends upon the complexity and freshness of the product. GEIS (GE Insurance Solutions) has a unique way of developing an idea into a product. The GEIS way of product development uses a concept called 'toll gates'. The toll gates are the checks for the different stages of new product development. Each stage involves value addition leading to the final stage when the product is launched in the market. Exhibit 8.2 explains how an idea from the idea repository of GEIS goes through the various stages of product development

Exhibit 8.2

Product Development at GE Insurance Solutions (GEIS)

GE Insurance Solutions group, formerly GE Global Insurance Holding, is a leading provider of commercial insurance, reinsurance, and risk management services with operations in 28 offices in Asia, Europe, and North America. Its subsidiary 'Employers Reinsurance' is the group's flagship company and the number 2 reinsurer in the US behind General Re. GE has developed the 'toll gate' system where each stage of the new product development is called a 'gate.'

Gate 1 - Team formation: Here the in-house formal team begins the task of developing a product. At GEIS, the team is cross-functional and it represents members from marketing to the actuarial departments.

Gate 2 - Heavy lifting period: A check on the underwriting aspects and the financial analysis of the insurance cover is done by the product development team. The underwriting team looks into all the financial aspects. The analysis is done in terms of the scope of the insurance cover.

Gate 3 - Draft and launch: At this stage, the policy document is completely drafted in detail. The policy draft developed is a result of concept development, business analysis, and marketing mix development. After working out the policy draft, the company launches the product in the market for the use of customers.

Gate 4 - Incubation period: After the launch of the product in the market, it is subject to incubation for a period of one year. During this incubation period, the product is monitored on various parameters. Product audits and risk reviews related to the product are also conducted to gauge the performance and suitability of the product.

The time taken from gate 1 to gate 4, i.e., the length of the product development varies from product to product from as low as 60 days to as high as about one year.

Adapted from Cenlceros, Roberto, Rupal Parekh, "Product Development Requires Appetite for Risk." Business Insurance, Vol. 39 Issue 3, February 2005.

Branding of Life Insurance Products

Insurance companies have not yet been able to establish strong brands for various life insurance products in India. This could be because of the very nature of insurance business — that it is based on the level of trust built between the insurer and the insured. Besides, it is the insurance agent who is the face of the company and develops a relationship with the customer. The low level of brand recognition in insurance products also arises due to the relative similarity of product features of different insurance companies. Corporate branding is the most commonly used branding strategy.

Brand communications

Brand communications must keep in mind the people element along with the product attributes. This is because the agents, brokers, and financial planners engaged in selling the service are integral to the brand. The customer assesses the product based on its features and also the attitude and selling approach of the sales personnel. Exhibit 8.3 illustrates the communication efforts of Tata AIG Life to create a new corporate brand identity.

Branding decisions

Insurance marketers focus primarily on attracting and retaining customers. This is followed by an attempt to create a relevant brand proposition. The branding decisions of insurance marketers are dependant on their ability to meet customer expectations and achieve a more realistic brand positioning.

Customer expectations: The services sector is driven by customer choices and preferences. This applies to the insurance industry as well. Therefore, it is essential for insurance marketers to learn about customer expectations. Then a branding strategy targeting the identified customer expectations should be formulated. The basic expectation of customers is hassle-free settlement of claims. This is given top priority by 49% of the customers (See Fig 8.1 for details). Insurance marketers must therefore ensure that the claims settlement process is made easier. Besides, better services and security for the investments are important. In addition, other factors like the distribution network and lower premiums are considered by customers when deciding on an insurance company.

Exhibit 8.3

Brand Communications at Tata AIG Life Insurance Company

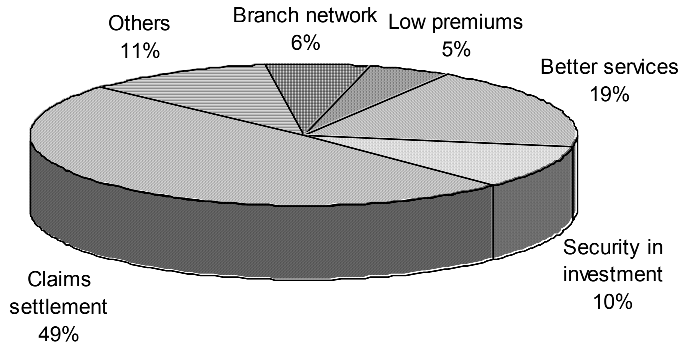
Tata AIG Life Insurance Company (Tata AIG) is a joint venture between the Tata Group and AIG (American International Group, Inc.). Tata AIG provides a wide range of life insurance products that cater to the requirements of individuals, businesses and associations. The company started off its operations in the year 2001; initially it used the tagline 'With you always'. The objective was to drive home the point that Tata AIG would always be there to take care of the insurance and financial needs of their customers. This was necessary as customers are not very sure whether a private player would remain in the market at the end of the policy period, which could be as high as 35 years.

After three years, the company attempted to create a new brand identity that would encompass aspects beyond trust and relationships. From 2004, the tagline was 'A new look at life' (as shown in the figure). The objective of the new brand communications campaign was to communicate the company's continuous process of anticipation of the present and the future requirements of the entire insurable population of India and the wish to produce innovative products that satisfy the anticipated needs of the customers. Tata AIG launched path-breaking products such as Mahalife[4], Nirvana[5] and Healthfirst.[6] The campaign also attempted to highlight the high standards of corporate philosophy and innovating culture of Tata AIG.

The company used different channels to communicate the new brand image. It made use of both television commercials and print advertisements. It also made effective use of other sources like hoardings, outdoor publicity, Internet, and the radio. These media vehicles were used at different points of time. The company adopted a media scheduling plan and advertisements were scheduled during the period October to December and January to March, to coincide with the period when most people in India plan their investments for the financial year.

Source :< http://www.tata.com/tata_aig_life/releases/20040607.htm >

Figure 8.1: Customer Expectations in Insurance



Source: Lahari, Suranjita "Brand Identity-Its Influence in Customer Decision Making." The Journal of Insurance Institute of India. Vol.XXX July-December 2004

Brand positioning: Insurance marketers must invest a considerable amount of time, money, and human resources to establish a successful brand and ensure its continued existence. A brand must be built based on a well-differentiated and credible positioning. Most marketers generally fall back upon their organizational history to create such a positioning. This is followed by other positioning approaches. Table 8.2 shows some of the brand positioning approaches in terms of the brand messages, as conceived by insurance companies in India.

Table 8.2: Brand Positioning Approaches of Indian Insurance Marketers

Company	Message	Focus
ICICI Prudential	We cover you at every step of life	A holistic approach to the entire gamut of needs for a lifetime.
HDFC Standard Life	Making life easier for you	A favorable impression on the minds of the people
Max New York Life	Your partner for life	A unique approach which is receptive to the service demanded by the customer

Source: "Need for Branding in Insurance."
http://www.insuremagic.com/Content/articles/General/branding.asp

Importance of branding insurance products

The branding of insurance products needs constant evaluation. The brand image created based on the positioning approach needs to be managed. Managing the brand image in tandem with the products is a big challenge that insurance marketers face. There are certain advantages as well as risks associated with branding insurance products. These are described here.

Diversification: A good brand image would enable the company to leverage on its existing brand image when diversifying the product portfolio. It would enable new products to penetrate the market more easily. For instance, LIC has been able to use its corporate brand image to establish a sizable market share for its new endowment-cum-whole life insurance product 'Jeevan Anand' in a short time of four years. The product was launched in 2002.

Corporate image: Insurance marketers with a good brand image need to be watchful when developing new products. This is because, if such products fail to perform as per the expectations of the customer, then it may have a negative cascading effect on the image of the other insurance products of the marketer.

Brand images that are created are not constant. Even a good brand image cannot carry a given product for a very long time. It needs to be suitably supplemented with product quality, service standards, and marketing techniques.

PRICING OF LIFE INSURANCE PRODUCTS

Pricing varies for different insurance products. It may also vary across companies offering a similar type of policy. This is because every marketer takes into consideration various factors when deciding on a price for a policy. The premium paid for the same policy varies based on the time period and the frequency of payment. Some of the other factors that are considered when pricing products are -- mortality, investment earnings, and administrative expenses.

Underwriters are specialized personnel who look into the risks associated with various policies. They identify and calculate the risk of loss from policyholders, establish appropriate premium rates, and develop policies that cover this risk. This section focuses on the importance of pricing, the different approaches to pricing, the concept of underwriting, and the different rating methods used in risk assessment.

Importance of Pricing

The pricing of insurance products is important due to the economics involved. The price of a product has a direct impact on the amount of revenue the insurer earns and also the margin. In addition, it affects the volume of insurance policies sold. This is because price is one of the factors that a potential customer will consider when deciding which insurance product to buy and which insurance provider to buy from. The intangibility of insurance services also increases the importance of insurance pricing. The premium charged by an insurance marketer impacts the customer expectations in terms of the quality of services they can expect.

Pricing Approaches

Insurance pricing is complicated by the fact that the levels of premium offered by an insurer must cover anticipated claims and other expenses. There are several different methods for pricing insurance, based on the insurance marketer's corporate objectives. They are the survival approach, the sales maximization approach, and the profit maximization approach.

Survival approach: When there is intense competition in the market, an insurance marketer may opt to price products at a low level. This is similar to penetration pricing. The objective of the marketer is to forego profit margins initially and focus on surviving in the market.

Sales maximization approach: This strategy is aimed at increasing volumes of sales for new insurance products. Initially the pricing may be low, even leading to losses. This is necessary to lure customers away from competitors' products. The focus is on the number of policies sold without emphasis on the revenues generated.

Profit maximization approach: The basic focus of this pricing approach is on earning profits through large margins. This kind of pricing is similar to the market skimming approach of pricing for consumer goods. This is a viable option only when the product is unique or competition is minimal.

Underwriting

Underwriting is a crucial component of pricing life insurance products. It is the process by which insurance marketers assess the risk profile of individuals. In simple terms, the marketer decides the rate (premium) that the individual has to pay based on the study of the risk profile of the individual. This entire process of assessing the risk profile of the individual and then fixing the rate of premium is called risk classification or underwriting. In general, the risk can be classified into four categories -- preferred, standard, rated, and declined. Table 8.3 gives an overview of the four risk categories.

Table 8.3: Types of Risk Classification

Risk category	Risk level	Premium charged
Preferred	Lower than average risk	Premium charged will be as preferred by the individual or at the lowest end.
Standard	Average risk	Standard rate as decided by the insurer will be charged to the individual.
Rated	Above average risk	A higher premium will be charged.
Declined	Uninsurable	Insurance cover may be denied.

Compiled from various sources.

The category of risk assigned for the individual is not for life. An individual who has been denied an insurance cover may be eligible for it in the future after he/she has reduced the risk levels. This the individual can do, for example, by shedding weight, avoiding smoking or drinking, etc.

Rating Methods

Insurance rating assesses the cost of the insurance product. Depending upon the type of rating, the price that the buyer has to pay may be — (a) entirely different from the one paid by another customer, (b) the same as that paid by other customers, or (c) similar to that paid by others, but higher or lower in one or two aspects. The various methods of rating are class rating, merit rating, and judgment rating. These are described here.

Class rating

This is the most common type of insurance rating in the insurance sector. The classification of risks is based on a set of common parameters. Risk under the same class is standard. Class rating is also called manual rating as the different classifications of classes and their respective rates are in the form of printed manuals. This type of rating is used for life insurance products where the class rates are similar. The rates are determined based on age, gender, health conditions, habits, etc.

Merit rating

This is a modified version of the class rating. The rate of a particular insured class of products is modified based on the loss experiences. This type of rating is based on the assumption that the loss experienced by individuals will substantially differ from one policyholder to another. Hence, risk rating is based on the extent to which a specific risk differs from others in the same class.

Judgment rating

This type of rating is used when the customer seeks risk coverage for certain unusual risks. These risks are peculiar because there is no statistical information available about similar risks. Besides, the factors to be considered are so varied that it is difficult to determine a common rate for a class of insurance products. The premium determined for such risks is unique and is based on the opinion of the judgment maker. This type of rating is not common in life insurance. It is more often used for non-life insurance products such as marine insurance.

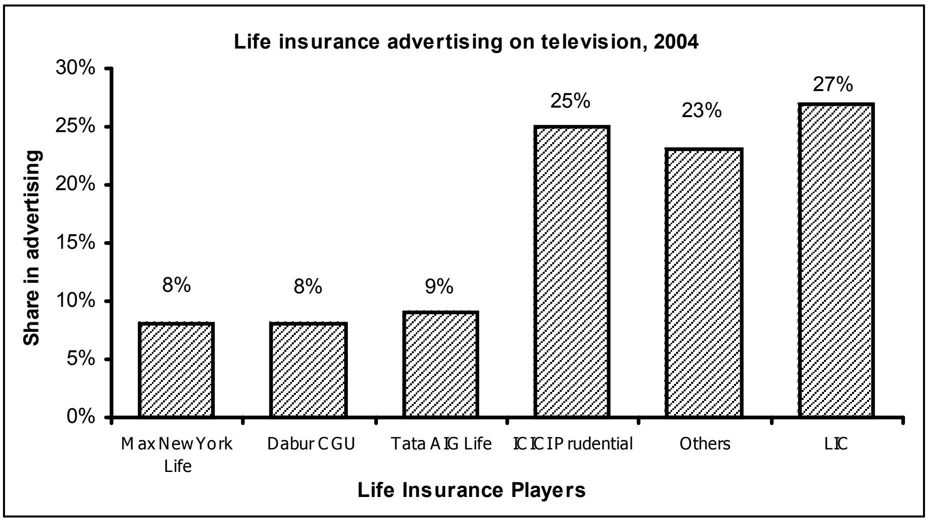
PROMOTIONAL MIX IN LIFE INSURANCE MARKETING

The promotional mix includes advertising, sales promotion, public relations (PR), and personal selling. In financial services, advertising occupies a key role. The nature of services, i.e., intangibility, makes advertising a necessity in insurance marketing. Sales promotional offers to prospective customers are in the form of riders given along with the core product. The more the number of features added to a product, the more attractive it becomes to the end consumer. PR activities are often used to provide the life insurer with a good corporate image. The different PR activities include seminars, awareness workshops, press releases, and special campaigns. The elements of the promotional mix are discussed here.

Advertising

Before liberalization and deregulation, the advertising efforts in the life insurance sector focused on educating the consumers on the significance of life insurance. Consumers looked at life insurance products as a tax saving tool rather than as a product beneficial in times of emergency or risk. The entry of private and foreign players, to some extent, helped shift the focus back to the use of an insurance policy as a risk management tool. Insurance advertising in India is regulated by IRDA regulations. The advertisements are required to be registered with the IRDA. The companies allocate a part of their marketing budget for the purpose of advertising. This share of expenditure is determined based on factors such as the competitor's budget, change in the product line, etc. The year 2004 witnessed a massive spending on the television advertisements by the life insurance companies. Figure 8.2 compares the television advertisement expenditure (in 2004) of the major life insurance companies operating in India.

Figure 8.2: Life Insurance Advertising in 2004



Source: "Indiantelevision.com Presents AdEx India Analysis," 4 January, 2005, http://www.indiantelevision.com/tamadex/y2k5/jan/tam1.htm

From the figure, it is clear that Life Insurance Corporation (LIC) is still the leading advertising spender in the life insurance segment accounting for 27% of the total advertising spend, closely followed by ICICI Prudential, the most successful private player, with 25%. Players such as SBI Life Insurance, OM Kotak Life, Metlife India, together account for 23% of the advertising spend in this segment. The new entrants in the life insurance industry led by ICICI Prudential have used advertising as a tool to gain an edge over the competitor.

Benefits of advertising

The advertising expenditures in the insurance segment have witnessed a phenomenal rise over time. Marketers are banking on advertising to increase their reach and get a firm hold on the market. The benefits of advertising are manifold, especially in insurance services due to their characteristics of intangibility, perishability, inseparability, and heterogeneity. Some of the potential advantages of advertising are discussed here.

Wider reach: Advertising results in wider reach, taking the message to the masses. A major portion of the population, especially the rural segment, gets information from advertisements on television and radio. The cost per individual is also substantially lower in advertising than in sales promotion or direct marketing. Wider reach could result in the conversion of viewers into potential customers.

New product information: Increasing competition has led to the development of many products with each player trying to differentiate itself from others based on the product benefits. Advertising helps insurance marketers convey information about new products and about the special features of their products. Advertisements are also a way of educating the uninsured population about the insurance products of a particular firm and the potential benefits of specific products.

Improved brand image: Advertisements lend the extra edge that a brand needs to enhance its image. Insurance marketers make use of celebrities to endorse their products. For instance, Birla Sun Life has the former Indian cricketer Kapil Dev endorsing its products. Indian cricket captain Rahul Dravid endorsed Max NewYork Life's insurance products.

Sales Promotion

Financial product marketers have a tough time convincing first time users to buy a given product. This is also true of insurance products where the customers have to be repeatedly persuaded to buy a policy. This is primarily due to the nature of insurance products. In such cases, promotional offers serve as a means to attract customers. Insurance marketers and agents are prohibited from using traditional sales promotional tools like free gifts, coupons, contests, etc. The promotional offers are, therefore, often in the form of 'riders', with or without any additional premium having to be paid. These riders are chosen carefully keeping in mind the needs of the customers. Different types of riders and the process of selecting riders are described here.

Riders

Most insurance plans offer life cover to the policyholder. But risk coverage of life alone may not be able to meet the expenses arising due to medical emergencies. Marketers have identified an opportunity here and offer some add-ons to the basic life insurance product to ease the financial burden of the policyholder during hardships. Riders are add-on features (extensions) of an insurance cover that provide special benefits to the customer. They are flexible and can be added to the basic product based on the needs of the customer. The common riders provided by almost every life insurance marketer are critical illness benefit, level term cover, waiver of premium benefit, and accident disability benefit.

Critical illness benefit: This allows product differentiation to a great extent. For instance, Birla Sun Life insurance and LIC of India offer a critical illness benefit rider specifically for women policyholders. This rider provides cover to women from any gynecological and pregnancy related problems.

Level term cover: This rider provides an option to the customer of increasing the risk cover. The insurance cover may be increased for an additional premium, the maximum additional coverage amount being equal to the basic sum assured. For instance, ICICI Prudential's Life Guard (a term assurance plan) offers level term cover in different ways. The risk coverage can be increased equivalent to the sum assured. The other option offered is to initially increase the risk cover for about 50% of the sum assured with the option of securing a further cover for 50% of the sum assured in the event of marriage. Another option is double the sum assured in the case of death during the policy term for an additional premium.

Some insurance marketers have added waiver of the premium as the rider. Under this rider, in the event of disability, a policyholder is allowed a waiver on the premium to be paid on the life insurance cover. It also permits the skipping of premium owing to illness. Some of the other promotional offers could be premium discounts/waiver for a limited period (for the first year), loyalty bonuses, and special premium reductions.

Public Relations (PR)

Building a recognizable corporate image is of increasing importance to insurance marketers. Present day consumers and agents are very demanding and insist on getting as much information as possible about the organization with which they intend to enter into a relationship. Insurance marketers use PR activities to increase the level of awareness about their life insurance products, highlight the use of an insurance product other than as a tax saving instruments, etc. Life insurance marketers issue press releases and conduct seminars, roadshows, and consumer awareness workshops as part of their PR initiatives. Also, some of the insurance marketers engage in social activities to improve company image.

Social initiatives

Social initiatives are a means for the insurance companies to project their social responsibility, either toward society as a whole or toward a particular segment of society. For example, Birla Sun Life has tied up with Sitagita.com, one of the leading Indian portals for women. As part of this tie-up, a portal www.bsliflexitimecareers.com was designed with the objective of creating awareness among women about taking up insurance marketing as a convenient part-time income option. Under this initiative, the company offers women the opportunity to sell life insurance policies of Birla Sun Life as per their convenience. Through this initiative, Birla Sun Life has made an attempt to highlight its focus on empowering women.

Awareness campaigns

The basic use of PR is to disseminate information and create awareness among potential customers. Insurance marketers generally conduct awareness workshops to achieve this objective. To create interest among participants, some marketers have added an element of fun in the form of contests, games, etc. For instance, 'Zindagi Express,'[7] a campaign of the LIC, was launched to celebrate 50 years of LIC's existence. It was an innovative way of exhibiting the history of the life insurance company. A special train christened 'Zindagi Express' was used, with all the bogies being converted into exhibition halls. The exhibits included some rare collections like the insurance receipt of Mahatma Gandhi, insurance policy copy of Rajiv Gandhi, etc. A free diabetes check-up, competitions for children, and lucky draws were other features of the exhibition, to which the general public was allowed free entry.

Personal Selling

To project various products and highlight key benefits to prospective buyers based on the latter's profile and requirements, insurance marketers use personal selling through the company sales force as well as agents. Insurance selling in India is still dependent on the trust and relationship between the seller and the buyer.

The agent, before offering any product, has to know a customer well enough; he/she should get to know the savings habits, health, occupation, financial position and income, moral character, family history, and all other related aspects of the customer, as these will help in field underwriting of a case. After gathering the required data, if the life is found to be insurable, the agent has to prepare a case proposal. Personal selling personnel have a long-term stake in the health of an insurance organization; therefore, they tend to canvass and procure only such business as will be profitable for the insurance company in the long run.

Agents and the sales force are associated with promotions as well as acting as a channel of distribution. Both agents as well as the direct sales force are discussed in the next section on distribution channels for life insurance products.

DISTRIBUTION CHANNELS FOR LIFE INSURANCE PRODUCTS

The distribution strategy adopted by an insurance company is critical for its survival. For years, the insurance companies have been religiously using traditional distribution channels like the direct sales force, network of agents, and the branch network. The dependency on these channels is more because of the nature of the life insurance products. When selling life insurance products, personal interaction is of paramount importance (as discussed earlier). The prospective customer needs constant reassurance about the facts; in this context, one-on-one interaction acquires more significance (direct sales force, agents, brokers, branch network). Alternate channels may provide the extra reach that an insurer looks for but cannot replace the personal attention elements that is the hallmark of the traditional distribution channel.

Direct Sales Force

They are recruited by the insurance company and are directly on the rolls of the company. They establish direct contact with the customer and are paid a salary, unlike agents who are paid a commission based on the number of policies they sell. The sales personnel are responsible for identifying potential customers, garnering information from them to ascertain their risk profile, offering a suitable product, and finally convincing the customers to purchase the life insurance product.

Keeping in mind the potential life-time value of the customer to the marketer, insurance marketers nowadays prefer to use the soft selling or consultative selling approach. This approach also helps them develop a proper risk profile of the customer. In a competitive environment, a loss of trust will lead to a permanent loss of the prospect, and along with it, the opportunity to cross-sell a range of financial products.

As a result, most of the private and foreign players have their own training centers for their sales force or they get corporate trainers to train them. The objective of the sales personnel is to sell the right kind of policy to the right customer. This is expected to reduce the forced selling that agents resort to solely for the purpose of earning higher commissions.

Network of Agents and Brokers

An agent sells insurance policies as a representative of an insurance company. Brokers are intermediaries who negotiate directly with the customers. They are free to fix the premium of the policy after understanding the risk profile of the customer.

Every insurance marketer has their own qualification criteria for the recruitment of agents. These agents are trained on the various facets of the financial products and in personal selling skills. The role of the agents in the life insurance segment varies from that in the non-life insurance segment. In life insurance, the orientation is toward a long-term relationship between the customer and the agent.

Some of the private players have begun to use retired employees as agents as they are able to better connect with people of their own age group and sell specific policies. For instance, Max New York Life recruits such agents who have a large network of friends and acquaintances. Such elderly agents also symbolize experience and wisdom.

Role of agents

As per the IRDA regulations, the agents have certain roles and responsibilities.

- They have to provide full information to the prospect at the point of sale to enable him/her to decide on the best cover or plan.
- They should be well versed in all the plans and the selling points, and should also be equipped to assess the needs of the customer.
- The agents need to adhere to the prescribed Code of Conduct. They must, therefore, familiarize themselves with provisions of the Code of Conduct.
- They must provide the insurance company with accurate information about the prospect for a fair assessment of the risk involved.
- Agents must also possess adequate knowledge of policy servicing and claim settlement procedures so that the policyholders can be guided correctly.
- They must submit proposal forms and proposal deposits to the branch office immediately to avoid delays and to enable the office to take timely decisions.
- The agents should have available with them a leaflet or brochure containing relevant features of the plan that is being sold.

Branch Network

Insurance companies use branches to market their insurance products and provide associated services to the customer. A branch office provides increased reach to facilitate easy availability of the products to the customer. It also helps build a personalized relationship with the customer. The strength of the distribution network of insurance companies can be ascertained by the level of branch network that they possess. The larger the branch network, the greater the reach. LIC has adopted a geographic organization structure where it has offices in every district headquarters in the country.

With Internet technology and telecommunication networks, many decisions that earlier needed the approval of the head office – such as underwriting and the basic risk profile assessment -- are done at the branch itself. As a result, the marketer is able to issue the policy document within a week of the first premium payment.

The branch network is very useful for cross-selling. Customers walking into a branch can be a potential source for purchasing other policies. They can also be a source for word-of-mouth promotions. The next section discusses this aspect.

Cross-selling Life Insurance Products

Cross-selling is an extended form of the distribution process in the insurance segment. It involves a tie-up with an external organization to sell the company's products. Cross-selling attempts to make use of the strength of the partner's channel. It is widely prevalent in the financial services sector. Of late, the insurance segment has realized the potential of cross-selling as a distribution strategy. Life insurance companies have begun to tie up with non-life insurance companies to utilize their branch network and cross-sell products. Exhibit 8.4 describes how New India Assurance & AMP Sanmar (now Reliance Life Insurance Company) have entered into a tie-up to cross-sell insurance products.

Exhibit 8.4

AMP Sanmar & New India Assurance

AMP Sanmar, a private life insurer, has entered into a cross-selling pact with New India Assurance Company Ltd., one of the four public sector companies in the general insurance business. As per their Memorandum of Understanding (MoU), each company would cross-sell the other's products. Under this agreement, New India Assurance Company Ltd. will sell the life insurance products of AMP Sanmar through its 'agency network'. Similarly, AMP Sanmar will sell the general insurance products of New India Assurance Company through its 'Advisor' network. The tie-up with AMP Sanmar will give the personal line products of New India Assurance (personal accident insurance, householder's insurance and health insurance) the much-needed reach in both the rural and urban areas.

The agents and the advisors of both the companies will undergo training on each other's products. This tie-up will make effective use of those agents already trained to sell financial products and who sell on the basis of commissions. The tie-up will also enable the agents of both companies to offer a wider basket of insurance products and play a greater role in a household's financial or wealth management issues. On the whole, this cross-selling agreement is expected to serve three purposes -- increasing the potential income level of the advisor/agent, ensuring a wider reach for both companies, and bringing greater benefits to customers.

Both the insurance companies are exploring the possibility of launching customized co-branded products suited to the customer requirements.

Adapted from "New India Assurance & AMP Sanmar – Join Hands for Selling of Insurance Products" <http://www.niacl.com/pr040819.html>

Cross-selling, though considered a key strategy in selling of insurance policies, is yet to gain prominence because of the restrictions placed by the IRDA on the functioning of agents and sub-agents. Agents can sell only the insurance products of one life insurance company and one non-life insurance company. Besides, IRDA has set restrictions on the appointment of sub-agents. ING Vysya Life uses a judicious mix of branch network and agents. It depends on the Vysya Bank branch network in South India and agents in Northern India.

Bancassurance

In bancassurance, banks sell the insurance products of an insurance company through their branch network. The term bancassurance originated in France around 1980. The bancassurance method also makes use of alternate channels like the ATMs, telebanking, etc., where there is very little one-to-one interaction with the personnel of the service provider. Many insurance marketers have already turned their attention toward banks as a major channel of distribution. Dabur CGU[8] has entered into tie-ups with banks that have a strong regional presence. One such tie-up is with Lakshmi Vilas Bank, a reputed private sector bank. As per IRDA regulations, many banks can market the products of one life insurance company. However, one bank cannot market the products of multiple life insurance companies.

A life insurance marketer has to thoroughly check for the suitability of the bancassurance channel. The criteria for deciding whether to use a bancassurance channel are cost effectiveness, lower dependency, greater penetration, and better quality of service. If the bancassurance model of the insurer satisfies all these four basic criteria, then its inclusion in the distribution channel would be appropriate.

Cost effectiveness: The insurance marketer must be clear and check if the adoption of the bancassurance model would prove cost effective and help increase the distribution reach. The additional volumes in terms of new policies must justify the tie-up costs.

Extent of dependency: Currently, players in the insurance segment depend a lot on the bank to increase distribution. Bancassurance could prove effective if the insurance company is not over-dependent on a single bank.

Penetration: By adopting the bancassurance channel of distribution, the insurance companies should be able to penetrate new market segments, which would have been difficult with other channels of distribution.

Quality of service: The insurance company should be able to display a higher level of service quality to customers. The better service levels of the bank could have a positive rub-off on the image of the insurance marketer.

In the Indian scenario, the concept of bancassurance as a dependable distribution strategy is fast catching the attention of the insurance companies. In India, most of the banking customers maintain their relationship with banks based on the element of trust built up over the years. Insurance products, like banking products, also need to gain the trust of the consumer. Therefore, linking insurance products with the banks would serve to build up the trust between the insurance marketer and the prospect. Besides, banks would have the necessary information about their customers to offer them suitable insurance products and correctly assess the risk profile of the individual.

Estimated figures indicate that in India, less than two percent of the total insurance premium comes through the channel of bancassurance. Of this, the non-life insurance has a very little share compared to life insurance. The insurance companies foresee a huge potential for this channel of distribution, given the vast infrastructure (branch network) of the banks.

SUMMARY

The life insurance business differs from the non-life insurance business on several aspects that range from product nature, risk covers provided, and the agent's role. Life insurance products cater to the needs of the individual and groups of individuals. Generally, insurance products are categorized broadly under term life, whole life, endowment, money back, annuities and pensions, and unit linked schemes.

New product development can play an important role and serve as a key differentiating factor for the insurance marketer. The new product development process consists of a series of steps. They are idea generation (from internal and external sources), idea screening, concept development and testing, business analysis, marketing mix development, test marketing, and commercial launch.

Corporate branding is more common in life insurance than product branding. Brand communication is cautiously done by the insurer to project the right kind of image in the minds of the customer. Customer expectations form a key element of the brand strategy based on which a suitable brand positioning is evolved.

The pricing of insurance products not only affects the sales volume and profitability but also influences the perceived quality in the minds of the consumers. There are several different methods for pricing insurance, based on the insurance marketer's corporate objectives. They are the survival approach, the sales maximization approach, and the profit maximization approach. To determine the insurance premium, marketers consider various factors such as mortality rate, investment earnings, and expenses, in addition to the individual risk profile based on age, health, etc., and the time period/ frequency of payment.

The process of assessing the risk profile of the individual and then fixing the rate of premium is called risk classification or underwriting. In general, the risk can be classified into four categories -- preferred, standard, rated, and declined. The insurance rating methods used to assess the price to be paid by a buyer are -- class rating, merit rating, and judgment rating (more applicable for non-life insurance).

In the promotional mix of life insurance products, where ad spending on the media is concerned, it is more on television than on print ads. The benefits associated with insurance advertising include -- reaching a wide range of population, communicating new product launches, and enhancing the brand image of the insurers and their products. Advertising in the insurance sector has to adhere to the norms set by the IRDA. Public Relations (PR) activities generally include seminars, awareness workshops, and social initiatives.

Insurance marketers and agents are restricted from using traditional sales promotional tools like free gifts, coupons, contests etc. However, they may use riders, which are add-on features of an insurance policy, to customize the product for the customer. The inclusion of riders may provide a larger cover and other instant benefits in times of risk. Agents and the sales force play an important role in both the promotion and the distribution of life insurance products.

The distribution system is composed of the traditional and the alternate channels. The fact that greater reliance is laid on the traditional channels of distribution is due to the nature of the life insurance products, which requires personal interaction. The direct distribution channels adopted are the direct sales force appointed by the company, insurance agents, and the branch network of the insurers. Cross-selling and bancassurance are alternate channels of distribution. Cross-selling is a mutual agreement between two companies to sell each other's products as a part of their distribution process. Bancassurance involves the selling of insurance products through banks. Bancassurance is suitable for the insurer if it can achieve cost effectiveness, avoid over-dependency on a single bank, increase the level of market penetration, and enhance the service quality of the marketer.

End Notes:

[1] Phadnis, Atul. "Insurance Shows Diverse Trends for Life versus Non-life." indiantelevision.com. March 13, 2003.

[2] <http://www.iief.com/wiki/index.php/Postal_Life_Insurance>

[3] Cenlceros, Roberto, and Rupal Parekh. "Product Development Requires Appetite for Risk." Business Insurance. Vol. 39 Issue 3, February 2005.

[4] The Mahalife policy provides income and insurance coverage for life. This can be used to cover the future expenses of the children. Premium is payable only for the first 12 years.

[5] The Nirvana policy is a flexible retirement plan from Tata AIG Life. Accident, critical illness and term riders are available for added protection. The lumpsum paid at retirement or death is tax-free.

[6] Healthfirst guarantees a lumpsum amount, irrespective of the medical bills.

[7] A special train exhibition launched by the LIC of India. The train was flagged off on April 26, 2006, from Safdargunj Railway station, New Delhi, and traveled throughout the country.

[8] It is a joint venture between Dabur and CGU. Dabur is one of India's oldest reputed group of companies with an interest in ayurvedics, pharmaceutical medicine, and personal care. CGU is the wholly owned subsidiary of Aviva Plc.

Chapter 9

Small Savings and Retirement Planning

In this chapter, we will discuss:

- Types of Products
- Pricing
- Advertising, Sales Promotion, and Public Relations
- Distribution
- The Changing Scenario

The concept of pension dates back to 1889 when Otto van Bismarck, Prussia's chancellor, first introduced pension throughout the state. Since then, the governments of all countries have sought ways to provide an income to its citizens post-retirement. The same is the case with India, where the government has attempted to provide financial support to the citizens directly through central/state pension schemes and indirectly through small savings schemes like the postal savings schemes.

Small savings products were marketed in India even prior to independence through the National Savings Organization (NSO), which was later renamed as the National Savings Institute (NSI). The main objective of the NSO was to mobilize finance for the British Government. Over the years, the NSO gradually metamorphosed into the nation's largest savings organization. The NSI is a not-for-profit welfare organization whose objective is to improve the economic condition of the average citizen by creating savings awareness and contributing toward nation building activities by attracting deposits to various small savings schemes. Figure 9.1 gives an overview of India's social security system. It has six components – the Employee Provident Fund Organization (EPFO) schemes, the civil service schemes, the schemes of public enterprises, superannuation plans of the corporate sector, voluntary tax advantaged schemes, and social assistance schemes.

The chapter begins with a description of the various savings and retirement products. The focus is primarily on the small savings and pension schemes of the Government of India. Other sections discuss pricing, promotion, and distribution with respect to small savings schemes and retirement products.

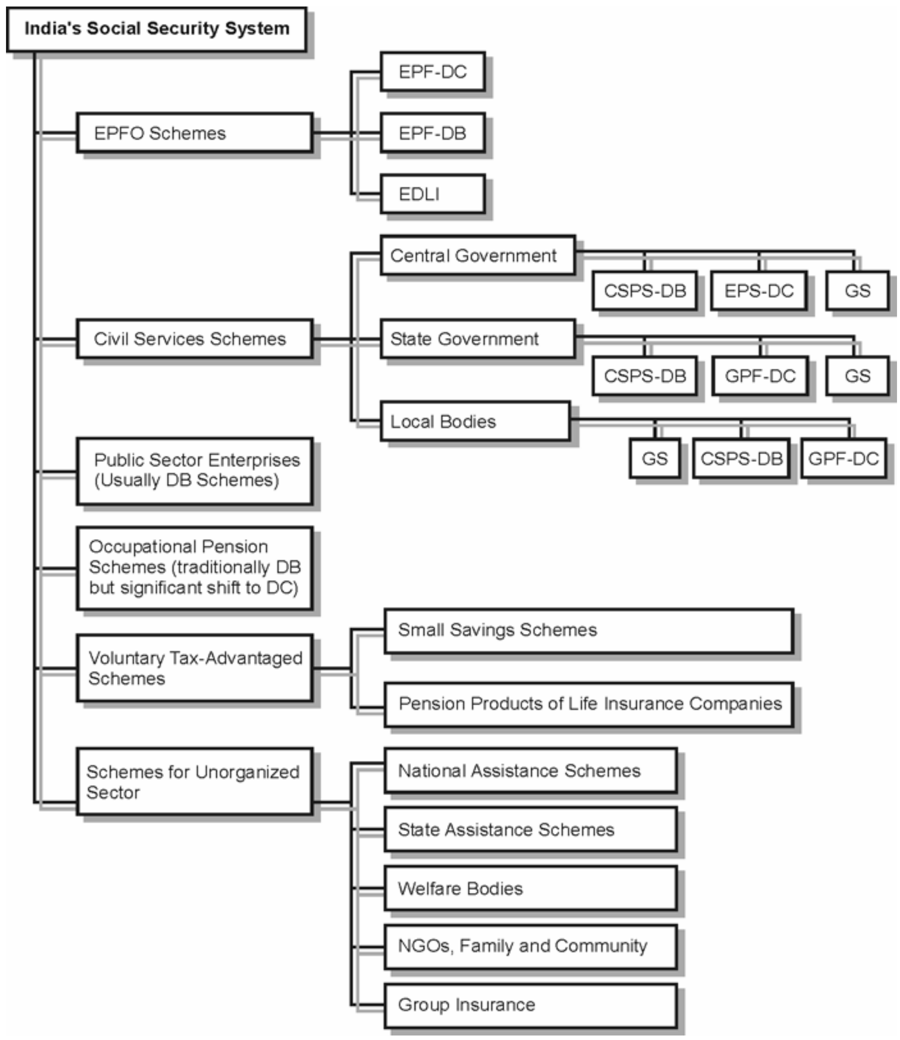
TYPES OF PRODUCTS

The ability to save depends on a lot of factors. These factors include income levels, disposable income available, and spending habits. People save for various reasons such as for anticipated future needs, unforeseen events, to increase wealth with the hope of increasing the standard of living in the future, etc. For instance, an individual may buy a new house out of his/her savings. This is a long-term investment as the individual has the option of selling the house at an increased price in the future. Small savings schemes generally serve the purpose of generating income in the form of interest for the money invested in a particular scheme. Table 9.1 mentions some of the areas into which household savings have been channeled over the years. The majority of the savings flowed into bank deposits, government securities and savings, insurance, provident and pension funds.

Savings Schemes

To promote savings among the people, the ministry of finance has developed many small savings schemes. There are different types of small savings schemes and they differ from one another on parameters like investment limits, maturity period, liquidity and returns, interest rates offered to the depositors and tax concessions, if any. Whenever individuals have small amounts of money at their disposal, the best option for investment is the small savings schemes. Though various other investment products are available, small savings schemes are usually preferred due to their higher safety (lower risk) levels and attractive returns. Some of the small savings schemes available are listed in Table 9.2.

Figure 9.1: India's Social Security System



[EPFO] – Employee Provident Fund Organization
[DC] – Defined Contribution
[DB] – Defined Benefit
[EPF] – Employee Provident Fund
[EPS] – Employee Pension Scheme
[EDLI] – Employee Deposit Linked Insurance
[CSPS] – Civil Service Pension Scheme
[GPF] – Group Provident Fund
[GS] – Group Superannuation plan

Source: Asher, Mukul G. "Pension Issue and Challenges Facing India." Economic and Political Weekly. November 11 2006.

Table 9.1: Break-up of Household Savings (Rupees in billion)

Nature of Savings	2003-04	2002-03	2001-02	2000-01	1999-2000	1998-99	1997-98	1996-98	1995-96	1994-95	1993-94
(1) Gross domestic savings – household sector [2 + 3]	6716.92	5746.81	5131.10	4522.68	4044.01	3268.02	2684.37	2329.14	2155.88	1993.58	1583.10
(2) Net financial savings	3142.61	2544.39	2539.64	2167.74	2057.43	1803.46	1467.77	1411.28	1051.66	1207.33	947.38
(3) Physical assets	3574.31	3202.42	2591.46	2354.94	1996.58	1464.56	1216.60	917.86	1104.22	786.25	635.72
(4) Gross bank deposits	1695.40	1223.04	1027.37	808.80	728.31	698.00	649.25	407.09	327.18	514.00	305.48
(5) Gross claims on Govt.	740.01	626.50	519.40	390.07	289.86	282.20	221.62	117.86	95.88	131.86	69.08
(6) Investment in small savings	572.69	479.96	351.00	348.15	267.89	268.61	193.68	111.01	91.49	131.04	64.51
(7) Shares & debentures	56.99	55.04	77.77	102.14	181.18	69.93	50.60	104.07	91.01	173.81	147.72
(8) Life insurance funds	408.34	402.05	455.46	321.14	268.94	219.36	181.94	151.02	129.34	104.39	87.84
(9) PF & pension funds	504.39	479.32	465.97	478.72	539.07	464.24	322.67	303.89	223.44	214.14	183.23
(10) Net domestic savings – household sector	5799.17	4921.64	4362.88	3861.87	3425.87	2695.51	2160.00	1853.62	1736.59	1654.25	1293.69

Source: www.thehindubusinessline.com/2005/09/12/stories/2005091200150900.htm

Table 9.2: Types of Small Savings Schemes

Title of the Savings Scheme	Deposit Amount Limits (INR)		Maturity Period	Interest Rate	Is Interest Tax-free?
	Minimum	*Maximum*			
Post office Savings Bank Account (POSB)	50	100,000	Open ended	3.5 %	No
Post Office Recurring Deposit Account (PORD)	10	No limit	5 years	7.5 %	No
Post Office Time Deposits (POTD)	200	No limit	1,2,3 & 5 yrs	6.25-7.5%	No
Post Office Monthly Income Scheme (POMIS)	1,000	300,000	6 years	8.0 %	No
Public Provident Fund (PPF)	500	70,000	15 years	8.0 %	Yes, under Sec.80-C
National Savings Certificate (NSC)	100	No limit	6 years	8 % compounded half yearly	Yes, under Sec.80-C
Kisan Vikas Patra (KVP)	No limit		8 yrs 7 months	Deposit is doubled	No
Senior Citizens Savings Scheme	1000	1,500,000	Minimum of 5 years	9.0 % p.a.	No

Adapted from "Small Savings Schemes of the Government of India."
http://finmin.nic.in/the_ministry/dept_eco_affairs/budget/SMALLSAVINGSSCHEMES.pdf

Target audience

The Government of India has a wide range of small saving schemes. Not all products are suitable for everyone. The suitability of products depends on the occupation, age, and the income level of the customers. Table 9.3 shows the kind of customer segments that some of the different small savings schemes are targeted at.

Retirement Schemes

In India, consumers tended to focus their efforts on fulfilling their current requirements and saving for the children. But very little attention was given to post-retirement savings. While doing their financial planning, most people tended to overlook the fact that in the post- retirement stage, a self-support mechanism is necessary. Now, retirement products have slowly become an important component of the financial planning activity. But their market penetration in India is comparatively low when compared to developed nations. Pensions are expected to achieve the goals of minimizing poverty in old age, smoothening inter-temporal life consumption which has significant fluctuations, and ensuring that the retirees' savings last for as long as they live.

Table 9.3: Segmentation across Small Savings Schemes

Target Population	Small Savings Schemes			
	KVP	PORD	NSC	POMIS
Low income group	Yes	Yes		
Middle income group		Yes	Yes	
High Income group			Yes	Yes
Tax payers			Yes	
Non-tax payers	Yes	Yes		
School students				
Farmers, carpenters, small shopkeepers, etc	Yes	Yes		
Industrial workers	Yes	Yes		
Retired officers/ officials				Yes

Note: 'Yes' indicates the scheme in the column, is meant for the target group in the row.

Adapted from www.nsiindia.org

The pension systems in most countries follow a three-pillar structure. The first pillar is made up of publicly-funded schemes providing modest benefits, or social security schemes. The second pillar consists of occupational schemes sponsored by employers for the benefit of employees or private mandatory pension programs. The third pillar consists of additional voluntary contributions to meet retirement needs. Unlike in many developed countries, the 'first pillar' is not very relevant in the Indian context. The 'second pillar' is substantially wider in terms of coverage but is still limited as it does not fully include self-employed professionals and workers, casual laborers, and workers in the unorganized sector. This category of 'unorganized' sector workers needs to resort to the 'third pillar', of voluntary and family-based retirement schemes. Table 9.4 lists the various retirement solutions in India.

Compulsory schemes

The range of retirement planning products is still in its early stages in India compared to that in the developed nations. The compulsory schemes include the employees' provident fund, the employees' pension fund, civil service pension scheme, and government provident fund. These schemes have been the mainstay of the government's effort to provide some social security cover. The drawback of these schemes is that they are limited to employees working with the organized sector. These beneficiaries comprise a very small percentage of the total working population of India. Let us look into two of these schemes in detail.

Table 9.4: Various Retirement Solutions

Program	Legal Coverage	Financing
Compulsory Program:		
Employees' Provident Fund	Employees in firms with more than 20 employees	Employer and employee contributions
Employees' Pension Fund	Employees in firms with more than 20 employees	Employer and government contributions
Civil Service Pension Scheme	Civil servants at state and central level	State or central government budgets
Government Provident Fund	Civil servants at state and central level	Employee contributions
Voluntary Program:		
Public Provident Fund	All individuals	Contributions
Group Superannuation plans	All employees	Contributions
Personal pensions	All individuals	Purchase of annuity-like products
Social Assistance:		
State level social assistance	Varies by state	State budgets
National Old Age Pension Scheme	Destitute persons over age 65	Central budget
National Family Benefit Scheme (NFBS)	People with income below Rs.11,000/- per annum and in the age range 18-64 yrs.	Central budget

Source: Subedhar, S.P "Past to Future- A Look at Pension in India." *IRDA Journal.* *Vol. II No.8, July 2004, pp 8-13.*

EPFO: Established in 1952, this national provident fund offers a defined benefit (Employees Pension Scheme, EPS, introduced in 1995) and a defined contribution (Employee Provident Fund, EPF) scheme for its members. The membership is confined to 181 designated industries, in firms employing more than 20 workers. The total contribution for the EPFO schemes amounts to 25.6 per cent of the wages. The administrative charges, amounting to 4.4 per cent of the contributions, are levied separately. As of 2006, the investment guidelines of the EPFO provided for only debt instruments, and even these were almost fully of the public sector organizations. The investment guidelines of EPFO differ from the insurance regulator's guidelines for the pension products of life insurance companies. In the latter, investment in domestic equities is permitted up to 40 per cent of the total investment funds.

Civil service pension scheme: In January 2004, the central government introduced the national pension scheme (NPS) for civil servants entering government service. The NPS is a defined contribution (DC) scheme, with no pre-retirement withdrawals until age 60. Each employee has an individual account, which is transferable to facilitate the issue of relocation during service. The contribution rate is 10 per cent (of gross salary) each by the government as an employer and by the employee. A member may allocate the balance among a limited number of investment schemes. At age 60, the accumulated amounts will be divided into a compulsory annuity component and a lump sum withdrawal component.

Voluntary schemes

All individuals are eligible for voluntary schemes, irrespective of whether they are employees, self-employed, or businessmen. Voluntary pensions are not mandatory for employees. It is left to the employees' discretion to subscribe to these products. Voluntary pension plans in the formal sector include superannuation schemes. Private players have entered this segment in a big way with a range of retirement solutions.

Public Provident Fund: The public provident fund (PPF) is meant for individuals, whether employed, self-employed, or part of the unorganized workforce. The minimum investment required every year is Rs. 500 and the maximum permitted investment is Rs.70,000. . The rate of interest is 8 % and the term period is 15 years. Interest is tax free under section 80-C. The PPF is both a savings as well as a retirement instrument.

Group Superannuation schemes: These pension schemes are instituted by employers in the interests of the employees. Contributions can be made by only the employer or by both the employer and the employee. Employee contributions can be fixed (for the defined contribution scheme) and defined as a percentage of the salary of the employee (for instance, say 18% of the basic salary). The accumulated amount is paid out in the form of retirement income. Superannuation schemes are implemented in arrangement with a life insurance company or a trust. For instance, ICICI Prudential offers the Group Superannuation plan. The minimum group size required is 25 and the pension is available with different annuity options.

Personal Pension Plans: The pension plans sold by the insurance companies in India can be broadly categorized into unit-linked pension plans and annuities.

In the unit-linked pension plans, the customer is given the option of choosing where to invest his/her amount. The premiums for these pension plans can be paid periodically or in lump sum. The premium so collected from the individuals is invested in funds. The choice of funds is at the will and the interest of the customer and based on the prevalent prices. A portion of the premium amount is used in the fund investment. This percentage of the premium is called the investment content rate. In addition, there is a fund management charge. As per the Insurance Regulatory and Development Authority (IRDA) regulations, the fund management charge cannot exceed 2% per year.

Based on the area of investment and risk associated, unit-linked pension plans can be categorized into liquid funds, secure-managed funds, defensive-managed funds, and balanced-managed funds. In liquid funds, the premium paid is deposited in bank deposits and short-term money market instruments. There is a very low level of risk associated with such an investment portfolio. In secure-managed funds, the premium collected is invested in government securities and bonds issued by various companies. Though unit prices vary, the level of risk attached is low.

In defensive-managed fund, the premium is invested in high-end equities (blue-chip) and the risk associated is moderate. Finally, in balanced-managed funds, the areas of investment include equities, government securities, and bonds. The risk level associated is high.

Besides the pension plans from insurance companies, pension plans are also marketed by mutual fund companies. But they are sold by very few companies in India. Some of the notable pension plans are the Templeton India Pension Plan and the UTI Retirement Benefit Plan. The Templeton India Pension Plan is an open-ended scheme. The feature of this scheme is a balanced allocation between the assets and the equities. Here, 60% of the amount invested goes into the debt instruments and the remaining 40% into equities. The investment into debt instruments gives stability to the portfolio and investment in equities gives capital appreciation in the long term.

The annuities market is quite small in India. If the annuitant starts receiving pension payments immediately after the payment of premium, it is known as an immediate annuity. Generally the premiums in such cases are high, and are paid in lump sum. The Life Insurance Corporation of India (LIC) sells an immediate type of annuity.

Almost all the insurance companies in India offer the deferred type of annuities. In the deferred type of annuity, the annuitants receive pension payments after the deferment period. (The deferment period is the time period over which the annuitant pays the premium in installments). Premiums are generally low in deferred annuities. This is because the deferment period gives an opportunity for the annuity provider (the insurance company) to invest the premium for profits. This brings down the cost of the annuity for the customer. In deferred annuity, one third of the accumulated amount can be withdrawn as lump sum at the time of retirement, and the remaining two-third has to be put into one of the four types of annuities -- life annuity, joint life annuity, annuity for certain (5 /10 /15) years, and annuity with return of capital on death. The UTI Retirement Benefit Plan is a notified pension plan under the UTI Act. This plan provides for pension for the salaried, the self-employed, and professionals. It has certain tax benefits and post retirement income on the maturity of the scheme. It does not guarantee any form of fixed returns, but generally they are in the range of 11-13% depending on the long-term interest rates. The units are sold at a price based on the net asset value (NAV).

Social assistance schemes

The GoI has made efforts to extend the benefits of pension plans to people who do not belong to the 'working class'. Such plans are even more necessary for the large workforce present in the unorganized sector, as they are not entitled to compulsory pensions and are not in a position to opt for voluntary pensions. Generally, the beneficiaries of social assistance schemes include contract/casual labor, farmers, agriculturists, and women workers. There are certain schemes that aim at providing the required financial assistance to the weaker sections of the community. These social assistance programs are called 'Targeted Social Assistance Program' and are instituted by the state and the central governments. The central schemes are the National Old Age Pension Scheme (NOAPS) and National Family Benefit Scheme (NFBS). Let us understand them in further detail.

National Old Age Pension Scheme (NOAPS): An important constituent of the National Social Assistance Program is the National Old age Pension Scheme (NOAPS). Only senior citizens aged 65 years and above are eligible for this scheme. The individual should be a destitute with insignificant or no regular source and support for income. This is determined by the rules of the states and union territories. The pension amount is Rs. 200 per month. Exhibit 9.1 refers to a pioneering social assistance program offered by UTI.

Exhibit 9.1

UTI Offers Pension Scheme for the Unorganized Sector

The central and state governments try to reduce their burden of providing social security to the public. They prefer to give more scope for self-financing social security schemes, which involves some contributions from the individual. In this scenario, UTI has come out with a novel product that would benefit the poorest among those employed in the unorganized sector.

Under this program all the policy holders will be eligible to receive a pension when they retire. This scheme was launched for the women working with SEWA (Self Employed Women's Association). Every woman employee between 18 and 55 years needs to make a minimum contribution of Rs.50/- every month throughout their life. This amount gets accumulated in their pension account and they can draw the amount only after the age of 58. The intermediary between the employed and UTI is the SEWA Bank. It collects the amount, keeps a record, and transfers it to UTI.

Source: Goyal, Malini "Poor Can Retire to a Pension Too." May 01, 2006. < http://economictimes.indiatimes.com/articleshow/msid-1511119,curpg-1.cms >

National Family Benefit Scheme (NFBS): Under this scheme, a consolidated amount of Rs.10,000/- is given on the death of the head of the family. This assistance is given when the age of deceased is above 18 years and up to 64 years. The annual income should be below Rs. 11,000/-.

PRICING

Pricing is an important component of financial product marketing. The pricing structure of the small savings schemes is quite simple. The pricing for retirement products, on the other hand, is more complex. It involves a lot of actuarial calculations. The pricing complexity arises due to the long-term nature of these products. As the future is uncertain, it becomes difficult to evaluate, estimate, and measure costs and returns. The pricing of a retirement system is determined by actuarial valuation.

Small Savings Schemes

The characteristic of the small savings scheme is such that it is difficult to ascertain the exact pricing structure. Small savings were created with the motive of inculcating the savings habit amongst the population. These savings schemes are more as a means of providing social security to the people who are not able to subscribe to savings plans with higher investments. The pricing approach is not uniform for these schemes.

There are many small saving instruments with maturities ranging from less than one year to 15 years, carrying different interest rates. On some instruments, interest is calculated on a quarterly basis or an annual basis, with or without being compounded. Further, certain schemes enjoy the facility of withdrawal after a prescribed lock-in period and certain schemes have to be held up to maturity. According to the budget estimate of 2000-01, the average interest cost incurred by the GoI on these schemes was around 12.22 per cent, as compared to 9.99 per cent on the total borrowings.

The role of Government

The central government has, over the years, reviewed the entire gamut of tax benefits on small savings schemes, with the objective of gradually phasing out the various schemes to rationalize the cost of government borrowing. Many of the small savings schemes offered by the postal department have undergone a reduction in interest rates over the years. Some of the more prominent include the postal savings deposits, postal life insurance, National Savings Certificate, Indira Vikas Patra, and Kisan Vikas Patra. The government has already withdrawn the RBI Relief Bonds and special deposit schemes for retired employees and public sector employees following the report of the Rakesh Mohan Committee on small savings. The report opined that in order to reduce the cost of the government borrowing, the number of small saving schemes should be rationalized and be made taxable. When the interest income is tax exempt, return on these instruments comes to 11-12% (effective return), which is way above the market rates.

Retirement Plans

The cost of a retirement plan is the difference between its assets and liabilities. The 'assets' considered are the sum of return on investment and the contributions made to the pension plan by the individual. The liabilities include the amount to be paid as per the pension plan and the administration expenses. The formula to calculate the cost of the retirement system is as follows:

Cost of retirement system (C) = Assets (A) - Liabilities (L)

C = [Investment returns + Contributions to the plan] (A) – (Benefits to be paid + Administration expenses] (L)

As the cost components as mentioned here cannot be known until the last benefit is paid, these are assessed and statistically estimated by actuarial valuation. A discussion of actuarial valuation techniques is beyond the scope of this book.

Table 9.5 lists certain economic, demographic, and actuarial assumptions that are made during actuarial valuation.

Table 9.5: Assumptions for Actuarial Valuations

Assumptions	Examples of Factors Considered
Economic assumptions: These assumptions relate to the expected long-term financial experience of the plan.	• Annual investment returns • Total inflation • Annual salary increases • Post retirement health premium trend
Demographic assumptions: These assumptions relate to the pension plans' consumer population and their changes over a period of time.	• Mortality rates • Total turnover rate • Retirement rates • Assumed retirement date if before 50 years of age
Actuarial assumptions: These assumptions are used, in addition to the economic and demographic assumptions, in actuarial analysis.	• Spouse's age • Contribution refund rate • New entrants • Dependent children • Medical benefit valuation

Source: "Actuarial Valuation."
http://www.akrepublicans.org/senfin/24/pdfs/senfin_sb141_04.pdf

ADVERTISING, SALES PROMOTION, AND PUBLIC RELATIONS

Small savings and term deposits are believed to account for more than 50% of the annual savings by Indian households. This is the case even after many policy changes have considerably eroded the attractiveness of many of these instruments. Over the years, the central and state governments have been promoting small savings schemes. Most of the small savings schemes have been promoted by the National Savings Organization (NSI), along with its state and district level branches. The postal department also has played a significant role in promoting various savings schemes. One of the reasons for the continuing popularity of these instruments is the extensive network of bank branches and post offices. Distribution of other financial products is only now penetrating into Tier-2 cities. Another explanation could be tax evasion. If no tax were to be paid, returns from these instruments would be superior to the returns from debt mutual funds.

For small savings, promotional efforts have been largely driven by commissions, incentives, sweepstake offers, and lucky draws. See Exhibit 9.2 for promotional efforts by the Small Savings wing of the Finance Department of Government of Andhra Pradesh.

Exhibit 9.2

Promoting Small Savings – Government of AP

The Small Savings wing of the Finance Department of the Government of Andhra Pradesh has used various means to market small savings schemes to the people of the state. By a large-scale increase in the number of agents, the Small Savings wing has been able to penetrate deeply into rural areas. The department has also identified certain districts with high potential, such as East Godavari, which can yield better collections. Special campaigns have been conducted in such districts.

In the urban markets, it has highlighted the attractive interest rates being offered in comparison to the market rates. Some of the department's ads have also highlighted the fact that PPF savings cannot be attached by courts, in case of any legal dispute. The department adopted a novel approach to increase deposits from the Old City region of Hyderabad, with an eye on tapping the huge receipts from Gulf-based NRIs. It took the help of girl students above 18 years of age to promote the small savings schemes.

Compiled from various sources.

When compared to small savings, retirement products have witnessed better promotional efforts in terms of advertising and brand-building, especially with the entry of private players and nationalized banks. Also, PR activities serve the purpose of creating awareness, and making the brand presence felt. The media strategy, advertisement appeals, promotions, and public relation activities are discussed in the following sections. (For details on the personal selling component of the promotional mix, refer to the next section on distribution.)

Media Strategy

If creating well-structured advertisements is one aspect of communication that is important, the medium of communication itself is much more critical. A plethora of media options are available for the financial product marketers to reach out to consumers.

Media strategy for small savings

Small savings schemes are promoted by the central/state governments. Advertising is not a major factor since these schemes are much sought after by the public. The small savings schemes reach out to consumers using the print media, films, television, distribution of leaflets, audiovisual material, and the radio. The radio (All India Radio) is the mainstay of advertising small savings schemes, especially to target the rural population. Leaflets are a common tool to get the message across to the consumers. These leaflets are educative in nature and provide a snapshot of the savings schemes currently in force. The regional offices, depending on their financial health, try to grab the attention of the public with the help of TV commercials. The ads cater to a wider audience. In addition, viewers can educate their near and dear ones about the small savings schemes.

Media strategy for retirement plans

Marketers of retirement products use multiple communication media such as television, press, radio, the Internet, direct marketing, etc. Due to the increased competition in the retirement products segment, the media expenditures are high.

The television is considered to be the main medium for reaching out to a wide audience and with the potential to deliver a considerable amount of impact. Also, this medium has the advantage of having an audio-visual effect that is usually required in order to use various advertising appeals to attract customers. For example, one of the ads of Life Insurance Corporation of India (LIC) shows a doting father holding his young daughter and saying, “I fulfill all her needs so that she can stand on her feet.” The next shot shows him dutifully filling out his LIC pension premium so that he can take care of himself in the years to come. Then the father sees himself as an elderly man and visualizes himself handing over a gift to his grandson. The next shot shows the young father leaning back in his chair with a big smile, after filling up a cheque to pay the premium for his pension policy with LIC.

The advertisements in the form of print ads are intended to reinforce the benefits of saving early. The special features of the retirement product as provided by the company are highlighted in the ads. The best press medium is chosen basing on the response rate in relation to the ads. The growing popularity of FM radio channels has also been exploited for promoting retirement products. Since most of the youth listen to FM channels, it is an ideal channel to communicate information about retirement products to young adults. Exhibit 9.3 describes the media strategy of ICICI Prudential for its retirement solutions.

Exhibit 9.3

ICICI Prudential’s Multi-dimensional Communication Strategy

ICICI Prudential (ICICI Pru) was the first financial marketer in India to effectively implement a multi-dimensional communication strategy for its retirement solutions. The creative strategy was to offer a fresh perspective to adults in the 30-35 age group on retirement planning. The objective was to highlight the ‘never-say-die’ attitude of this age group. . Keeping this in mind, ICICI Pru designed the advertising message “Retire from work – not life!” The basic focus of the media strategy was to target the prospective customers through various media channels so that they were exposed to the advertisement at some time or the other in a day, through any of these multiple touch points. The media channels used in this campaign included television, print, radio, outdoor hoardings, the Internet, and direct mail.

Television: This medium was used to gain greater reach, and have better impact since the audio-visual advantage could be exploited for communicating the emotional benefits of taking a retirement plan. The initial ads were 40 seconds in duration. The later ads were shorter (20-30 second) versions.

Print: ICICI Pru made use of print advertising that focused on the rational appeal by highlighting the basic features of the retirement products. The media vehicle to be used (newspaper, magazine) was selected on the basis of cost per response. An educative booklet in the form of a planner was developed and distributed along with the Brand Equity supplement of *The Economic Times*, a leading business newspaper.

Radio & outdoor advertising: ICICI Pru targeted urban consumers through FM channels like Radio Mirchi and Radio City. The ads were aired during the morning and evening hours to target 30-35 year-olds who tuned in to FM radio while commuting to or from office. Outdoor ads in the form of hoardings were put up at major traffic junctions in select cities.

Internet and direct marketing: Banner ads and pop-up ads were used in major financial websites and other popular sites of general interest. Besides, a retirement calculator was hosted on the company website, which helped prospective customers calculate the current savings required to meet post-retirement expenses. Also, mailers and brochures were used to educate the consumer on the rationale behind planning early for retirement and the advantages of ICICI Pru Retirement Solutions. The database of existing customers of the ICICI group was used to send mailers.

Compiled from various sources

Advertisement Appeals for Retirement Solutions

Advertisements are a means to communicate with the end consumers. Financial marketers can make use of different advertising appeals to market their products. Such appeals are incorporated into the advertisements to make the consumers perceive the products in the manner desired by the marketer. Creation of an advertising appeal depends on the message that the marketer wishes to communicate. This section focuses on advertising for retirement products using emotional appeal, fear-based appeal, and zealous appeal.

Emotional appeal

The nature of the pension product category leads marketers to build on the emotions of the individuals. Pension products are positioned so that they act as safeguards in the life of the individual, in times of financial irregularities or unexpected events. An emotional appeal is the most common type of appeal used by the pension marketers. Exhibit 9.4 describes the use of the romantic appeal in advertisements of SBI pension plan products.

Fear-based appeal

This is a traditional appeal that has been used by most insurance marketers, especially for retirement products. This type of appeal tries to address the basic fear factor about retirement, i.e., financial instability. Many individuals are apprehensive about losing their financial independence after retirement. The fear-based appeal tries to address this fear and to convince the prospect that planning early could lead to a more joyous life after retirement.

For instance, HDFC Standard Life used such an appeal to promote its retirement solution. The television commercial (TVC) was set in the context of a grandfather–grandson relationship. The TVC begins with a boy (Binku) pleading with his grandfather to present him with a bicycle on his birthday.The boy's father overhears the boy's plea. . The next day, Binku's father approaches his father (Binku's grandfather) and says: "Babuji, Binku *ne kal jo* cycle *dekhi thi na, toh maine socha…*" (Dad, Binku saw a cycle yesterday, didn't he? So I thought…) and hesitantly hands over a cheque for the required amount. He adds, "*Warna usey bura lagega*" (otherwise Binku will be upset).

Exhibit 9.4

'Unretiring Romance' with SBI Life Pension Plan

Of late, the trend in India is toward nuclear families. This has led to a situation where many elders are having to face the hardship of trying to sustain themselves in the absence of proper financial support from their children. So it is commonly believed that retirement brings in its wake an end to all the pleasures and precious moments of a youthful and vibrant life. And it was just this notion that State Bank of India's life insurance venture (SBI Life) sought to dispel. It did so with its advertisement for its pension plan. The ad campaign was targeted at the 25-30 year segment to drive home the message that even after retirement there could be romance and lots of color in life. The thrust of the message was that one should invest early to reap the benefits during the post-retirement phase of life.

The advertisement for the pension plan had an emotional appeal. It tried to leverage on the emotions of the elderly. The objective of the advertising campaign was to prove the point that financial constraints should not act as an inhibitor in expressing love.

The TV Commercial (TVC) first shows an elderly woman working at her sewing machine. She leans forward, concentrating on her task. The next scene shows her husband talking to her. A few moments later, he gives her a Valentine Day's gift — a small red colored box. She opens it and to her surprise, sees a sparkling diamond ring nestling inside. She gazes at it longingly but exclaims that it is too costly and not suitable for someone her age. Her husband gets around her objections by remarking, "Arre, heere ko kya pata tumhari umar!" (The diamond does not know your age!). The advertisement ends with a reminder "Taake pyaar ke beech kabhi paison ki kami na aaye" (So that money never comes in the way of love) followed by a mention of the company's retirement soution.

Source: Dixit, Sumita Vaid. "Life is beautiful at 60, courtesy SBI's pension plan." November 08, 2004. < http://www.agencyfaqs.com/news/stories/2004/11/08/10232.html. >

The grandfather gives a slight smile, and calls out to his grandson. Binku comes riding on a new bicycle — just the one he had asked for. The astounded father turns to look at the grandfather who returns the cheque to him, saying, , "*Rakh lo, warna mujhe bura lagega!*" (Keep it, otherwise I will be upset!). The advertisement concludes with a voice-over "Pension plans from HDFC Standard Life. Retirement *ke liye aaj hi* plan *kare. Taaki yeh haath jab bhi badey, dene ke liye badey.*" (Plan for retirement today so that whenever you extend your hand, it is to give).

Zealous appeal

Zealous appeals tend to infuse energy into the viewer by presenting facts in a humorous way. The use of this type of advertising appeal makes the viewers more optimistic and eager to experiment with the advertised product or service. As zealous appeals create more positive interest, financial product marketers have resorted to using such appeals as traditional ads for financial products are generally considered to be quite boring. An example of an advertisement with zealous appeal is the TATA AIG ad for its retirement solutions (Nirvana, MahaLife, etc).

The television ad shows a young man going to an apparel store to check out some T-shirts for himself. The store manager helps him find the right size but the man buys a larger one. The manager is surprised but accepts the payment. The next few shots feature the man coming in day after day and buying larger T-shirts (relative to his size). The last shot shows a scene 20 years later. The manager meets the buyer and sees him wearing the same set of clothes he had bought from the store. The voiceover states "Zindagi hamein sikhati hai aage ki sochna. Jiyo apni man chahi zindagi new life retirement options ke saath. From Tata AIG Life. Aap kya karna chahenge? (Life teaches us to think of the future. Live life the way you want with new life retirement options from Tata AIG Life. What do you want to do?)

Sales Promotion

Sales promotions for retirement products are very limited as products like PPF are primarily promoted through agents. IRDA guidelines stipulate that consumer promotions such as gifts to induce prospects to purchase an insurance product or pension plan, are not permitted. Contests and prizes are restricted to trade promotions, that is, for the agents. On the other hand, sales promotions are an important component of the marketing plan for small savings schemes. All the promotional activities for small savings schemes are undertaken by the National Savings Organization (NSO)[1]. On its direction, the small savings offices across the states carry out the promotional activities. Every state has a Directorate for Small Savings that is responsible for the overall marketing activities in the state. In this section we will focus on sales promotions of small savings schemes.

Sales promotions for small savings schemes generally include sweepstake offers, contests, etc. In addition, special campaigns may be conducted to collect deposits in postal savings schemes. For instance, the state government of Tamil Nadu encourages small savings through a sustained publicity campaign and payment of incentives for agents and officers of local bodies. To encourage local bodies to actively participate in small saving collections, incentive (in the form of grants) are sanctioned by the state government every year, based on the incremental net collection achieved over the previous year. This scheme aims at creating a healthy competition among the district officers in mobilizing small savings in the areas within their jurisdiction. For 2005-06, a sum of Rs. 400 million was sanctioned as incentive to the districts that performed well. The funds were utilized for improving infrastructure facilities like school buildings, noon meal centers, health centers, etc. Let us now focus on sweepstakes and special campaigns.

Sweepstake offers

Sweepstake offers are often used to promote small savings schemes. Through these schemes, the consumers stand a chance of winning a prize, generally in the form of a new car or a large amount of cash. The winners are generally selected through a lucky draw. The directorates under each state adopt unique ways of promoting the small savings schemes. For instance, the Directorate of Small Savings, Madhya Pradesh[2], instituted the Bhagyodaya Yojana (2004-2005) effective for the period June 01, 2004, to March 31, 2005. As a part of this campaign, prospective customers who invested at least Rs. 5,000/- in any of the small savings schemes [Kisan Vikas Patra, 6 year National Saving Certificate (VIIIth Issue), 5 year Post office Recurring deposit Account (on deposits of amount in new accounts opened between June 01, 2004, and March 31, 2005), Post Office Monthly Income Scheme, Post Office 2, 3, 5 years time deposit account, 15 years Public Provident Fund Account, Senior Citizen Savings Scheme] during the period were issued a free coupon. Everyone with the coupon became eligible for a bumper prize of Rs. 2,500,000 as cash. In addition to the bumper cash prize, there were other cash prizes ranging from Rs.25,000/- to Rs.200,000/-. There were 6,664 prizes to be won; the total worth of the prizes under this promotional campaign was Rs.54.1 million.

Special campaigns

The central or state government may also organize special drives to collect deposits from the public. These campaigns are carried out by the district small savings department from time to time. The objective is to highlight the benefits of particular products and educate the public on the importance of small saving schemes. Special campaigns help the government achieve a set target for a specific savings scheme in a given geographical region. For instance, the Kerala Government offered a jeep to district collectorates for every Rs 50 million mobilized in the districts that exceeded their individual targets as part of the National Savings Scheme (NSS) drive. The collectors of the districts where the achievements exceeded the target were separately rewarded[3].

Public Relations

Public relations (PR) activities are another important component of the promotional strategy used by marketers of small savings and retirement products. The objectives of using PR are more or less similar for both small savings as well as retirement products, that is, to educate and create awareness among the public about the importance of small savings and retirement planning. However, the activities undertaken as part of the PR campaign differ slightly between small savings and retirement products.

PR in small savings

Creating awareness about the savings schemes is the major focus of all the publicity campaigns. The objective of different types of publicity campaigns is to try to educate the population about the need and importance of the savings schemes and their uses. There are different ways by which the small savings offices engage in the PR activities. They are distribution of pamphlets and stickers, putting up hoardings, conducting dramas in villages, putting up exhibition, distributing handbills, organizing seminars, giving out press kits, using the publicity van, organizing events, etc. Some of these are discussed here.

Publicity vans: A majority of the small savings offices use vans to promote the savings schemes. For instance, the Directorate of Small Savings, Tamil Nadu, makes extensive use of van campaigning in each panchayat. The personnel use the vans to travel across villages and educate the rural population on the various small savings schemes through small skits, speeches, etc[4].

Events: Different events conducted by the small savings offices help attract people in larger numbers. Some of the popular events are the celebrations associated with Women's Savings Day, Sanchayika Day, and World Thrift Day. For illustrative details, refer to Table 9.6.

Table 9.6: Events to Promote Small Savings

Event	Day	Significance
Women's Savings Day	April 14	Conducted in each district across the country, the Mahila Pradhan Kshetriya Bachat Yojana (MPKBY) agents are felicitated and their services are recognized on this day.
Sanchayika Day	September 15	The importance of savings and thrift is imparted to the school children across the country, by agents and personnel (of the small savings department) who deliver talks in various schools.
World Thrift Day	October 30	The agents, investors etc., who mobilized highest collection under small savings, are given awards on that day.

Compiled from various sources

PR in retirement solutions

The PR efforts of marketers are mainly focused on the achievement of two objectives — consumer awareness and brand receptivity. Every activity related to the future like education, career path, etc., needs lot of planning. But retirement planning needs even greater awareness and planning from consumers, as they tend to postpone it. Most government schemes such as PPF and EPF, focus on this objective. The private players providing retirement schemes also make this the focal point of their publicity campaigns. They try to create an awareness about the importance of retirement planning by targeting the potential segments, especially those in the 25-35 age bracket.

The other objective of PR for retirement products marketers is brand receptivity. This is especially important for private players. The marketers make efforts to ensure that their brand(s) are easily recognized and become the preferred choice(s). The PR activities try to highlight the legacy of the corporate brand, successes with previous products, superiority over competitor products, etc.

To achieve these objectives, the marketers of retirement solutions engage in various PR activities. The most commonly used PR activities are conducting seminars, issuing retirement planner booklets, and providing retirement calculators on the website of the company. The financial products need to gain visibility and acceptance as the most trusted player in the given segment of operation. The public relation activities provide this advantage.

Seminars: These seminars serve the purpose of educating the consumers about the need for retirement planning and how it would give them a head start for a comfortable retired life. These seminars are for the general public and generally do not have any entry fees. For instance, ICICI Prudential organized retirement solutions seminars through a tie-up with *The Times of India*. Full-page educative advertorials were released in three metros, inviting consumers for a free seminar on early retirement planning.

Retirement planners: Marketers also use retirement planners as part of their PR activities. Educative booklets in the form of planners are developed and distributed. These are used to convince prospects about the advantages of retirement planning early in life.

Retirement calculators: This an interactive approach adopted by most retirement product marketers. The retirement calculators are available on the respective websites of most financial marketers. With the help of these calculators, prospective customers could calculate the current amount of savings required in order to support the retirement expenses in the future. They could also learn about the various retirement solutions offered.

DISTRIBUTION

Distribution is another important function in the marketing of small savings and retirement products. The small savings schemes are distributed both through direct and indirect distribution channels. The distribution system for the retirement products is similar to that of life insurance products. It makes use of the personal selling channel, along with alternate channels of distribution like direct selling agents and bancassurance. These distribution channels also perform the function of promoting these products in terms of creating awareness, interest, and desire to consume these products. The distribution methods across small savings schemes and retirement products are discussed here.

Distribution of Small Savings Schemes

The National Savings Institute, under the Union Ministry of Finance, Department of Economic Affairs, Government of India, is responsible for mobilizing small savings across the country. The distribution mechanism is coordinated across the NSI, State directorates, and district small savings offices. The small savings schemes are distributed through direct and indirect distribution channels. Direct distribution is through personal selling by agents recruited by the small savings office. The channels of indirect distribution are post offices, branch networks of nationalized banks, and select branches of private banks. The distribution mechanism and the distribution intermediaries are discussed here.

Personal selling through agents

Small savings schemes are primarily sold by the small savings offices through field agents. The agents are classified based on the type of schemes they promote and the authorities they have to liaise with. The most common categories of agents are those under the Standardized Agency System, Mahila Pradhan Kshetriya Bachat Yojana (MPKBY), and the Public Provident Fund Agency Scheme. The role of these agents and the eligibility requirements vary across the categories. Table 9.7 lists the common types of agents and the schemes they sell, eligibility criteria, liaison activities, and commission levels as a percentage of the savings mobilized.

Table 9.7: Types of Agents

Characteristics	Types of Agents		
	Standard Agency System (SAS)	***Mahila Pradhan Kshetriya Bachat Yojana (MPKBY)***	***Public Provident Fund Agency***
Type of scheme	To promote the sale of Kisan Vikas Patra (KVP), National Savings Scheme (NSC), Time deposit, Monthly Income Scheme (MIS) etc.	To promote the sale of Recurring Deposits (RDs).	To promote the Public Provident Fund Scheme (PPF).
Eligibility	• Individuals Co-operative societies • Scheduled banks • Registered social service organizations • Universities • Gram panchayats.	Only individual women and women's organizations (The organization should be involved in social, religious, educational, recreational, or charitable work).	Literate adults. The individuals should be residents of the concerned district and possess wide contacts.
Liaise between	Investor/ depositor and small savings offices.	Investor, post office, and small savings offices.	Investor, post office, authorized banks and small savings offices.
Commission	0.5% to 1%	4 %	1 %

Compiled from various sources

In addition to those mentioned in Table 9.7, agents also come under the Payroll Savings Groups, School Savings Bank (Sanchayikas), and the Extra Departmental Branch Postmaster categories. Certain small savings offices make effective use of these additional agent categories that are also a part of the small savings distribution system.

Payroll savings groups: Under this scheme, every salaried employee is a prospect. From the salary of the employee, a pre-decided amount is deducted every month after arriving at a mutual agreement. The agents need to associate with the employers to sell the scheme to the employees. Every district small savings office decides on targets for this scheme.

School savings banks (Sanchayikas): The objective of these savings schemes is to inculcate the habit of saving at an early stage, in school students. There are special agents to make school students subscribe to these savings groups. This scheme is monitored with the help of the school faculty.

Indirect distribution

Indirect distribution channels, as mentioned earlier, include post offices, branch networks of nationalized banks, and select branches of private banks. These are indirect channels as the agents do not directly meet the customers. The customers come to the branches to purchase the small savings scheme.

Post offices: Post offices are the most preferred distribution channel for small savings schemes due to their high reach in terms of number of branches spread across the country. There are 154,000 post offices present across the country and they are easily accessible, especially to the rural population.

Branch network of nationalized banks: Small savings products are also distributed through the branches of the nationalized banks. There are more than 8,000 branches of nationalized banks across the country and the government makes use of them to sell certain savings schemes, such as the Senior Citizens Savings Scheme.

Private bank branches: The Ministry of Finance has permitted select branches of a few private banks to sell the small savings schemes. The private banks authorized are IDBI Bank, ICICI Bank, HDFC Bank, and UTI Bank. For example, ICICI Bank is authorized to collect funds for PPF at branches mandated by the Ministry of Finance. It can also receive subscriptions and act as a collecting and servicing agent for the Senior Citizen Savings Scheme, 2004.

Distribution of Retirement Products

Depending on the size and the financial strength of the company, the number of channels used increases. For retirement solutions, direct distribution includes a direct sales force (personal selling) and direct marketing efforts. Retirement product marketers have begun to make greater use of indirect distribution channels. Direct Selling Agents (DSAs) and bancassurance are two such channels that the marketers focus on, as their indirect channels of distribution.

Direct sales force (DSF): Personal selling is the most effective medium of distribution for retirement products. This is because personal selling ensures relationship building through direct contact. Personal selling is done by the direct sales force, who are directly employed by the company. The direct selling process usually consists of seven stages: Prospecting, Pre-approach, Approach, Sales presentation, Handling objections/sales resistance, Close, and Post sales follow-up. At each stage, the salesperson adopts different selling techniques, which depend on the product and the type of customer.

During the process of selling, the sales personnel try to build up trust, which lays the foundation for a truly rewarding long-term relationship. Well-established relationships are essential for selling financial services, including retirement planning products. Due to this reason, some of the private players recruit people aged above fifty years to be part of the sales team. Such senior people usually have a vast network of friends, and adults tend to respect product advice from experienced elders.

Direct marketing: In this form of direct distribution, the marketer tries to establish contact with the end customer without the use of personal selling. This is achieved through postal mail, telephone, and e-mail. In direct marketing, a more focused approach with due caution in the selection of the target group is needed. For instance, ICICI Prudential (as discussed earlier) made use of the existing database of its customers to target potential customers in the target age group for its retirement products. The databases included customers/subscribers to other products offered by ICICI Bank like credit cards, Safety Bonds, etc.

Direct Selling Agents: DSAs are agencies (intermediaries) involved in selling financial products on behalf of the financial product marketer. Any financial products marketer can enter into a mutual agreement with the DSAs to sell their products. The effectiveness of the DSAs in marketing financial products depends on their reputation and previous experience with the clients.

However, marketers in India tend to look at distribution of retirement products through DSAs with some concern as it results in a lack of control over the selling activities and approaches that may not be up to the marketers' standards. The retirement products marketer has to ensure that the agreement with a DSA includes stipulations that the DSA's personnel follow the code of conduct[5] while interacting with customers. The DSA and its Tele-Marketing Executives (TMEs) & field sales personnel must agree to abide by this code before undertaking any direct marketing operation on behalf of the financial marketer. It should be stipulated that failure to comply with this requirement will result in termination of the business of the DSA with the financial marketer and may even lead to permanent blacklisting by the industry.

Bancassurance: Bancassurance is the selling of insurance products (including pension products) through the branch network of banks. Insurance companies stand to gain a lot by using this indirect channel of distribution. Banks in India have been able to gain the trust of customers. Nationalized banks with their wide networks of branches can ensure better coverage of the market, including in rural areas. Another advantage of opting for the bancassurance channel is the reduction in distribution costs of the insurance marketer.

THE CHANGING SCENARIO

The Ministry of Finance has been focusing on rationalizing the hitherto unwieldy small savings schemes and pension plans offered by the Government. The authorities have, over the past few years, reduced the over-reliance (by the general public) on some of these products as tax saving instruments. For instance, earlier, interest earnings from investment avenues like fixed deposits, National Savings Certificate (NSC), and Post Office Monthly Income Scheme (POMIS) were eligible for tax exemption under Section 80L. These benefits were later removed. Removal of these benefits has considerably reduced the attractiveness of these schemes in terms of effective post-tax returns. Pension plans have also been hit. Subscribers to the Employees' Provident Fund (EPF) have witnessed a reduction in the interest rate. It was reduced from 9.5% in 2004-05 to 8.5% in 2005-06. The rates are subject to annual review, and may be slashed further in the forthcoming years.

These reforms have already begun to show their effects, from 2006. Gross small savings collections have started to decline on a year-on-year basis. There has been the shift in household preferences to bank deposits, especially long-term deposits with tax exemptions attached. Besides, the threat of rising inflation is leading to a preference toward equity products, though only to a limited extent, as a hedge against the decline in the value of savings. This shift in preferences augurs well for the non-traditional financial products being offered by the private players, while agents of small savings schemes could find their job becoming tougher.

SUMMARY

The objective of savings is to cater to future needs. The small savings schemes introduced by the Government of India help people develop the habit of savings to finance their future needs. The concept of retirement planning in India is still at a nascent stage. This could be attributed to the low income levels and the lack of awareness about the importance of retirement planning early in life.

There are different types of small savings schemes and they differ from one another on parameters like investment limits, maturity period, liquidity and returns, interest rates offered to the depositors and tax concessions, if any. When individuals have small amounts of money at their disposal, the best option for investment is the small savings schemes. The pension plans can be categorized under compulsory, voluntary, and social assistance schemes. The compulsory schemes include the employee provident fund, employee pension fund, civil service pension scheme, group superannuation plan, etc. Pensions under the voluntary category include products offered by private banks, the post office, insurance, and mutual fund companies. The targeted social assistance programs are meant for a specific target group, usually from the economically weaker sections of the society. They include the National Old Age Pension Scheme (NOAPS) and National Family Benefit Scheme (NFBS) under the center.

Pricing of the small savings schemes is not rational in the sense that different savings schemes have differing interest rates, maturity terms, liquidity, and returns. Most of the savings schemes were launched by the government as a social security measure and to mop up funds for social development. The determination of the cost of a retirement plan is a difficult task. The cost of a retirement plan is the difference of the assets (the sum of investment returns and the contributions made to the pension plan) and liabilities (benefits to be paid as per the pension plan and the administration expenses) possessed by the retirement solutions marketer. These components of the cost system are measured and estimated by the complex process of actuarial valuation.

Promotions are very important in marketing small savings schemes and retirement products. They are used by both the public as well as the private sector. Advertising in the small savings category makes effective use of radio and print ads. The media strategy of retirement solution providers includes greater emphasis on television advertising supported by radio (FM radio) and print advertising. Various appeals used by marketers for advertising include emotional, fear-evoking, and zealous appeals.

The sales promotion activities with regard to the small savings are managed by the National Savings Institute (NSI). These promotional activities include contests, special campaigns, and sweepstake offers. Sales promotions are restricted in retirement products, especially pension plans of insurance marketers as there are certain restrictions imposed on offering gifts and conducting contests.

The public relation activities of small savings marketers include distribution of pamphlets, hoardings, conducting dramas in villages, exhibition, handbills, seminars, press release, etc. The PR activities of marketers of retirement products primarily focus on two objectives – increasing consumer awareness and improving brand receptivity among customers. Increasing awareness is preferred by the government and branding is the focus of private players. The PR activities include conducting seminars on retirement solutions, distributing retirement planners, and providing retirement calculators.

Distribution for small savings as well as retirement products is through direct and indirect channels. The direct distribution is through the personal selling. Personal selling is done by the agents who are categorized based on the type of the scheme and the target group. The agents are crucial in the mobilization of savings. There are generally three types of agents, viz., Standard Agency System, Mahila Pradhan Kshetriya Bachat Yojana (MPKBY), and the Public Provident Fund Agency. Indirect distribution makes use of channels like post offices, and the branch network of public and private banks. The distribution of retirement products is also done through the direct sales force and agents (direct distribution) and through the bancasssurance route and Direct Selling Agents (indirect distribution).

End Notes:

1 The National Savings Organization promotes the sale of savings certificates and other savings schemes. NSO appoints agents for its promotional activities.

2 The Directorate of Small Savings, Madhya Pradesh, was established in 1966 with the objective of motivating people to invest in the small savings schemes. This directorate supervises the functioning of the small savings offices located across the district headquarters of the state. At the district level, they are monitored by the respective District Collectors.

3 "Kerala CM for Drive to Meet NSS Target." The Hindu Business Line. 03/2/2003.

4 http://www.tnsmallsavings.com/pclip.htm.

5 The Model Code of Conduct for the Direct Selling Agents (DSAs) is a non-statutory code issued by Indian Banks' Association, a voluntary association of banks in India, for adoption and implementation by DSAs while operating as agents of Banks and Financial Institutions.

Chapter 10

Mutual Funds

In this chapter, we will discuss:

- Evolution of Mutual Funds in India
- Organizational Set-up of a Mutual Fund
- Types of Mutual Funds
- Innovation and New Fund Launches
- Pricing
- Distribution
- Promotion

In a mutual fund scheme, funds are obtained from a large number of investors and invested in a portfolio of investment avenues like equities, debt instruments, and money market instruments. Mutual fund schemes help the lay investor benefit from the expertise of professional fund managers who invest the pool of funds in a diversified basket of securities. The mutual fund companies charge for the service of professionally managing the investors' funds.

Every mutual fund scheme comprises several units with a face value for each unit. A mutual fund unit is the smallest part of the share that an investor can buy/hold in the mutual fund. The income (dividend) that one obtains depends on the number of units owned. Similarly, capital appreciation is also based on the units owned.

The performance of a mutual fund scheme is assessed in terms of the net asset value (NAV) of the fund on a particular day. NAV is the sum of the value of all the securities invested under a scheme minus all the liabilities, divided by the total number of units. As the prices of securities keep changing daily, the NAV of a mutual fund also keeps changing. SEBI rules stipulate that financial institutions should declare the NAV of the different schemes regularly; normally, the NAV is declared on a daily basis.

The mutual fund market in India, though in a nascent stage, has shown steady growth since 1987, when the monopoly of the Unit Trust of India (UTI) was broken by the public sector mutual funds set up by public sector banks. (The mutual fund industry in India started in 1963 when Unit Trust of India (UTI) was established by an Act of Parliament. It was set up by the Reserve Bank of India and functioned under its regulatory and administrative control.) Increasing competition led to the aggressive marketing of mutual fund products. The fund houses adopted more or less similar marketing techniques and marketed similar products in the late 1980s. It was in the 1990s when private fund companies entered the picture and started vying with each other for market share that product differentiation became quite visible.

This chapter starts with a description of the evolution of mutual funds in India, discusses the organization of a mutual fund, and goes on to explain the different types of mutual funds. The next section discusses product innovation and new fund launches. Pricing, distribution (including mutual banking), and promotion of mutual funds are discussed in detail subsequently.

EVOLUTION OF MUTUAL FUNDS IN INDIA

The evolution of mutual funds in India can be divided into different phases. The first phase stretches from 1963, when the UTI was set up, to 1987, when bank sponsored mutual funds entered the market. The second phase was from 1987 to 1993; mutual fund regulations came into force in 1993. The third phase began when the Securities and Exchange Board of India (SEBI) replaced RBI as the regulatory body. The fourth phase began when the government repealed the UTI Act (1963). Let us take a look at each of these phases.

Phase I

The evolution of mutual funds in India can be traced back to 1963, when the Government of India (GoI) set up the Unit Trust of India (UTI) after the UTI Act (1963) was passed in Parliament. UTI, which introduced its first product 'US 64' in 1964, was a monopoly in the mutual funds industry until 1987, when the government allowed bank sponsored mutual funds to enter the industry. RBI regulated the operations of mutual funds during this phase.

Phase II

The establishment of bank-sponsored mutual funds marked the second phase in the evolution of the industry. SBI Mutual Fund[1] was established in June 1987, Canbank Mutual Fund[2] in December 1987, and Punjab National Bank Mutual Fund[3] in August 1989. The Life Insurance Corporation of India (LIC) and General Insurance Corporation of India (GIC) also floated their fund companies in June 1989 and December 1990 respectively. By the end of 1993, the mutual fund industry had total assets under management[4] (AUM) of Rs. 470 billion.

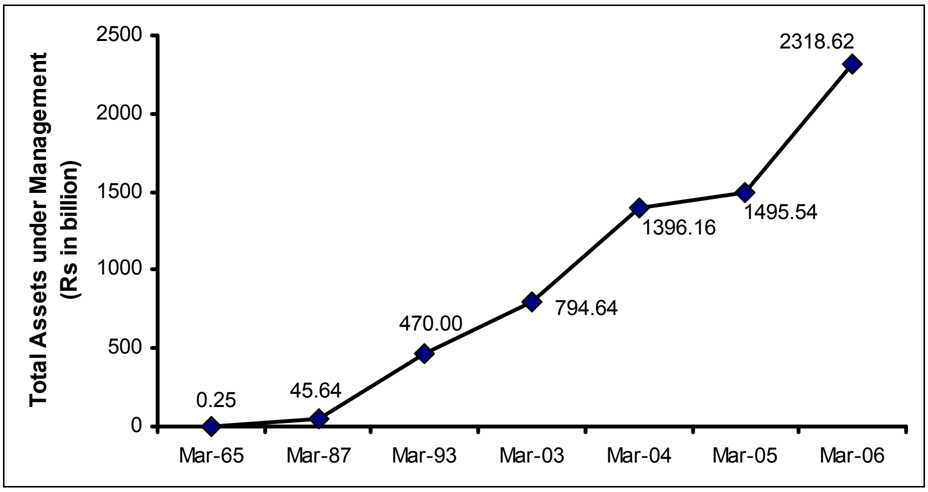
Phase III

In 1993, the third phase of the evolution began when the Mutual Fund Regulations came into being and SEBI replaced RBI as the regulator of the mutual fund industry. Private mutual fund marketers also entered the industry in 1993, further increasing the competition. In June 1993, Kothari Pioneer became the first private mutual fund to be registered. Apart from domestic private mutual funds, this phase also witnessed the entry of many foreign companies like Franklin Templeton. Most of the foreign players partnered with the local institutions to market their mutual fund products. Prudential ICICI and HDFC Standard Life are popular examples of such joint ventures.

Phase IV

The fourth and current phase of evolution started in 2003 when the UTI Act was repealed and UTI was reorganized into two entities – Specified Undertaking of the UTI and UTI Mutual Fund Ltd. Specified Undertaking of the Unit Trust of India, with AUM of Rs. 298 billion as of January 2003, functions under a separate administrator and does not come under the purview of the Mutual Fund Regulations of SEBI. Its regulations are framed by the GoI. UTI Mutual Fund Ltd. is sponsored by SBI, Punjab National Bank, Bank of Baroda, and LIC. As of March 2006, the total AUM of the entire mutual funds industry stood at Rs. 2,319 billion. Figure 10.1 shows the growth of the total AUM from 1965 to 2006.

Figure 10.1: Total Assets under Management: From 1965 to 2006



Adapted from http://www.amfiindia.com/showhtml.asp?page=mfindustry

From Figure 10.1, it is evident that the mutual fund sector remained quite dormant until 1987. The momentum picked up with the entry of bank-sponsored fund houses, and became even greater after the private players entered the market. The AUM recorded a maximum growth (in a year) of 55%, between March 2005 and March 2006. The AUM, which was Rs. 2,319 billion as of March 2006, further rose to Rs. 3,259 billion by December 2006. Table 10.1 shows the top performing fund houses as on December 31, 2006, in terms of assets under management.

Table 10.1: AUMs of Top Mutual Funds

(As on December 31, 2006)

Mutual Fund	Assets Under Management (Rs. billion)
UTI Mutual Fund	381
Reliance Mutual Fund	369
Prudential ICICI Mutual Fund	333
HDFC Mutual Fund	296
Franklin Templeton Mutual Fund	234
Birla Sun Life Mutual Fund	171
SBI Mutual Fund	151
DSP Merrill Lynch Mutual Fund	135
Standard Chartered Mutual Fund	126
Tata Mutual Fund	122
Kotak Mahindra	121
Other mutual funds	**820**
Mutual Fund Industry (Total)	**3,259**

Source: http://www.amfiindia.com/pu-showfundwiseaum.asp?admin=yn

ORGANIZATIONAL SET-UP OF A MUTUAL FUND

Any financial institution that desires to come out with a mutual fund must form a trust. The key players involved in the organizational set-up of a mutual fund are:

- The sponsor(s)
- The trustees
- The Asset Management Company (AMC)
- The custodian

The role of the sponsor(s) is similar to that of a promoter of a company. The trustees are like the directors of a company. They give directions to the Asset Management Company (AMC) and monitor their operations. It is the responsibility of the trustees to ensure that the mutual fund abides by the guidelines laid down by SEBI. The property of the trust is held by the trustees who are primarily responsible for ensuring the profitability of the fund. The AMC is the functional wing of a mutual fund responsible for deciding on the investments to be made in various securities. The custodian has to register with SEBI and is primarily the caretaker of the securities and other assets of the mutual fund.

In order to regulate the functioning of mutual funds and exercise proper control, SEBI has laid down certain stipulations[5]. Some of them are:

- All mutual funds must be registered with SEBI before they are launched in the market.
- At least two-thirds of the members of the board of trustees must not be associated with the sponsors.
- 50% of the directors of the AMC must be independent.
- The AMC must be approved by SEBI.
- The custodian must be registered with SEBI.

TYPES OF MUTUAL FUNDS

Mutual fund marketers have always attempted to launch new and customer-friendly products on a regular basis. The objective is to gain immediate recognition and capture the market. Despite the large number of products, all the mutual fund products (commonly termed as schemes) can be classified in three ways: classification based on the structure of the mutual fund, classification based on the investment objectives, and classification based on specific purpose. In this section, we discuss these different classifications in detail.

Classification Based on the Structure of the Mutual Fund

The first classification is based on the structure of the mutual fund. Depending upon the extent of capitalization, redemption conditions, lock-in periods, etc., mutual funds can be classified into 'close-ended funds', 'open-ended funds', and 'interval funds'. Let us discuss the functioning of close-ended funds and open-ended funds in detail. Interval funds combine the features of both close-ended and open-ended funds.

Close-ended funds

Close-ended funds are characterized by constant capitalization, which means the initial total capital of the fund, available for the purpose of investment, cannot exceed a certain limit. The subscription amount is accepted from investors only during a particular period at the time of the launch of a scheme. These funds are issued through new fund offers; subscription for them is closed on a predetermined date. Subsequently, the funds are listed on a stock exchange and investors can either sell their units through the stock exchange to other investors.

Another feature of close-ended funds is that there is a 'lock-in' period (such as 3 years, 5 years, 7 years), during which the units cannot be liquidated. An example of a close-ended mutual fund is the SBI Magnum Tax Profit 94 Fund, which was launched in December 1993. It had a three-year lock-in period, before the fund house could repurchase the units at NAV.

Open-ended funds

Under open-ended fund schemes, investors can pool in their subscription at any time, as there is no limit on capitalization. Besides this, there are no restrictions on the purchase and sale of units of such funds. In other words, they can be bought and sold at any time directly from the fund house. Such sale and purchase of units are based on the NAV of the fund, which is normally calculated on a daily basis. Unlike close-ended funds, no lock in period exists for open-ended funds, which means there is greater liquidity for the investors. SBI Magnum Equity Fund is an open-ended diversified equity fund with a portfolio of select blue chip stocks.

Classification Based on the Investment Objectives

The second type of classification is based on the investment objectives of the investors, that is, their risk appetite (willingness to take risks). Thus, based on the risk-taking capacity of the investor, funds can be classified into growth funds, income funds, balanced funds, and money market funds. These are discussed in detail here.

Growth funds

The basic investment objective of growth funds is to provide capital gains to the investors, that is, to provide high returns on the money invested. Basically, growth funds are invested in fast growing equity stocks in the stock market. The stocks invested in can be of large or mid-size companies (established stocks), and companies in the SME sector (emerging stocks). As the returns are high, so are the risks. The risks associated with these funds are generally above average to high. Mutual fund managers may alter the investment portfolio based on the fluctuations in the stock prices. As a result, the mix of underlying stocks in the portfolio may be altered regularly, leading to a high stock turnover in such growth funds. The funds are marketed to those investors who have a high risk- taking attitude and whose investment horizon varies from medium term to long term. Reliance Equity Fund, for example, invests in the top 100 companies by market capitalization to provide long-term growth to its investors.

Income funds

The basic investment objective of income funds is to provide a regular income to the investors. Thus, income funds are typically invested in fixed income securities like bonds and debentures, which are also called debt instruments. Income funds are also invested in those stocks (equity), which have a good track record of dividend payment. Income accrued from these funds is paid out to the unit-holders, either on a monthly basis or on an annual basis.

Income funds are invested broadly in a portfolio of short-term money market funds (which include government bonds and treasury bills), long-term debt instruments, and in stocks that have a good dividend payment record. Debt market and money market instruments are usually associated with low risk. Due to their low risk characteristic, the stock turnover in income funds is also very low. Typically, income funds are marketed to those investors who are very conservative in terms of risk taking and have a long-term investment horizon. The Reliance Monthly Income Plan is an income fund with the objective of providing regular income to the investors. It invests 80% of the corpus in debt and money market instruments and the remaining 20% in equities.

Balanced funds

Balanced funds are aimed at providing regular income along with some capital appreciation to the investor. To achieve this objective, capital collected under such funds are invested in both equity and debt markets. A typical portfolio of a balanced fund can be 60% of the capital in debt market and the remaining 40% in equity market. Due to this combination, the risk involved is higher than that of income funds and lower than that of growth funds. Balanced funds are marketed to those investors who are conservative, yet are willing to take some amount of risk. Birla Balance Fund is an open-ended balance fund with the objective of providing regular income and long-term growth.

Money market funds

In money market funds, the fund managers invest in short-term money market instruments like treasury bills, certificates of deposits, commercial papers, and inter-bank call money. The objective of such funds is to provide easy liquidity and capital preservation, and to generate reasonably moderate income. Returns in these funds depend on the prevailing interest rates in the market.

Classification Based on Specific Purpose

The products in this classification are a combination of the funds of the other two classifications mentioned. They are developed for a specific purpose and are targeted at specific customer groups. Such schemes can be tax saving schemes, index funds, or theme-based funds (including industry-specific funds). Let us discuss each of these classifications in detail.

Tax savings schemes

There are various tax savings schemes in India and one such popular scheme is the Equity Linked Savings Scheme (ELSS), which is a generic mutual fund product. Most mutual fund companies offer ELS schemes under their respective brands. Under an ELSS, investments up to a maximum of Rs.100,000 are deductible from the investor's taxable income, under section 80C of the Income Tax Act. Funds collected under this scheme are invested in equity markets. ELSS funds have a minimum lock-in period of three years, and the risks associated with them are high as they are invested in equities. These fund products are marketed to those investors who are ready to take a high risk and are not worried about immediate liquidity. Tata Tax-Saving Fund is an equity-linked, tax saving fund with a minimum investment of Rs.500 and further investment in multiples of Rs.500.

Index funds

Under index funds, investments are made on the stocks that are present in standard indices like the BSE Sensex (Sensex) and S&P CNX Nifty (Nifty). When such investments are made, the returns from the portfolio behave in the same manner as that of the corresponding indices (Refer to Table 10.2 for various index funds based on Nifty). For example, the UTI Nifty Fund, launched in 2000, is based on the S&P CNX Nifty index. The capital pooled from this fund is invested in all the fifty stocks present in the Nifty. So, the performance of this fund almost mirrors the performance of Nifty. In other words, if Nifty gains, the fund also gains and vice versa.

Index funds are considered to be low risk equity funds as they are less volatile than other equity funds. These funds are marketed to those investors who look for less risky, long-term investments. Index funds in India are considered to have higher operating expenses compared to those in the US. This is reflected in the expense ratio (expenses/net assets). For example, Fidelity Spartan 500 Index Fund in the US has an expense ratio of 0.10%, while HDFC Index (Sensex) Fund has an expense ratio of 1.50%.[6] If mutual fund marketers are able to focus on this metric and reduce their cost of operations, investors will find index funds an attractive option.

Table 10.2: Some Index Funds Based on S&P CNX Nifty

Sl. No.	Index Fund Scheme	Mutual Fund	Month and Year of Launch
1.	IDBI Index I-NIT`99	IDBI Principal Mutual Fund	July 1999
2.	UTI Nifty Fund	Unit Trust of India	March 2000
3.	Franklin India Index Fund	Franklin Templeton Mutual Fund	June 2000
4.	Franklin India Index Tax Fund	Franklin Templeton Mutual Fund	February 2001
5.	Magnum Index Fund	SBI	December 2001
6.	Prudential ICICI Index Fund	Prudential ICICI Mutual Fund	February 2002
7.	HDFC Index Fund – Nifty Plan	HDFC Mutual Fund	July 2002
8.	Birla Index Fund	Birla Sun Life Mutual Fund	September 2002
9.	LIC Index Fund – Nifty Plan	LIC Mutual Fund	November 2002
10.	ING Vysya Nifty Plus Fund	ING Vysya Mutual Fund	January 2004
11.	Canindex Fund	Canbank Mutual Fund	September 2004
12.	Reliance Index Fund	Reliance Mutual Fund	January 2005
13.	Principal Junior Cap Fund	Principal PNB	May 2005

Source: http://www.nse-india.com/content/indices/ind_indexfunds.htm

Theme-based funds

Theme-based funds are based on thematic ideas such as leadership, lifestyle, or industry/sector. Theme-based funds have all the associated characteristics of equity funds. Some of the popular theme-based funds are ABM AMRO Future Leaders Fund, Birla India GenNext Fund, Kotak Life Style Fund, Prudential ICICI Service Industries Fund, etc.

Industry specific funds, also called sectoral funds, are based on the theme of an industry/sector. They are special purpose funds meant for investing only in specific industries. The same will be stated in the offer documents specifying the industry in which they may be invested. For example, industries like IT, pharmaceuticals, textiles, etc. have attracted investments through such funds. Sectoral funds under SBI Mutual Fund, for instance, include the FMCG Fund, the Emerging Businesses Fund, the I.T. Sector Fund, and the Pharmaceuticals Fund.

INNOVATION AND NEW FUND LAUNCHES

Entirely new products are rarely developed in the mutual fund industry. This is more so in the case of India, which lags behind mature markets like the US and UK, in terms of product innovation. Product innovation in mutual funds in India is associated more with business compulsions and usually involves cosmetic changes of existing products. In this section, we will first discuss the different components that must be considered while designing the mutual fund. This is followed by a description of systematic investment plan (SIP), and the factors that have led to the launch of new funds in India.

Designing a Mutual Fund Product

According to Panda and Tripathy[7], five factors govern the marketing of a mutual fund. They are core product, market performance (tangible product), service behavior (augmented product), persuasive communication, and the confidence factor. The consumers look into each of these components before deciding on the purchase of a mutual fund. The marketer has to decide on the combinations of the various components while designing a particular product.

Core product

The core product is associated with product features that include product awareness, ownership of the product, the lock-in period, brand name, the target audience (e.g. retail investor), and the sector the company belongs to (private or public sector). These are essential for any mutual fund product, and hence form the core product.

Market performance

The second component is market performance. Market performance can be related to safety, extent of liquidity, regularity in income, tax benefits, etc. Customers expect at least some of these attributes to be present in a mutual fund product.

Service behavior

The third factor, service behavior, describes the delivery of the product and the extent of transparency adopted by the marketer in the entire process of purchase and post-purchase interactions. These augmenting attributes increase customer loyalty and create word-of-mouth publicity for the mutual fund company.

Persuasive communication

Persuasive communication is necessary on the part of the fund houses to explain the product differentiation and influence the customer to purchase the products. Persuasive communication for a mutual fund can be done through advertisements, sponsor reputation, broker/agent recommendation, and referrals from friends/relatives (in the case of satisfied customers).

Consumer confidence

Finally, the confidence that is formed as a result of performance guarantee, assured returns, degree of capital appreciation observed, and experience of the customer over a period of time, is influential in maintaining a healthy ratio of loyal customers to total customers. Thus it is imperative for the fund houses to maintain such loyal customers who help bring in new customers.

Mutual fund marketers need to ensure that a particular kind of product developed contains the different components in varying proportions. For example, the component mix for an index fund would be different from that of a tax savings scheme.

Systematic Investment Plan (SIP)

A Systematic Investment Plan is an innovation in the payment options for mutual fund investors. It is designed for those who are interested in gradually accumulating wealth over a long term in a disciplined manner. An SIP is not an investment product by itself; it just offers investors a different process of investment. For many retail investors in India, especially those belonging to the salaried class, it would be quite difficult to save a sizable sum and then invest the lump sum amount in the market in traditional mutual fund schemes. SIPs offer them a viable option to invest for the long term. The emergence of SIPs in India has been due to the host of benefits that they offer. Some of these benefits are aligned to the various factors identified by Panda and Tripathy (discussed earlier) that govern the successful marketing of a mutual fund product.

Core product

The product is primarily targeted at the retail investor and it leads to disciplined savings and wealth accumulation over a period. Most marketers offer SIPs under equity fund as well as debt fund, and open-ended as well as close-ended variants.

Market performance and consumer confidence

SIP is now a preferred financial product for retirement planning. The advantage that SIPs offer over pension schemes is that the investor has the flexibility to manage the risk. One can invest in select funds according to the changing risk-return profile. An SIP also offers instant liquidity whenever required. The income accrued has also been consistent over time. (See Table 10.3 for details)

Table 10.3: SIP Returns of Leading Schemes

(Three-year annualized return for Rs. 1000 invested every month for three years)

Scheme	Units accumulated	NAV (on Jan 31, 2007)	Capital appreciation	Returns (%)
Equity Diversified Schemes				
Reliance Growth Fund	283.76	276.61	78489.88	118.03
Birla Sun Life Equity Fund	404.20	186.87	75533.08	109.81
DSP Merrill Lynch Equity Fund	628.40	118.40	74402.53	106.67
Franklin India Prima Plus	506.71	142.93	72424.52	101.18
Prudential ICICI Power	868.92	83.32	72398.23	101.11
Equity Linked Saving Schemes				
SBI Magnum Tax Gain 93	643.21	143.09	92038.39	155.66
HDFC Tax Saver Fund	509.25	146.13	74418.73	106.72
Sundaram BNP Paribas Taxsaver	1300.77	56.98	74114.96	105.87
Balanced Schemes				
HDFC Prudence Fund	494.89	130.30	64483.29	79.12
Prudential ICICI Balance Fund	1673.43	35.63	59624.27	65.62
Tata Balanced Fund	1172.65	50.55	59276.01	64.66

Source: http://content.icicidirect.com/mailimages/SIP_return.htm

Two specific advantages of SIPs that have helped build consumer confidence and reduce risks are the power of compounding and the concept of rupee cost averaging.

Power of compounding: The growth potential of an investment increases over time, especially when the dividends and capital gains are reinvested. The earlier one invests and the longer the money stays invested, the greater is the wealth accumulation.

Rupee cost averaging (RCA): When investors invest the same amount in a fund at regular intervals over time, they are effectively buying more units when the NAV is lower and fewer units when the NAV is higher. Thus, the average cost per unit (share) reduces over time. The investor has to worry less about fluctuations in share prices or interest rates. SIPs reduce the risk of investing in volatile markets; however, this approach does not guarantee a profit.

Service

Convenience is another benefit that SIPs offer. The investors may submit post-dated cheques or opt for the electronic clearing scheme (ECS). The periodicity is usually one month and the payments may be as low as Rs. 500 or Rs.1,000 per month. This ensures that the investor does not need to spend time every month on making the investment; there is also a greater discipline in the investment process.

Factors Influencing New Fund Launch

New product (new fund scheme) launches in the mutual fund industry have been very frequent only since the late 1990s after many new fund houses, including private and foreign fund houses, set up base in the country, leading to increased competition. Such competitive pressures have led mutual fund marketers to realize that their survival depends on customer-oriented new product launches. According to K Madhavakumar, President, Department of Business Development and Marketing, UTI Mutual Fund, "…Development of niche products that aim at satisfying the investor's financial goals will become a trend in the future." [8] The major factors that have led to the launch of new fund schemes are presence of opportunities in terms of gaps in product portfolio, intention to increase assets under management, competition, customer confidence, and interest fluctuation.

Gaps in product portfolio

New mutual funds are launched to plug the gaps in the existing product portfolio of marketers. Many companies that have entered this industry strive to launch as many funds as possible, in order to cater to all possible customer segments and also increase the asset base.

More assets under management

It is a practice for the fund houses to launch new funds to attract more investments and increase the total value of assets under their management. It is assumed that the more assets a fund house manages, the greater will be its profitability. Often, many fund houses come out with industry- specific funds or other theme-based funds.

As mentioned earlier, industry-specific funds are intended to be invested in the development of particular industries. An industry that experiences good growth attracts more investors. For example, recognizing the boom in the real estate sector, real estate funds were introduced in mid-2006 so that people could invest in the real estate companies in India. Theme-based funds were also developed on certain themes like leadership, etc. to bring more assets in under management. UTI Mutual Fund launched the Leadership Fund in early 2006. By March 2006, 3.6 million investors had invested in this fund, helping UTI garner Rs.21 billion[9].

Competition

Competition is another major factor that has forced mutual fund marketers to come out with new fund launches. Fund companies have to differentiate themselves from the competition and this compulsion leads to the launch of many new products.

Investors' confidence

Despite the good growth rates achieved by the industry, investors' confidence in mutual funds is still very low in India. Thus, fund houses are constantly vying to come out with more customer-friendly fund schemes to encourage the customers to invest in them. For instance, when the Indian stock markets crashed in May 2006, many of the retail investors who had invested in the equity markets lost a fortune. After this incident, many fund houses introduced market neutral funds[10] and arbitrage funds[11] that had features capable of withstanding such market fluctuations.

Interest fluctuations

Debt market funds prove to be less profitable to investors when high interest rates prevail. This is because the prices of debt funds fall when the interest rates increase. This also forces the fund houses to invest more in equity funds to maintain profitability. In this process, they bring out new fund schemes, which can yield good returns.

PRICING

For a mutual fund, the term 'price' has multiple meanings. Mutual fund houses employ different pricing during sale of the fund units to investors and during the repurchase/redemption of those units from investors. In this section, we will examine the different terms used in the pricing of mutual funds, followed by the different pricing strategies adopted by the fund houses across the industry.

Terms in Pricing

The commonly used terms in pricing a mutual fund are: net asset value (NAV), offer price/sale price, repurchase price, redemption price, entry load, and exit load.

Net asset value

The NAV of the scheme is that value which is arrived at by adding the market value of all the assets (securities) in the scheme portfolio and subtracting various outflow items like operational expenses, interests, and dividends paid to the investors. The NAV per unit can be arrived at by dividing the NAV of the scheme by the number of units outstanding on the date of valuation. The NAV is used in selling and redemption of the units in open-ended funds.

Offer/ sale price

Investors invest in various fund schemes by purchasing the units of those schemes. The price that an investor has to pay for purchasing units under a scheme is called the offer/sale price. This price in some cases may contain an entry load (discussed later).

Re-purchase price

It is the price at which investors sell back their units (of a close-ended fund) to the fund house. This price is also called 'bid price' and may also contain an exit load.

Redemption price

Redemption price is to open-ended funds what repurchase price is to close-ended funds. Redemption price is the price at which the fund house repurchases its units from the customers. It is calculated with the NAV as the basis.

Entry load

Entry load is the amount charged by the fund house while selling the units to the investor. The fund house levies these charges so as to cover the marketing and distributing expenses that it incurs. It is not mandatory for the fund house to charge such fees on all its schemes. Thus, entry loads are sometimes included as part of the sale price. For instance, Birla Balance Fund and DSP ML Balance Fund are two open-ended schemes; an entry load is applicable in the former while it is not levied in the latter.

Exit load

Exit load is the amount charged by the fund house while repurchasing/redeeming the units from the investors. Table 10.4 lists the entry and exit loads for different schemes of Kotak Mahindra Mutual Fund, as on June 29, 2006.

Fund houses use entry and exit loads to cover their marketing and distribution expenses. These loads are charged as a percentage of the prevailing per unit NAV of the scheme and SEBI allows the fund houses to charge up to a maximum of 7%. But fund houses usually charge around 2.5% as entry and exit loads and pass on a part of this to the distributors. For example, let us assume the NAV of a scheme is Rs. 20 and entry and exit loads applicable are 2% each. If an investor buys 100 units of the scheme, then he/she has to pay Rs. 2,000 toward the NAV and Rs.40 toward the entry load. This would add up to Rs. 2,040, which is the total amount payable by the investor. The pricing of entry and exit loads is decided by the fund house considering factors like competition, costs incurred in marketing and distribution of the scheme, etc.

Table 10.4: Entry and Exit Loads for Select Fund Schemes in Kotak Mahindra Mutual Fund (As on June 29, 2006.)

Scheme Name	Applicable From	Entry Load	Exit Load
Kotak 30 - Dividend	Mar 6, 2006	For amount less than Rs. 50 million, entry load is 2.25%. There is no entry load if the investment amount is greater than Rs. 50 million.	If redeemed before the completion of 6 months, exit load is 1%; else, no exit load.
Kotak 30 - Growth	Mar 6, 2006	For amount less than Rs. 50 million, entry load is 2.25%. There is no entry load if the investment amount is greater than Rs. 50 million.	If redeemed before the completion of 6 Months, exit load is 1%; else, no exit load.
Kotak Bond Regular Plan - Annual Dividend	Jul 21, 2005	Entry load is 0%.	If redeemed before the completion of 6 months, and the redemption amount is less than or equal to Rs. 1 million, then exit load is 0.5%; else, no exit load.

Kotak Bond Regular Plan - Bonus Plan	Jul 21, 2005	Entry load is 0%.	If redeemed before the completion of 6 months, and the redemption amount is less than or equal to Rs. 1 million, then exit load is 0.5%; else, no exit load.
Kotak Bond Short Term Plan - Growth	Apr 30, 2003	Entry Load is 0%.	Exit Load is 0%.
Kotak Gilt - Investment Regular Plan - Growth	Apr 30, 2003	Entry Load is 0%.	Exit Load is 0%.
Kotak Tech Fund	Mar 6, 2006	For amount less than Rs. 50 million, entry load is 2.25%. There is no entry load if the investment amount is greater than Rs. 50 million.	If redeemed before the completion of 6 Months, exit load is 1%; else, no exit load.

Source: http://www.mutualfundsindia.com/exit_entry.asp (Last accessed: June 29, 2006)

New Fund Pricing

Mutual fund marketers do not have much leverage in pricing their products. This is because SEBI has a strong say in the functioning of mutual fund companies. SEBI has made some provisions for the mutual fund houses to recover the costs that they incur on advertising and other efforts to promote their new fund offers. SEBI allows the fund houses to spend up to a maximum of 6% of the total amount (corpus) that is collected under a new fund scheme and this amount can be amortized (written off) over a five-year period.

Initially this provision was applicable to both open-ended and close-ended funds. Later, in April 2006, SEBI ruled that open-ended funds could not avail of this provision. For open-ended funds, companies were asked to cover the expenses by charging an entry load, or adjust it against the NAV or from the resources of the AMC.

Thus, if a close-ended fund garners an amount of Rs. 500 million in a new fund offer, it can spend a maximum of Rs.30 million (6% of Rs. 500 million) as promotional expenses. This amount can be amortized over the next five years, that is, Rs. 6 million (1.2% of Rs. 500 million) may be written off each year. As Rs. 6 million is deducted from the corpus every year, there is a corresponding reduction in the NAV. Apart from the promotional expenses, SEBI allows mutual fund houses to charge an additional 2.5% per annum on the corpus on an ongoing basis, to cover other expenses like salaries and maintenance.

DISTRIBUTION

The mutual fund industry in India has evolved from being a monopoly for decades to an industry where many of the global giants have entered. The consumer can now choose from a wide array of products. This increased competition has revolutionized the way in which the mutual funds are distributed. When bank-sponsored fund houses entered the market in 1987, they adopted the bancassurance route to sell their mutual funds. Private and foreign players, when they entered the market in the post-liberalization era, adopted a different strategy. They decided to take the third party distribution route, where channel intermediaries were encouraged to take up the distribution of mutual funds for a commission. Bajaj Capital, Karvy, Integrated Enterprises, etc., are examples of such intermediaries.

On the legal front, it is mandatory for fund houses to comply with Know Your Customer (KYC) norms while selling their schemes through different distribution channels. KYC norms lay out customer identification procedures and processes that help in reducing/eliminating money laundering activities. Effective from January 2007, investors who invest Rs. 50,000 or more in a single fund scheme, are required to possess a Mutual Fund Identification Number (MIN) as part of the KYC norms laid out by SEBI. The Association of Mutual Funds in India (AMFI), the industry association which initiated this move, has announced that the Rs.50,000 limit may be brought down in future to bring in more investors under the scanner.

In this section, we will discuss the common channels of distribution that are adopted by the mutual fund companies to sell their products.

Types of Distribution Channels

There are five common channels of distribution that a mutual fund marketer can adopt. They include direct channel, advice channel, retirement plan channel, fund supermarkets, and institutional channel. Of the various channels, the institutional channel caters primarily to the businesses, financial institutions, endowments, foundations, and other institutional investors. The other four channels primarily serve individual investors.

Direct channel

Under the direct channel, investors have the option of buying units directly from the fund companies, and of selling/redeeming the units directly to/from them. The fund companies maintain Internet websites and telephone servicing centers (call centers) for selling and repurchasing the fund units. They do not offer any investment advice to the investors on purchasing or selling the fund units. So investors have to undertake their own research in order to decide on the choice of investment. The fund company provides all the standard services to its investors, like providing quarterly statements, recordkeeping, transaction processing, etc. As these services are routine in nature, the fund companies using this channel incur relatively fixed costs over a period of time. Though advice from financial experts is not provided by the fund house, basic services like assistance in decision making, transaction processing, quarterly statements, etc, are provided on an ongoing basis.

Advice channel

Fund houses use this channel to offer expert advice and investment guidance with the help of experts in the mutual fund industry. They include third parties like full service brokers, independent financial advisors, and registered sales representatives at banks and financial institutions. They guide the investors in taking decisions on purchase of units in different fund products, maintenance of product portfolio, sale of units, switching from one option to another within a scheme, etc. Professional broking firms like Karvy, Sharekhan, etc, make use of the advice channel. LIC agents, who earlier sold only insurance products, also offer advice on purchase and sale of mutual funds.

Apart from providing advice, the channel also offers basic services like transaction processing, handling customer queries, distribution of financial reports, prospectus, and proxy statements on behalf of the fund houses. For all such services, the fund houses pay a fee and commissions to the brokers and advisors (as discussed under Pricing). Further, brokers and advisors may (sometimes) charge additional fee/charges from the investors for providing such services.

Retirement plan channel

The retirement plan channel is in use when an employer, as part of the retirement benefits offered to the employees, does salary deductions for eligible, willing employees and remits the deducted amount to a mutual fund for purchase of units. The end customer is the individual employee, with the employer acting as a channel intermediary for the convenience of the employees.

Fund supermarket channel

A fund supermarket offers a wide portfolio of fund schemes from different mutual fund companies for the investors to choose from. Fund supermarkets do not provide expert advice to the investors, but assist them by providing inputs for decision making. Such inputs include literature on fund schemes, and other information to arrive at purchase decisions. In India, Bajaj Capital is a well-known example of a fund supermarket. As these distributors (fund supermarkets) deal with a large number of fund companies, they provide a wide range of fund schemes, either at discounted rates or with no transaction fee. In other words, investors may not be required to pay a transaction fee like entry load or exit load when purchasing or selling their fund units through the supermarket channel. For this reason, these distributors may also be called discount brokers.

Fund supermarkets not only help the fund houses to reach the customers, but they also promote competition as the fund schemes of many fund houses are sold under the same roof. Such competition increases the need for product differentiation and leads to the development of products that satisfy the needs and requirements of investors in more effective ways.

Fund supermarkets maintain separate accounts with each of the fund houses and provide the respective customer information to the fund houses. They also provide transaction processing facilities to investors in addition to distributing prospectuses and financial reports of the different fund houses and their respective fund schemes.

Institutional channel

Institutional investors comprise business enterprises, financial institutions, government, and corporations. Institutional investors invest hugely in the fund schemes. The objective of investing in various fund products is to earn short-term capital gains. Institutions predominantly invest in money market funds and new fund offers. They purchase funds directly from the fund houses or from the distributors. For the fund house, the per unit cost of transacting with such institutional investors is low as the average account balance of these investors is very high.

Cross-selling through Mutual Banking

Mutual fund marketers have tied up with retail banks to tap the cross-selling opportunity, as a means of distributing mutual fund products to the existing customers of retail banks. This concept of selling mutual fund products through banks is called mutual banking. Mutual banking is an emerging concept and has huge potential for the mutual fund marketer as well as the bank. The fund house gets business in terms of increased sales and the bank gets fee-based income in the form of upfront commission, mobilization incentives, special incentives, etc. for selling the fund schemes to its customers. Mutual banking is also discussed in Chapter 12.

The retail segment is considered to have a very high potential in the mutual fund market. To tap this segment, fund houses tie up with the retail banks to cross-sell their products to the bank's customers. Mutual banking involves three approaches from the bank's perspective. A bank can sell the mutual fund products of its own subsidiary; it can also sell the mutual funds of another fund company, and third, it can sell the mutual funds of multiple fund houses. For example, SBI mobilized Rs.10.9 billion by cross-selling mutual funds of its subsidiary SBI Mutual Fund in the year 2004-05.[12] SBI also established a strategic tie-up with UTI Mutual Fund in March 2006 to sell the mutual fund schemes of UTI through select branches. Refer to Exhibit 10.1 for information about the strategic tie-up between UTI Mutual Fund and SBI.

Exhibit 10.1

UTI Mutual Fund Sells its Fund Schemes through SBI

As of February 28, 2006, UTI Mutual Fund (UTI) was the largest mutual fund in India with assets under management of over Rs.276 billion and over 7 million investor accounts under 57 different domestic schemes. It had a wide distribution network comprising 68 Financial Centers, 276 Chief Representative Offices, 103 Chief Advisors and 22,000 AMFI Certified Financial Advisors. It also distributed its products through the Department of Posts.

In March 2006, SBI and UTI entered into a strategic tie-up for cross-selling the fund schemes of UTI through select branches of SBI across the country. Incidentally, SBI is one of the sponsors of UTI Mutual Fund. This tie-up is primarily aimed at getting retail customers to invest in UTI's fund schemes. UTI hopes to gain as this tie-up would enable the customers of SBI to select from a wide product range of UTI at their banking premises itself. As per the tie-up, SBI initially identified 48 branches from where fund schemes of UTI could be cross-sold, with a provision of extending this arrangement to other SBI branches in the future.

Adapted from the Press Release: UTI Mutual Fund Ties up with India's Largest Bank. http://www.utimf.com/News/NewsFile/125/125.htm

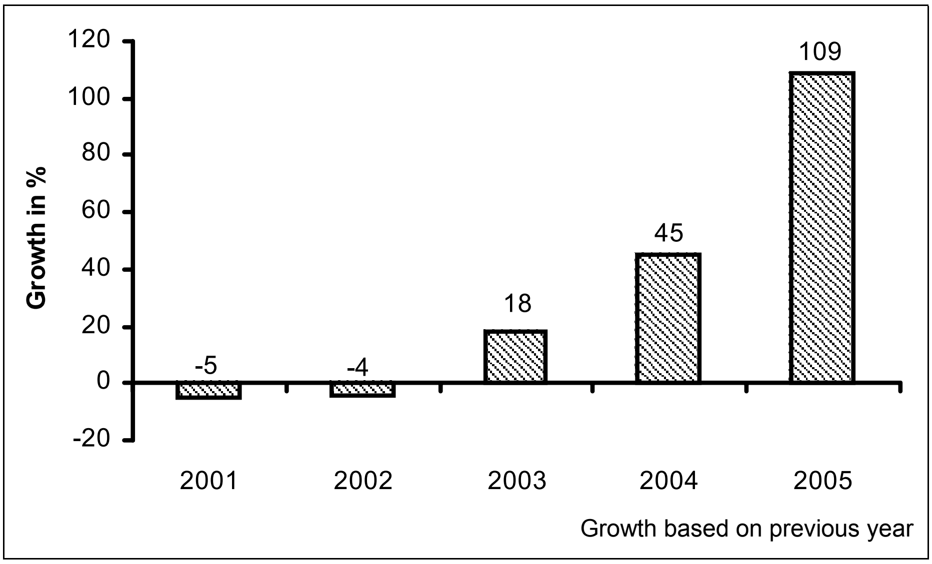
PROMOTION

Promotion of mutual funds has long been associated with the agents of the Unit Trust of India. Mutual fund marketers have come of age in the post-liberalization era and have begun to make use of other options in the promotion mix. Advertisements have become a major communication option to promote the benefits of different fund schemes. Marketers also take the support of sales promotion techniques to promote their products. Offering of gifts and incentives to the investors is the most common approach toward consumer promotion. Trade promotions have also increased considerably, especially when the same distributor sells fund schemes of more than one fund house. Apart from this, fund houses have gone in for an image makeover by branding their fund schemes with attractive titles. Such brand building efforts have become prominent in the 2000s. In this section, we discuss the advertising, sales promotion, and branding initiatives that fund houses have employed to promote their schemes. We also discuss the importance of public relations and the contribution of AMFI – the industry association, in this regard.

Advertising

Advertising of mutual funds began in the late 1990s in India. The early phase of advertising was restricted to informing the investors about mutual funds and highlighting the benefits of investing in these funds. Thus, most of the ads made use of a rational appeal. Advertising by mutual fund marketers gained intensity in 2003 with the players in the industry striving to achieve market expansion and greater penetration. They used both print and electronic media for advertising their schemes. Spending on television advertising has been growing since 2003 and it rose by 109% (year-on-year) in 2005, as depicted in Figure 10.2. SBI Mutual Fund topped the list of highest spenders in television advertising in 2005, with a 22% share. Refer to Figure 10.3 for further details.

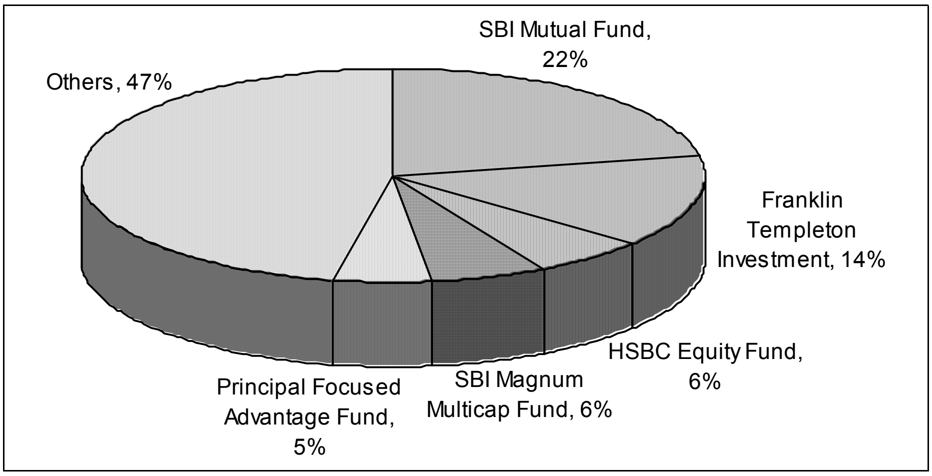
Figure 10.2: Television Advertisement Spending by Mutual Fund Companies from 2001 to 2005



Note: Growth based on previous year

Source: http://www.indiantelevision.com/tamadex/y2k4/dec/tam92.html

Figure 10.3: Mutual Funds in 2005 – Top Five Spenders in Television Advertising



Source: http://www.indiantelevision.com/tamadex/y2k6/jan/tam5.htm

The Internet has become another popular communication channel. Fund houses use the Internet to attract net savvy investors and try to make them purchase the fund units and avail of other services through the Internet channel. Mutual fund marketers make use of two types of advertisements on the Internet. One is the rotating ad where the space for the advertisement displays ads of different companies one after the other. The other approach, which is more expensive, is to purchase dedicated ad space so that only the ads of that fund house are showcased.

In 1996, SEBI developed an advertising code for mutual fund advertisements. Under the code, fund companies are prohibited from providing misleading statements about their performance. The code further states that all the claims about performance should be adequately supported with relevant data, and that risk factors should be explicitly stated. Exhibit 10.2 contains the risk factors from a web page which showcases the benefits of Reliance Vision Fund.

Exhibit 10.2

Disclosure of General Risk Factors in Mutual Funds: An Example

Investment Objective: Reliance Vision Fund aims to achieve long-term growth of capital by investment in equity and equity-related securities through a research-based investment approach.

Sponsor: Reliance Capital Limited.

Trustee: Reliance Capital Trustee Co. Limited.

Investment Manager: Reliance Capital Asset Management Limited.

Statutory Details: The Sponsor, the Trustee, and the Investment Manager are incorporated under the Companies Act 1956.

General Risk Factors

- Mutual funds and securities investments are subject to market risks and there is no assurance or guarantee that the objectives of the Scheme will be achieved.
- As with any investment in securities, the NAV of the Units issued under the Scheme can go up or down depending on the factors and forces affecting the capital markets.
- Past performance of the Sponsor/AMC/Mutual Fund is not indicative of the future performance of the Scheme.
- Reliance Vision Fund is only the name of the Scheme and does not in any manner indicate either the quality of the Scheme, its future prospects, or returns.
- The Sponsor is not responsible or liable for any loss resulting from the operation of the Scheme beyond their initial contribution of Rs.100,000 toward the setting up of the Mutual Fund and such other accretions and additions to the corpus.
- The Mutual Fund is not guaranteeing or assuring any dividend/ bonus.
- The Mutual Fund is also not assuring that it will make periodical dividend/bonus distributions, though it has every intention of doing so.
- All dividend/bonus distributions are subject to availability of distributable surplus.
- For details of scheme features apart from those mentioned above and scheme specific risk factors, please refer to the provisions of the offer document.
- Offer Document and Key Information Memorandum cum Application Forms are available at AMC office/Investor Service centres/AMC website/Distributors.

Source: http://www.reliancemutual.com/default.aspx

Sales Promotion

The sales promotion of mutual funds involves both consumer promotion and trade promotion. Under consumer promotion, mutual fund marketers use gifts and incentives to attract customers to purchase their schemes. Bajaj Capital, one of India's largest mutual fund distributors is considered the pioneer in using incentives as a sales promotional approach. Another example is of Cholamandalam Mutual Fund[13], a group company of the Chennai-based Murugappa Group, which entered the market in 2001 with Chola Triple Fund, a debt fund. The fund house paid its investors Rs.75 per application and a cash incentive of 0.2 percent of the invested amount.

The incentives given to consumers need not always be in the form of cash. Gifts that suit the season -- such as gold coins on festive occasions, umbrellas for the rainy season, etc. -- also have been used by mutual fund marketers. Many brokers adopt such techniques in selling mutual fund products.

Trade promotions have also helped the fund companies to gain more sales. Cholamandalam Mutual Fund gave 1.25% on the investment mobilized as commission to the distributors for its Chola Freedom Income, and 0.75% for Chola Growth. Apart from cash incentives, fund companies also provide gifts such as motorcycles, neon signboards, etc. to induce the distributors to promote their fund products.

The incentives approach has led to many distributors overselling some schemes, keeping in mind the associated consumer promotion and trade promotion schemes. Such practices have often led to selling of the wrong schemes to investors. For instance, if a high risk growth fund (with a high incentive) is sold to a senior citizen who expects a regular income, it would lead to customer dissatisfaction. Further, small investors, who usually rely on the distributor's advice, may first lose confidence in the mutual fund marketer, and eventually refrain from investing in mutual funds.

Branding

The penetration level of mutual funds (as an investment class) has been quite low in the retail consumer segment, which has a huge potential. In spite of recording good growth over the years, the mutual fund industry has failed to attract huge volumes from this segment. As part of their efforts to attract retail consumers, some fund houses have revamped their brand image. Many of the major fund houses in India have increased their spending on branding activities since the early 2000s.

UTI Mutual Fund was formed in 2003 after UTI was split into two entities. It took up certain initiatives to establish itself and break away from the traditional image associated with UTI. It took the help of McKinsey, its business consultant, and went ahead with the exercise of developing a corporate identity. Rediffusion was the advertising agency that supported this new branding initiative.[14] Refer to Exhibit 10.3 for details on the new corporate logo developed by UTI Mutual Fund as part of its branding exercise.

Public Relations (PR)

In India, PR activities for the mutual fund industry as a whole, are primarily carried out by the AMFI. AMFI is the apex body of all the registered Asset Management Companies and was established on August 22, 1995, as a non-profit organization. AMFI acts on behalf of its members in promoting mutual funds at two levels – at the domestic level where it strives to create awareness in the domestic retail investors, and at the international level by promoting India as a favored investment destination across the world.

Exhibit 10.3

The Corporate Logo of UTI Mutual Fund

The new corporate logo of UTI Mutual Fund was part of its move toward building a new and distinct corporate identity. The logo was that of a small vessel with a coconut and some leaves. In India, this is a traditional symbol of good luck and prosperity. The logo conveys a sense of approachability, humility, dynamism, and strength of character. It also portrays a clean corporate with a down-to-earth image, and a mix of the modern with the traditional.

The colors used in the logo were used to depict certain specific meanings. Orange conveyed dynamism – a sunny, cheerful, and young image. The blue color attempted to represent a sense of calm, mature, serene, and down-to-earth attitude. The white color in the letters, 'uti', on a deep blue background, depicted a pure and neutral image.

Adapted from "Chiefly Speaking ... Future Sales Will Come from Niche Products." Strategic Marketing. *http://www.etstrategicmarketing.com/smjuly-aug3/art6.html.*

At the domestic level, AMFI promotes the mutual fund industry by providing a wide range of information on mutual fund products and investments through its website. In this manner, it creates awareness among the public about the mutual fund industry and the way the industry operates. AMFI also runs online certification courses on mutual funds for anyone who wishes to take up a career in the mutual fund industry. The objective of the course is primarily to equip the individual agents with proper knowledge to sell mutual funds to different customer segments. Earlier, little or no training was offered to these agents by the fund houses, and the agents often faced difficulties in convincing the investors to invest in their funds. AMFI has made it mandatory for its member fund houses to recruit only AMFI certified people as their agents. The training courses and self-regulation have helped create a better impression of the industry, and have also helped to improve the image of the agents and instill confidence among the public.

At the international level, AMFI sponsors many events and hosts several conferences and meetings to promote the Indian mutual fund industry. For instance, from March 3 to 7, 2004, AMFI hosted the 9th Asia Oceania Regional meeting of the International Investment Fund Associations in New Delhi. The meeting was attended by representatives of investment fund associations and regulators of twelve countries: Australia, Bangladesh, China, Hong Kong, Japan, Korea, Malaysia, Philippines, Pakistan, Singapore, Taiwan, and India.

Apart from AMFI, individual fund houses also undertake PR activities, mainly by providing educational information about mutual funds. Every fund house provides conceptual content about mutual funds in general, to help lay investors who are interested in investing in mutual funds. This information is provided in printed documents as well as posted on their respective websites. Further, press releases are posted on their corporate websites from time to time, to provide glimpses about the activities of the fund house.

SUMMARY

Mutual funds in India have come of age to cater to the needs of investors. SEBI, which also controls the stock market operations, is the regulatory body of the Indian mutual fund industry. Mutual funds can be classified into open-ended funds, close-ended funds, and interval funds, based on the fund structure. Based on the investment objectives, they are divided into growth funds, income funds, balanced funds, and money-market funds. Based on the specific purpose of use, mutual funds are classified into tax savings schemes, index funds, and theme-based funds (including industry-specific or sectoral funds). Many fund marketers have come out with innovative and customer friendly products that aim at satisfying the investors' financial goals. Systematic Investment Plan (SIP) is an innovation in payment option for mutual fund investors. It is designed for those who are interested in gradually accumulating wealth in a disciplined manner over a long term.

Mutual funds are priced based on their net asset value, which the fund houses declare on a daily basis. Investors can sell their units back to the fund at the prevailing NAV. Some funds attract entry and exit loads. Such loads are used to recover the costs spent on distribution and other marketing costs.

Mutual funds are distributed through five channels of distribution, namely, direct channel, advice channel, retirement plan channel, fund supermarket channel, and institutional channel. Apart from these channels, mutual banking is also adopted, where cross-selling is used in association with banks to sell the fund schemes through the banks' branches.

Mutual fund marketers use advertising, sales promotions, brand communications, and public relations to attract investors and to increase their sales. Advertising includes print and electronic media, including the Internet. Fund marketers give away incentives and gifts to the investors for investing in their funds and such incentives and gifts may act as a catalyst for attracting more sales. They also give incentives (in cash or kind) to their trade partners and their representatives. Further, the fund houses have started the process of overhauling their brand image to promote themselves more effectively to the customers. AMFI, the industry association, has been actively involved in public relations (PR), by promoting the mutual fund industry, both at the domestic level and in the international arena.

End Notes:

1 SBI Mutual Fund is one of the largest mutual fund companies in India with more than 2 million investors, as of 2006.

2 Canbank Mutual Fund is sponsored by Canara Bank.

3 Punjab National Bank Mutual Fund later on became Principal PNB Asset Management Company Pvt. Limited. This is a joint venture between Principal Financial Group, PNB, and Vijaya Bank.

4 All the financial assets under the management of a fund company, including all types of mutual fund schemes under the company.

5 Gajra, Rajesh. "Mutual Fund Constituents." Outlook Money. June 2, 1999. http://www.outlookmoney.com/scripts/IIH021C1.asp?sectionid=10&categoryid=3&articleid=512

6 "Too Expensive?" Business India. July 18, 2005.

7 Panda, Tapan K., and Nalini Prava Tripathy. "Customer Orientation in Designing Mutual Fund Products – An Analytical Approach to Indian Market Preferences." http://dspace.iimk.ac.in/handle/2259/198.

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[8] "Chiefly Speaking … Future Sales Will Come from Niche Products." Strategic Marketing. http://www.etstrategicmarketing.com/smjuly-aug3/art6.html.

[9] "UTI MF Garners Rs.21 bn from Leadership Fund." http://in.mutualfunds.yahoo.com/060222/93/62nt0.html. March 3, 2006

[10] Market neutral funds are arbitrage funds where investment is predominantly made in equities, and equity related securities and derivatives. A small portion is also invested in debt instruments.

[11] Arbitrage is a way of reducing risk of loss caused by price fluctuations of securities held in a portfolio. Funds designed for this purpose are called arbitrage funds.

[12] Working Results for H1 2004-05, http://www.statebankofindia.com/viewsection.jsp?id=0,170,171,340.

[13] Cholamandalam Mutual Fund was renamed as DBS Chola Mutual Fund after the Murugappa Group entered into a joint venture with DBS Bank of Singapore.

[14] "Chiefly Speaking … Future Sales will Come from Niche Products." Strategic Marketing. http://www.etstrategicmarketing.com/smjuly-aug3/art6.html.

Chapter 11

Fee-based Services

In this chapter, we will discuss:

- Importance of Fee-based Services
- Corporate Fee-based Services
- Retail Fee-based Services
- Pricing
- Distribution and Promotion
- People
- Process

The revenue streams of banks can be broadly classified into two categories – interest income and non-interest income. Interest income depends on the financial assets -- loans and advances given to the customers — and investments in money markets and government securities. Non-interest income includes fees, commissions, service charges, handling charges, inspection charges, etc. levied on various regular and value-added services offered to customers. Non-interest income is commonly termed as fee-based income and has become an important component in the revenue pie of banks. In India, private sector banks have been able to cash in on fee-based services by investing in technology and thereby increasing their fee-based income. Public sector banks, on the other hand, still have a large portion of their revenues coming from interest-based income. For instance, the fee-based income of private sector banks increased by 39% from 2004 to 2005, while for the public sector banks, there was a decline of 22.5%[1].

We discussed interest-based income in the chapters on retail and corporate banking. In this chapter, we will focus on the marketing of fee-based services. In addition to the fee-based services offered by banks, we will also discuss the fee-based services offered by other financial institutions. The chapter begins with a discussion on the importance of fee-based services. Next, various corporate and retail fee-based services are outlined. This is followed by a discussion on pricing, distribution and promotion, people, and process aspects of fee-based services.

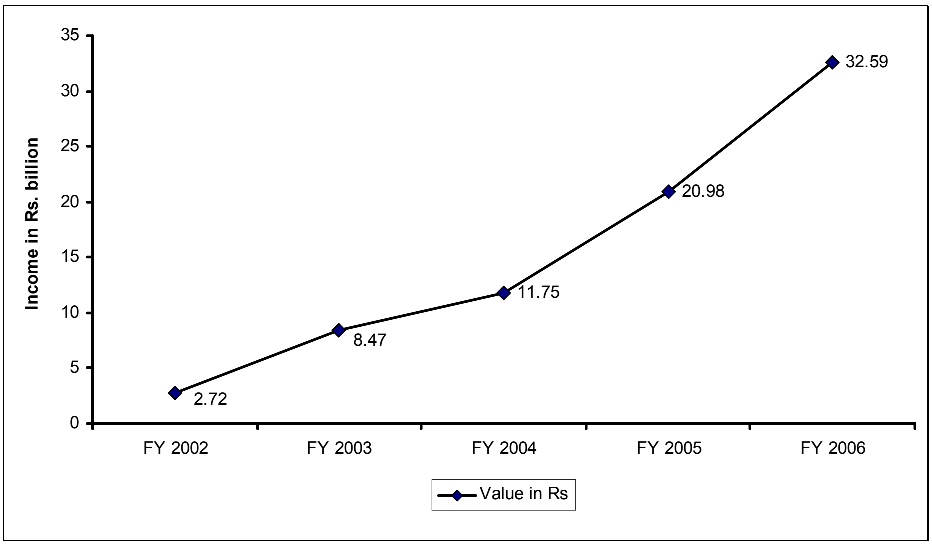
IMPORTANCE OF FEE-BASED SERVICES

An organization may have diverse financial requirements at various stages of its existence. It may need short-term loans and advances to meet the working capital requirements as well as long-term capital to meet business expansions like mergers & acquisitions, new plant installations, etc. The financial system has evolved in such a way that every financial need can be met by some or the other financial intermediary. An organization, instead of approaching a bank for a working capital loan, can sell the invoice bills (also called credit bills) of its debtors to the bank to meet its working capital requirements. In addition to banks, other specialized financial intermediaries also render such services for a fee. The long-term financial needs of the organization can be met by the capital market. Various financial intermediaries help the organization by providing their specialized services in raising the required capital. They include merchant bankers, underwriters, registrars, etc. Another class of intermediaries known as credit rating service providers helps the organization by assessing its creditworthiness and assigning a credit rating. A favorable credit rating helps the organization attract better creditors and get better deals. All these fee-based services help the organization at various stages to meet its financial/operational requirements.

Apart from these services, which are primarily corporate fee-based services, there are certain other services that are primarily rendered to retail customers. Banks are the major players in this arena and they provide a host of such services. The banks have begun to show more interest in fee-based services in order to increase their share of income in this area. This is evident from a shift in the income stream from interest-based income to that of fee-based income. In India, fluctuations in the interest rates have led to a decrease in interest margins and interest spreads. For instance, the net interest margin[2] of the public sector banks in India fell by 10 basis points from 3.24% in 2004-05 to 3.14% in 2005-06.[3] Bank of Baroda's net interest margin decreased from 3.40% to 3.31% during the same period of time. To reduce the business risks associated with the interest rate fluctuations, many banks have shown an increasing interest in fee-based services. For example, ICICI Bank's fee-based income increased from Rs.2.72 billion in 2002 to Rs.32.59 billion in 2006[4] (refer to Figure 11.1).

Besides, banks that were already in traditional fee-based services such as providing bank guarantees, letter of credit, and cash management services for many decades, have entered into other fee-based services like merchant banking services and other capital market services in the 2000s. Banks have also introduced high margin earning fee-based services like underwriting services, custodial services, and other services. A high profit margin is one of the major factors that is attracting banks to these services. This shift in focus has led to an increasing impetus on the marketing of fee-based services.

Figure 11.1: Fee-based Income of ICICI Bank



Source: www.icicibank.com

CORPORATE FEE-BASED SERVICES

Corporate fee-based services is a collective term given to all those financial (and related) services that various financial institutions (banks, intermediaries, brokers, etc.) offer to corporate customers on payment of a fee. Table 11.1 provides a snapshot of the various fee-based services provided by banks and other institutions to corporate customers.

Table 11.1: Common Fee-based Services Offered to Organizations

Service Head	Services
Cash management services	• Collection & disbursement of outstation cheques. • Payment of dividends, interest, and refund. • Liquidity management.
Letter of credit/ Bank guarantees	• Letter of credit given to SMEs, exporters, and contractors • Bank guarantee given on behalf of contractors and professionals
Bill discounting/ Factoring/ Forfaiting	• Providing advances against a bill • Factoring of invoices and other bills to facilitate working capital for the corporate customers. • Factoring of foreign bills is termed as forfaiting

Service Head	Services
Forex services	• Providing foreign exchange management services
Merchant banking	• Corporate & project counseling • Issue management • Project preparation & appraisal • Capital structuring • Portfolio management
Registrar services/ Underwriting services/ Custodial services	• Acting as registrars to initial public offerings (IPO) and subsequent public offerings. • Acting as underwriters and providing underwriting services for the clients during the public offers. • Acting as custodian for the client's shares and debentures in both physical form and de-materialized from.
Leasing	• Leasing and/or hire purchase of plant and building, machinery, and equipment.
Credit rating	• Providing credit rating services to organizations to help them attract creditors and get favorable pricing.

Compiled from various sources

Cash Management Services

Cash management is the effective management of cash in order to minimize transaction costs, exercise greater control, and maximize returns. Banks offer cash management services to their corporate customers. Usually corporate customers maintain multiple current accounts for various purposes such as to make payments, receive payments, etc. This prompts the need for management of cash in the accounts and between the accounts.

Cash management services can be broadly divided into three sub-categories. They are: (a) collection and disbursement of cheques, (b) payment of dividends, interest, and refunds, (c) liquidity management. Let use take a brief look at each of these sub-categories.

Collection services

Collection and disbursement of cheques for the clients forms an important part of the cash management services. Clients continuously receive payments from their distributors and customers in the form of cheques and demand drafts. Many of these may be outstation cheques and drafts which have to be settled as early as possible. Technologies like Real Time Gross Settlement (RTGS) have helped further in processing the cheques in a much shorter time. To do away with cheques and drafts, clients' customers can also make payments directly into the bank accounts through electronic fund transfer.

Payment services

Payment services include payments to clients' vendors and suppliers, dividends to the shareholders, payment of interest on commercial bills and debentures, payment of salaries to employees, etc. Such payments also involve inter-bank payments as the recipients' accounts may be with different banks. Payments can be made through cheques or demand drafts or electronic fund transfer.

Liquidity management

Liquidity management involves pooling and distributing funds across the client's multiple accounts with the bank. It helps in maximizing the returns on the excess or surplus funds in the accounts of the clients. It also helps in reducing the overdraft expenses as the surplus cash in one account can be transferred to the account through which payments are made to minimize the need for overdrafts. Liquidity management involves either actual movement of funds between accounts or notional pooling services where notional aggregation of balances is done without actually moving the funds from one account to another.

Letter of Credit and Bank Guarantee

A letter of credit is a document issued by a bank as per the instructions of the buyer of goods authorizing the seller of goods to withdraw money from the bank or its branches, on the basis of satisfying certain terms and conditions agreed upon by the buyer, seller, and the bank. A letter of credit is valid for a specified duration of time after which the seller cannot exercise the right to withdraw money from the bank. A letter of credit is commonly used in import & export of goods. Foreign importers issue letters of credit through the Exim Bank of India[5]. Some companies take advantage of the letter of credit and indulge in fraud to make quick money. See Exhibit 11.1 for such an instance where the State Bank of Patiala lost money as a result of letter of credit fraud.

A bank guarantee is an undertaking/commitment made by the bank to pay a certain sum of money to the third party if the client on behalf of whom the guarantee is issued fails to fulfill the contract obligations. Bank guarantees are very common in the construction and other similar industries. Contractors are expected to provide a bank guarantee for a certain sum of money as part of the contract.

Exhibit 11.1

Letter of Credit Fraud

Hamco Mining & Smelting Ltd. (HMSL) is an Indian manufacturer and exporter of aluminum alloys, tin metal ingots, tin-lead solders, and lead alloys. It has a plant in Bishnupur in West Bengal to produce lead from lead ore and lead concentrate, with a capacity of 10,000 tons per annum. In the late 1990s, HMSL requested a letter of credit from State Bank of Patiala (SBP) for importing tin ingots from Frobevia SA of Switzerland. Accordingly, the bank issued an irrevocable letter of credit to United Bank of Switzerland (UBS). Payment was made to Frobevia by UBS when the relevant documents were produced. After the payment was made, SBP came to know that Hamco, Frobevia, and other such companies were cheating Indian banks. In this case, no consignment of tin ingots was imported by HMSL. SBP immediately sent caution notices to UBS about the fraud. In 1999, UBS asked for a refund of the entire amount for all transaction up to 1999. But the Indian banks like SBP refused to pay the amount stating that it had already cautioned UBS about the fraud. UBS moved the Mumbai High Court and lost the case. Subsequently, it appealed to the Supreme Court. UBS won the case for the refund of the entire amount in 2006.

Adapted from Antony, M.J. "Honoring Letters of Credit." Business Standard. June 7, 2006.

Bill Discounting, Factoring, and Forfaiting

Organizations often sell their goods on credit basis and give their customers some time (say 1 month to 6 months) to pay for those goods, as per the payment terms. But they need a constant flow of funds to meet their working capital requirements.

Working capital is short-term capital used to meet the short-term capital needs like purchase of raw material, components, supplies, etc.; manufacturing costs and distribution costs; and other miscellaneous costs. Therefore, to meet the short-term working capital needs, organizations take advances on the receivables from their debtors. These receivables include credit bills and invoices. The common modes of meeting short-term needs are bill discounting, factoring, and forfaiting.

Bill discounting

Bill discounting is the process of providing advance against a bill – which can be a promissory note, bill of exchange, credit bills, etc. – to the clients such that the clients can meet their short-term needs. Bill discounting is done by both banks and other financial institutions. Under this arrangement, the bill is treated as a security to the advance and a certain percentage is discounted from the value of the bill.

The value of the bill is first ascertained and a discount rate is arrived at. Once the agreed upon rate is discounted from the value of the bill, then the remaining amount is given as the advance to the client. If the value of the bill is Rs.100,000 and the discounting rate 10%, then the remaining amount (that is, Rs. 90,000) is paid to the client as advance. The client has to repay the value of the bill in total within the mutually agreed time or before the expiry of the bill. The difference between the original bill value and the discounted rate is considered as the interest income for the amount.

Factoring

Factoring involves converting invoice credit bills (receivables) into cash. It is the process by which a factor (a special firm) purchases the invoice credit bills from its client, discounts the invoice, and pays the remaining amount to the client. Usually 80% of this amount is released immediately and the remaining 20% is released once the debtor pays the bill. Factoring facilitates liquidity for the client. A factor does not factor all the bills of the client's customers. It takes up only creditworthy customers after a credit appraisal is done on them.

Factoring can be done in two ways – with recourse or without recourse. In factoring with recourse (or recourse factoring), the credit risk of non-payment of bills will have to borne by the client (seller of the bills). That is, the factor provides finance to the client, in the form of advance payments. But in factoring without recourse (non-recourse factoring), the credit risk of non-payment is borne by the factor. Hence, in this case, the factor provides finance as well as credit protection to the client.

Factoring is done by both banks as well as other financial institutions. Banks in India provide factoring services through separate subsidiaries. For example, SBI provides factoring services through its subsidiary SBI Factors and Commercial Services Pvt. Ltd., specially floated for rendering such services.

Forfaiting

Factoring of foreign bills is termed forfaiting. Forfaiting is the process of purchase of credit instruments such as credit bills from an exporter drawn on an importer in another country. Forfaiting is always done without recourse, i.e. the credit risk of non-payment is borne by the forfaiter. In addition to the credit risk of the debtor, forfaiting involves debtor country risk[6], currency risk[7], and transportation risks[8]. Forfaiters first value the bill and arrive at a discount rate, taking into the account the various risks to be borne by them. Forfaiting is usually done on big amounts. For example, the many US-based forfaiters do not accept bills worth less than $100,000 for forfaiting. Nowadays, the time frame for forfeiting can be as low as six months and as high as ten years.

Foreign Exchange Services

Foreign exchange services refer to converting foreign currency into Indian currency and vice-versa. The need for such services is felt by organizations whose executives travel abroad, and importers and exporters of goods and services. Banks and other non-banking financial companies operate in this market and they charge a fee for providing such services. A detailed discussion of foreign exchange services is outside the scope of this book.

Merchant Banking

Merchant banking refers to the rendering of services to corporate clients, which include issue management; preparation, planning, and execution of new projects; corporate and project counseling; floatation of new companies; services during mergers & acquisitions; portfolio management; etc. Merchant banking in India has gained importance since liberalization. Capital markets have gained importance for mobilizing long-term capital, either equity or debt. With more companies choosing this channel to mobilize their capital, the need for providing merchant banking services has also increased. Merchant bankers perform a whole gamut of services. They help the companies to smoothly execute the mobilization process, provide advisory services in executing various projects, mergers, acquisitions, get necessary clearances from the government, etc. The major functions of merchant banking are corporate counseling, issue management, project preparation & appraisal, capital structuring, and portfolio management, as summarized in Table 11.2.

Table 11.2: Functions of a Merchant Banker

Area	Functions
Corporate counseling	▪ Advisory services on joint ventures, mergers & acquisitions, turnarounds, and valuation. ▪ Counseling on credit management and working capital management
Issue management	▪ Floating public issues ▪ Acting as lead managers ▪ Assisting clients in appointing registrars and underwriters ▪ Supervising the smooth execution of the issue
Project preparation & appraisal	▪ Project identification ▪ Planning ▪ Getting approvals ▪ Execution of the project ▪ Project appraisal
Capital structuring	▪ Managing the capital structure of the client ▪ Maintaining an optimal capital structure in the long run.
Portfolio management	▪ Managing and providing advice on all the investments made by the client in the stock market, commodities market, or forex market.

Compiled from various sources.

Corporate counseling

Merchant bankers provide corporate advisory services in a range of situations such as joint ventures, mergers and acquisitions (M&A), and corporate restructuring and turnaround. They also advise corporates on credit management, working capital management, and other important areas of managerial decision making.

Issue management

Issue management is considered one of the major functions of merchant banking. It involves flotation of initial public offers and subsequent public issues. Merchant bankers act as the lead manager during the issue and oversee the smooth flotation of the issue. They assist the client in appointing registrars and underwriters to the issue. Some merchant bankers also act as underwriters and provide underwriting services.

Project preparation and appraisal

This function deals with identifying the project, planning it, getting the necessary approvals from the government and other regulatory bodies, executing the project, and appraising it. For instance, if a client decides to acquire another company, then the merchant banker, on behalf of the client, has to do the necessary groundwork like planning for the process of acquiring that company; getting necessary permissions and approvals from the Government, SEBI, and other authorities; planning and acquiring the finances; executing the process smoothly; and appraising the execution of the project.

Capital structuring

The term 'capital structure' refers to the composition of equity and debt capital. Merchant bankers help their clients in maintaining an optimum capital structure by making changes to this structure. More equity capital can be raised when trends show that interest rates are on the rise. Alternatively, the percentage of debt capital can be increased in a low interest rate regime. Equity capital can be raised through issuing shares; debt capital can be raised through issuing debentures, corporate bonds, commercial papers, etc. Merchant bankers help in deciding the optimum capital structure so as to minimize the cost of capital.

Portfolio management

In portfolio management, the merchant banker takes care of the client's stock market operations and manages the client's investment portfolio. Investments are made in stock markets, commodity markets, or forex markets. Advice is given on investing in the right stocks and to make changes to the portfolio reflecting the market changes.

Registrar, Underwriting, and Custodial Services

There are certain services that every company going public needs to avail of. Such services are rendered only during the issue of shares and debentures by a special class of financial intermediaries. They include registrar services, underwriting services, and custodial services. These services are discussed in detail in this section.

Registrar services

A registrar is usually a company appointed for keeping a record of the owners of a corporation's securities. Registrars are appointed by the organization in consultation with the merchant bankers during the issue. The scope of a registrar's functions include information collection from the share applications of investors, classification of the information, allotment of shares, dispatch of allotment letters, and refund orders for unallocated applications. Thus, the services of registrars are used only during a public issue. Registrars work along with the merchant bankers during a public issue.

Underwriting services

Banks and other financial institutions provide these services to corporates in order to cover the risk of under-subscription or non-subscription during a public issue, and charge a percentage of the issue value as a fee/commission for their services.

Custodial services

Custodial services provide for the safe custody of the shares and debentures in physical form (certificates) and/or in dematerialized form (demat form). Any service provider who does this function is termed as a custodian. The National Securities Depository Ltd. and the Stock Holding Corporation of India Ltd. are the two major organizations offering custodial services in India. Apart from them there are many bank-owned custodians who also offer similar services for retail investors as well as mutual fund houses.

Many banks have begun to render such services to corporate and retail clients. They also keep accounts of after-sales services like collection of dividends, bonus, transfer of shares, etc. Exhibit 11.2 outlines the custodial services offered by HDFC Bank.

Exhibit 11.2
HDFC Bank's Custodial Services

Custodial services are one of the major thrust areas of operation of HDFC Bank. HDFC Bank has put in place a custodial services group to oversee the operations in these services. The bank boasts of a customized information processing system, which oversees the customization of the service offerings to different customers. The bank is also physically equipped with computerized premises and storage vaults for better safe keeping of the securities.

HDFC Bank offers custodial services to domestic and international investment companies, which include financial institutions and mutual fund companies. Its list of clients includes Alliance Capital, Canbank Mutual Fund, Cholamandalam Cazenove, Escorts Mutual Fund, GIC Mutual Fund, Jardine Fleming, JM Mutual Fund, Prudential ICICI Mutual Fund, SBI Mutual Fund, Zurich India Mutual Fund, etc. It also offers custodial services to corporate customers and high net-worth individuals.

Adapted from http://www.hdfcbank.com/wholesale/fit/Custodial_Service.htm.

Leasing

Leasing is not considered by many as a pure fee-based service due to the involvement of an asset, say a piece of machinery. But since the lessor charges a rental, and not an interest, for the machinery or equipment leased, this is a fee-based service. A lease can be divided into an operating lease and a financial lease. Operating lease, also called short-term lease, is applicable for low investment assets. Here the asset is used for a certain period of time and then returned to the lessor. A rent is paid for that period of time. A financial lease is a long-term lease, where the cost of the asset and a markup profit is divided into small installments over a period of time (usually the lifetime of the asset). The lessee is required to pay those installments as rentals for the same period. After that period, the lessee gains ownership as the cost of the asset was paid in the lease rentals.

Credit Rating

The credit rating service is a corporate fee-based service where a credit rating agency gives its expert opinion on the relative willingness and ability of the company that is interested in taking a debt in any form. The credit rating agency assigns a rating to the company, based on its borrowing and repayment history. The agency provides this service to its customers to determine their current credit rating. As the credit market has become more organized than ever before, the need for credit rating has also increased. Credit rating differs with the type of organization. For example, the method of rating a large corporate differs from that of a small enterprise and the credit rating for a bank differs from that of an NBFC. In India, the credit rating service is offered by many prominent players like CRISIL, ICRA, CARE, Onicra, etc. While CRISIL, ICRA, and CARE perform credit rating on organizations and business establishments, Onicra undertakes credit rating of individuals apart from SSI/SME to assess their credibility. Usually a AAA rating (pronounced triple A) is given to a company with least risk while a C rating is given to a highly risky company, in terms of probability of timely repayment of credit.

RETAIL FEE-BASED SERVICES

Let us now understand the various retail fee-based services marketed by banks as well as other financial institutions. Retail fee-based services are essentially marketed to retail consumers to help them meet their specific financial requirements. Banks offer many retail fee-based services. But there are also certain fee-based services like 'online trading' and 'wealth management', for which other financial institutions are competing with banks. In this section, we discuss some of the prominent fee-based services that are marketed to retail consumers.

A retail fee-based service can be a pure fee-based service or may be linked to certain fund-based products. The latter can be called a value-added fee-based service as they add value to the existing fund-based products. For instance, savings bank account holders can access the ATM network of their bank to withdraw cash when and where required. They can also use the internet banking and phone banking facilities to transfer funds electronically and/or check account balances, order cheque books, etc. As all these services are linked to (and add value to) the savings bank account (which is a fund-based product), they may be referred to as value added fee-based services. Banks charge a certain fee for each of these services provided to the retail customers. In this section, retail fee-based services are classified under three heads for the sake of simplicity. They include (a) money transfer and payment services, (b) wealth management services and online trading services, and (c) other value added services.

Apart from these services, banks act as channels of distribution and have tied up with different insurance and mutual fund companies to distribute their products. In this process, banks get hefty commissions (fees) from these companies for selling their products through the branch network of the banks.

Money Transfer and Payment Services

As the name implies, the services listed under this head are used to transfer money from one place to another and/or from one account to another. There are different ways of transferring money – it can be through traditional products like demands drafts, cheques, travelers cheques, etc. or through electronic fund transfers. Some of the popular money transfer and payment services are discussed here.

Demand drafts and pay orders

This is a written order to a bank, to pay (on demand) the amount specified in the order. Demand drafts/pay orders are one of the traditional and common modes of payment and fund transfer. Money can be directly paid to the beneficiary (who receives the payment) or it can be transferred to his/her bank account. Banks normally charge a commission to issue the demand draft. The commission may be waived in certain cases, as for example, in the case of demand drafts issued from a salary account.

Banker's cheques

A Banker's cheque is a cheque drawn on the bank itself and made out to somebody. Banks usually give banker's cheques to make third party payments on behalf of its customers. Banker's cheques are very helpful when the third party does not accept the customers' personal cheques fearing that they may bounce. For instance, if a bank sanctions a vehicle loan to a customer, it can issue a banker's cheque to the seller on behalf of the customer for an amount equal to the loan sanctioned.

Travelers' cheques and travelers' cards

Travelers' cheques are used by travelers, usually by those traveling to foreign countries. They are used to make payments in other countries in their respective currencies. American Express was the pioneer in developing this product in the late 19th century. People visiting foreign countries can carry travelers' cheques conveniently instead of cash. According to the Foreign Exchange Management Act, any Indian visiting a foreign country is allowed to carry cash (in the respective foreign currency) only worth up to $2,000. Any amount above this has to be in the form of travelers' cheques. Travelers' cheques can be bought in specified denominations from any bank in either dollars or euro or pound sterling or any other currency.

Though travelers' cheques have become very popular with foreign travelers across the world, they have certain disadvantages. Searching for a moneychanger in the foreign destination (where they are intended for use) can be tiring and cumbersome.

To overcome some of the problems associated with travelers' cheques, banks have introduced a new product -- prepaid foreign card, also known as travelers' cards. These are essentially prepaid debit cards which contain a certain amount of money. They can used as ordinary debit cards in foreign locations while shopping or paying bills. ICICI Bank's Travel Card, HDFC Bank's Forexplus, and SBI's Vishwa Yatra Foreign Travel Card are examples of such cards. If the card becomes empty, it can again be reloaded with cash. Some travelers' cards can also be used to withdraw cash from ATMs at a nominal transaction charge.

Money order

A money order is one of the most traditional and common forms of money transfer. The Department of Posts in India is the major player providing money order services in the domestic circuit. Under this service, money is transferred from the one place to another through the branches of the postal department. A commission is charged on the amount of money that has to be sent. The department also provides a quicker version of the money order, the 'telegraphic money order', where the telegram charges have to be borne by the remitter. Instant money order (IMO), which is a relatively new service, is offered at select post offices. IMO uses the speed of e-mail to transfer the money and the reliability of the postman to deliver it. Select post offices across the country have been designated to provide this service.

Some banks have also tied up with the postal department to provide the money order facility to their customers. Such tie-ups provides synergies in terms of reach to the banks and revenues to the postal department For example, ICICI Bank offers Smart Money Order to its internet banking customers who can send money from bank accounts to any destination in India. The money is physically delivered at the destination by the local postman.

Remittances

The money sent by immigrant workers to their families living in their native countries is termed as global remittance. Remittances are important and stable sources of funds that help developing countries maintain a favorable balance of payments position. India, China, Mexico, and the Philippines are among the top receivers of remittance flows in the world. The United States of America, Saudi Arabia, Germany, and Switzerland are the major sources of remittance.

There are different channels offering remittance services with varying speed of delivery. The remittance services are offered by banks, online portals, postal departments, etc. The remittance products/services offered by banks were discussed in Chapter 5 – Retail Banking. Apart from banks, the postal department has tied up with Western Union Financial Services, USA, to provide the remittance services in all of its branches across the country. This channel is useful if the remitter does not know the bank account of the receiver or if the receiver does not have a bank account. In addition to these channels, there are some new age remittance services providers who render the services through the Internet medium. Remit2India, ikobo, Xoom.com, etc. are some of the online players who have tie-ups with banks and courier service companies to provide remittance services.

Electronic fund transfer

Electronic fund transfer (EFT) uses an electronic medium to transfer funds from one bank to another. Unlike the traditional modes of fund transfer (like demand draft, cheques, telegraphic transfer, or mail transfer), it can be used to transfer the funds between two bank branches within the same day. The RBI has introduced two mechanisms to transfer funds -- National Electronic Funds Transfer (NEFT) and Electronic Funds Transfer (EFT). Of the two, NEFT is faster and the funds are transferred within the same day. But EFT takes three days to complete the transaction. The RBI issued an order that banks should not charge their customers for this service till March 31, 2006. After this date, they had the discretion to fix their own charges for providing this service.

The postal department also has plans to offer EFT services in partnership with banks. It has its existing dedicated countrywide, satellite-based communication network to provide the service. It has already tied up with the UTI Bank as a pilot project where it provides local cheque clearance, high value fund transfer, and warrant payment services to the bank.

Debit card services

Banks provide their accountholders with the convenience of payment through debit cards/ ATM-cum-debit cards. Customers can pay for their shopping at merchant establishments and online shopping websites through their debit cards. Payment through debit cards reduces the hassles of carrying the cash or cheques while shopping. It helps the customers to make effortless payment through the debit card and helps the merchants as the invoice amount is credited directly to their bank accounts. Debit cards are preferred by customers who fear that possessing and using a credit card would lead them into a debt trap, due to overspending and/or due to irregular repayments.

Banks also charge their debit card customers on an annual basis for providing this payment facility. They charge the merchant establishments on a monthly basis for providing this collection facility.

Utility bills payment

Utility bills payment helps the bank's customers to pay their utility bills such as electricity bill, water bill, phone bills, etc., in a hassle-free manner. This service helps customers to avoid the inconvenience of standing in long queues just to pay the amount billed by different utility service providers. Banks gain through charging a nominal fee for this service. The payment can be done either through the ATM or through Internet banking.

Wealth Management and Online Trading

Certain services help the customers to manage/maximize their wealth. The surplus funds available with a customer can be judiciously invested in various financial avenues to reap handsome returns. But almost every financial avenue is associated with a certain risk. The individual (retail) investor may not be well equipped to manage this risk. At this juncture, specialized service providers, who provide wealth management services and other risk management services, can be of immense help to the investors.

Wealth management

Services like investment planning, tax planning, management of assets, etc. that help in managing the wealth of the customers are termed as wealth management services. These services are typically aimed at the affluent class as the cost of service per customer is huge. Wealth management services have gained importance in India, with the robust performance of the economy. Other factors like increasing incomes of the salaried and business classes, and the increase in spending power have fuelled the growth of these services.

The objective of wealth management services is to put to use the investible surplus of the clients in such a way that their wealth is maximized over a period of time. Typical services in this field include investment planning and advice, taxation advice, portfolio management, and asset management. Investment planning involves evaluating the various investment options and identifying the most beneficial avenues, keeping in mind the customer's risk profile. Taxation advice refers to providing tax planning and advice to reduce the net tax liability. Portfolio management and asset management services deal with the management of various assets held in the form of investments, physical assets, etc. such that they yield maximum returns, within the constraints of the individual's risk appetite.

Marketers offering wealth management services have to follow a customer-centric approach. Every client has to be allocated with a relationship officer who will be the liaison between the marketer and the client. Initially, the relationship officer (who may handle, say, 20 to 25 such clients) has to spend some time to understand the client's financial requirements thoroughly. Once a firm relationship is established, then the actual benefits (in terms of profits for the marketer) can be reaped from the relationship. In a mature relationship, the client places full confidence in the marketer and does high value transactions. Marketers can benefit from such transactions by earning handsome commissions and fees for their services.

Online trading

Online trading is one of the latest fee-based services offered by banks and other financial institutions -- brokers (or) depository participants. Online trading involves trading in shares, debentures, commodities, and foreign exchange in the respective markets. Any retail customer wishing to trade online in securities has to open a demat account with a broker. The selling and buying transactions are updated in this account.

The broker charges a commission for every customer transaction. Brokers may also provide investment advice and risk management services to their customers. Commercial banks have also recently made forays into providing these services to their customers by floating subsidiaries

Other Value Added Services

Other miscellaneous value added services offered by financial institutions are discussed under this head. After deregulation of the banking sector by the government, banks had to differentiate themselves from the growing competition. In this process, they introduced many value-added services. Revolution in technology has helped further in delivering these services to the customer in more effective ways. Such services include drawing money from ATMs, availing of Internet banking, phone banking and mobile banking services, and usage of safe deposit lockers.

ATM, Internet banking, and phone banking

It has become a common feature for every bank account to be accompanied with an ATM card, Internet, phone banking and mobile banking facilities. Banks provide these facilities so as to enhance the value of the fund-based product. They also charge a certain nominal amount from the customers for providing such services. A certain annual fee is charged for the use of the ATM network, Internet, and phone and mobile banking facilities. Every bank has its own ATM network. When the customer of one bank uses the ATM network of another bank, certain charges are levied on that customer depending on the type of transaction. For example, in the case of balance enquiry, the bank (whose ATM was used) may charge a fee. For cash withdrawal, both the banks involved may charge separate fees. But due to the pressure of competition, banks have formed certain groups to share their ATM infrastructure and deliver better service to their customers. Customers of any of these member banks can use this shared infrastructure without paying any additional fee.

Locker facility

A safe deposit locker facility is a facility offered by many banks, but only at select branches. It is used to safeguard valuable items kept in the safe custody of the banks. Safe deposit lockers come in different sizes and the banks charge rentals for them according to their size. In practice, a person may be asked to take a term deposit with the bank as a collateral, for the privilege of availing of this facility. Banks may charge an opening fee for the locker facility, apart from the annual rentals. Some banks (e.g. UTI Bank) encourage people to become customers (by opening an account) and avail of the locker facility without any deposit.

PRICING

The pricing of fee-based services is mostly based on the relationship with the customers. The customers of fee-based services include both corporate and retail customers. Large corporations are characterized by high value, bulk transactions; the pricing of these transactions depends on the relationships with the service providers. Thus, service providers adopt a one-to-one pricing for each transaction. The pricing also depends on the size of the transaction. If the value of the transaction is high, the price (per unit of value) is reduced and vice-versa. In the mid-sized corporate and SME (Small and Medium Enterprise) segment, prices are determined primarily based on the transaction size, in addition to the relationship that exists between the service provider and the client.

The prices of most retail fee-based services are fixed by the top management as in the case of demand drafts, cheques, money orders, remittances, online trading, locker facility, etc. But certain services like wealth management services are again relationship based and the service providers adopt a relationship-based one-to-one pricing.

Factors Influencing Pricing

Banks usually charge the clients based on the size and volume of the fee-based transactions. A bigger size and more volume may lead to lowering of the fees, while small-sized transactions and low volume transactions attract fees at a higher rate. The fee charged is also determined based on the duration and quality of the relationship with the client.

Regulations also influence the charging of fees by banks. Earlier, most banks did not charge any fee for cash management services, which include payment of salaries, collection and disbursements of cheques, liquidity management, etc. This was because the money that was collected in the banks before payment of cheques and drafts, called float money, was profitably invested in the overnight money markets. In this way, banks earned good income from the cash management services without charging their customers anything. But the situation changed in March 2004 when the RBI introduced the Real Time Gross Settlement (RTGS) system. This is a new technology using which outstation cheques can also be cleared on the same day and fund transfers between different branches of the same bank or between different banks can be done instantaneously. As a result of this change, banks were left with no float money to invest in the overnight markets. They thus lost a sizeable income, of which nearly 70% was attributed to cash management services. Banks now charge a certain fee for the entire spectrum of cash management services as the new technology helps transfer funds in real time. For example, Bangalore-based Karnataka Bank introduced a new service called Money Quick[9] in July 2005, using the RTGS system to transfer funds. The bank charges a fee for this service.

Pricing of Different Fee-based Services

Retail fee-based services like issue of demand draft, banker’s cheques, etc. are charged a certain fee called a commission. The commission is fixed by the top decision making authorities. They also charge a fee for certain services such as issue of new cheque books, ATM usage, debit card and credit card usage, instant fund transfers, etc. Banks now offer certain value-added services like ordering for demand drafts, transfer of funds, utility bill payments over the Internet or on the phone. Internet banking, phone banking, and mobile banking technologies have made this a possibility. A fee is charged for such value-added services. This has proved to be a good income source as the number of customers availing of such services has increased manifold. Rentals are charged for safe deposit lockers. Table 11.3 lists the fees charged by the State Bank of India (SBI) for various fee-based services.

Other fee-based services like underwriting services, registrar services, etc. are charged as a percentage of the total issue value. The total issue value is the price of each share (or instrument) multiplied by the number of shares (or instruments) issued. For instance, according to the Indian Companies Act, Section 76, underwriters can charge a maximum of 5% of the price at which shares are issued or the rate authorized by the articles of the agreement with the client.[10] In case of debentures, they can charge a maximum of 2.5% of the price at which debentures are issued, or rate authorized by the articles of the agreement with the client.[11]

Table 11.3: SBI's Service Charge and Fees for Fee-based Services – A Partial List

1.	ATM Services Annual Maintenance Fees	Rs.50 Applicable for all ATM/ debit card holders and will be levied at the start of 2nd year.
2.	Issue of demand drafts For remittances in cash above Rs. 10,000/-	Upto 10,000 Rs. 30/- >Rs10000/- Rs.3.5 per Rs. 1,000 (Min. Rs. 50; Max. Rs. 12,500) (+ Rs. 100 per telegram for Telegraphic Transfers) For remittances by cash deposit above Rs. 10,000/-, Rs.10/- extra will be charged
3.	Electronic Fund Transfer (online with RTGS)	Rs.1.50 per Rs. 1,000/- Min. Rs.100/- Max. Rs.1,500/-
4.	Bankers' cheque For remittances in cash above Rs. 10,000/-	Upto Rs. 10,000/- Rs. 30/- > Rs. 10,000/- Rs.3.5 per Rs 1,000 Min. Rs. 50/- , Max. Rs. 12,500/- (For remittances by cash deposit above Rs. 10,000/-, Rs.10/- extra will be charged)
5.	Issuance of duplicate demand draft	50% of the applicable exchange- Min. Rs.110
6.	Issue of duplicate banker's cheque	Rs.100/-
7.	Stop payment instructions	Rs.110 per instrument Rs. 220 for a range of cheques
8.	Minimum balance service charges	Savings Account: Rs. 300 per quarter (Rs.150 per quarter for Rural branches/ Semi-urban branches) Current Account, for individuals: Rs.750/- per quarter Current account, for organizations: Rs 1,350/- per quarter

Source: http://www.statebankofindia.com/viewsection.jsp?lang=0&id=0,10,547

DISTRIBUTION AND PROMOTION

The channels for the distribution of fee-based services are quite similar to those discussed in the banking chapters. Marketers utilize the same distribution channels to increase efficiency and to reduce costs. However, marketers do not use the conventional promotion mix for promoting fee-based services.

Distribution of Fee-based Services

Distribution in corporate and retail banking was discussed in detail in the earlier chapters. In corporate banking, the marketer lays more emphasis on direct marketing and personal selling. Relationship building is given prime importance in selling these products. Banks adopt similar strategies to distribute fee-based services. Cash management services, merchant banking services, factoring & forfaiting services, etc., are distributed using the same distribution channels as discussed in Chapter 4: Corporate Banking. These channels include branches, Internet, and phone banking. Distribution of retail fee-based products is through branches, ATMs, Internet, phone banking, mobile banking, etc.

Branches

Cash management services were traditionally offered to the corporate customers through telephone calls, fax, and mails, and when the customers visited the bank. The treasurer of the company used to carry out the transactions of the company (on behalf of the company) in the bank. But with the revolution in communication technologies, web-based channels such as the Internet and e-mail have helped banks to automate many of the cash management services.

Despite the advent of many new technology-enabled channels, branch banking continues to be the most important distribution channel. Bank marketers have focused on retaining complex fee-based services at the branch as it involves more in-person interaction. Merchant banking, factoring, foreign exchange services, and issue of bank guarantees/letters of credit are managed from the branch.

The less complex services have been shifted to other distribution channels like phone banking, Internet banking, and mobile banking. For instance, issuing a demand draft, which is less complex than the merchant banking services, can be availed of via the Internet and phone banking.

Bank branches are also used to cross-sell the insurance and mutual fund products of other companies. Exhibit 11.3 explains how Jammu & Kashmir Bank was able to leverage on its branch network to distribute the insurance products of Bajaj Allianz and earn a sizeable revenue from the arrangement.

Exhibit 11.3

Jammu & Kashmir Bank – Bajaj Allianz: A Win-Win Tie-up for Bancassurance

In 2003, the Jammu & Kashmir Bank, a profitable public sector bank with a national presence, tied up with Bajaj Allianz, a leading life and non-life insurance company promoted by the Bajaj Group. The bank sold the insurance schemes of Bajaj Allianz through its branch network in return for commissions on the premium.

The bank trained its staff to sell the insurance products to existing customers. It appointed a team of trained and licensed insurance managers to analyze the prospective customers. This arrangement helped Bajaj Allianz gain about an 85% share of the general insurance market in Jammu & Kashmir.

In order to earn fees for sales of insurance policies, the bank took various initiatives. Some of them were:

- The bank insured around 8000 of its own employees under Group Insurance Personal Accident Cover.
- It introduced a Group Personal Accident Insurance Policy to its account holders and borrowers, which received an overwhelming response.
- A free insurance scheme was introduced for those term deposit holders who deposited in any deposit scheme with maturity of six months and above.
- The bank also provided ‘on the spot insurance cover’ to about 150,000 Amarnath-bound pilgrims every year, through its 88 designated branches in Jammu & Kashmir.

Adapted from Drabu H.A. “Jammu & Kashmir Bank – Bancassurance Channel.” Bajaj Allianz Newstrack. March 2006.

The Internet

Most of the retail fee-based services have been shifted to the Internet channel. This channel has proved to be cost effective for the banks and time saving for the clients, which explains its growing popularity. Customers can use this channel to transfer funds, check balances, request for cheque books, order for issue of demand drafts, etc. Cash management services like liquidity management services have been mostly transferred to this channel. Technologies like electronic funds transfer and electronic data interchange have facilitated these changes.

Phone banking and mobile banking

As of 2006, Indian private sector banks and foreign banks have used phone banking and mobile banking more extensively, as compared to public sector banks. Though basic services are provided through these channels, they save a huge amount of time and money for both the banks as well as the customers. Checking of balances, order drafts, funds transfer, and request for cheque books are some of the services offered over these channels.

Promotion of Fee-based Services

Fee-based services are seldom promoted using the traditional promotion mix. Such services are more relationship oriented and hence build on relationships with the clients/customers. For instance, a merchant banker gains business from the customers through the competitive bidding process or based on the strength of the relationship between them. Private banks were the pioneers in using personal selling as a means of marketing financial products and improving market share. Personal selling is a prominent form of promotion at the branch level, where the sales personnel of the branch develop contact lists of potential customers and contact them in person to sell the bank's products. Personal selling is more prevalent in corporate fee-based services than in retail. Issue management, underwriting services, etc. use relationships to clinch deals. Often relationship officers and other financial experts from banks go to the clients' premises to provide consultation, advisory services, and project planning

The Internet has become a popular promotion medium. The websites of banks and financial institutions promote their products and services aggressively. Apart from the Internet, public relations activities like sponsoring major events and conferences, press releases of the latest developments, etc. may also help the marketers improve their public image and attract more customers.

Discounts and concessions in pricing are also used to attract the customers as part of the sales promotion strategies. For instance, SBI, a late entrant to the business of providing online trading services, has partnered with Motilal Oswal Securities Limited (MOSL) to provide online trading services to its customers. The demat account and the concerned savings or current account will be opened with SBI while the trading account will be opened with MOSL. All the three accounts have been collectively named eZ@sbi account. To promote this service, SBI has waived the account maintenance charges for customers who open the eZ@sbi accounts on or before March 31, 2007.

Other than these ways, retail fee-based services have also been promoted in some unique ways. For instance, ICICI Bank, in 2004, announced that its branches would remain open until 8:00 PM in the evening to allow customers to avail of various banking services. The bank undertook a nationwide promotional campaign, which included television and print ads, publicizing the fact that it was the first bank in the country to remain open for twelve hours a day (from 8:00 AM to 8:00 PM), six days a week.

PEOPLE

When compared to fund-based products, the fee-based services are more inclined toward the service end in the product-service continuum. The marketing of fee-based services demands people with high caliber who can respond effectively to the customer's needs and deliver superior results within a given timeframe.

To provide effective service, marketers have to recruit people with high caliber to deliver such service. For instance, most of the popular financial institutions recruit candidates from top business schools in India. Once recruited, the candidates have to be trained and motivated to deliver quality service. They should be capable of handling unstructured situations. This trait is more important for customized fee-based services than for standardized fund-based products.

Customers who form the other part of the people factor in services marketing, have to be educated about the services offered by the marketer. A well-informed customer can be of more value than an ill-informed customer. Satisfied customers can serve as ambassadors for a company's fee-based services.

PROCESS

Every service marketer has to understand the importance of the process in the marketing mix. They should understand how the process of the service affects the profitability. According to Zeithaml and Bitner, the process of a service can be discussed in terms flow of activities, number of steps involved, and the extent of customer involvement. Flow of activities is considered in terms of whether the service is standardized or customized. Simple and routine services like issue of demand drafts and banker's cheques have to be standardized. As process standardization reduces service time, more customers can be serviced in the given time. That is, the more the demand drafts issued in a given time, the more the revenues. On the other hand, complex services like merchant banking services, online trading, wealth management services, etc. have to be customized according to the requirements of individual customers. Customization in such services leads to customer satisfaction.

The next factor under process is the number of steps involved in delivering a service. The more the number of steps in the delivery of a service, the more complex the service becomes. For this reason, marketers should ensure that customers do not feel dissatisfied with the service due to lengthy processing. For instance, office automation in the banking industry has changed the functioning of banks. It has also reduced the time spent as part of the human involvement in delivering the service. Electronic fund transfer has reduced the hassles of long waiting time and lengthy processing in the traditional fund transfer mechanisms. Though a certain amount of processing is involved, that is in effect hidden from the customer and gives the impression of delivering the service in much shorter time.

The final factor in a service process is customer involvement. The marketer has to involve customers in the service to achieve superior quality. Customer feedback has to be considered, both for upgrading existing services and for developing new services. Customer involvement in service delivery creates a sense of ownership of service in the customers and helps the marketers in delivering better quality.

SUMMARY

Fee-based services can be broadly classified into corporate and retail fee-based services. Organizations avail of such services for meeting both their short-term and long-term financial requirements. The common fee-based services offered to corporate clients are: cash management services, letter of credit, bank guarantees, bill discounting, factoring/ forfaiting, forex services, merchant banking, registrar services, underwriting services, custodial services, lease and hire purchase, and credit rating. Retail fee-based services are availed of at large by the retail customers for payments, money transfers, personal wealth management, online trading, etc.

While pricing of corporate fee-based services are relationship oriented and relatively flexible, retail fee-based services have standardized pricing. Though fee-based services are not promoted using the traditional promotion mix in a major way, their distribution is similar to that of banking products. For corporate fee-based services, marketers use branches extensively, whereas their retail counterparts use advanced technology channels such as the Internet. For wealth management services in the retail segment, relationship-based personal selling is combined with the technology-oriented channels of distribution.

The active involvement of people is necessary for rendering fee-based services as the people factor decides the quality of service delivery. Many of the service providers recruit candidates from reputed colleges and institutions, and train them to handle the customer requirements.

The process factor in service delivery can be analyzed in terms of the flow of activities, the number of steps involved in each activity, and customer involvement. Providers of fee-based services take all these factors into account for achieving high levels of service quality.

End Notes:

[1] Ramachandran, Chhaya. “Boosting of Fee-based Income of Banks – Ways and Means.” IBA Bulletin. December 2005.

[2] The NIM is the difference between interest earned and interest expended as a proportion of average total assets. This is one of the key parameters to measure the efficiency of banks.

[3] Srisat B.G. “Banks Feel a Pinch on Interest Margins.” Business Standard.” June 29, 2006.

[4] www.icicibank.com

[5] Export-Import Bank of India was set up by an act of Parliament in 1981 and commenced operations in 1982, for the purpose of financing, facilitating, and promoting foreign trade of India.

[6] The financial risks of a transaction which relate to the political, economic, or social instability of the country of the debtor.

[7] The risk of incurring losses resulting from an adverse movement in exchange rates.

[8] The risks associated with the transportation of goods by land, air, and sea. Such risks include delay in transportation, destruction of goods due to natural calamities and accidents, etc.

[9] “Karnataka Bank RTGS Facility for Customers.” The Hindu Business Line. July 13, 2005.

[10] http://www.vakilno1.com/forms/agreements/agr23.doc

[11] http://www.vakilno1.com/forms/agreements/agr23.doc

Part III
Trends and International Perspectives

Photo: Rodolfo Clix

Chapter 12: Trends in Banking and Insurance Marketing

Chapter 13: The Global Scenario

Chapter 12

Trends in Banking and Insurance Marketing

In this chapter, we will discuss:

- Technology and Marketing
- Trends in Bank Marketing
- Trends in Insurance Marketing

The financial products and services market has seen a transformation over the last two decades in India. The demand for financial services has seen a huge growth with the increase in per capita disposable income. Competition has intensified with new players entering the market after deregulation of the insurance and banking sectors. The level of consumer expectations also has gone up with increased awareness and information on financial products, supplemented by the promotional efforts of the marketers. These changes have forced financial product marketers to innovate, both on the marketing front and on the service delivery front.

Technology has played a significant role in the marketing of financial products. Marketers have taken the help of technological advancements for new product development, segmentation and targeting, alternate modes of service delivery, and innovative promotional campaigns. In this chapter, we first discuss the influence of technology on marketing financial products, in terms of service delivery, customer satisfaction, etc. The subsequent sections describe the trends in the marketing of banking products and insurance products.

TECHNOLOGY AND MARKETING

The last decade has seen remarkable technological advancements which have aided operations in the financial services segment. The three most important segments of technology relate to computerization, automation, and information technology. Computerization helps collect, store, and interpret the huge amount of demographic information. Computer programs also help underwriters, agents, and financial planners. Computerization and automation increase the efficiency of the system by reducing the extent of paperwork required, and the associated hassles of storage and retrieval.

Information technology (IT) has changed the way financial marketers function. IT encompasses telecommunication, multimedia, relational database management systems (RDBMS), image technology, etc. The common applications of technology in financial product marketing include the use of ATMs and kiosks, phone and Internet banking, cashless transactions, online payments of insurance premiums, stored value cards, digital security, etc. CRM, Business Intelligence solutions, and enterprise-wide IT solutions are important software applications that are used by financial product marketers. In this section, we explore the trends in the use of kiosks, stored value cards, digital security, Business Intelligence solutions, and enterprise-wide IT solutions.

Kiosks as Marketing Tools

Financial product marketers were quick to identify the marketing potential of kiosks. Kiosks are primarily used as a tool to provide information. In addition to disseminating information, kiosks also help reduce the cost of operations significantly. A kiosk costs around one-fourth of an ATM machine[1].

In the banking industry, many banks now have information kiosks in the branches that inform customers of their various product offerings. For instance, HDFC Bank has installed kiosks that provide details on the entire range of offerings of the bank. Customers can use the touch screen facility to search for the required information.

Kiosks are not only used as a tool to provide information, but also aid in implementing customer relationship management and as a means of brand communication. Most marketers design their kiosks using the colors and logos of their respective organizations. The colors and logo thus act as a means of brand communication. For example, HDFC Bank is associated with blue, UTI Bank with maroon, and Bank of Baroda with orange.

Financial marketers have begun to use kiosks to market products and services to the rural population. For instance, ICICI Bank has tied up with Hindustan Lever Ltd. to provide a new delivery channel for rural India. HLL delivers information services to millions of rural people across thousands of villages through the project 'i-shakti.' It uses kiosks to offer information in the form of audio-visuals on health & hygiene, education, agriculture, employment, legal services, veterinary services, etc. ICICI Bank plans to use this channel to offer life and general insurance products in the first phase. Later, the bank plans to introduce other financial services including personal credit, rural savings accounts, and remittances.

Stored Value Cards

The credit card segment is slowly moving toward the Stored Value Card (SVC), a type of plastic currency. The cash amount is stored in an electronic form on the microprocessor chip of the credit card. The card enables a customer to transfer cash from his/her bank account on to the chip of the card and use it. SVCs come in two variants -- disposable SVCs and re-loadable SVCs. In the disposable type, the amount is entered only once. When the amount is exhausted, the card is of no use and can be disposed of. In the re-loadable SVC, the value stored in the card can be replenished by the users, based on their requirements.

The Reserve Bank of India (RBI) has classified SVCs into three types based on their utility[2]. They are single purpose cards, closed system cards, and general or multipurpose cards. The single purpose card is suitable only for transactions of one type, that is, for transactions related to one service provider, one product category, etc. as for example, payment of telephone bills, or parking charges. A closed system card is generally used in a limited geographic territory like a company or university campus. The multipurpose card, on the other hand, can be used at various locations many times for various purposes like bill payments, online payments, in-store purchases, etc.

Financial marketers have made good use of the stored value card concept to provide banking products to customers. Table 12.1 lists some of the SVCs issued by banks in India.

Table 12.1: Stored Value Cards in India

Issuer	Type of SVC issued
State Bank of India	Travel Easy card
HDFC Bank	Kisan card, Forex Plus Travel card, Gift Plus card
ICICI Bank	Prepaid Travel card

Source: "Stored Value Cards." http://www.expresscomputeronline.com/20060626/technology03.shtml 26 June 2006

Digital Security

Transactions related to financial services involve a lot of paperwork, signatures on documents, etc. They can become tedious, especially if the service provider has a large customer base. There are also security concerns. Digital signatures and digital cheques are two technological developments that assure security. Digital signatures were given legal sanctity by the Information Technology Act of 2000. The Act legalized digital signatures and equated them with signatures on paper for most financial instruments. The entire process of issuing certificates with digital signatures is managed by the Certifying Authority (CA), licensed by the Controller of Certifying Authorities (CCA). The IDRBT (Institute of Development and Research in Banking Technology) is one of the institutions channelizing its efforts to implement the concept of digital certificates in Indian banking.

Business Intelligence

In today's world of intense competition, the insight gained from information is the key to competitive success. Business intelligence tools like data warehousing and data mining are used by financial marketers to obtain relevant information on every aspect of the customer value chain. Information systems provide a knowledge database that many marketers use to target specific customer segments and also to cross-sell products to existing customers. These systems are used for decision making on customer lifetime value in credit card marketing, level of health risk in health insurance marketing, offering customized solutions, etc.

Enterprise-wide IT Solutions

In recent years, insurance companies and banks in India have been adopting technology at a rapid rate. The insurance segment has embraced technological advancements to deliver higher standards of service. The same trends have been witnessed in banks. This is in contrast to the early 1990s when there was huge resistance from the employees of public sector banks to computerization.

Technology has made it easier for insurance marketers to collect premium payments, increase awareness and knowledge of products, communicate the status of the premium paid, facilitate claim settlements, etc. LIC, the major public sector player in the insurance segment, has effectively implemented technological changes. For instance, it has introduced MAN (Metro Area Network). Under this initiative, about 100 of its divisional offices have been networked. This has enabled customers of LIC pay their premium for a policy at any of the branches connected to the network. Customers can also check the status of the premium paid. LIC has entered into tie-ups with some reputed banks to facilitate online payment of premiums. Besides, it has deployed touch screen kiosks to provide informational services to customers.

In India, private banks were the pioneers in leveraging on technology to increase consumer reach through better products, service delivery, and customer management. Public sector banks too have followed the new generation private sector banks in taking steps to harness the benefits of information technology. For instance, SBI has taken the lead and has gone ahead with implementing 'core banking' across the entire branch network. Exhibit 12.1 describes the core banking initiatives taken by SBI.

Exhibit 12.1

Core Banking Initiative of the State Bank of India (SBI)

The core banking solution (CBS) was implemented by the SBI as part of its efforts to streamline its back-end processes and offer better customer service. CBS is a common technological platform that provides ease of functioning across four broad areas -- retail banking, corporate banking, trade finance, and the general ledger. Implementation of the CBS was an integrated cross-functional effort, addressing issues of systems, processes, and governance.

SBI gained immensely after the implementation of the CBS. The major technological benefits were standardization of platforms and improved IT governance. CBS helped streamline the various processes and reduce the number of activities done manually. The customer response time also went down to a great extent. Another benefit that SBI achieved through the implementation of CBS was the ability to operate as a single entity. The magnitude of this technological implementation can be understood from the fact that the CBS was expected to help 13,984 branches handle an array of products serving more than 100 million customers (and 120 million accounts), at an average of 25 million transactions per day.

Source: "State Bank of India: Transforming a Giant." http://www.tcs.com/htdocs/State_bank_of_india.pdf

TRENDS IN BANK MARKETING

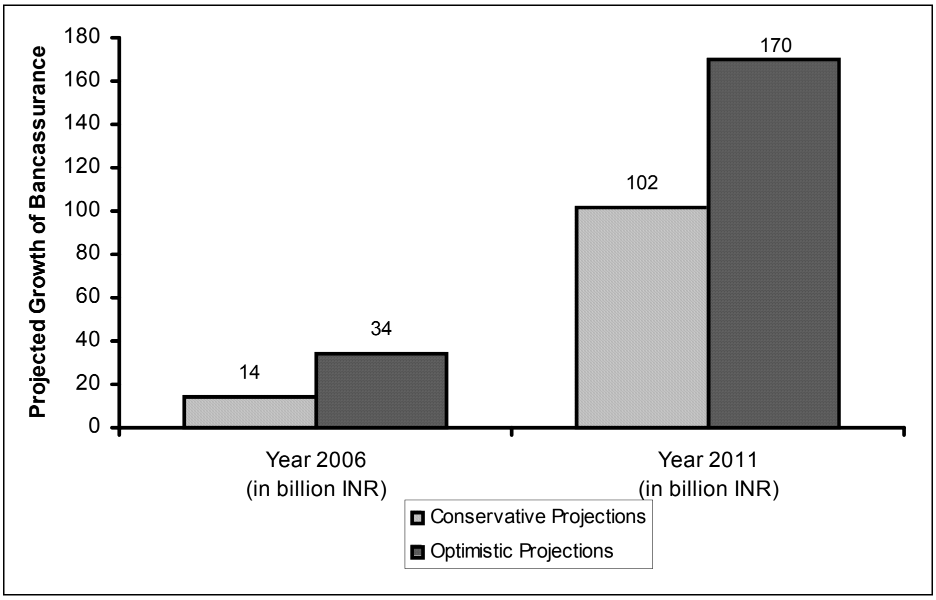
Almost all major banks are investing significantly on technology upgradation, to improve their customer management abilities. However, the huge spending on IT has led to a significant increase in their operational costs. The banks are trying to compensate for these rising costs by earning additional (non-interest) income by distributing third party products such as insurance (bancassurance) and mutual funds (mutual banking). Another significant trend has been the focus on rural banking, financial inclusion, microfinance, and Small and Medium Enterprises (SMEs). A few banks are looking at geographical expansion through organic or inorganic growth, not only to serve non-resident Indians but also to firmly establish themselves in selected countries. Some banks are attempting to become one-stop-shops for financial products through the concept of 'universal banking.'

Bancassurance

Bancassurance is the selling of insurance products through banks and their associated distribution channels like ATMs, tele-banking, and Internet banking. In India, bancassurance is still in its infancy. Over the next few years, the bancassurance channel is expected to contribute significantly in generating new business. For instance, Bajaj Allianz Life Insurance has more than 25% of its new business coming through its bancassurance tie-ups in 2005[3]. Bajaj Allianz has bancassurance tie-ups with Standard Chartered Bank and Syndicate Bank. Public sector banks have just begun to see bancassurance as a source of additional income. For instance, Union Bank of India has a tie up with HDFC Standard Life Insurance to sell the latter's insurance policies. The bank expects to earn around Rs. 12 million in the form of annualized fee from HDFC Standard Life.

Studies have estimated that bancassurance has a very high potential in India. Figure 12.1 depicts the projected growth (conservative estimates as well as optimistic estimates) of the bancassurance channel in India.

Figure 12.1: Projected Growth of Bancassurance in India: 2006 – 2011



Source: Singh, Deepti and Zia Hajeebhoy "Bancassurance: Indian Expectations." *http://www.ciionline.org/sectors/62/Images/BANCASSURANC%20INDIAN.pdf*

The IRDA has issued guidelines that place restrictions on the partnerships between insurance companies and banks. Each bank can offer the insurance products of only one general insurance company, and only one life insurance company. Table 12.2 lists the various bancassurance tie-ups by Indian general insurance companies with banks.

Table 12.2: Bancassurance Tie-ups

Insurance Company	Partner Banks
Bajaj Allianz	Deutsche Bank YES Bank United Bank of India Punjab & Sind Bank Jammu & Kashmir Bank Karnataka Bank IDBI Bank UTI Bank
National Insurance Co. Ltd.	Vijaya Bank Allahabad Bank UCO Bank State Bank of Bikaner State Bank of Patiala State Bank of Jaipur
New India Assurance	State Bank of India United Western Bank Central Bank of India Corporation Bank
Oriental Insurance	Oriental Bank of Commerce Dena Bank Canara Bank State Bank of Saurashtra Tata AIG HSBC
United India Insurance	Dhanalakshmi Bank Syndicate Bank Bank of Maharashtra Federal Bank
IFFCO Tokio	Sardar Bhiladwala Co-op Bank Janakalyan Sahakari Bank
Royal Sundaram	Citibank Lakshmi Vilas Bank ING Vysya Standard Chartered Bank

Compiled from various sources.

Mutual Banking

A number of alliances have been forged between mutual fund marketers and banks in recent times. The different alliances that marketers prefer are arranged alliance, alliance between families, and multiple alliances. The arranged alliance is between sister concerns — a bank and a mutual fund company belonging to the same group. An example is SBI Bank and SBI Mutual. An alliance between families happens when the banks and the mutual fund companies are two separate standalone units as for instance, the tie-up between Federal Bank and Franklin Templeton Investments Ltd. Under this tie-up, Federal Bank distributes the mutual fund products of Franklin Templeton through its bank branches. Multiple alliances happen when a bank ties up with more than one mutual fund. For example, ICICI Bank has tied up with several mutual funds to offer its customers the convenience of varied investment. ICICI Bank offers customers the choice of investing with more than a dozen players offering around 300 schemes. Some of them include Cholamandalam Mutual Fund, Kotak Mahindra, ING Vysya, and Alliance Mutual Fund.

Mutual banking offers various income generation avenues for banks like upfront mobilization incentives, special incentives, commission, loyalty commission, and collection charges. The wide customer base of banks is the key factor that makes mutual fund companies choose banks to distribute their products. The leading distributors of mutual fund products are HSBC Bank, ICICI Bank, Standard Chartered Bank, and Citibank.

Rural Banking and Technology Inclusion

While rural banking has been in practice for many years with its focus on disbursing credit, it has been observed that the rural population in India, unlike the urban population, does not have the required access to advanced technology or a wide range of financial services. Many banks have started making focused efforts in an effort to bring connectivity and make services more accessible to the rural population. This has gained momentum with the government's initiative on 'financial inclusion' (discussed later in the chapter). Some initiatives of the banks for the rural sector are listed in the Table 12.3

Table 12.3: Rural Initiatives by Banks in India

Bank	Initiative	Features
ICICI Bank	Rural business Centers	The 'Rural business Centers' were developed by ICICI Bank with the assistance of Wyse[4] (a reputed company in the field of network centric computing solutions) and Comat[5] (an IT business solutions company headquartered in Bangalore). This initiative, which relies on the benefits of thin-client structure[6], tries to provide the much required services (educational, financial and social services) to rural citizens in real time. This initiative was first implemented in select rural areas in the state of Karnataka.
	Rural banking/ microfinance initiative	ICICI Bank has introduced Smart Cards, embedded with a 32 KB memory chip, for the rural poor. This chip stores information relating to the individual account like name, address, loan transactions, etc. Smart Cards do away with the need to carry passbooks and other banking documents. The Point of Transaction (POT) terminal is enabled with biometric identification.

Bank	Initiative	Features
Union Bank of India	Rural initiative	Union Bank of India has also implemented certain technology initiatives to cater to rural banking. They include kisan call centers, kiosks, and offices attached to the rural branches spread across the nation. These technologies help farmers access information relating to agriculture, weather, and other information from web portals such as agmarket.nic.in, apeda.com, krishiworld.com, etc.
YES Bank	Wageningens agro food park model	The Mumbai-based YES Bank has entered into a tie-up with the Netherlands-based Wageningens University Research Center to introduce the Wageningen's Agro-food Park model. YES Bank plans to open a branch in Nashik (Maharashtra). Since grape is a major crop in this region, the bank intends to finance the infrastructure required for vineyards and provide information on technology, processing, etc.
NABARD	Kisan credit card	NABARD introduced the Kisan Credit Card scheme for farmers, in 1998. Initially, banks did not take much interest in the scheme. However, the scheme has picked up over the years, with the government's emphasis on priority lending. The Kisan credit card offers the farmers an easier option to avail of loans. The cards are simple to use. The banks have designed a convenient repayment schedule to avoid problems related to bad loans.

Adapted from Manghani, Hanil and Sunil Kumar "Technology as an Inclusion Factor." http://www.cxotoday.com/cxo/jsp/article.jsp?article_id=73802&cat_id=912 June 09, 2006 and "Indian Banks Discover Appetite for Rural, SME Segments." http://ibef.org/download/indianbanks.pdf September 16, 2005.

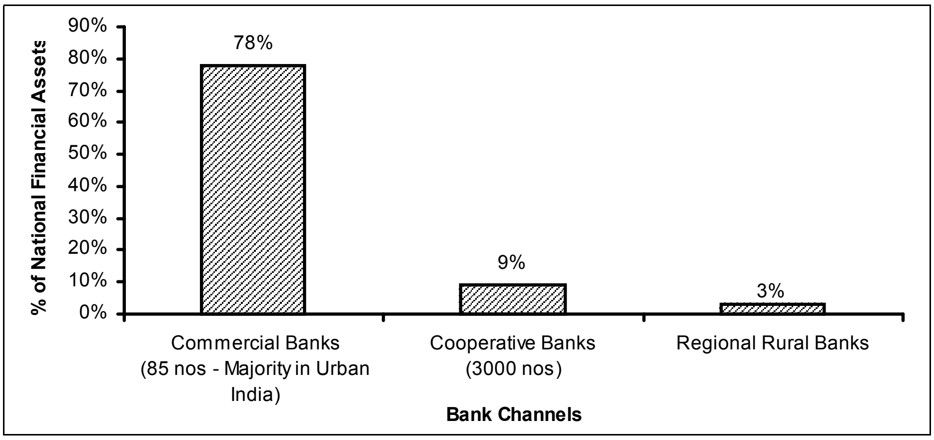
Financial Inclusion

The Government of India has been taking various socioeconomic initiatives to reduce the gap between the haves and have-nots. Financial inclusion is one such policy initiative that it has taken to bring banking services well within the reach of the common man.

It has been the intention of the Indian government to provide banking services to the rural areas in the country. As early as in the 1970s, it set up Regional Rural Banks (RRBs). However, there has not been any significant increase in the assets of these banks in the last few decades. Figure 12.2 makes it amply clear that a major portion (78%) of the financial assets is with the commercial banks, which are present mainly in urban areas.

Though there are 3,000 co-operative banks, they have not been able to build significant financial assets. The regional rural banks, which were created to provide banking services for the rural masses, have proved ineffective. They account for a mere 3% of the total financial assets. As part of recent efforts in financial inclusion, the Reserve Bank of India (RBI) has asked the banks in India to introduce the 'No-frills' account.

Figure 12.2: National Financial Asset Distribution across Bank Channels



Source: Punnathara, C J "No-frills Bank Accounts: Financial Inclusion is Good Economics."http://www.thehindubusinessline.com/2006/06/08/stories/2006060800251000.htm June 08, 2006

'No-frills' account

The RBI proposed the 'no frills' account in 2005. The main benefit of this account is 'zero-balance' or a minimum balance facility. Earlier, the minimum balance required for opening bank accounts ranged from Rs. 100 (without cheque book facility) to Rs. 1,000 (with cheque book facility). Some private banks required minimum deposits of as high as Rs. 5,000.

The concept of a no-frills account has been well received by the nationalized banks. Many private and foreign banks also have shown keen interest on this product. Table 12.4 gives an overview of the response of the banks to the 'no-frills' account initiative. The no frills account is a low margin high volume business. The banks restrict the nature and the number of transactions for these accounts. If managed well, it could become a profitable product.

Table 12.4: 'No-frills' Account Initiatives in India

Name of the Bank	Minimum Balance for 'no frills' account	Extra features
Allahabad Bank	Rs.5/-	Cheque book & ATM facilities (at Rs.250 per year)
UCO Bank	Rs.5/-	Cheque book & ATM facilities (at Rs.250 per year)
Deutsche Bank	Rs.500/-	Free quarterly consolidated account statement Free personalized payable-at-par cheque books 3.5% interest per annum.

Compiled from various sources

Microfinance

Financial services still remain inaccessible to more than a billion people across the world. More than 200 million of this population lives in India. Micro-finance enables the weaker sections of society to gain access to financial products and services. By getting access to these services, the poorer sections of society have a way of getting out of the clutches of poverty. Micro-finance generally focuses on poor women. The products marketed are generally term loans, which vary in terms of the tenure of the loan.

Micro-Finance Institutions (MFIs) and NGOs were the first to offer credit to the poor. The scenario has changed a lot and banks (local as well as foreign) are also catering to the financial requirements of the masses living below/near the poverty line. For instance, ABN Amro has a strong focus on micro-finance in India. It makes use of MFIs to distribute its products.

SMEs: The New Focus of Banks

What the banks were reluctant to do in the late 1990s is now turning out to be their prime focus. Bank marketers have begun to focus on Small and Medium Enterprises (SMEs). The role of SMEs in the global supply chain and the availability of third party ratings on the SMEs have led to bank marketers realizing the long-term potential of this segment. This is because of the greater reliability of assessing credit worthiness than earlier, and the government's push toward priority sector lending. Organizations like SMERA[7] provide rating on the creditworthiness of the SMEs. To harness the potential in the SME segment, banks have developed specific products for this segment. For instance, Andhra Bank offers the Laghu Udyami Credit Card (LUCC) and the Artisans Credit Card (ACC) Scheme. Table 12.5 gives an overview of these two credit cards.

Table 12.5: Special Credit Cards of Andhra bank

Card	Features		
	Purpose	**Eligibility**	**Loan limits**
Artisans Credit Card (ACC) Scheme	To provide for working capital and/or term loan requirements of artisans in the handicrafts, handlooms and other such sectors.	Artisan groups registered with the Development Commission (Handicrafts). Beneficiaries of other government schemes are not eligible.	Maximum limit of Rs. 200,000 in the case of groups.
Laghu Udyami Credit Card (LUCC)	Provision of credit to the SMEs.	Small business units, retail traders, artisans, village industries, self-employed professionals, tiny/ small scale or medium scale units.	Maximum limit of Rs 1 million.

Source: http://www.andhrabank-india.com/scripts/ArtisansCreditCardScheme.aspx; and http://www.andhrabank-india.com/scripts/ BLaghuUdhyamiCreditCardSME.aspx

Overseas Banking

The deregulation of the banking sector followed by the ease of restrictions in operating abroad has led to several Indian banks catering to customers outside India by setting up branches. To begin with, the target customers are mainly the Non Resident Indians (NRIs) and Indian expatriates living abroad. For instance, Andhra Bank made its first international foray by opening its office in Dubai in May 2006. It plans to set up offices in Kuwait, Qatar, Saudi Arabia, and Oman in an attempt to cover the Middle-East market. The objective of setting up of offices in these countries is to cash in on fees accrued through remittances from a large Indian working population.

Similarly, ICICI Bank, the leading private sector bank, has set up operations in Bahrain in response to the recent change in the Bahrain labor law regulations, which mandates transfer of salaries into salary accounts. This offshore banking unit of ICICI Bank is also engaged in the distribution of the other asset and liability products to NRI customers in Bahrain. ICICI Bank has also opened branches in other overseas locations like the US, the UK, Singapore, and Canada. It plans to promote corporate salary accounts through doorstep account opening or the direct banking model in various overseas locations.

International banking

In another approach to expanding their base and reach to a global population, Indian banks are relentlessly making efforts to acquire banks in foreign countries. This is international banking in the true sense (banking products for local citizens in different countries, and not just for NRIs). For example, State Bank of India has acquired IOIB (Indian Ocean International Bank), the fourth largest Mauritian Bank. This acquisition will strengthen SBI's operations in Mauritius.

Universal Banking

The concept of universal banking is fast catching up in India. Universal banking is akin to the phenomenon of supermarkets. Banks which have adopted this concept provide customers with the entire range of financial products, including those beyond the scope of traditional banking. This includes offering equity products, mutual funds, loans, insurance, pension products, etc., under one roof. This is in contrast to the earlier model where each marketer focused on a single area of operation -- commercial banks provided loans to corporate houses; development financial institutions such as ICICI, IDBI, and IFCI provided funds to companies for their capital expenditures; and HDFC was the leader in providing home loans.

Regulatory framework

A regulatory framework is being created to help the development of universal banking. The formulation of regulatory norms is done by the three apex regulatory bodies -- RBI (bank regulator), the Securities and Exchange Board of India (SEBI) (capital market regulator), and the Insurance Regulatory and Development Authority (IRDA) (insurance regulator). Table 12.6 gives an overview of specific provisions developed by the apex regulators to facilitate the progress of universal banking in India.

Table 12.6: Provisions for Universal Banking

Regulatory Body	Provision
The Reserve Bank of India (RBI)	Allows marginal investment by banks in equities.
The Securities and Exchange Board of India (SEBI)	The development financial institutions can convert themselves into banks by satisfying certain norms that are stipulated for banks, such as the statutory liquidity ratio and the cash reserve ratio.
The Insurance Regulatory and Development Authority (IRDA)	'Arms length relationship' between a bank and an insurance entity; that is, commercial banks can enter the insurance business by acting as agents or by entering into a joint venture with insurance companies.

Source: "India's Emerging Universal Banks: Size Does Matter." http://ibef.org/artdisplay.aspx?cat_id=461&art_id=5167, January 2005.

Electronic Fund Transfers & Clearing Services

Electronic fund transfer (EFT) was introduced by the RBI to facilitate easy transfer of funds across banks, for the benefit of customers. EFT involves the transfer of money electronically from one account to another. The accounts should be in branches that have EFT facility. There are no transaction limits on the transfers. This facility will be available without any processing charges till March 31, 2007, for unlimited individual transactions.[8]

Banks also offer electronic clearing services. There are two types of clearing -- debit clearing and credit clearing. The debit clearing mode of payment allows institutions to collect due payments from their customers. Examples include utility bills, credit card payment, insurance premium, etc. For example, LIC policyholders who have bank accounts in select cities can pay the premium as well as receive interest irrespective of the servicing LIC branch they belong to. Credit clearing is a simple and quick mode of payment. Many organizations use this facility to pay interest, dividend, salary, pensions, etc. It also eliminates cumbersome paperwork and is quite convenient for customers because money is directly credited to the account.

M-Commerce

Electronic transactions using mobile communication equipment is referred to as M-Commerce. The SMS (short messaging service) is extensively used by mobile users in India. Financial service marketers have begun to use this medium to communicate with customers and promote their products. A logical development of M-commerce in banking applications is the mobile banking trend. The mobile banking services provided by banks generally comprise verification of account balance and transaction details, ordering of cheque books, and movement of funds between accounts.

For instance, consider the mobile banking services launched by the Karur Vysya Bank (KVB). The savings and the current account customers of KVB can use the SMS facility to check account information such as balance, transaction statistics, and cheque status. Customers can also make a request for a cheque book, issue stop-payments on cheques, and enquire about term deposits. All these services are provided free of cost by the bank. As an introductory offer, KVB provided free SMS alerts for debit and credit card transactions for a limited period. These services were later charged at the rate of Re.1 per alert.

Code of Commitment from Banks

The Banking Codes and Standards Board of India (BCSBI), an autonomous body, was established with the objective of designing a code which would set minimum standards of service delivery, increase transparency, improve operating standards, and boost the confidence level of customers. It is voluntary for banks to join the body but member banks have to follow the code without fail. The adherence of members to the code is monitored by the directors of the BCSBI, who are members of the governing council. The way banks operate and market financial products will change significantly with the introduction of the code of commitment. Some of the components of the code are discussed here.[9]

Products and services: The BCSBI has drafted certain guidelines for the various financial products/services. They include:

No-frills accounts: The charges applicable for various services and products involved in a 'no-frills account' have to be provided in the form of a separate tariff schedule. Restrictions, if any, on the nature and the number of transactions should be made known at the time of opening the account.

Credit cards: Credit card transaction statements should be provided free of cost, either by postal mail or the Internet every month, in order to enable customers manage their credit card account.

Special accounts: Banks should make their best effort to serve special customers like senior citizens, physically challenged, and illiterate persons. This includes framing convenient policies and introducing appropriate products and services.

Remittances: In case of any delay in remittances, the bank should compensate for the loss or the additional expenses incurred by the customer, as per its compensation policy

Advertising: The advertisements should be clear and not mislead the audience. If any ad makes a reference to the interest rate, then the banks should indicate if any other fees or charges will apply and also provide full information upon request

Information: If any changes are made in terms of the fees and the charges, then these changes have to be intimated one month in advance before becoming effective.

Privacy and confidentiality: Information to the credit reference agencies has to be provided on the personal debts if the customer has due payments to be made, the amount owed is not in dispute, and if no satisfactory proposals are made by the customer for repayment after formal demands from the bank. The information provided to the credit reference agencies should be intimated in writing to the customer.

TRENDS IN INSURANCE MARKETING

The insurance sector has witnessed many changes since 2000. With privatization and with the government permitting up to 26% foreign direct investment (FDI) in the sector, the competition has increased. This has led to the insurance companies devising new ways to grow and expand the market for insurance products. Micro-insurance is one such offering from insurance marketers. Insurance for the poor is termed micro–insurance, similar to micro-finance. In addition, insurance marketers have begun to provide insurance to new sectors like film making. With films being accorded industry status, insurance companies have begun to provide insurance cover for films. Health insurance has shown impressive growth rates since the deregulation of the insurance industry. This segment now forms a major component of the non-life insurance business. The launch of women-specific policies is another notable development in the Indian insurance sector.

Micro-insurance

Micro-insurance helps provide insurance cover to the rural masses and economically weaker sections of society. It remains largely unregulated in many parts of the world. The IRDA, however, has made efforts to regulate the micro-insurance environment in India. The authority has amended the regulations for the micro-insurance sector. Now even NGOs (Non-Government Organizations) and SHGs (Self Help Groups) can function as agencies for life and general insurance companies. For micro-insurance, the minimum sum assured has been placed at Rs.10,000 (whereas the minimum sum assured for a regular life insurance policy is Rs. 20,000).

With a more supportive regulatory framework and the easing of norms, micro-insurance could become another major marketing opportunity for insurance companies. Foreign players too have shown interest in offering micro-insurance products. For example, Germany-based reinsurer, Munich Re plans to offer micro-insurance products in India, through the Munich Re Foundation.

Film Insurance

The Indian film industry is one of the largest in the world. On an average, around 800 films are made every year in the country. The film sector was given industry status only in 2000. This gave insurers an opportunity to target this segment. United India Assurance Company was the first to come out with an insurance policy titled 'Cine Mukta Policy'. This policy provides accident insurance cover for the cast and crew. It also covers loss due to natural calamities and theft during shooting. The film negatives are also insurable against any kind of damage. With the Indian film industry expected to post high growth rates and with corporate houses entering into film production, insurance marketers can hope to increase their volume of business from this sector.

Health Insurance

The demand for health insurance is on the rise in India. According to figures given by McKinsey & Co., the premium collected through health insurance would grow to 6.2 to 7.5% of the GDP by 2012, from 5.2% of the nation's GDP in 2005.[10] The growth in the healthcare segment is remarkable given the fact that the concept of healthcare databases, which would help insurance marketer's price policies more scientifically, is still not very developed in India.

The demand for health insurance has increased due to demographic changes as well as new product offerings. There is greater awareness of lifestyle-related diseases among the urban population. There is also an increase in the number of nuclear families, which are more vulnerable to financial emergencies than joint families.

At the same time, health insurance marketers have introduced new products and features such as cashless claim facility, where the third party administrator directly pays the bills for hospital expenses. The variety of health riders offered by insurance marketers also has increased the attractiveness of health insurance products. For instance, many insurance marketers offer customers the facility to pick and choose riders of their choice along with the basic policy and bundle them into a single product offering.

Exhibit 12.2 describes the importance of providing rider options in the health insurance segment as a differentiating strategy.

Exhibit 12.2

E-opinion Rider of Bajaj Allianz General Insurance

Bajaj Allianz, one of India's major players in the insurance segment, came up with a new rider — the e-opinion rider — in its health insurance policies. This rider offered the policyholder the benefit of seeking a second opinion on a health issue from a panel of doctors across the world. Bajaj Allianz offered this facility through a tie-up with WorldCare, a global health care services provider. WorldCare, in turn, tied up with reputed hospitals like the Cleveland Clinic, the Massachusetts General Hospital, and the Duke University Health System. The rider covered second opinions for about 12-13 critical illnesses. As of 2005, the premium to be paid for the rider was Rs. 525 for one year and Rs. 839 for two years.

If a policyholder developed a serious illness such as cancer or heart disease, Bajaj Allianz would forward the digitized and encrypted medical records of the policyholder to the WorldCare office in Cambridge, United States. In a matter of seven days, second opinions supplemented by diagnosis and a recommended treatment plan would be sent back.

Under this rider, the following restrictions were applicable for every policyholder:

- The number of opinions permissible for the same health condition: 2
- The number of opinions permissible in a year: 3
- The number of opinions permissible in the lifetime of the policyholder: 6

Source: Monga, Rachna "What do you think is wrong?" Businessworld. 28 November, 2005.

Insurance for Women

Insurance companies have realized the potential of targeting women with specific insurance products. The insurance policies for women provide fund assistance for education, marriage, sickness, etc., with guaranteed and loyalty additions during the tenure of the policy and after maturity. These policies provide coverage for certain illnesses that are specific to women, such as uterine cancer, breast cancer, and pregnancy-related complications. These policies are money back policies but the premium is similar to term plans. Table 12.7 gives an overview of two such policies.

Table 12.7: Insurance Policies for Women: Examples

Name of the Policy	Insurer	Features
Jeevan Bharati	LIC	An amount up to Rs. 200,000 can be availed of by the policyholder for medical treatment under additional cover. This amount is over and above the sum assured. In the case of children born with congenital problems, an additional 50% (up to a maximum of Rs. 100,000) of the sum assured can be availed of.
Birla Sun Life - the First Woman Plan	Birla Sun Life	This is a unit linked plan. Two withdrawals within a year are free. 20% of the sum assured is transferred to the holding account every five years, if required. A unique feature is the critical illness rider that covers illnesses specific to women.

Adapted from http://www.insuremagic.com/content/PlanInfo/Life/women_whoshould.asp

SUMMARY

The financial services segment has witnessed many trends in recent times and this chapter takes a comprehensive look at some of these trends. The technological changes in the financial services segment have been impressive. Though banking services are the major adopters of high-end technology, other financial services like insurance are also leveraging on technology for delighting customers and gaining a competitive edge.

Kiosks are used as a cost-effective tool for product communication, customer management, and brand building. Stored Value Cards (SVC), also called electronic purses, eliminate the need to carry hard cash. Digital security is a technological endeavor that enables safe and secure digital transactions and has gained legal acceptance. Digital certificates will soon gain prominence with increasing focus on e-governance, online trading, and online transactions. Business intelligence is a widely implemented decision making tool. It includes OLAP, data warehousing, and data mining. Business intelligence systems help the marketer to analyze information and take suitable decisions. Enterprise-wide IT solutions, such as Core Banking Solutions, have helped financial product marketers in streamlining their internal operations and delivering greater value to the customers.

The banking sector is going through a major transformation. Notable trends witnessed in the banking segment are bancasssurance, mutual banking, rural banking and technology inclusion, financial inclusion, increasing focus on Small and Medium Enterprises (SME), overseas and international banking, and universal banking. Micro-finance involves providing financial services to weaker sections of the society. Electronic Fund Transfer (EFT) and Electronic Clearance Service (ECS) schemes have been introduced by the Reserve Bank of India. EFT enables the quick transfer of funds on the same day or by the next day. ECS is used for both credit and debit clearing. M-commerce or mobile commerce is another emerging trend. Customers can send SMS messages to banks to get information. This service is available for viewing account balance and transaction details, requesting issue of new cheque books, etc. Banks can also opt for self-regulation, by voluntarily adopting a code of conduct that has been laid down by the Banking Codes and Standards Board of India (BCSBI),

Post-liberalization, the insurance industry has seen a lot of changes. Insurance marketers have introduced new products. Micro-insurance, film insurance, health insurance, and specific insurance products for women, are some emerging avenues for insurance marketers.

End Notes:

[1] Padmanabhan, Chitra. “Kiosk Market Comes of Age.” http://www.expresscomputeronline.com/20030421/indtrend1.shtml. April 21, 2003.

[2] “Report of the Working Group on Electronic Money.” http://www.rbi.org.in/scripts/PublicationReportDetails.aspx?FromDate=07/11/02&SECID=21&SUBSECID=0 July 11, 2002.

[3] “Bancassurance.” http://210.210.18.120/MLE2CandK/news/nl_july.asp. Newsletter. Vol.1 Issue 1, July 2005.

[4] Wyse is a reputed company in the field of network centric computing solutions. Its client base includes governments and companies across the globe. Its clients include Fortune 100 and Fortune 1000 companies like FedEx, Quaker Foods, CON-WAY Transportation, Best Buy (Canada), etc.

[5] Comat Technologies, headquartered in Bangalore, is an IT business solutions company, serving market verticals such as government, healthcare, and legal support services. It specializes in the domain of e-governance projects. Its mission is to improve the quality of life in rural areas with the help of IT.

[6] Thin client architecture refers to a computer architecture, where the client system does not have a hard disk drive. Data storage and data processing are done on the server side.

[7] Small and Medium Enterprises Rating Agency is a joint venture of SIDBI (Small Industries Development Bank of India), Dun & Bradstreet Information services, and CIBIL (Credit Information Bureau of India Limited). SMERA provides rating on the creditworthiness of small and medium enterprises.

[8] http://www.rbi.org.in/scripts/ECSUserView.aspx?Id=20

[9] http://bcsbi.org.in/images/Banks_Commitments_Customers.pdf

[10] "Health Insurance." www.ibef.org/attachdisplay. aspx?cat_id=95&art_id=2293. April 2004.

Chapter 13

The Global Scenario

In this chapter, we will discuss:

- Marketing Financial Products in the United States
- Marketing Financial Products in the United Kingdom
- Marketing Financial Products in China

The financial services industry across the globe has been transformed over the last few decades. A large part of this transformation has been witnessed in the segments of banking, insurance, mutual funds, and retirement products. The changes in the banking sector have revolved around adoption of technologies that help offer better customer experiences. The insurance segment has seen the introduction of new products, new pricing approaches and strategies, and segment-specific marketing approaches. Besides, a majority of mutual fund companies have started offering online trading facilities to their customers.

This chapter covers some of interesting aspects of financial product marketing practices across three continents, with specific reference to the US, the UK, and China. The following sections discuss the marketing of financial products, specifically banking, insurance, mutual funds, and pension products, in these countries.

MARKETING FINANCIAL PRODUCTS IN THE UNITED STATES

The marketing of financial products in the US has evolved over the years. Erstwhile banks are repositioning themselves as financial supermarkets. Credit card companies have innovated in terms of association/affinity marketing and differential pricing. Besides, the insurance segment uses ethnic marketing and worksite marketing strategies. On the other hand, mutual fund marketers have laid increasing focus on Internet-based advertisements to promote their products. The following sections describe these marketing approaches prevalent in the US.

Bank Marketing in the US

Banks in the US have focused on shifting their image from that of a traditional bank offering banking products, to that of a one-stop-shop where all kinds of financial products -- insurance, banking, mutual funds -- are offered to customers. Banks have also shown a preference for promoting fee-based services over the traditional banking products. These developments are discussed here, along with the innovations in credit card marketing.

Reduced usage of the terms ‘bank’ and ‘branch’

A new phenomenon being witnessed in the US banking sector is the decrease in the use of the terms ‘bank’ and ‘branch’. Many banking companies have removed the word ‘bank’ from the corporate name because they have begun to sell insurance and equity products also. For example, Harris Bank, based in Chicago, has removed the word ‘bank’ and is now known as just ‘Harris’. Similarly, the New York-based Citibank sells credit cards and mortgage products under the ‘Citi’ brand. It was believed that in the perception of prospective customers, the use of the word ‘bank’ would narrow down the range of products offered.

The term ‘branch’ is also on the way out. Banks are replacing it with the term ‘Stores’. This is believed to be more appropriate for the retail-oriented approach adopted by banks, in terms of people, process, and physical evidence. Commerce Bank, US Bank, and BankAtlantic are some of the prominent banks that have chosen this makeover.

Shift toward fee-based services

The banks in the US are making a transition by changing the composition of their revenue streams so that there is a greater portion of revenues coming from fee-based services. This is in contrast to their earlier dependence on fund-based products. Now, there is an increasing focus on asset management. For example, the Pittsburgh-based Mellon Financial Corporation (Mellon)[1] witnessed an increase in its revenues and market capitalization, after it began to focus more on fee-based services. The non-interest income/operating revenues were 47.34 percent of the total revenues in 1993; this share nearly doubled to 89.42 percent by 2005[2].

Association/Affinity marketing

Approximately 90 percent of Americans belong to one association or the other, either on the professional front or on the personal front[3]. Financial marketers have used such associations as a target base for marketing financial products. To be successful in this approach, a marketer needs to gain knowledge on certain aspects like societal trends, voting patterns, member behavior, civic participation, etc.

The use of this marketing approach has yielded good results. Branded affinity cards are the best example to highlight the success of association marketing. For instance, the response rate for the association cards of Visa USA[4] was in the range of 3-8 percent, well above the meager response rate of 1-2 percent for its standard credit card offers. The purchase of association cards has shown a phenomenal increase from 20.8 million in 1990 to more than 250 million in 2002.

In addition to credit card marketers, insurance marketers are also adopting the association marketing approach. For instance, Hartford[5] expected to derive around 20 percent of its premium by the year 2010 through association marketing[6].

Credit card pricing

The pricing of credit cards has undergone significant changes in the last two decades in the US. Different marketers have been using different pricing approaches; however, the pricing has, in general, declined with increasing competition.

In the 1980s and 1990s, credit card marketers charged high interest rates and a fixed amount as annual fee. However, they did not collect over-limit fees or late fees; even when they did collect late fees, the amount was miniscule. In the mid-1990s, with the competition for new members increasing, most credit card companies did away with annual fees. Currently, annual fee is almost non-existent for premium credit cards unless they are associated with some kind of reward program. Credit card marketers have replaced annual fees with two other types of fees – convenience/service fees and risk-based fee. In some cases, the computational methodology has also been changed to increase the profitability of the marketer, without any apparent increase in the price.

Convenience/ Service fees: Card issuers charge separate fees for any additional service that they provide to the customers. Some examples are cash advance fee, minimum finance charge, stop payment fee, additional credit card fee (for extra cards), phone/Internet payment fee, person-to-person money transfer fee, statement or sales slip photocopy fee, balance transfer fee, and foreign currency conversion fee.

Risk-based fee: Till the 1990s, the credit card pricing was dependent on the nominal annual percentage rate (APR) of interest. A common pricing, irrespective of the varying risk profiles of the customers, was prevalent. (The risk was assessed for prospective customers and checked against a pre-determined risk threshold level. If the risk behavior exhibited was above the threshold level, the customer was denied the credit card). This approach of undifferentiated pricing changed with the increase in price sensitivity among consumers and increase in competition.

Modeling and analysis show that credit card customers who score high on late fees, over-limit fees, and bounced check fees show a higher probability of default. To compensate for the costs of these increased risks, the concept of risk-based fee was introduced. Risk-based fee generates a considerable amount of revenue. To some extent, this fee income compensates for the revenues lost by marketers as a result of removal of the annual fee and lowered value of APR for low-risk cardholders.

Over the years, credit card marketers in the US have developed many variants of APRs and all of these are linked to the risk profile of the customer. The two risk-based APR approaches commonly used by credit card marketers in the US are the risk-based solicitation APRs and the risk-based penalty APRs.

- **Risk-based solicitation APRs:** Customers with lower risk profiles are offered rate discounts while consumers who have high unpaid credit debt are issued credit cards with the highest fees. The interest rates are also higher for such customers. This approach enabled the credit card marketers to issue credit cards with different pricing levels to different segments like immigrants, those without any previous credit experience, etc.
- **Risk-based penalty APRs:** Though the risk-based solicitation APRs help marketers, the pricing approach does not take into consideration the fact that the risk profiles of customers change across different stages of life. To overcome this limitation, risk-based penalty APRs have been introduced, wherein the marketer has the flexibility to modify the charges even after the credit card has been issued. Charges could be increased or decreased depending on the level of risk in terms of promptness in payments, increase in debt, etc.

Changes in computation methodology: Apart from the adoption of risk-based pricing and the inclusion of convenience/service fees, credit card marketers have also incorporated changes in the computational practices without affecting the nominal APRs. For instance, by 1997, credit card companies in the US had replaced monthly compounding with daily compounding. There was a change in the calculation procedure for the daily average outstanding balance. In the new method, the marketer took into consideration the starting balance of the day, transaction fees and any finance charge on the earlier day's balance, subtractions of any credits or payments, etc. By adding the finance charge to each day's balance, the credit card issuer was able to increase the finance charge revenues without increasing the APR. For example, the portfolio yield on a loan with an APR of 18.9 percent when interest is compounded monthly (12 times a year) is 20.73 percent; when the interest for the same loan is compounded daily (365 times a year), the return is 20.91 percent.

Insurance Marketing in the US

The marketing of insurance in the US, especially life insurance, has also seen a change. Segmentation of the target audience has gained in importance. Marketers have started focusing on products that target specific groups. For instance, life insurance companies are segmenting the population on the basis of ethnicity, and launching insurance products to suit different ethnic groups. Also, most Americans have shown a tendency to purchase financial products -- including insurance -- at the workplace. Worksite marketing is, therefore, adopted more often as a promotional technique.

Ethnic marketing

Although ethnic marketing was prevalent in many industries like cosmetics in the US, financial product marketers were slow to adopt this approach. Now, many financial institutions in the US have created separate marketing units to cater to the requirements of different ethnic groups. The objective of these units is to scout for new prospects using localized marketing campaigns. For instance, MasterCard International developed special TV campaigns in Spanish to target the Hispanic community. Similarly, Washington Mutual[7] has commercials in Spanish, Vietnamese, and French. Apart from the language used, the messages are customized on the basis of lifestyle, preferences, etc., of the different ethnic groups.

Worksite marketing

Worksite marketing of insurance products has become popular in the US. This involves insurance marketers targeting specific organizations to sell insurance products. Americans have shown an increased level of interest in purchasing insurance products as well as other financial products at the workplace. This may be largely due to the convenience that it brings. Premiums can be paid through salary deductions. Besides, employees have the advantage of consulting colleagues and making an informed choice. Table 13.1 lists the proportion of insurance products sold at the workplace (in the US), for the year 2004. Worksite marketing has helped insurance marketers reap rich dividends as the traditional agents tended to focus on either mass markets or niche markets (high net worth individuals) and ignore the salaried class.

Table 13.1: Workplace Sales of Insurance Products in the US: 2004

Products	Proportion of the products sold at the workplace
Disability insurance	23%
Life insurance	24%
Accident insurance	15%
Dental insurance	10%
Health insurance	12%
Long Term Care	1%
Others	3%

Adapted from Lowerre, Gill and Bonnie Brazzell "The Worksite Market Keeps on Growing." <u>National Underwriter.</u> *September 26, 2005.*

Role of independent agents in insurance marketing

With various channels of distribution being increasingly used, the emphasis on independent agents, who were the major distribution channel for insurance products earlier, went down. In an attempt to regain their importance and establish a distinct brand identity, the independent agents themselves began to undertake promotional campaigns

The Independent Insurance Agents of America (IIABA), an association of independent insurance agents and brokers, created a new brand identity for themselves through their branding initiative that began in 2001. Trusted Choice^{SM} is the branding initiative designed to educate consumers on the value of having independent agents on their side in the insurance transaction. The campaign was titled 'Trusted Choice^{SM}' and the message strategy revolved around three components -- choice, advocacy, and customization.

The campaign made nationwide use of television, radio, and outdoor advertising. This was followed by tailor-made local ad campaigns for agents to broadcast in their respective community radio stations. The national ad campaign for Trusted Choice^{SM}, involved television commercials appearing on the nation's prominent cable news channels: CNN, MSNBC, FOX News Channel, and CNBC. The campaign targeted professionals aged 35 years and above. Three different commercials were aired: one featuring automobile insurance, one for homeowners' insurance, and another for business insurance. The outdoor campaign had large billboards with the statement 'TrustedChoice – A smart way to buy insurance.' It was followed by the website address, trustedchoice.com.

This kind of campaign was necessary because the consumers felt that insurance transactions were complex. Further, there was a general feeling of mistrust toward insurance companies and their agents. The campaign improved the image of independent agents and revived their importance, so that customers could look at them as trusted partners who provided valuable guidance, and also simplify insurance transactions. The amount of business done through independent agents also improved after this campaign was launched.

Marketing of Pension Plans and Mutual Funds in the US

The retirement products market and the mutual fund (MF) industry in the US are considered to be highly evolved. Many countries study the US pension system to build a new pension system or undertake reforms in their existing systems.

Pension plans

The US pension system consists of three components -- compulsory federal plan (public pension plan), employer financed pension schemes, and individual retirement accounts. About 95 percent of the working population is covered under the compulsory federal plan. The average pension paid under this plan to the beneficiaries is approximately US$ 930 per month. Employer financed pension schemes cover about 50 percent of the working population in the US. About 20 percent of the working population opts for individual retirement accounts.

Mutual funds

About 72 percent of the people purchasing mutual funds in the US use the online trading option. Therefore, mutual fund marketers make extensive use of the Internet to advertise. In the US, websites like AOL (America Online) present well-researched financial details on a wide variety of funds. They also provide the performance statistics of the funds. More than 10 million customers use the facility of online asset management[8].

MARKETING FINANCIAL PRODUCTS IN THE UNITED KINGDOM

Like in the US, the marketing of financial products in the UK has also witnessed changes across the banking, insurance, and mutual fund segments. The banking segment has seen technological changes focusing on improving the level of service delivered at the bank branches. Bank marketers have made use of technology to understand customer behavior and offer customized services. The concept of preferred lives (discussed later) has become common for major life insurance companies in Europe. The life insurance segment has seen the inclusion of lifestyle-linked obesity as one of the factors in pricing. The IFAs (Independent Financial Advisors) have become the prominent channel of distribution of life insurance and pension products. The phenomenon of fund supermarkets is picking up in the UK, as an intermediary in the marketing of mutual fund products. The following sections describe some of the significant developments in marketing financial products in the UK.

Bank Marketing in the UK

The banking sector in the UK has shown an inclination to go in for new technology adoption and new product development. Branch-based banking has got a new look with the banks adopting technology to monitor customer behavior at the banks. Credit card marketers have launched new products for different customer segments. These aspects are discussed here.

Technology and customer behavior at the banks

Technological advancements have made banking operations easier. Bank branches have adopted advanced technology to monitor customer behavior. This is crucial as the service level offered by the bank at the branches has a direct effect on the level of customer loyalty. The radio frequency identification (RFID) technology has gained momentum in the recent years. The RFID chips are embedded in credit cards or loyalty cards. This helps the bank track the movement of customers within the bank from the time of entry to the time of exit. For instance, a customer walks into a bank and looks for details on car insurance. The moment he/she picks up a brochure on car insurance products, the information is aired on a plasma screen and the concerned staff is immediately alerted. Some banks, such as the Halifax Bank of Scotland (HBOS)[9], have used specialized cameras to monitor the behavior of customers under different situations like when standing in long queues, etc.

Insurance Marketing in the UK

Owing to the increasing awareness of the health implications of obesity and the understanding of lifestyle as an important determinant of obesity, insurance marketers in the UK consider lifestyle-induced obesity as a factor in the pricing of life insurance policies. On the promotion-cum-distribution front, life insurance marketers in the UK are relying more on using IFAs (Independent Financial Advisors). The IFAs are regarded as the most significant distribution channels, even more significant than the direct sales force. This is in contrast to the US, where other channels of distribution have gained prominence.

Lifestyle-linked obesity and life insurance pricing

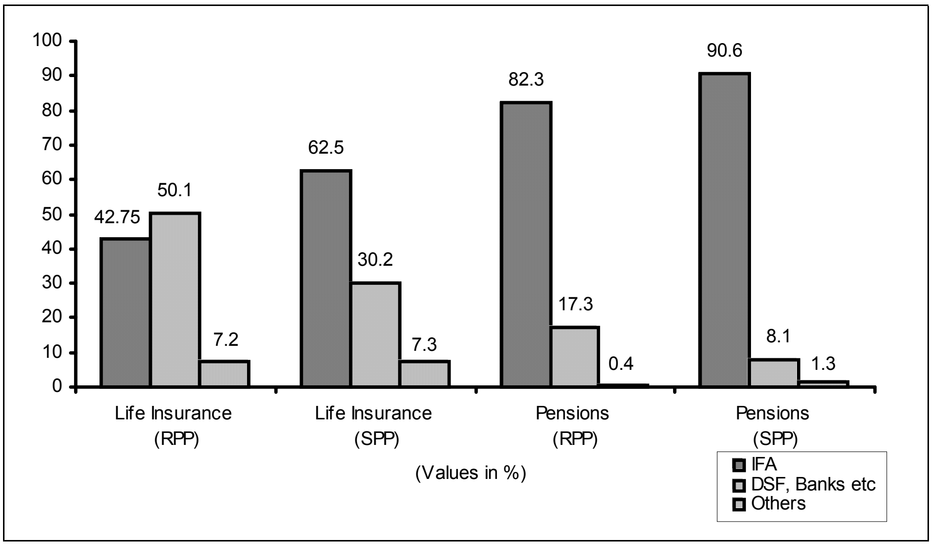
Traditionally, premiums were calculated on the basis of age and sex. However, it was felt that some people (in a particular age group) exhibit lower levels of risk than others and therefore, for the sake of equity, should be charged lower premiums. For example, non-smokers were a low risk group when compared to smokers. Swiss Re[10] took obesity into consideration when determining the premium. The current Body Mass Index (based on height and the weight) was assessed to determine whether the customer was overweight or obese. This led to the concept of ‘preferred lives’. The preferred lives concept was used as a criterion for deciding on premium rates for life insurance products. Separate premium rates were decided for preferred and residual lives of the same age. The preferred group was expected to exhibit, on an average, lower mortality than the residual group. Now, insurance marketers have begun to use lifestyle-linked obesity as a predictive tool for risk assessment. The propensity to become obese in the later stages of life is related to current lifestyle and is thus considered to be an important factor when determining premiums.

However, in the UK, the concept of preferred lives did not meet with the desired success as in the US. One of the reasons for the less than satisfactory performance of preferred lives was that the term insurance rates were already very low in the 1990s, due to severe competition. Also the underwriting process became more time consuming with an increased number of medical checks, blood sample tests, etc. Besides, the agents were hesitant to classify some customers outside the preferred lives bracket.

IFAs as the prominent channel of distribution

In the UK, life insurance and pension products form a major portion of the personal financial assets of the population. Prior to the 1990s, the direct sales force was the most preferred channel of distribution. With the introduction of polarization rules[11] in 1988, the distribution pattern underwent a change. Insurance companies began to outsource their sales activities. This led to the emergence of the IFAs (Independent Financial Advisors). Now, the IFAs account for a major share of distribution with respect to life insurance and pension products. The IFA channel is also used for other products like unit trusts[12] and OEICs[13]. Figure 13.1 highlights the dominance of IFAs as the most preferred distribution channel in the UK.

Figure 13.1: Distribution Channels for Life Insurance and Pensions in the UK



Note: RPP and SPP denote regular premium payment and single premium payment respectively.

Source: Zeniya, Kayori "Dynamism in Reforming Financial Product Distribution in the United Kingdom" NRI papers No.95 September 01, 2005 and http://www.nri.co.jp/english/opinion/papers/2005/pdf/np200595.pdf

The emphasis placed by the life insurance companies on the IFAs is increasing. The insurance marketers have dedicated personnel who interact and liaise with the IFAs. For instance, consider Norwich Union[14], one of the largest life insurance companies in the UK. It has 16 representative offices across the nation and each office is staffed by about 25 personnel. These personnel do not engage in any kind of sales activity but only liaise with the IFAs. In contrast, it has only four offices for the direct sales force personnel.

Marketing of Mutual Funds in the UK

The mutual funds market in the UK has shown a remarkable improvement in terms of the services provided to customers. The emergence of fund supermarkets is the most significant change.

Fund supermarkets

The concept of fund supermarkets is mature in the US and is slowly gaining momentum in the UK. Fund supermarkets are brokerage firms that provide access to different mutual fund products under different fund families. They are similar to grocery supermarkets. In grocery supermarkets, the customers can buy a host of products of various producers at one common place. Similarly, in the fund supermarkets, a brokerage firm is the common place of purchase, the investors are the customers, and the mutual fund companies are the producers. The main benefit of fund supermarkets is the ease in operations. Investors have an option to invest in funds of different companies and get the information related to all the transactions in a single report. For example, a fund company may charge an initial fee[15] of around 5.5 percent of the investment amount, whereas a fund supermarket could charge as low as 4 percent as costs are distributed due to the large portfolio of products handled. Interactive Investor[16] and Cofunds are two well-known fund supermarkets in the UK.

MARKETING FINANCIAL PRODUCTS IN CHINA

The financial services industry in China is gradually evolving. The banking industry has begun to increasingly focus on the retail segment. Since local Chinese banks do not have the experience and expertise in retail banking, foreign banks have entered China in a big way. Many foreign banks are also investing in Chinese banks. The insurance sector has grown rapidly in the recent years. Similarly, the mutual fund industry has witnessed a transformation after the Chinese government permitted the commercial banks to enter this segment in 2005.

The Banking Sector in China

The Chinese banking sector is undergoing major reforms. The foreign banks were promised step-by-step access to the Chinese banking market and complete removal of the restrictions by December 2006 (as per the WTO agreement in December 2001)[17]. Though some problems like regulatory environment and the lack of skilled workforce hinder the growth of foreign banks, they are confident of cashing in on the opportunity. Retail banking in particular is going to be the focus of the foreign banks. The Chinese consumer credit market is also quite attractive for foreign players and they have already made their presence felt.

Investment by foreign banks in the Chinese banking system

Bank of America, Temasek Holdings, Royal Bank of Scotland (RBS), Standard Chartered, ING, and HSBC are some of the foreign banks that have made strategic investments in Chinese banks, such as Bank of Communications, Bank of Beijing, Bo Hai Bank, and Bank of China. The total value of these investments is over US$ 1.2 billion. Issues that could hinder the flow of such investments include poor corporate governance in Chinese banks, inefficient capacity to manage risk, and the evolving regulatory system. Foreign banks see a huge potential in the form of fee-based banking services in the near future. It is estimated that fee-based banking services would grow at the rate of 30 percent a year, from 2006 to 2013[18].

Vehicle financing

In China, vehicle financing services have received a lot of attention in the recent years. The demand for vehicle financing has been fuelled by the sales growth in the automobile sector. With the Chinese government's decision to relax the regulations for foreign auto manufacturers to set up operations in the country, many auto majors from across the world have lined up to set up shop in China. As of 2004, the Bank of China had given car loans amounting to around US$ 5 billion.[19] PSA Peugeot Citroen, a French auto major, planned to enter into a joint venture with the Bank of China (BOC) for vehicle financing.

Competition in the Chinese credit card market

The credit card industry in China is the next big thing for foreign players. The Chinese consumer credit market (credit cards, mortgages, and personal loans) is considered to be a hugely profitable segment. The share of the banking sector's profits from consumer credit business is expected to increase from a mere 4 percent in the year 2005, to 14 percent in the year 2013[20]. The foreign banks are eager to exploit this profitable segment.

Though the attractiveness of the market justifies the entry of foreign players, they will have to overcome a few challenges before they can benefit from the growth. The challenges are in the form of a large percentage of unprofitable customers, downward movement of fees, and the larger distribution network of domestic banks. Studies show that more than 85 percent of the credit card holder population pays the entire bill each month. Only about 2 percent of them frequently pay less that the total outstanding amount, thus making use of the revolving credit facility. (Usage of the revolving credit facility increases the bank's profits from credit card customers). Also, there is increasing pressure on the foreign players to lower the fees in an already low fee operating environment[21]. In addition, the foreign players need to acquire skilled employees in the areas of risk management, marketing, and product development.

The Insurance Sector in China

The CIRC (China Insurance Regulatory Commission) is the regulatory body of the insurance sector in China. The insurance market in China has witnessed an increase in the life insurance products that have a single premium. Single premium products, with a term of 5 years, are believed to have the highest potential in future. Also, there is an increased emphasis on bancassurance as a channel for life insurance products.

In the property and casualty insurance segment, there is increased competition with the entry of foreign players. Three major local players viz., PICC (People's Insurance Company of China) (in property and casualty)[22], China PiingAn Property Insurance[23], and China Pacific Property Insurance (in casualty)[24] are expected to lose their dominance with the advent of new entrants. The aggregate market share of the three players fell from 89.3 percent in 2003 to 79.9 percent in 2004.

Marketing of Mutual Funds in China

In 2005, the Central Bank of China permitted commercial banks in China to venture into the mutual fund market. This was expected to help the comercial banks to invest in less risky market instruments and bonds. The entry of commercial banks into the mutual fund business marked (?) an end to the 10-year ban, which had prevented them from investing in stocks. The domestic insurance companies, pension firms, and the foreign fund management firms were encouraged to increase their stake in the mutual funds set up by banks. The estimated size of the mutual fund assets in China is 300 billion yuan, as of 2005. There were about 40 mutual fund companies operating in China, with total assets worth 379 billion yuan[25]. The largest fund management house is the China Southern Fund Management with assets worth over RMB 36 billion[26] under management, at the end of 2004.

SUMMARY

This chapter covers financial products marketing across three different continents with specific focus on the US, the UK, and China. The section on marketing of financial products in the US focuses on banking, insurance, and credit cards. The banking system in the US has undergone a transformation over the years. The universal banking concept has matured. Some of the banks have done away with the terms 'Bank' and 'Branch' and expanded their business into other financial services. Many banks in the US are making a shift from a reliance on fund-based products to fee-based services. Pricing of credit cards has also evolved over the years with changes in pricing policies (based on risk) and computational methods. Ethnic groups in the US form a major customer segment for insurance marketers. The marketers have tailored the communication patterns to appeal to these groups and this approach has paid rich dividends. The trend of worksite marketing has also shown tremendous growth, especially for insurance products. Most financial products in the future will continue to be marketed through this channel. Among the three broad categories of pension plans, only about 20 percent of the workforce opts for individual retirement accounts. Mutual fund marketers make extensive use of online advertising.

In the UK, the banking sector has adopted technologies (such as RFID) to monitor/ understand customer behavior. This would alert staff to the customer needs and also help devise methods to improve delivery of services. In life insurance pricing, lifestyle-linked obesity risk has begun to play a major role in premium determination. However, the preferred lives concept has not been very successful due to operational difficulties. The IFAs (Independent Financial Advisors) have gained prominence as a new channel of distribution for a majority of financial products like life insurance, pension, and mutual funds. The emergence of fund supermarkets is a recent development in the UK. These are like grocery stores where a wide variety of funds are available for the customers at one place. The fees levied are lower compared to dealing directly with a fund house due to the large number of mutual fund products that the fund house sells.

The Chinese financial services industry is a major target destination for global financial players. The magnitude of foreign investments in the Chinese banking sector is huge, especially in retail banking and vehicle financing. The consumer credit market, which includes credit cards, loans, and mortgages, is another attractive segment for global players. The mutual funds sector is undergoing a major change with commercial banks being allowed to deal with mutual funds.

End Notes:

1 A global financial services company headquartered in Pittsburgh, Pennsylvania with approximately $5.5 trillion in assets under management, administration or custody.

2 Streeter, Bill. "Why fee-based banks look so good." ABA Banking Journal. May 2006, Vol. 98, Issue 5.

3 Smagalla, David, "Tapping into Association Marketing." MIT Sloan Management Review. Vol.44, Issue 4, Summer 2003.

4 In the year 1958, three variants – blue, white and gold BankAmericard – were launched by Bank of America in California. An association by name National Bank Americard was formed in 1970. It represented the US banks issuing Bank Americards. The international licensees of Bank of America created an International company called IBANCO in 1974. In 1976, IBANCO became Visa International and National Bank Americard Inc. became Visa USA.

5 Hartford is a leading property casualty insurance company.

6 Smagalla, David, "Tapping Into Association Marketing." MIT Sloan Management Review. Vol.44, Issue 4, Summer 2003.

7 Washington Mutual conducts its business across four broad areas -- retail banking and financial services, home loans, commercial banking, and the card services.

8 "Global Scenario." http://www.indiainfoline.com/mufu/ch09.html 15 December, 2005.

9 The successful merger of Halifax and Bank of Scotland in 2001 created HBOS - Halifax Bank of Scotland. It is the largest mortgage and savings service provider in the United Kingdom and a leading player in the new current accounts and the credit cards market.

[10] Swiss Re is a Switzerland-based reinsurer. Founded in 1863, Swiss Re provides reinsurance products and financial services to its clients across the globe.

[11] Under this rule, a firm would have to choose between selling the investment products of a single company or acting as a genuinely independent broker who scans the market for the best possible investment product.

[12] It is a pool of money collected from small savers and is used to buy shares. This is an effective way to reduce the risk faced by the customers, as the professional fund manager ensures that the money goes into well-balanced spread of investments.

[13] OEIC, pronounced 'Oik', is short for Open Ended Investment Company. It has replaced the Units Trust as UK's most widely held mutual fund.

[14] It is an Aviva company. It is the world's sixth largest insurance company (based on gross worldwide premium) and it is the biggest in the United Kingdom. It markets life insurance and pension products in Europe and primarily deals with long term savings, fund management and general insurance.

[15] When a Unit trust is bought, about 5 percent of the price goes in to the charges. This is to pay for the administration and commission to the unit trust company.

[16] It is one of UK's leading online financial services providers. It offers independent and transparent tools and information to enable its 1.6 million registered users to solve all their financial needs.

[17] Hope, Nicholas and Fred Hu. "Can Foreign Entry Transform China's Banking System?" Policy Brief. November, 2005.

[18] "Foreign Banks Eye Retail Banking Sector." http://www.chinadaily.com.cn/english/doc/2005-11/25/content_498013.htm.

[19] "Asia and Australasia." Economic Intelligence Unit. December 2005.

[20] Emloh, David von and Yi Wang "Competing for China's Credit Card Market." The McKinsey Quarterly. November 2005.

[21] The interchange fees in China averages between 0.7 - 0.8 percent of the spending, when compared to the 1 to 1.5 percent in other international markets.

[22] PICC Property and Casualty Ltd is a joint stock company with limited liability. It accounted for about 70 percent of China's P&C market for the year 2002.

[23] Ping An insurance group is the holding company of both the Ping An Life Insurance Company of China, Ltd and Ping An Property & Casualty Insurance Company of China Ltd.

[24] China Pacific Property Insurance Company, Ltd (CPIC Property) was formed in the year 2001 in Shanghai and is held by the CPIC group. This company engages in RMB-foreign currency denominated property, short term health and personal accident business.

[25] "China Mutual Funds Era Opens for Banks" The Standard. February 21, 2005.

[26] RMB is the acronym for the Chinese word 'renminbi'. The renminbi (literally people's currency) or the yuan is the official currency in the mainland of the People's Republic of China (PRC).

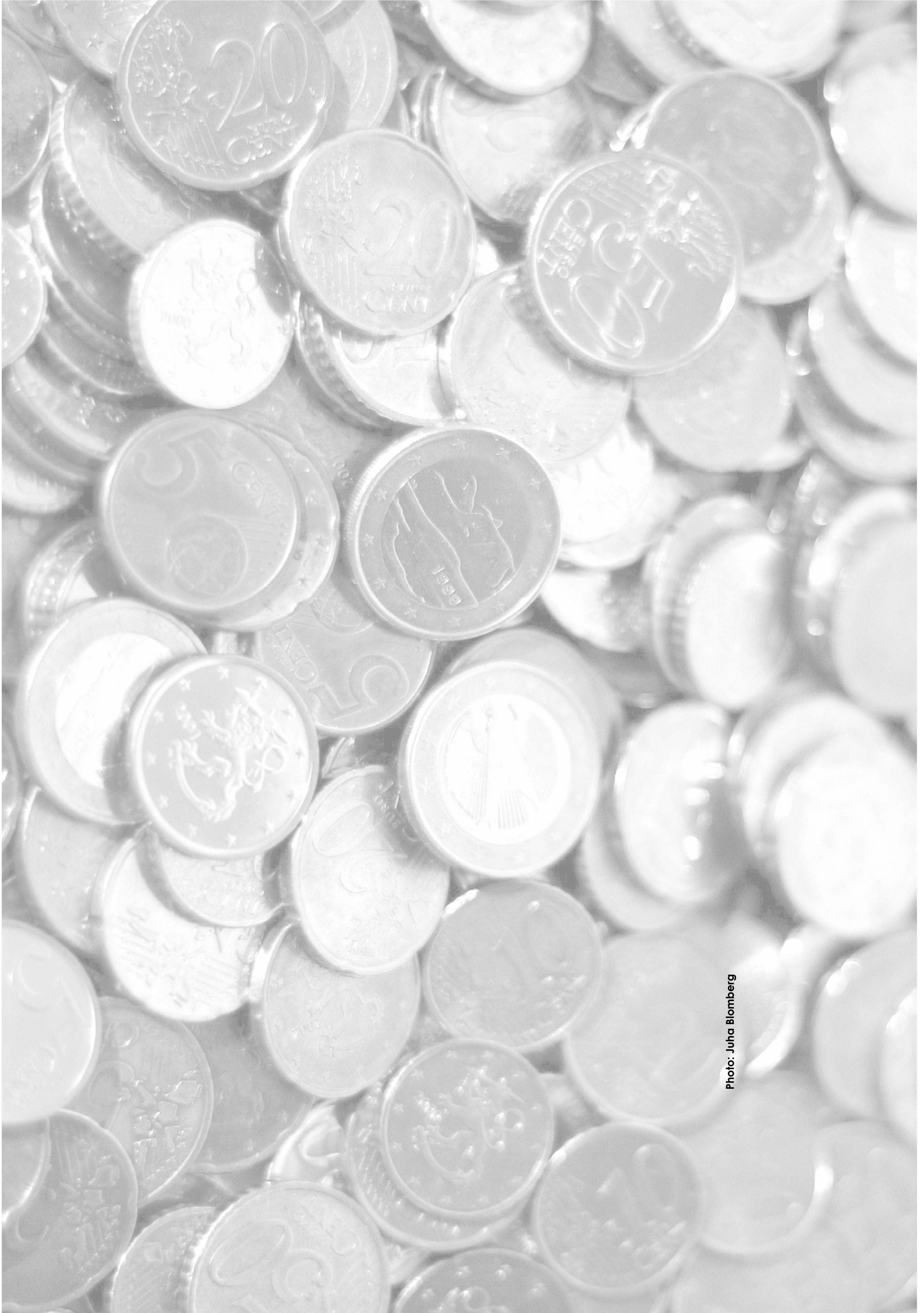


Photo: Juha Blomberg

Glossary

A

Advertising appeal: It is the manner in which a message is developed and expressed in anticipation of a specific customer response.

Affirmative loyalty: It is characterized by trust, commitment, and a long-term relationship between the customer and the marketer. It develops when the marketer sincerely implements trust building measures and provides superior customer care.

Analytical CRM: They help the back office employees and the management in analyzing the customer information collected using operational CRM tools.

Annual percentage rate (APR): It states the interest rate that a consumer has to pay in the event of the credit balance being carried over, a cash advance being taken, or transfer of a balance from another card being done.

B

Baggage insurance: The policy provides for cover against loss or damage to accompanied personal baggage due to fire, riot and strike, terrorist activity, or theft or accident during the course of the journey including stoppages en route anywhere in India.

Bancassurance: A form of distribution where banks sell the insurance products of an insurance company through their branch network.

Bill discounting: It is the process of providing advance against a bill – which can be a promissory note, bill of exchange, credit bills, etc. – to the clients such that the clients can meet their short-term financial needs.

C

Cash back schemes: In this method of promotion, the card user gets a discount on purchases made through the credit card. The marketer stipulates a minimum purchase limit and in some cases makes the offer exclusive to the purchase of a particular good or service.

Cash Reserve Ratio: CRR is the percentage of a bank's total deposits that it has to deposit with the RBI. The RBI can increase or decrease the CRR to manage liquidity.

Class rating: This is the most common type of insurance rating in the insurance sector. The classification of risks is based on a set of common parameters. Risk under the same class is standard.

Close-ended funds: They are characterized by constant capitalization, which means the initial total capital of the fund, available for the purpose of investment, cannot exceed a certain limit. The subscription amount is accepted from investors only during a particular period at the time of the launch of a scheme.

Co-branding: A process by which an existing brand (product or service) partners with another well established brand, for mutual benefit.

Competitive intelligence: It refers to gathering, storing, and analyzing information about competitors in the market. Competitive intelligence is used in decision making and for developing marketing strategies and tactics.

Covert pricing: It refers to costs, which are not explicitly charged to the customers against the product consumed.

Cross-selling (through partners): It is an extended form of the distribution process. It involves a tie-up with an external organization to sell the company's products. Cross-selling attempts to make use of the strength of the partner's channel.

Cross-selling (to banking customers): It refers to selling additional products of the bank to the existing customers. The bank uses its entire portfolio to match the requirements of the customer and sell the product that best suits those requirements.

Custodial services: It provides for the safe custody of the shares and debentures in physical form (certificates) and/or in dematerialized form (demat form). Any service provider who does this function is termed as a custodian.

Customer grading: It is the process of evaluating and defining the customer's worth and assigning a grade or score to individual customers to reflect their worth from the marketer's perspective. Grading helps in identifying the high net-worth individuals and targeting the marketing activities around this segment.

Customer relationship management (CRM): It involves all activities that help identify, establish, maintain, enhance, and, when necessary, also terminate relationships with customers and stakeholders, at a profit, so that the objective of both parties are met.

Customer switching: It occurs when an existing customer defects and becomes a customer of a competing marketer. Customer switching results in erosion of market share and reduced profits.

D

Data mining: It is used to identify and retrieve useful information from the huge volumes of data present in a data warehouse. The data mining tool recognizes patterns in the available data and provides support for decision making.

Direct Selling Agents: DSAs are agencies (intermediaries) involved in selling financial products on behalf of the financial product marketer. Any financial products marketer can enter into a mutual agreement with the DSAs to sell their products.

Direct-response advertising: It is a variant of direct mail where a product is first advertised without the full details being given. Interested customers are requested to contact the financial marketer for more information.

E

Electronic Fund Transfer (EFT): It uses an electronic medium to transfer funds from one bank to another. Unlike the traditional modes of fund transfer (like demand draft, cheques, telegraphic transfer, or mail transfer), EFT can be used to transfer the funds between two bank branches within the same day.

Electronic Funds Transfer at Point of Sale (EFTPOS): It enables the customer to carry out cashless transactions at merchant establishments, where the invoice amount of the goods purchased by the customer is debited from the customer's account and transferred to the merchant's account.

Emotional appeal: It portrays human feelings so as to evoke a favorable response from the target consumers. These appeals highlight the social or psychological needs that the product aims to satisfy.

Entry load: The amount charged by the fund house while selling the units to the investor.

Ethnic marketing: Financial marketers create separate marketing units to cater to the requirements of different ethnic groups. The objective of these units is to scout for new prospects using localized marketing campaigns.

Exit load: The amount charged by the fund house while repurchasing/redeeming the units from the investors.

F

Factoring: It involves converting invoice credit bills (receivables) into cash. It is the process by which a factor (a special firm) purchases the invoice credit bills from its client, discounts the invoice, and pays the remaining amount to the client.

Fidelity insurance: Fidelity insurance covers against financial losses caused by acts of infidelity like forgery, embezzlement, larceny, misappropriation, and default of the insured's employees.

Fiduciary responsibility: It is the marketer's responsibility to manage the customers' funds and provide financial advice so that customers achieve their financial goals.

Financial supermarkets: All types of financial products are made available under one roof by the financial marketer.

Forfaiting: It is the process of purchase of credit instruments such as credit bills from an exporter drawn on an importer in another country.

Fragmented market: This is a market where marketers have many opportunities to differentiate themselves from other players but these opportunities are small.

Fund supermarket: It offers a wide portfolio of fund schemes from different mutual fund companies for the investors to choose from. Fund supermarkets do not provide expert advice to the investors, but assist them by providing inputs for decision making.

G

Group Superannuation schemes: These pension schemes are instituted by employers in the interests of the employees. Contributions can be made by only the employer or by both the employer and the employee.

Growth funds: The basic investment objective of growth funds is to provide capital gains to the investors, that is, to provide high returns on the money invested. Basically, growth funds are invested in fast growing equity stocks in the stock market.

H

Heterogeneity: There is variability in service delivery from one service encounter to another.

House-of-brands or product branding strategy: The marketer chooses different names for each new product launched (without the organization's name).

Hull insurance: The policy covers loss/damage to the property insured due to a fire or an explosion, stranding, sinking in sea; overturning, derailment (of land conveyance); collision; etc. This insurance is applicable to loss or damage to ships, tankers, bulk carriers, smaller vessels, fishing boats, and sailing vessels.

I

Idea screening stage: Idea screening helps to check the feasibility of the idea and to decide if it can achieve the set business objectives in the new product development process.

Income funds: The basic investment objective of income funds is to provide a regular income to the investors. Income funds are typically invested in fixed income securities like bonds and debentures.

Industrial insurance: An industrial insurance policy insures the movable and/or immovable property of organizations against losses that arise due to accidents.

Industry specific funds: Also called sectoral funds, industry specific funds are based on the theme of an industry/sector. They are special purpose funds meant for investing only in specific industries.

Inseparability: Financial services are produced and consumed at the same time.

Intangibility: A service cannot be physically touched or felt. It can only be experienced.

L

Letter of credit: It is a document issued by a bank as per the instructions of the buyer of goods authorizing the seller of goods to withdraw money from the bank or its branches, on the basis of satisfying certain terms and conditions agreed upon by the buyer, seller, and the bank.

Level term cover: This rider provides an option to the customer of increasing the risk cover. The insurance cover may be increased for an additional premium, the maximum additional coverage amount being equal to the basic sum assured.

Liability products: Those products that are a liability to the bank as the bank has to maintain the funds of clients and pay interest on them. Banks utilize these funds in other options for revenue generation.

Liquidity management: It involves pooling and distributing funds across the client's multiple accounts with the bank. It helps in maximizing the returns on the excess or surplus funds in the accounts of the clients. It also helps in reducing the overdraft expenses as the surplus cash in one account can be transferred to the account through which payments are made to minimize the need for overdrafts.

M

Market potential: It is an estimate that presents information about the expected sales of all the players in the entire market during a given period (say one year).

M-Commerce: Electronic transactions using mobile communication equipment is referred to as M-Commerce.

Merchant banking: It refers to the rendering of services to corporate clients, which include issue management; preparation, planning, and execution of new projects; corporate and project counseling; floatation of new companies; services during mergers & acquisitions; portfolio management; etc.

Micro-insurance: It helps provide insurance cover to the rural masses and economically weaker sections of society.

Mixed branding strategy: An organization uses corporate names for some of its products and individual names for others.

Multi-tier branding: Financial marketers develop a two or three-tier strategy. The first tier consists of the master brand or the corporate brand, which conveys the values of the organization. The second tier consists of the banner or core brands. The third tier of brands are the sub-core brands.

N

No-frills account: A type of savings banks account with zero-balance or low minimum balance facility. In 2005, the RBI directed banks to provide such accounts as part of a broader agenda of financial inclusion of poor people in the financial system.

O

Offer/sale price: The price that an investor has to pay for purchasing units under a scheme.

One-to-one marketing: It essentially involves knowing about each and every possible need of the targeted customers and developing tailor-made solutions for them.

Open-ended funds: Under open-ended fund schemes, investors can pool in their subscription at any time, as there is no limit on capitalization. Besides this, there are no restrictions on the purchase and sale of units of such funds.

Operational CRM: It is a category of CRM software tools that assists the frontline employees who directly interact with customers in their day-to-day operations. These operations are mostly transactional in nature.

Overt pricing: It refers to the explicit charges that a bank collects directly from a customer for its product offerings.

P

Payment card: Used by organizations to make payments to their business partners by avoiding the problems associated with cash payments. Payment cards are operated within a closed group that should be pre-specified by the customer.

Perishability: Services are highly perishable in that a service not rendered/utilized is lost forever.

Preferred lives: Used as a criterion for deciding on premium rates for life insurance products. Separate premium rates are decided for preferred and residual lives of the same age. The preferred group was expected to exhibit, on an average, lower mortality than the residual group.

Price appeal: This appeal is mainly used by the manufacturer to communicate special offer prices, price cuts, sales, or new price points.

R

Rational appeal: Also called logical or informational appeal, it is used to provide information on product features and their benefits. The information provided in such ads focuses on how the product satisfies the needs of the customers.

Redemption price: The price at which the fund house repurchases its units from the customers. It is calculated with the NAV as the basis.

Reinsurance: Reinsurance is a means by which insurance companies transfer the whole or part of the risk of losses arising from their issued policies to other insurance companies or to reinsurance companies.

Repo Rate: It is a credit management tools used by the RBI to regulate liquidity (customer spending). This is the rate at which the RBI lends money to the banks.

Re-purchase price: It is the price at which investors sell back their units (of a close-ended fund) to the fund house.

Rider: They are add-on features (extensions) of an insurance cover that provide special benefits to the customer. They are flexible and can be added to the basic product based on the needs of the customer.

Risk-based penalty APRs: The marketer has the flexibility to modify the charges even after the credit card has been issued. Charges could be increased or decreased depending on the level of risk in terms of promptness in payments, increase in debt, etc.

Risk-based solicitation APRs: Customers with lower risk profiles are offered rate discounts while consumers who have high unpaid credit debt are issued credit cards with the highest fees. The interest rates are also higher for such customers.

Roaming current account: The account allows the customers to access, operate, and conduct transactions across different branches of the bank across the country.

Rupee cost averaging (RCA): The average cost per unit (share) reduces over time when investors invest the same amount in a fund at regular intervals over time. They are effectively buying more units when the NAV is lower and fewer units when the NAV is higher.

S

Sales maximization approach: This strategy is aimed at increasing volumes of sales for new insurance products.

Savings account: It is a financial product that allows a customer of a bank to save small amounts of money with the banks. Customers can either deposit into or withdraw from the account.

School savings banks (Sanchayikas): The objective of these savings schemes is to inculcate the habit of saving at an early stage, in school students. There are special agents to make school students subscribe to these savings groups.

Specialized market: A specialized market has many opportunities and each opportunity for differentiation can yield larger profits.

Stalemated market: In this type of market, opportunities for differentiation are fewer and also each opportunity is small. Profitability in this market is not related to the market share of the respective marketers.

Stored Value Card (SVC): It is a type of plastic currency. The cash amount is stored in an electronic form on the microprocessor chip of the credit card. The card enables a customer to transfer cash from his/her bank account on to the chip of the card and use it.

Structured products: Those products that are specially designed for some needs that cannot be met through other loan products.

Systematic Investment Plan: It is designed for those who are interested in gradually accumulating wealth over a long term in a disciplined manner. An SIP is not an investment product by itself; it just offers investors a different process of investment.

T

Tiered APRs: A form of credit card pricing where different rates are applied to different levels of the outstanding balance.

Total Bank Automation (TBA): Indian banks have attempted to automate their back-end processes to reduce excessive reliance on people, which led to heterogeneity of services.

Transit insurance: The policy covers loss of or damage to household assets when shifting house due to fire, theft, pilferage, water, etc

U

Underwriter: Underwriters are specialized personnel who look into the risks associated with various insurance policies. They identify and calculate the risk of loss from policyholders, establish appropriate premium rates, and develop policies that cover this risk.

Underwriting: The entire process of assessing the risk profile of the individual and then fixing the rate of premium is called risk classification or underwriting.

Universal banking: Banks, which have adopted this concept provide customers with the entire range of financial products, including those beyond the scope of traditional banking. This includes offering equity products, mutual funds, loans, insurance, pension products, etc., under one roof.

V

Volume market: In this type of market, opportunities for differentiation are few but the potential is large for business growth and profitability. Profitability depends on the size of operations and volume of sales.

W

Wealth management services: Services like investment planning, tax planning, management of assets, etc. that help in managing the wealth of the customers are termed as wealth management services

Whole life insurance: The whole life insurance policy provides a comprehensive insurance cover for life without any limitation of time period. The premium is fixed and it is paid for a longer period after which the sum assured is paid to the policyholder.

Worksite marketing: It involves insurance marketers targeting specific organizations to sell insurance products.

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