ALTERNATE DISTRIBUTION CHANNELS OF BANKING INDUSTRY IN INDIA

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In India, the banking industry has undergone a paradigm shift in its business operations and management – from 'brick and mortar' banking concept to 'virtual' banking concept. After the economic liberalisation, a number of developments have taken place in the field of banking product/service mix, place mix, promotion mix channel of distribution mix. Apart from the traditional ones, the new distribution channels, like, CBS branches, ATMs, telephone banking and call centres, Internet banking, Plastic cards and Intermediaries were added in the existing channel of distribution. These technology based distribution channels provide the banking organisations systematic way to render their services to their customers by making them more comfortable and ease with speed and accuracy. But these channels are not providing that level of benefit which was expected by the banks. They pose major challenges over banking organisations, such as, major investments in implementation of CBS, Wide Area Network (WAN), ATM network, etc., high cost of operation, hesitation of customers towards security of transactions and accounts, low level of literacy, no legal recognition of electronic contracts etc. In the present paper, an attempt has been made to look into the development of technology based distribution channel in the banking industry. An attempt has also been made to analyse the problems and challenges prevailing in the field of these alternate channels and also to suggest the remedial measures to turn these alternate channels into electronic weapon to compete these challenges.

Key words: ECS, NEFT, RTGS, PoS Terminal, CBS, MICR, CTS Cheques, Virtual Branches, Paperless Distribution.

Introduction

The banking industry in India has been witnessing a paradigm shift in its business operations and management. From a limited-site, limited-service and limited segment strategy, the banking industry has, now-a-days, adopted a multi-site, multi-service and multi-segment strategy to attract more and more new customers and to establish a long-term relationship with the existing ones. In this process not only the product / service

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mix, but also the price mix, promotion mix and channel of distribution mix have changes significantly. The policy of economic liberalization and deregulation initiated during the beginning of 1990s has paved the way for creating a new competitive banking environment. The entry of modern private banks and foreign banks has changed the entire scenario of banking in India. The new modern private and foreign banks have threatened the public sector banks having a dominant place in banking business. As a result, the public sector banks either of their own or by the direction of the regulator, i.e. the Reserve Bank of India have to adopt new tool and techniques of marketing.

In reality, channels of distribution play a significant role in successful business operation. In banking industry, too, channels have a great role to play. Keeping this in mind, the banking sector in the country has also taken steps to modernise and integrate its channel of distribution – from paper-based distribution to paperless distribution and from place-based distribution to space-based distribution. Information and communication technology has been playing a vital role in creating a new, effective and efficient distribution system. As a matter of fact, technology based delivery system is capable of handling volumes of business with high efficiency and low cost.

Objectives of the Study

The present paper examines the various aspects of modern distribution system evolved and adopted by the banking industry in India. In particular, the study aims at:

1. Assessing the development of technology-based distribution channels in the banking industry;
2. Identifying the problems and challenges prevailing in the field of alternative channels of distribution adopted by the banking industry; and
3. Suggesting remedial measures, wherever possible, to strengthen the alternative distribution channels of the banking industry.

Research Methodology

The study is based on exploratory research design. It, thus, concentrates on an analysis and evaluation of channels of distribution, at present, in vogue in the banking industry in India. The study is based on secondary data gathered from the official web-site of the Reserve Bank of India. For the purpose of this study, an eight-year period beginning from 2005 onwards has been taken. The data so gathered have been suitably tabulated, analysed and interpreted with the help of appropriate statistical tools and techniques.

Alternate Channels of Distribution of Banking Products and Services

Since the start of the banking activities, there was only one channel of distribution of banking products and services, i.e., through the branch premises. Customers were allowed to make transactions only through their home branches and hence, the banks were forced to equip their branches in all the respect to attract and satisfy their customers. This investment, however, results in low returns and high cost of transactions. In addition to this, a lot of time, of both customers and bank officials was wasted in performing these transactions. With the entry of foreign and private banks and the introduction of modern technology in the daily banking activities, the cost of transactions got reduced to a great extent. In order to implement these technologies, banks started the process of branch automation with consolidation and virtualisation of database and servers.

Table 1 depicts the trends in computerisation of public sector bank branches during the period 2005 – 2010. An analysis of the table shows that proportion of computerisation in public sector bank branches increased during the period under study. In the year 2005, about 93 percent bank branches were computerised. Out of computerised branches, the share of fully computerised branches was more than two-third which gradually went up to nearly 98 percent in the year 2010. As far as the share of public sector bank branches under Core Banking Solution (CBS) is concern, it was too low with 11 percent share in the year 2005. It also increased to 90 percent by the year 2010. These trends show that continuous progress is being made by the public sector banks to achieve a higher target, as more number of banks has moved into the "more than 90 per cent but less than 100 per cent" category so far as computerisation is concerned. As the banking industry has almost arrived at the final stage of complete computerisation along with the adoption of CBS, now the main concern is the adoption of more advanced technologies. These technologies help to enhance Customer Relationship Management (CRM), to improve internal effectiveness including Management Information System (MIS) and to manage risks regarding IT implementation.

Table 1: Trends in Computerisation in Public Sector Banks

(As at end-March)

(per cent of total bank branches)

Category	2005	2006	2007	2008	2009	2010
Fully Computerised Branches (i+ii)	71	77.5	85.6	93.7	95.0	97.8
i) Branches under Core Banking Solution	11	28.9	44.4	67.0	79.4	90.0
ii) Branches already fully computerized#	60	48.5	41.2	26.6	15.6	7.8
Partially Computerised Branches	21.8	18.2	13.4	6.3	5.0	2.2

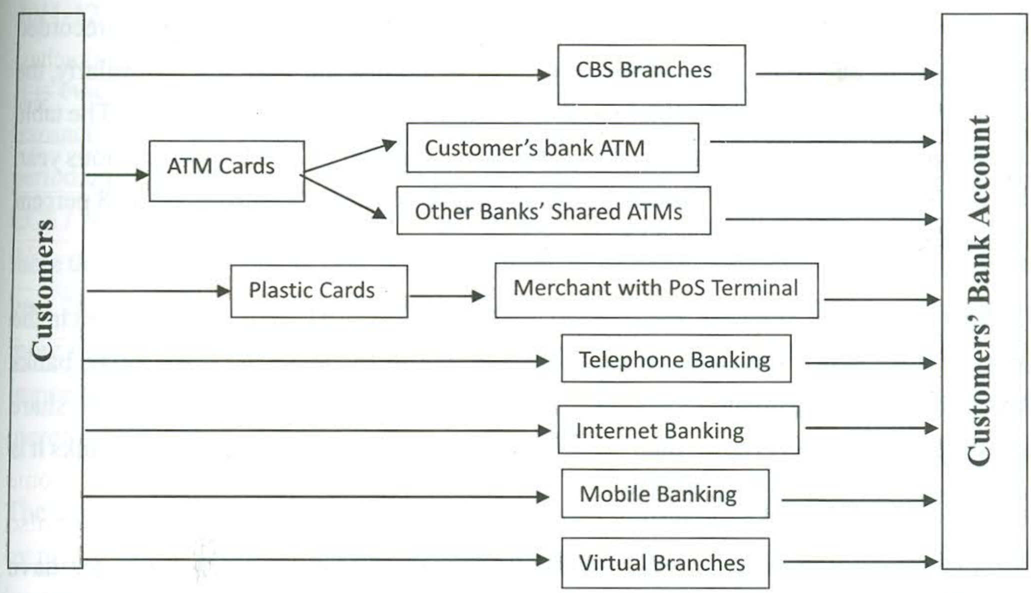
#: Other than branches under Core Banking Solution.

Source: RBI, Report on Trend and Progress of Banking in India (various issues).

With the advent of ATMs, the working of the banking organization has also become much easier, faster and popular among the customers. The banking organization is also benefited by the ATMs as they help in lessen the work load of branches and cost of distribution or delivery of banking services. A top functionary from the Indian Banks Association (IBA) avers, "At present about 60-80 percent of individual transactions from withdrawals are being handled by ATMs". Similarly, Managing Director (2011), State Bank of Hyderabad (SBH) says, "Retail customers now rarely come to a branch for withdrawals. In our banks, 87-90 percent withdrawals happen through ATMs". ATMs are very useful for those areas where the establishment of bank branches is a difficult task due to lack of infrastructure facilities.

The various distribution channels, based on information and communication technology, provide relief in the form of more effective work processes for the banking organisations. These alternate channels help in reducing costs of processing and in enhancing capability to handle relatively large transaction volumes with remarkable ease. For example, if teller-made transaction costs Rs. 1 whereas ATM transaction costs 45 paise, phone banking costs 35 paise, debit card costs 20 paise and internet banking costs 10 paise per transaction.

Figure 1: Channels of Distribution for Bank Services



Source: Mary Ann Pezzullo (1999) Marketing Financial Services Ed. 1st (USA: American Bankers Association) P. 201.

CBS branches make it easy for the customers to transact through any branch of the same bank. These branches are interconnected which provide access to the account of customers belonging to any branch. This helps the branch to cover wide area of business market and to generate more profit. The existence of CBS branches enables the bank to provide various services, especially those related to remittances, collection services, trade facilities, investment facilities etc.

Automated Teller Machines (ATMs) are technology based distribution channels which make banking services more accessible and convenient for the customers. They are available round the clock and business transactions can be made by the customer at his convenient time. Transactions through ATMs help in maximizing the profit of banks as the cost per transaction is very low as compared to the branch. Along with this, ATMs, by facilitating self-service to the consumers, make the bank staff free from routine work for other high-end functions. Further, all banks have been linked with ATMs network since April 1, 2009 to provide wider access to their customers. Thus, ATMs have made the banking services, particularly cash related services, more accessible and convenient for the customers.

Table 2 shows the trends in onsite and offsite ATMs of scheduled commercial banks in India during the period 2004-05 – 2011-12. The table reveals that there has been a sustained increase in the total number of ATMs during the period under study. It recorded an increase of about 5.5 times in the year 2012 as against the year 2005. Similarly, the same is true in the case of the total number of onsite ATMs and offsite ATMs. The table also depicts the percentage of increment in the total number of ATMs over previous year. It is obvious that in the year 2009-10, the total number of ATMs increased by 38 percent over the previous year which is the highest during the period under study.

Of the total number of ATMs, the share of onsite ATMs was a little over 43 percent in the year 2004-05 which increased to nearly 50 percent in the year 2012. Recently, banks have planned to open onsite ATMs in every bank branch. Of total number of ATMs, share of public sector banks is more than 60 percent, while that of new private sector banks it is close to one-third of the total ATMs.

Computerization of banking operations and the spread of personal computer have opened up a new channel for banking. Now banking services are being provided through internet. Under internet banking, the customers can access their accounts through the internet from anywhere and can conduct certain limited types of business, like balance enquiry, transfer of amount from one account to another account having same bank or may be of another banks, bill payment, request for demand draft and cheque books, etc.

Now-a-days, a new kind of channel for banking transactions has been initiated by various banks, called mobile banking. Under mobile banking, a customer can conduct certain banking functions, like balance enquiry, bill payment, transfer of small amount, etc. Along with this channel, banks are also taking the assistance of intermediaries, call centre and business correspondents.

All the channels, stated earlier, provide the banking organisations systematic way to render their services to their customers by making them more comfortable and ease with speed and accuracy.

Transactions through Technology based Distribution Channels

In India, after the introduction of RTGS system (2004) and NEFT (2005), each year the volume and the value of transactions transacted is increasing in multiples. Table 3(a) and Table 3(b) show the trends in and growth of banking transactions made through electronic distribution channels (in volume and value terms) during the period 2004-05 – 2011-12.

It is evident from the table that the total number of transactions and the total value of transactions through electronic distribution channels increased significantly during the period under study. The table shows that the total number of credit transactions through ECS / NECS increased by more than 3 times during the period under study, as it was more than 40 million in the year 2004-05 which increased to more than 122 million in the year 2011-12. In value terms, credit transactions through the same mode increased by more than 9 times (from Rs. 202 Billion to Rs. 1838 Billion) for the same period. It is important to note that in the year 2007-08 growth in the value of credit transactions increased by more than 8 times over previous year.

The table also reveals that the total number of debit transactions through ECS increased by more than 10 times during the period under study whereas in value term, it increased by more than 28 times. In the year 2004-05, the total number of debit transactions through ECS was more than 15 million which increased by more than 160 million in the year in the year 2008-09. After taking a dip in the year 2009-10 (with 149 million) it again took up speed to grow with more than 165 million in the year 2011-12. In value term, it increased from Rs. 29 Billion (2004-05) to Rs. 834 Billion (2011-12). Similarly, transactions through EFT /NEFT, credit cards and debit cards (in both forms) also increased during the period under study.

Table 3 (a): Trends in Transaction through Electronic Distribution Channels

(volume in millions)

Year	ECS Credit	ECS Debit	EFT/NEFT	Credit Cards	Debit Cards
2004-05	40	15	3	130	42
2005-06	44 (10.0)	36 (135.0)	3 (0.0)	156 (20.0)	46 (9.5)
2006-07	69 (56.8)	75 (108.3)	5 (66.7)	170 (8.9)	60 (30.4)
2007-08	78 (13.0)	127 (69.3)	13 (160.0)	228 (34.1)	88 (46.7)
2008-09	88 (12.8)	160 (25.9)	32 (146.2)	260 (14.0)	128 (45.5)
2009-10	98 (11.4)	149 (-6.9)	66 (106.3)	183 (-29.6)	182 (42.2)
2010-11	117 (19.4)	157 (5.4)	132 (100.0)	265 (44.8)	237 (30.2)
2011-12	122 (4.3)	165 (5.1)	226 (71.2)	320 (20.8)	328 (38.4)
Index 2011-12 Base Year 2004-05	**305**	**1100**	**7533**	**246**	**781**

Source: RBI, Report on Trend and Progress of Banking in India (various issues).

Note: Data in brackets are percent increase/decrease over previous year.

Table 3 (b): Trends in Transaction through Electronic Distribution Channels

(value in Rs. billion)

Year	ECS Credit	ECS Debit	EFT/NEFT	Credit Cards	Debit Cards
2004-05	202	29	546	257	54
2005-06	323 (59.9)	130 (348.3)	613 (12.3)	339 (31.9)	59 (9.3)
2006-07	833 (157.9)	254 (95.4)	774 (26.3)	414 (22.1)	82 (39.0)
2007-08	7822 (839.0)	489 (92.5)	1403 (81.3)	580 (40.1)	125 (52.4)
2008-09	975 (-87.5)	670 (37.0)	2520 (79.6)	654 (12.8)	185 (48.0)
2009-10	1176 (20.6)	695 (3.7)	4095 (62.5)	618 (-5.5)	264 (42.4)
2010-11	1817 (54.5)	736 (5.9)	9391 (129.3)	755 (22.2)	387 (46.6)
2011-12	1838 (1.2)	834 (13.3)	17903 (90.6)	962 (27.4)	532 (37.5)
Index 2011-12 Base Year 2004-05	**910**	**2876**	**3279**	**374**	**985**

Source: RBI, Report on Trend and Progress of Banking in India (various issues).

Note: Data in brackets are percent increase/decrease over previous year.

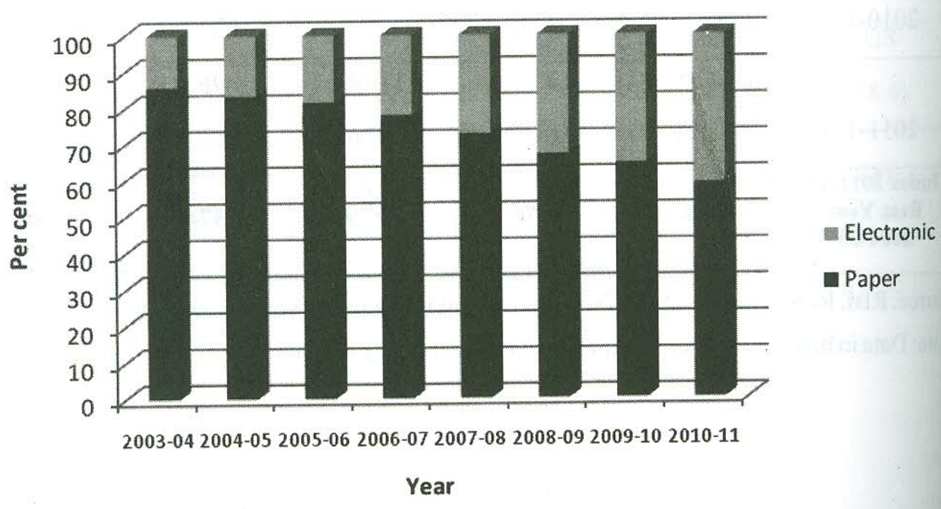
Now-a-days, transactions through electronic mode are increasing gradually. Table 4 provides the trends in the relative share of paper based versus electronic transactions in the banking industry during the period 2003-04 – 2010-11. As per Figure 2, the use of electronic means (in place of paper) for making payments has gone up sharply during the period under study. In terms of value, the share of electronic transactions has gone up from 30 per cent in 2003-04 to 89.7 per cent in 2010-11 (Figure 3).

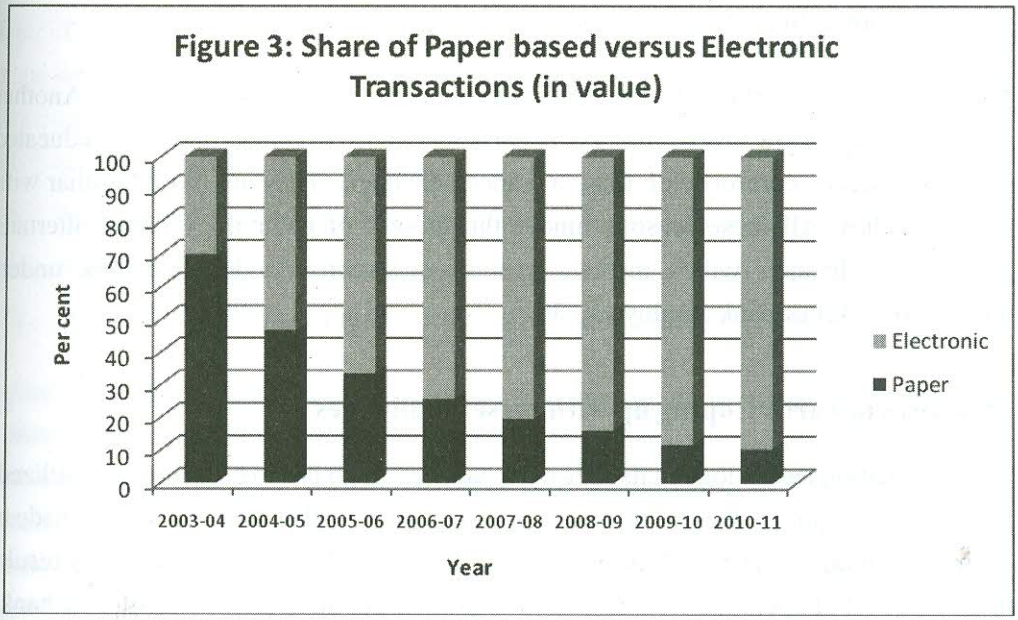
Table 4: Share of Paper based versus Electronic Transactions (in Percentage)

	Transactions in volume		Transactions in value	
Year	Paper	Electronic	Paper	Electronic
2003-04	85.9	14.1	70.0	30.0
2004-05	83.5	16.5	46.8	53.2
2005-06	81.7	18.3	33.5	66.5
2006-07	78.1	21.9	25.6	74.4
2007-08	72.9	27.1	19.6	80.4
2008-09	67.2	32.8	16.1	83.9
2009-10	64.7	35.3	11.7	88.3
2010-11	59.1	40.9	10.3	89.7

Source: Report on Trend and Progress of Banking in India, (various issues).

Figure 2: Share of Paper based versus Electronic Transactions (in volume)





Challenges faced by Banks in leveraging Technology based Distribution Channels

It was envisaged that the CBS would offer new opportunities for information management, better customer service and improved risk management. However, banks have not been able to reap the benefits of this technology in terms of reduction in costs of small value transactions, speed with which the transactions are done if both successful and unsuccessful transactions are considered, improved customer services and effective flow of information within the banks as also to the regulator. Banks have not gained in terms of efficiency partly because the much needed business process re-engineering was not done. Further, banks have deployed technology for transaction processing and the same has not been explored extensively for analytical processing like customer relationship management and decision making.

In the case of State Bank of India, under Lucknow circle more than 12 Lac savings accounts have been opened between the periods of 1 April, 2011 to 10 Oct. 2011. But the new registered mobile banking users are only 42000 and of internet banking are 44000. The percentage of mobile banking users and internet banking users are quite low, say 3.5 per cent and 3.6 per cent, respectively. This trend shows that the performance of banks towards leveraging technology in distributing banking products and services is very low. One of the important reasons responsible for the slow growth is the hesitation from the side of customers to use technology based channels.

They are, in fact, suspicious towards security of transactions and their accounts. Another reason may be the low level of literacy in particular areas. Illiterates and under-educated customers feel discomfort with these advanced channels. They are more familiar with their branches. All these reasons hinder the growth of technology based alternate distribution channels which increase cost of operation, flooded branches, under-utilisation of skilled bank employees, etc.

Measures towards Coping up with these Challenges

The information technology in itself is not a panacea and it has to be effectively utilized. Banks have to apply some effective measure towards it, so that the investments made in the implementation of CBS, Wide Area Network (WAN), ATM network, etc. may results in the low cost of operation with optimal use and leveraging of technology. As the banks have to face challenges arising from technology, such as, unwillingness of customers and security risk, banks must adopt the high level of security tools to prevent frauds and win customers faith. Further, banks would also have to gear-up for competition from non-bank players. For this, the banks need to modify and improve their distribution channels. Optimum leveraging of technology would critically hinge upon the following: (i) Skilled resources (ii) Supportive HR policy (iii) Appropriate IT governance structure, and (iv) Effective business continuity plan. The Reserve Bank of India has recommended to all scheduled commercial banks to implement CTS cheques (Cheque Truncation System) which is proposed to be implemented from 01 August, 2013. This system will help in fast clearing of cheques and will be safer and secure as its duplication cannot be done.

The most important requirement for the successful working of Internet banking and mobile banking is the adoption of the best security methods. This presupposes the existence of a uniform and the best available technological devices and methods to protect electronic banking transactions. In order for computerisation to take care of the emerging needs, the recommendations of the Committee on Technology Upgradation in the Banking Sector (1999) may be considered. These are:

1. Need for standardisation of hardware, operating systems, system software, application software to facilitate interconnectivity of systems across branches,
2. Need for high levels of security,

3. Communication and networking - use of networks which would facilitate centralised databases and distributed processing,
4. Need for a technology plan with periodical upgradation,
5. Need for business process re-engineering,
6. Need to address the issue of human relations in a computerised environment,
7. Need for sharing of technology experiences,
8. Need of Payment systems which use information technology tools.

Along with this, banks have to motivate their customers to adopt technology based distribution channel by conducting attractive campaigns. A team of skilled employees needs to be visit branch to branch to make their customers as well as their employees tech-friendly which helps in connecting more and more customers to these technology based distribution channels. Towards this, a few banks are offering lucrative schemes to increase the use of these alternate channels, such as exemption in bank charges by using these channels, cash back scheme – under which a percentage of transaction amount would be paid back by the bank to the users/ customers.

Conclusion

After the discussion on alternate distribution channels and its importance in the present economic world, it requires adopting the effective measure to remove the hindrances for the development of technology based distribution channels. It can be said that no technology driven payment system can be called fair unless it is able to bring about an overall overwhelming reduction in the cost of transactions - achieved through decreased overheads and increased processing volumes. If a bank succeeds in achieving the benefits for these advanced channels, it can be passed on to the customers in the form of reduction in bank charges on various banking products and services. Therefore, it is necessary for the all the banks and financial institutions to spread more and more of these technology based alternate channels among the customers so that these channels can be made strong and effective weapons for the banks as well as for the customers. To implement these technology based distribution channels, banks need to have appropriate and adequate arrangements for disaster recovery and business continuity plan to tackle any operational and technical failure.

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