ALL THE VERY BEST FOR YOUR EXAMS

SHORT NOTES FOR

CAIIB

RETAIL BANKING

Though we had taken enough care to go through the notes provided here, we shall not be responsible for any loss or damage, resulting from any action taken on the basis of the contents. Creation of these short notes is the efforts of so many persons. First of all we thank all of them for their valuable contribution. We request everyone to go through the Macmillan book and update yourself with the latest information through RBI website and other authenticated sources. In case you find any incorrect/doubtful information, kindly update us also (along with the source link/reference for the correct information).

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CAIIB – Retail Banking – Short Notes

Unit - 1 : Retail Banking - Introduction

"Retail Banking is a banking service that is geared primarily toward individual consumers.

Unlike wholesale banking, retail banking focuses strictly on consumer markets.

Although retail banking is, for the most part, mass-market driven, many retail banking products may also extend to small and medium sized businesses.

Pure retail banking is generally conceived to be the provision of mass market banking services to private individuals.

Attractive interest spreads since spreads are wide, since customers are too fragmented to bargain effectively; Credit risk tends to be well diversified, as loan amounts are relatively small.

There is less volatility in demand and credit cycle than from large corporates.

Higher delinquencies especially in unsecured retail loans and credit card receivables.

In some banks retail banking was christened as consumer banking as the focus was towards individual consumers.

Capgemini. ING and the European Financial Management & Marketing Association (EFMA) have studied the global Retail Banking market with the aim of providing insights to financial services community through the World Retail Banking Report(WRBR).

The pricing indices were developed based on three usage patterns viz., less active, active and very active users.

Introduction of the telegraph in the early 1850s which made the process of communication and information exchange faster and reduced the price differentials between stock markets.

Banking services follow the standard industrial development pattern in which prices decline with maturity.

The share of interest income had almost remained steady at about 84% and the share of non interest income also is almost stable at around 16%.This indicates that there were no serious efforts by banks to increase the non interest income through fee based product and third party distribution models.

Retail Banking as a concept in India has been initiated by the PSBs and nurtured by the foreign banks and new generation private sector banks.

It grew by a compounded annual growth rate of 30.5% between 1999 and 2004 and expected to grow at above 30% in 2010

The penetration level of retail banking in India is still very low as compared to the other Asian countries like China, Malaysia, Thailand etc..

The retail banking objectives of any bank would mainly focus on the following:

1. Generating superior returns on assets.
2. Acquiring sufficient funding
3. Enhancing risk management
4. Understanding customers and regaining their trust.
5. Coping with increased demands regarding product transparency and overall service levels.
6. Achieving multi channel excellence with fully integrated banking channels.
7. Moving toward higher levels of industrialization

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Unit - 2 : Retail Banking - Role within the Bank Operations

The business models for retail banking show interesting revelations across types of banks. The models adopted by banks vary among the public sector, private sector and foreign banks. The main approaches are as follows:

(a) Strategic Business Unit (SBU) Approach,
(b) Departmental Approach,
(c) Integrated Approach (part of the overall business plan).

Public Sector Banks in India generally have adopted the Departmental Approach as their retail banking business model.

The business model for retail banking is built as a part of the overall business plan and not done as a separate departmental activity, leave alone SBU.

In new generation private sector banks, the business model is very clear. They had set up Strategic Business Units (SBU) to have clear focus and business objectives.

The demarcation as a SBU is more a Management By Objectives (MBO) process wherein the business model is dealt as a modular strategy for achieving targeted profits with a provision to knockdown the module, if the retail plans are not translated as per the objectives.

Banks generally structure their retail banking models mainly on a positioning platform.

Foreign banks generally do not go by positioning objectives but purely on business objectives.

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Unit - 3 : Applicability of Retail Banking Concepts and Distinction Between Retail and Corporate/Wholesale Banking

The most common strategies are end to end outsourcing, predominant outsourcing, partial outsourcing and in house sourcing.

Regulatory prescriptions are one of the major determinants of outsourcing or lack of it in these banks.

In some foreign banks, both front and back end operations are outsourced and in some banks, the back end operations are outsourced while the front end operations like sourcing of HNI clients are done through captive resources.

The four broad classifications as envisaged by Boston group were defined based on the technology and customer interface capabilities of the banks and are

(i) Horizontally Organised Model
(ii) Vertically Organised Model
(iii) Predominantly Vertically Organised Model
(iv) Predominantly Horizontally Organised Model

Horizontally organised model is a modular structure using different process models for different products offering end to end solutions product wise.

Vertically organised model provides functionality across products with customer data base orientation and centralised customer data base is used across products.

Predominantly horizontally organised model is mostly product oriented with common customer information for some products. In predominantly vertically organised model, common information is available for most of the products.

In most of the PSBs, horizontally organised model is the standard norm. New private sector banks generally follow a vertically organised model.

As a part of overall segmentation game plan of the bank, branches are classified as Resource Centres, Profit Centres, Priority Centres and General Centres to have a clear business focus.

This concept is an effective business model for PSBs with large network and useful for focused strategies and already getting implemented in some public sector banks.

Liability products are offered to retail banking customers basically under three spaces - Savings Accounts, Current Accounts and Term Deposit Accounts. Product differentiation among these accounts is best achieved by adding different value propositions. (from a plain vanilla account to a value enriched account.)

Retail asset financing is a major component of retail banking model of banks.

Not all PSBs are in the credit card business since it is a big volume game and needs process efficiencies.

In the development process, geography is not given importance but type of branch and centre and business potential are given due importance.

Banks adopt different process models for retail asset products.

The common form of process models are Centralised Retail Assets Processing Centres where all the retail loans sourced at the branches and marketing team are processed at a single point and assets are financed through that centre or processing alone done at the centre and financing done at the branches.

Opening of account, issue of Pass Book, Cheque Book, ATM Card/Debit Card, PIN Mailers for the Cards are the stages in the tangibilisation process.(Centralized Processing)

Process time is a major differentiator in the efficacy of retail banking operations. Process Time is business sensitive and customer sensitive.

Stand alone pricing for different products and services is the basic structure.

Regarding Price Structuring quantum and volumes are two important determinants.

Structuring also involves price bundling where a holistic pricing is offered across a specific bundling of products and services so that the total price proposition is attractive than the stand alone pricing for the individual products of the bundle.

This structuring is a cross selling strategy to entice the customer to avail more products so that profitability per customer is enhanced.

The technology models basically adopted by banks are In House Models, Outsourced Models, Partially In House and Partially Outsourced Models.

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Unit - 4 : Customer Requirements

The basic segmentation of customers based on their income levels is presented below.

Income Levels (Rs. Lakhs)	Customer Segment
2-10	Mass Market
10-50	Mass Affluent
50-400	Super Affluent
400-4,000	HNW
4000-120,000	Super HNW
Above 120,000	Ultra HNW

MASLOW'S THEORY AND CUSTOMER REQUIREMENTS

Need Level Matching Banking	Investment and Insurance Products
Physiological Needs	Core Savings Accounts Personal Accident Cover Housing Loans
Security/Safety Needs	Recurring, Fixed Deposit Products.
Life Insurance Products	Endowment Products with low premium, long tenor and high maturity amounts. Tax Planning Banking, Insurance and Mutual Fund Products
Social Needs	Consumer Loans

	Personal Loans Home Loans Car Loans Loans for Professional Development for Doctors, Engineers, Lawyers, Chartered Accountants, Management Consultants, Architects etc., Insurance Cover tagged to above loans. Retail Gold Coins. Health Policies for self and family. Investment Products like Mutual Fund Schemes. Systematic Investment Plans of Mutual Funds. Unit Linked Insurance Products.
Esteem Needs	Special Term Deposit Products. Term Insurance Products. Second Housing Loans/ Home Improvement/ Home Decor Loans.
Self Actualization Needs	Pensioners Loans Retirement Solutions in Banking & Pension Plans in Insurance Senior Citizens Term Deposit Products

Expectations from the customers about the service quality of the bank basically depend on the following factors:

Tangibility in services- physical side of the service
Reliability- Sticking to agreed terms and promises.
Responsiveness- willingness to help and extend prompt service.
Assurance - Competence, Courtesy, Credibility and Security.
Empathy - Understanding the service expectations from the customers' point of view.

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Unit - 5 : Product Development Process

Ø Product is the fulcrum on which the entire retail banking revolves.

Ø Product is "Anything that has the capacity to provide the satisfaction, use and return desired by the customer".

Ø The first stage is the 'introduction' stage when the product is introduced. The sales volume will be low and revenue from the products will not be sufficient to cover the cost of producing, marketing and servicing it.

Ø In the 'growth' stage, which is the second stage in the product life cycle, the sales volume of the product picks up and the product is likely to break even and start generating profits for the organisation.

Ø In the third stage which is the 'maturity' stage, there is more growth and sales volume peaks. Here there is a wide customer base which will result in maximisation of sales with inflow of business and profits.

Ø In the fourth stage, which is the 'staleness' stage or 'saturation' stage, because of competition and better products available from the competitors, staleness will creep in, which will result in saturation of sales.

Ø the final stage of the product life cycle called as 'decline stage'. In this stage, the product becomes less attractive for the consumers due to various reasons and results in drop in sales volume and profits.

Ø Augmented products are products which are developed from formal products by combining two core products and adding value to the product in terms of benefits and comforts to the customer.

Ø Products can be broadly classified into following:

(i) Deposit Products or Liability Products
(ii) Asset Products or Retail Credit Products
(iii) Other Products and Services.

Ø The Generic Product - the core product.
Ø The Expected Product - adding additional features.
Ø The Augmented Product- adding value in addition to features.
Ø The Potential Product - futuristic features in anticipation.
Ø In the liability side, Banks offer different retail products like Demand Deposits, Time Deposits with different variations with regard to product features and duration.
Ø In the asset side banks offer mainly Home Loans, Auto Loans, Personal Loans and credit lines against credit card receivables.

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Unit - 6 : Credit Scoring

(i) Credit Risk - Customer fails to pay
(ii) Business Risk - Loosing money due to wrong strategy.
(iii) Market Risk - Change in market prices.
(iv)Operations Risk - Processing failures and frauds

Cibil-TransUnion model gives scores ranging from 300 to 900.

Credit Scoring Models are based on the following details of applicants:

(i) Family Size
(ii) Income Levels
(iii) Occupation/Business
(iv) Repayment History on earlier loans

The most common mistakes in credit score will be due to the following;

(i) Confusion of names
(ii) Human Input Error
(iii) Identity Theft

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Unit - 7 : Important Retail Asset Products

Important Retail Asset Products are :

Home Loans (Home Loans, Home improvement loans, Home decor loans)
Auto Loans
Personal Loans
Credit Card
Other Personal Loans

Personal Loans can be grouped under two segments:

(i) Big Ticket Personal Loans and
(ii) Small Ticket Personal Loans.

Big Ticket Personal Loans are loans in which the ticket size (amount of loan) is above Rs.50,000/- and an average ticket size of about Rs. 1,25,000/-.

Small Ticket Personal Loans are loans less than Rs.50,000/ - and an average ticket size of Rs.23,000/-.

Small Ticket Personal Loans are mostly extended by Non Banking Financial Companies (NBFCs)
Banks focus mainly on Big Ticket Personal Loans.

Banks adopt different models for processing of retail loans. The important models of retail loans processing are explained below:

Stand Alone Model

Stand alone model for retail loan processing refers to processing of retail loans independently at the branch level, based on the discretionary powers

Centralised Model

Centralised Model for retail loans processing refers to processing of loans at a centralised place depending upon the geography of branches. Banks adopt different centralised models for processing of retail loans. Some of the names, Banks give to these retail loans processing centres are :

(i) Retail Loan Factory
(ii) Retail Loan Hub
(iii) Retail Loan Processing Centres
(iv) Retail Asset Processing Centres
(v) Retail Loan Branches

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Unit - 8 : Credit and Debit Cards

Global Scenario

A credit card is a thin plastic card, usually 3-1/8 inches by 2-1/8 inches in size that contains identification information such as a signature or picture, and authorizes the person named on it to charge purchases or services to his account — charges for which he will be billed periodically.

- The concept behind Credit Card is "Buy Now, Pay Later".
- Credit Cards had their origin right from 1800s.

- The first universal credit card that could be used at a variety of stores and businesses — was introduced by Diner's Club Inc., in 1950.
- Another major universal card — "Don't leave home without it!" — was established in 1958 by the American Express Company.
- The first national bank plan was BankAmericard, which was started on a statewide basis in 1959 by the Bank of America in California. This system was licensed in other states starting in 1966, and was renamed Visa in 1976.
- Other major bank cards followed, including MasterCard formerly Master Charge.

Indian Scenario

- Citibank and HSBC were the pioneers in the Indian credit card market in the 1980s.
- Among the public sector banks, Andhra Bank, Bank of Baroda were the early starters followed by Bank of India.
- Citibank, Standard Chartered Bank, State Bank of India, ICICI Bank and HDFC Bank dominate the credit card market with more than 90% market share.

Mainly credit cards are issued by banks in two formats viz.,

The proprietary format - banks issue the card in different brand names like Classic, Silver, Gold, Platinum, Titanium etc. Credit limits, cash withdrawal limits and other facilities will depend on the type of card.

The Co branded format - banks tie up with service providers like Hotels, Oil Companies, Airline Companies etc. and offer the cards as a co branded product with the brand name of the tied up company also embossed in the card.

Credit Scoring Module for credit cards consists of two parts.

Part I deals with the criterion to take a decision to issue a card or not.
Part II deals with the scoring for various parameters submitted by the applicant.

Charges

Finance Charges
Minimum Amount Due
Maximum Interest Free Period
Annualised Percentage Rate (APR)
Other Charges & Penalties

Debit Cards

Debit Cards explain the concept of "Buy Now and Pay Now".

When debit cards were introduced initially, they were marketed with sub brand names Electron (Visa), Cirrus (Master).But the Electron and Cirrus are not seen nowadays and simply issued as International Debit Card by both Visa and Master.

Prepaid Cards or Pre Loaded Cards

- The card can be used by the bearer of the card only for purchases upto the amount loaded in the card.
- No cash withdrawal is permitted in the card.
- It is mainly intended as a Gift Card to be gifted to anybody.

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Unit - 9 : Remittance Products

Cheques, Demand Drafts, Bank Orders, Telegraphic Transfers are some of the earliest remittance products.

Retail electronic and card based payments registered a quantum jump mainly due to introduction of RTGS (Real Time Gross Settlement) and NEFT (National Electronic Funds Transfer).

NEFT (National Electronic Funds Transfer).

Reserve Bank of India has introduced an electronic funds transfer system called 'The Reserve Bank of India National Electronic Funds Transfer System"

The parties to a funds transfer under NEFT System are

(a) the sending bank
(b) the sending Service Centre
(c) the NEFT Clearing Centre
(d) the receiving Service Centre
(e) the beneficiary branch

RTGS (Real Time Gross Settlement)

Transactions are processed instantaneously and settlement made on a gross basis.
The remittances are communicated through a structured messaging process and settlement for the message is made on a gross basis from the liquidity maintained by the sender bank with the settlement bank.

The remittances are credited on a dynamic basis and settlement also made on a dynamic basis.

The transactions carried out by RTGS are :

Inter Bank Transactions
Customer Payment Transactions
Delivery Vs Payment Transactions

Electronic Clearing Services (ECS)

Electronic Clearing Services (ECS) is a mechanism to effect payments to a desired beneficiary on a periodical basis for the monies payable to them.

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Unit - 10 : Marketing in Retail Banking

Retail Banking unlike Corporate Banking is primarily driven by number of customers each bank possesses.

Bank Marketing can be defined as

'the creation and delivery of customer - satisfying services at a profit to the bank'
'the matching of bank's resources with the customer's needs in the most profitable manner'.

Customer is the centre of attraction in retail banking and marketing and all the activities have to be focussed towards

(a) Identifying the customers' needs,
(b) Developing appropriate products to satisfy their needs,
(c) Providing them with efficient delivery channels for availing the products.
(d) Making them avail the products continuously.

Fundamental ingredients of an effective marketing mix in retail banking which are as follows:
(i) Product

(ii) Price
(iii) Promotion
(iv) Place
(v) People
(vi) Process
(vii) Physical evidence

The success of the seven Ps and the marketing strategies are measured only by the responses from the customers from the point of view of need satisfaction.

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Unit - 11 : Delivery Channels in Retail Banking

Customer satisfaction has to happen through different channels and choices are to be offered to customers to experience the optimum channel mix for maximum satisfaction.

Direct channels may be the best fit for a conservative customer whereas young and tech savvy customers may opt for remote channels.

The channels through which retail banking services are offered are illustrated below:

Branch

The transactions carried out in the branch premises infuse a sense of confidence in the minds of the customers that they are not only physically involved in the transactions but also feel the service experience at the branch.

Though customers have accepted the electronic channels of delivery in retail banking with both hands, they still want to transact personally at the branch for their banking requirements. To put it short, they want a human intervention for their services than simply go through on-line or mechanical interventions like ATMs and Internet and Mobile Banking.

Branch layout may be broadly defined as the system of locating the various service facilities within the Branch in order to deliver the most convenient service to the customers.

"Personal Banking Branches" enhance the delivery effectiveness of services by prescribing TAT (Turn Around Time) for different retail loans. Only the formalities for opening the accounts are completed at the branch level and opening of accounts, issue of Pass Book/Cheque.

Book, Debit Card, PIN etc are carried out through a centralised back-office mechanism.

The areas of operations of Extension Counters were restricted to a closed group like Courts, Educational Institutions like Schools and Colleges or a specific company in their premises.

ELECTRONIC/REMOTE DELIVERY CHANNELS

Automated Teller Machines (ATMs)

There are basically two types of ATMs to deliver services to retail customers.
1. On Site ATMs and
2. Off Site ATMs.

On Site ATMs are intended to offer the facility of Cash Withdrawals, Cash Remittances, Balance Enquiry etc., at the branch premises itself.

Off Site ATMs are designed to be situated away from the branches at convenient and busy locations to enable the customers to access it for their different needs but not necessarily from the branch.

"National Financial Switch" was initiated for ATM operations.

ATMS are always complaint prone because of the break downs and cash out situations.

These two faults would result in reputation risk for the bank and may result in customer switching also.

Point Of Sale Terminal (POS)

Point of Sale terminals are the enablers of payment of credit and debit cards in merchant establishments. Whenever a customer makes a purchase in a merchant establishment.

Reserve Bank of India (RBI) allowed cash to be withdrawn from any merchant establishment with a POS terminal. The RBI has, however, put a ceiling of Rs 1,000 a day on withdrawal of cash at merchant outlets using debit cards.

Mobile Banking

Globally, mobile banking initiatives were stared by Wachovia in 2005 and the full fledged mobile browser in 2007. Banking can be done at your finger tips and right in the place where you are. It is convenient, simple and readily accessible.

Internet Banking

Internet banking would have great implications on

(1) Internet commerce
(2) new types of electronic retail payments
(3) electronic retail banking
(4) the movement more generally of retail financial services to electronic delivery, including insurance, discount brokerages, and mutual funds

Internet Banking as a service and channel was initiated by foreign banks and new generation private sector banks in the past decade. The level of acceptance of Internet Banking, generally, from the public sector bank customers was initially lukewarm though some banks were able to push it hard.

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Unit - 12 : Delivery Models

The success of the Retail Banking depends on how the products and services are delivered to the customer. Delivery effectiveness in physical channels is determined more by the persons who are delivering the services.

The three important human interventions in physical channels are

(i) Internal Customer - Staff of the Branch
(ii) Specialised Marketing Personnel
(iii) Direct Selling Associates (DSAs).

In many of the public sector banks, retail banking is carried on only as a separate departmental activity and not as a Strategic Business Unit (SBU).

DEDICATED MARKETING MANAGERS

- Dedicated Marketing Managers were appointed in addition to existing internal human resources.
- These specialist Marketing Managers (MBAs in Marketing) were young and energetic and recruited from the campuses of management Schools.
- Some banks appointed them in Junior Management and some other banks in middle management.

DIRECT SELLING AGENTS (DSAS)

- DSAs are agencies appointed by banks to source business for them on a fee basis.
- DSAs are primarily engaged in sourcing Credit Cards and Retail Loans.
- The employees of the DSAs missell credit card products and make the customers fall into a debt trap by misusing the cards.
- Same is the case with misselling of retail loans and in this space, the pricing for the loans are not explained clearly.
- Ultimately this will result in dissatisfaction for the customers and reputation risk for the bank.

Reputation Risk is always a threatening factor in the DSA model

DSAs focus on pure selling by pushing the products than effective marketing after verifying the needs of the customers and their actual requirements.

SALES THROUGH TIE UPS

Banks enter into tie ups with the following agencies for extending different types of loans.

- Tie up with Builders as a preferred financier for extending Home Loans to prospective buyers.
- Tie ups with auto dealers is another method adopted by banks for expanding retail credit.
- Sanctioning of Personal Loans under tie up with different institutions is another model adopted by banks to expand retail loans.
- Even educational loans are disbursed on a tie up basis. Banks set up special counters during the admission season in reputed educational institutions and offer education loans based on merit.

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Unit - 13 : Customer Relationship Management in Retail Banking

There are three elements in CRM viz.

(a) Customer
(b) Relationship
(c) Management

Bank has to manage the customer by offering the right product/s matching the needs of the customer.

Relationship with the customer means that the service quality of the bank should match the customer expectations in total and result in total satisfaction of the customer.

Customer Relationship Management (CRM) is basically having a 360 degree view of the customers and their profile, dynamically tracking their requirements, offering matching products and services, cross selling relevant products to his changing needs and keeping him happy for ever.

- The objectives of a good CRM are aimed at to build long term profitable relationships with specific customers.
- Offer optimal products and services on a dynamic basis and achieve life time value from customers.
- The purpose of CRM is to increase the share of wallet of the customer with the banks' services and increase the per customer profitability of banks.

Customer optimisation is the essence of CRM and can be addressed through three dimensions viz.

(a) Acquisition of New Customers who are immediately profitable to the bank.
(b) Retention of Existing Customers who are most profitable and valuable to the Bank for the longest duration.
(c) Expansion of the customer relationship with the bank encouraging more purchases and shifting the less profitable customers to lower - cost delivery channels.

CRM is not just an option for the banks but a compulsion to achieve business synergies and optimization of resources.

Needs for banks for implementation of a CRM program :

(i) Need to increase operational efficiencies
(ii) Need to derive more value from employees.
(iii) Increasing Competition in retail banking.
(iv) Rising NPAs.
(v) Increasing Importance of Fee Based Income.
(vi) Delivery Channel Efficacy
(vii) Application of Technology

IMPLEMENTATION PROCESS OF CRM IN BANKS

Different key issues in the implementation of CRM by banks are :

a. Business Processes
b. Information Processes
c. Information Systems
d. Internal Organisational Culture

IMPLEMENTATION STAGES IN CRM

There are four stages through which CRM is implemented

a. Identification of Customers
b. Classification of Customers
c. Interaction With the most Valued Customers
d. Customisation of Bank's Products and Services for Different Customer Segments

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Unit - 14 : Service Standards for Retail Banking

Banking Codes and Standards Board of India (BCSBI) prescribed the various compliance requirements for the promises made by the banks for offering services to retail banking customers and they have codified the promises into a document. This is a voluntary Code, which sets minimum standards of banking practices for banks to follow when they are dealing with individual customers.

The Code has been developed to:

(a) promote good and fair banking practices by setting minimum standards while dealing with you.
(b) increase transparency so that you can have a better understanding of what you can reasonably expect of the services.
(c) encourage market forces, through competition, to achieve higher operating standards.
(d) promote a fair and cordial relationship between you and your bank.
(e) foster confidence in the banking system.

BCSBI has spelt out various commitments regarding the various services which are detailed below for information.
1. Objectives of the Code
2. Application of Code
3. Key Commitments
4. Our key commitments to you
5. Information - Transparency
6. General

7. Do Not Call Service
8. Interest rates
9. Tariff schedule
10. Terms and conditions
11. Advertising, Marketing and Sales
12. Privacy and Confidentiality
13. Credit Reference Agencies
14. Collection of dues
15. Security Repossession Policy
16. Complaints, Grievances and Feedback
17. Internal Procedures
16. Banking Ombudsman Service
17. Products and Services
18. Deposit Accounts
19. Clearing Cycle/Collection Services
20. Cash transactions
21. Stop Payment Facility
22. Cheques/Debit instructions issued by you
23. Branch closure/shifting
24. Settlement of claims in respect of Deceased Account Holders
25. Safe Deposit Lockers
26. Foreign Exchange Services
27. Remittances within India
28. Lending
29. Guarantee
30. General Information
31. Credit Card
32. Insurance
33. Mobile Banking
34. Credit Counselling Facility
35. Getting Records
36. Protecting Your Accounts
37. Secure and Reliable Banking and Payment Systems
38. Keeping Us Up To Date
39. Checking your account
40. Taking care
41. Internet banking
42. Cancelling payments
43. Liability for losses.

Unit - 15 : Technology in Retail Banking

Technology is the foundation on which the retail banking edifice is built across the globe.

Horizontal or vertical organized refers to whether data is available product wise on a stand-alone basis or data is available customer wise on an integrated basis.

In terms of processes for integration of technology in retail banking, retail banks are using different approaches to modularise and standardise their processes. **Four distinct process models are** :

(i) Horizontally Organised Model where individual process platform supports one product only. The sub data in the model are not shared with other products and product platform.

(ii) Vertically Organised Model where functionality is provided across all products. In this model, customer information is centralised. Centralised customer information builds common origination and servicing processes across all its retail banking products.

(iii) Predominantly Horizontally Organised Model with some modularization within a product oriented feed back. Customer data integration is available to a certain extent for other products.

(iv) Predominantly Vertically Organised Model is a hybrid model that offers common information for most of the related services. The basic information is available across products for common services to the various products.

Some of the user friendly features and benefits offered for retail banking by a major player in the banking and financial services software solutions providers.

a. Advizor
b. Alerts
c. Customer Analytics
d. Wealth Management

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Unit - 16 : Recovery of Retail Loans

The unsecured nature of retail assets like Personal Loans and Credit Card Receivables made the portfolio more vulnerable for default as there is nothing to proceed against for banks except through money suits.

Default is the occurrence of an event which happens due to non-payment of agreed installments.

Default happens mainly due to the following reasons;

(a) Genuine defaults due to reasons beyond the borrowers' control and
(b) Willful defaults where the borrowers deliberately default with malafide intention

Recovery process is a scientific as well as an essential tool for maintaining the quality of retail assets.

- Giving Notice to Borrowers
- Repossession of Security
- Valuation And Sale of Proerty
- Opportunity for the Borrower to Take Back the Security

Recovery Agents

PSBs administer recovery management through their own staff in case of retail loans, private and foreign banks outsource their recovery process and entrust the same to Recovery Agents for end to end recovery management when the accounts become delinquent.

Reserve Bank has requested the Indian Banks' Association to formulate, in consultation with Indian Institute of Banking and Finance (IIBF), a certificate course for Direct Recovery Agents with minimum 100 hours of training. Once the above course is introduced by IIBF, banks should ensure that over a period of one year all their Recovery Agents undergo the above training and obtain the certificate from the above institute.

Taking Possession of Property Mortgaged/Hypothecated to Banks

The terms and conditions of the contract should be strictly in terms of the Recovery Policy and should contain provisions regarding :

(a) notice period before taking possession
(b) circumstances under which the notice period can be waived
(c) the procedure for taking possession of the security
(d) a provision regarding final chance to be given to the borrower for repayment of loan before the sale/ auction of the property
(e) the procedure for giving repossession to the borrower
(f) the procedure for sale/auction of the property.

Banks are encouraged to use the forum of Lok Adalats for recovery of personal loans, credit card loans or housing loans with less than Rs.10 lakh as suggested by the Honourable Supreme Court.

SARFAESI ACT

Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act was put in place to allow banks and FIs to take possession of securities and sell them.

The act envisaged the formation of asset reconstruction companies (ARCs)/Securitisation Companies (SCs).

The Act provides alternative methods for recovery of NPAs, namely:

(a) Securitisation
(b) Asset Reconstruction

Debt Recovery Tribunals (DRTs)

DRTs are governed by provisions of the Recovery of Debt Due to Banks and Financial Institutions Act, 1993, also popularly called as the RDB Act.

- Each Debt Recovery Tribunal is presided over by a Presiding Officer.
- The Presiding Officer is generally a judge of the rank of Dist. & Sessions Judge.
- The Presiding Officer of a Debt Recovery Tribunal is the sole judicial authority to hear and pass any judicial order.
- Each Debt Recovery Tribunal has two Recovery Officers.
- DRTs can appoint Receivers, Commissioners, pass ex-parte orders, ad-interim orders, interim orders apart from powers to Review its own decision and hear appeals against orders passed by the Recovery Officers of the Tribunal.

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Unit - 17 : Securitisation

Securitisation is the process of converting and breaking definable asset classes into tradable units and selling to others through a mechanism called as Special Purpose Vehicle (SPV).

The Special Purpose Vehicle converts assets into securities called as 'Pass Through Certificates' and sell them to the buyers who may require that particular asset class as a requirement or investment.

Since these certificates are backed by assets, they are also called asset backed securities (ABS).

If assets which have underlying mortgages are secuiritised, they are called as "Mortgage Based Securitisation".

EMI FOR REPAYMENT IN RETAIL LOANS

Recoveries are effected in retail loans by Equated Monthly Installments or simply EMIs.

The formula for calculation of EMI :

EMI = [P x r x(1+r)^n)] / [(1+r)^n - 1)]

where
p = principal (amount of loan),
r = rate of interest per month (eg.: if interest rate per annum is 10% then 10/(12*100))
n = no. of installments

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Unit - 18 : Other Issues in Retail Banking

Third Party Distribution In Retail Banking

- customers' needs extend beyond just banking services and encompasses insurance and other investment needs.
- Customers have to approach different service providers for their different needs like insurance, investment in mutual funds and other services like broking services, demat services etc..
- banks can offer the above services through the relevant service providers through agency arrangements with them.
- This concept of selling products other than banking products is called "Para Banking".

Main third party products distributed by Banks are :

- Marketing of life insurance products of life insurance companies.
- Marketing of non life Insurance products of general insurance companies.
- Distribution of mutual fund schemes of various mutual fund houses.
- Offering of Demat Services.
- Offering of Broking Services.

MF distribution offers good scope for augmenting fee-based income of banks. Upfront Commission, Trail (loyalty) Commission, Mobilisation Incentives, Special Incentives, Collection Charges are the income triggers for New Fund Offers.

Banks selling mutual fund schemes should clearly understand the implications mentioned in the following model called as PROPAGATE Model for distribution. PROPAGATE model refers to :

P - Product
R - Risk
O - Opportunities (Returns)
P - People
A - Appetite
G - Geography (Place)
A - Attributes
T - Training
E - Education

Cross Selling

- It is selling one or more additional products to the existing customer base so as to generate more business and profit per customer.
- Searching thyself (customer mining) will give definite clues for cross selling.
- It is generating new/additional retail asset(s) from a liability.
- If the bank is able to sell an asset product (housing/car/educational loan) to a savings/current/ deposit account holder successfully, then it is cross selling.
- Cross Sell Ratio (the number of products per client) in retail banking, is 2 for the US and slightly above 2 for the UK and Germany, above 2.5 for France and a high 3 for Scandinavia.
- Research study observed that selling three products to a customer who already holds one increases profitability by up to 500 per cent.

Why Cross Selling?

- Cost factor
- Profit
- Fosters brand loyalty
- Helps banks to plan, implement and maintain better customer relationship management programmes (CRM)

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Unit - 19 : Lender's Appraisal Procedure

Three major phases of loan origination are :

- Information acquisition
- Credit appraisal and sanction
- Disbursement

Appraisal Procedures

The appraisal process begins with an application form which normally contains.

- Personal Information
- Employment Information
- Loan Information
- Financial Information
- Existing Property Details
- Property Details
- LIC Policy Details
- General Details
- Appraisal

Agreements/letters/application/forms required for the appraisal process:

- Housing Loan application.
- Appraisal form.
- Term Loan agreement for Home Finance.
- Guarantee Agreement (if required).
- Arrangement letter (Terms and conditions for Housing Finance).
- Equitable Mortgage intent letter.
- Equitable Mortgage confirmation letter.
- Letter of undertaking (where finance is availed for purchase of plot).
- Letter to be addressed by the borrower to his/her employer.
- Letter to be addressed by the borrower's employer to the Bank. Letter when the applicant himself/ herself is the drawing officer. Mortgage Deed (in case of Registered Mortgage)
- Mortgage Confirmation Letter.
- Documents in connection with pledge of other securities, wherever applicable.

Appraisal form for a Home Loan

- Eligible loan amount
- Service Eligibility
- Age Eligibility
- Legal Opinion
- Valuation Details
- Inspection Details
- Rate of Interest
- Security Details
- Repayment Details
- Other Charges
- Litigation Details, if any
- Relaxation/Concession, if any
- Disbursement details

The house/flat should be insured against the risk of fire/ riots/ earthquakes/ lightning/ floods etc.

A repayment holiday may be allowed for a home loan when the construction is undertaken by a reputed builder, a Government agency etc. and the borrower makes payments in stages over the construction period. The moratorium will be upto 18 months after the first disbursement of the loan or two months after completion of construction.

The interest payable over the period of the loan is calculated and added to the loan amount to arrive at the total payable amount. This amount, divided by the total number of monthly instalments is called the Equated Monthly Instalment (EMI).

Until final disbursement and repayment commences, the borrower pays interest on the portion of the loan disbursed. This interest is called pre-EMI interest. Pre-EMI interest is payable every month from the date of each disbursement up to the date of commencement of EMI.

In a floating rate interest home loan, the total dues to the lender will change when the rate of interest is changed. The lender does not usually change the EMI amount. The number of installments is increased or reduced depending upon the change in the total dues.

Check-off facility - An appropriately worded irrevocable authority for making salary deductions and remittance to the lender should be taken from the borrower.

In order to ensure prompt repayment of home loans, lending banks obtain post-dated cheques towards Equated Monthly Instalments (EMI)

Mortgage

In India. Immovable property is accepted by the Banks as security usually by way of:

Registered or Simple Mortgage

- The Deed of Mortgage is required to be registered with the concerned sub-Registrar/Registrar of assurances.
- By paying applicable stamp duty and registration charges
- Within whose jurisdiction the whole or some portion of the property to which the document relates is situated
- Within four months from its date of execution

Registered mortgage involves preparation of mortgage deed duly witnessed by two witnesses, payment of ad valorem stamp duty and registration of deed.

Mortgage by Deposit of Title Deeds.

The essential requisites of a "Mortgage by Deposit of Title Deeds" are:

- There must be a debt, existing or future.
- There must be a deposit of documents of title to immovable property.
- The deposit must be made in one of the notified towns.
- The deposit must be made by the mortgagor or his agent with the mortgagee or his agent.
- The deposit must be made with an intent to create a security for the debt.
- Letter of intent should be obtained. Necessary entry should be made in the document register.

Right of Foreclosure

On default by a mortgagor, in case of mortgage by conditional sale the mortgagee has the right to sue for a decree from the court to the effect that the former be debarred forever to get back the mortgaged property. Such a right is called Right of Foreclosure, which is provided for under section 67 of Transfer of Property Act.

A suit for foreclosure must be filed within 30 years from the day the mortgage money becomes due.

Priority of Charge

- Where a mortgagor creates more than one equitable mortgage over the same property in favour of two financing institutions, the institution in whose favour the mortgage is created first, has priority of charge.

- Where a mortgagor has created separate registered mortgages over the same property in favour of two or more financing institutions, the priority of charge will be determined with reference to the date of the execution of the deeds which has been duly registered within four months of execution (not the date of registration).

- Where a mortgagor gives the same property in equitable mortgage to one financing institution and in registered mortgage to another financing institution, the priority of charge will be determined with reference to the date of deposit of title deeds in equitable mortgage and the date of execution of registered mortgage deed. An equitable mortgage in no way gives inferior rights compared to a registered mortgage.

Where immovable property (of which land is the main constituent) is taken as security (primary or collateral) either by way of registered mortgage or equitable mortgage, the following aspects should be looked into:

- Tenure
- Valuation
- Title of land

Post Sanction Activities

- Monitoring
- Inspection
- Recovery

Restructuring

Circumstances when a restructure may be considered:

- Unforeseen event/major illness/social functions requiring significant outlay of funds in the family of the borrower or any other circumstance that affect the repayment capacity.
- In case of salaried class, borrowers who are on "loss of pay" due to lock out/strike/disciplinary action/delayed payment of salary by employer
- Delayed completion of housing project.

- Death/Disability of the borrower.

However, willful defaulters should not be covered under restructuring programs.

The credit rating should be reviewed annually.

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Unit - 20 : Securitisation - Mortgage Backed Securities

'Securitisation' means the conversion of existing or future cash inflows to any person into tradable security which then may be sold in the market.

The market players have different characteristics, relating to:

- Risk Appetite:
- Maturity
- Return Expectations
- Periodicity
- Liquidity of Promissory Note

Structuring a mortgage backed securitisation effort would be unique and would depend upon :

- The quality of the home loans (mortgages), the security value, the receivable quality.
- The history of collections, delinquencies.
- The home loan lender's credit rating.
- The probable rating for the proposed security, by a rating agency.
- Issue costs, including credit enhancement costs, trust management costs etc.

Securitisation - Concept & Rationale

The process of converting mortgage loans (any loan for that matter) together with future receivables into negotiable securities or assignable debt, is called securitisation.

Securitisation is a process by which a selected pool of homogenous and quality credit assets (loans) of a lending institution is sold to investors through a trust/intermediary by packaging them in the form of securities, which are transferred by way of Pass Through or Pay Through Certificates (PTC).

Asset-backed securities (ABS) can be structured in two different ways

Pass Through Structure

Generally used for loans with a tenure of more than one year, such as, car or housing loans. In a Pass Through Structure, a bunch of loans are converted into ABS. The maturity of the ABS is usually comparable to the tenure of the loans. The returns on ABS are paid directly from installments of the loans.

Pay-Through Structure

Generally used for loans of short maturity such as credit card receivables.

Mortgage Backed Securitisation (MBS)

The home-loan assets are bundled into securities and sold to investors. These are called mortgage-Backed Securities (MBS) because the pool of receivables sold to the SPV is supported by the mortgaged home-loans.

The MBS have not been popular in India on account of two reasons

- Lack of stringent foreclosure laws
- Conversion of assets into securities attracts high stamp duty

In the case of NHB the process of securitisation of home loan receivables works as a two-stage process.

- First stage: Transfer of mortgage debt from the primary lending institution (Originator) to a Special Purpose Vehicle (NHB SPV Trust set up by NHB through declaration) with or without the underlying security.

- Second stage: The mortgage debt so acquired will be converted into tradable debt instruments (say in the form of pass through Certificates) without any recourse to the originator or the SPV.

Securitisation of Mortgage Debt: NHB SPV may purchase and convert the housing loans into securities/ PTCs concurrently and issue them in the capital market for investment by investing institutions.

Execution of Memorandum of Agreement with NHB: Based on the willingness to sell or securities its portfolio of housing loans, the Primary Lending Institution is required to enter into an umbrella agreement (called Memorandum of Agreement) with NHB to sell/securities its portfolio of housing loans. The Memorandum of Agreement encapsulates the entire MBS transaction and entitles NHB to take necessary steps to purchase or securities an identified pool of housing loans, including circulation of the Information Memorandum and collection of subscription amount from investors, as the case may be.

Selection of Pool of Housing Loans: The pool of housing loans would be selected by the Primary Lending Institution from its existing housing loans based upon a 'pool selection criteria'.

Valuation of the Pool and Consideration of Assignment

NHB will consider making payment of purchase consideration to the Primary Lending Agency under the following methodology:

- Per Pricing Methodology
- Premium Pricing Methodology
- Discount Pricing Methodology

Credit Enhancement

The credit enhancement may be provided in various forms such as setting aside a cash pool (called cash collateral account), limited corporate guarantee, third party guarantee, setting aside an additional mortgage pool (called over-collateralisation), investment in sub-ordinated MBS paper (in the event of securitisation) etc.

Custody of Mortgage Documents

While the mortgage debt or the receivables pertaining to the MBS transaction will be legally transferred to NHB/SPV Trust, the originator (primary lending agency) will continue to physically hold the title documents in respect of the housing properties obtained as security on the loans issued, in the capacity of a custodian to NHB/SPV Trust.

Hierarchy or Appropriation of Collection mounts (Payment "Waterfall")

The hierarchy of payments shall generally be as follows :

- Payment to Service Providers viz. Trustee, Servicing Agent, Rating Agency, & other service providers'
- Payment of Interest to Senior Class RMBS (Class A PTC) holders
- Payment of Principal to Senior Class RMBS (Class A PTC) holders
- Replenishment of Cash Collateral/Guarantee/such other form of credit enhancement

- Payment of Principal to Subordinate RMBS (Class B PTC) holders
- Payment of Residual income to Subordinate (Class B PTC) holders

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Unit - 21 : Housing Finance and Tax Planning

In respect of Loan taken for Purchase/Construction of a Residential Unit, the borrower can avail benefit of payment of interest as well as repayment of principal.

Interest on housing loan can be claimed as a deduction from income from property, salary, business/ profession, capital gains, or any other source upto a maximum of Rs. 1,50.000 under section 24(b) of the Income-tax Act, 1961 every year subject to fulfilment of the following conditions.

- Loan has been taken on or after 1st April 1999.
- Loan is for purchase or construction of a residential property or as re-finance (takeover) of the principal amount outstanding under a loan taken earlier for purchase or construction of a residential property. However, in case of loan for construction, the construction should get completed within 3 Years of raising the Loan. Deduction can be claimed only from the financial year when the purchase/construction is completed.

If any of the first 2 Conditions mentioned above is not satisfied, i.e., loan was taken before 1st April 1999 &/or loan is for repairs/renovation/reconstruction, deduction of only upto a maximum of Rs. 30000 every year can be claimed.

In case the Loan is for repairs/renovation/reconstruction, deduction on account of interest on that loan can be claimed only if the property is self-occupied or if the owner is not able to occupy the property only because of his employment/business/profession at another place, where he/she resides in a building not owned by him/her or his/her spouse/close blood relatives.

The deductions are permissible only in respect of one property of the borrower, i.e., if he/she has raised loans for multiple properties, interest can be claimed as a deduction only in respect of one property, depending upon the borrower's choice.

As regards principal repayment, it can be claimed as a deduction from the gross total Income only by an Individual/HUF borrower under section 80C of the Income Tax Act, 1961.

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Unit - 22 : Mortgage Advice

In India, mortgage advice profession is carried out without any regulations. There are regulations in US, UK and other countries regulating the mortgage advice services.

Home Information Pack

This concept is being introduced in UK from 1st August 2007. The content of the pack is list of documents to be provided. The important compulsory documents are :

- Sale statement providing basic information about the site including the address of the property being sold, whether the property is freehold, leasehold,whether or not the property is being sold with vacant possession.
- Evidence of title to prove that the seller owns the property and therefore has the right to sell it.
- Energy Performance Certificate indicating how energy efficient a home is on a scale of A-Q The most efficient homes - which should have the lowest fuel bills are in band A.

Time Value of Money - Interest and Annuities

Re. 1 received today is worth more than Re. 1 receivable at some future date, because Re. 1 received today could be earning interest in the intervening period. This is the concept of the time value of money.

The process of converting future sums into their present equivalents is known as discounting, which is simply the opposite of compounding.

What if interest is paid more frequently?

Annually = P(1 + r) = Annual compounding
Quarterly = P(l + r/4)4 = Quarterly compounding
Monthly = P(l+r/l2)12 = montly compounding

The Rule of 72

This rule allows you to determine the number of years before your money doubles whether in debt or investment.

Future Value of Money

For finding out future value (FV). we must use compounding formula which is given

FV = PV(1 + r)n

Where PV means present value, 1 means one rupee, r means rate of interest and n means period or term.

Example:
If Rs. 100000 is invested for a period of 5 years at interest at 10% p.a. find the maturity sum i.e. future value

Solution

The formula for finding FV is
FV = PV(1 + r)n

= 100000(1 +0.10)^5
= 100000(1.10)^5
= 100000(1.61)
= 1610000

So the maturity sum will be Rs. 1,61,000

Future value of annuities

Annuities are essentially series of fixed payments required from you or paid to you at a specified frequency over the course of a fixed period of time.

Ordinary Annuity : Payments are made/received at the end of each period.

F = A [(1+i)^n-1] / i or FV = Annuity x CV factor

Where,
F = future value of an annuity
A = annuity
i = interest rate
n = term

Annuity Due : Payments are made/received at the beginning of each period.

F = A [(1+i)^n - 1] / i x (1+i)

Where,
F = future value of an annuity
A = annuity
i = interest rate
n = term

Example :

Future value of annuity due of Rs. 1000 for a period of 5 years at interest rate of 5% would be

FV (Annuity Due) = A [(1+i)^n - 1] / i x (1+i)
= 1000[(l+0.05)^5 - 1)] / (0.05) x (1+0.05)
= 1000 x 5.525 x 1.05
= Rs 5801.91

Present Value

Present value is nothing but the reverse of future value. The formula :

PV = FV + (1 +r)n or PV = FV x PV factor

Where,
PV means present value
1 means one rupee
r means rate of interest
n means period or term
FV means future value

Example:

If Rs. 161000 is the maturity value(future value) of investment, invested for a period of 5 years at interest at 10% p.a. find the amount invested (present value).

Solution:
The formula for finding PV is
PV = FV/(1 + r)n

= 161000/(1 +0.10)^5
= 161000/(1.61)
= 100000

So the present value will be Rs. 100,000

Capital Gains

Any profit or gain from sale or transfer of a capital asset is chargeable to tax under the head "capital gains" Capital asset means any property whether movable or immovable, tangible or intangible.

The following assets are, however, excluded from the definition of capital assets :

- Stock-in-trade, stores, raw material
- Personal effects (excluding Jewellery)
- Agricultural land outside the limit of municipality or notified area.

Types of Capital Assets

Short-term capital assets

Short term capital asset means a capital asset held for less than 36 months immediately prior to the date of transfer. However in following cases, asset held for less than 12 months is treated as short term capital asset :

- Equity or pref. shares (quoted as well as unquoted)
- Debentures/Govt. securities listed in a recognized stock exchange.
- Units of UTI/Mutual fund specified under section 1()(23D)
- Zero coupon bonds (whether quoted or not)

Long-term capital assets

Long term capital asset means a capital asset held for more than 36 months immediately prior to the date of transfer. However in following cases, asset held for more than 12 months is treated as long term capital asset:

- Equity or pref. shares (quoted as well as unquoted)
- Debentures/Govt. securities listed in a recognized stock exchange.

- Units of UTI/Mutual fund specified under section 10(23D)
- Zero coupon bonds (whether quoted or not)

Capital Gains - When and to What Extent Exempt from Tax

- Capital gains arising from the sale of residential house property (Section 54) is exempted provided the property is held for more than 36 months before sate and transferor has purchased another residential house by utilizing the capital gain amount within one year before sale of old house or within 2 years from the date of sale or construct a new house within a period of three years from the date of sale. If the amount of capital gain is not fully utilized for above, then only proportionate amount that is utilized will only be exempt.

- Capital gains from transfer of land used for agricultural purpose (Section 54 B) is exempt if utilized for purchase of another land.

- Capital gains on compulsory acquisitions of land and building of an industrial undertaking - (Section 54 D) is exempt if utilized for purchase of another land and building

- Capital gain is invested in bonds issued by National Highway Authority of India or RECL (Section 54 EC)

- Capital gains on transfer of long term capital assets other than a house property - (Section 54 F) is exempt provided the transferor has purchased residential house by utilizing the capital gain amount within one year before the date of transfer or within 2 years from the date of transfer or construct a new house within a period of three years from the date of transfer. If the amount of capital gain is not fully utilized for above, then only proportionate amount that is utilized will only be exempt.

Long term capital gain on transfer of property is taxable at a flat rate of 20% (plus surcharge and education cess). The surcharge @ 10% is applicable if the total income including capital gains exceeds Rs. 10 lakh.

The documents relating to the following transactions of immovable properties are required to be compulsorily registered :

- Gift
- Lease of immovable property from year-to-year or for any term exceeding one year
- Instruments which create any right in an immovable property of a value of more than one hundred rupees

The registration fee for the following immovable property transactions is leviable on the market value of property on which stamp duty is charged.

- Conveyance
- Exchange
- Gift
- Partition
- Transfer of Lease by way of Assignment
- Sale
- Settlement
- Power of Attorney given for consideration
- Authorising the attorney to sell the property

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Unit - 23 : Valuation of Real Property

Valuation means assessment of the worth of an asset or property. It is distinct from cost, which refers to the actual amount spent in producing an asset. Cost is related to the past while value refers to the future.

The Income-tax Department grants registration to Valuers u/s 34AB of the Wealth Tax Act, 1957, on the basis of their technical background and experience. For the purpose, the Deptt. has classified Valuers under separate categories those for

- Immovable property
- Agricultural land
- Plant & machinery
- Jewellery

Types of Real Property

Agricultural land

The factors that influence the return from agricultural land are :

- Location
- Soil quality
- Availability of water & electricity
- Size of holding

- Clear Title of land
- Access by road and approaches
- Cottage or Farm house, fencing and gates
- Types of crops that can be cultivated

Valuation of agricultural land is done by following two methods :

- Income Capitalisation Method
- Sales Statistics Method

Urban land

The factors that have a bearing on value of vacant land are:

- Location
- Size, shape and level
- Soil quality, water availability
- Frontage & depth
- Restrictions on development
- Encumbrances

Valuation of open land is done by following methods :

- Comparative Method
- Rent Capitalisation Method
- Belting Method

The methods used for valuation of land with building are:

- Comparative Method
- Rent Capitalisation Method
- Valuation based on profits
- Valuation based on cost
- Development Method

Valuation of specialized buildings - Valuation is based on capitalization of average net profit over past couple of years at appropriate rate of interest. This method is also known as the balance-sheet method.

Sinking Fund

The fund set aside for the purpose of recovering the original capital is called sinking fund. The amount to be regularly set aside out of annual income to create the sinking fund depends on the compound interest it is supposed to earn over the life of the structure.

Depreciation

Depreciation means loss in value. A building also loses value due to obsolescence. There are several methods to calculate depreciation but the following two methods are usually adopted :

Straight Line Method

In this method, the depreciation is allocated uniformly over the life of the property and is generally adopted for tax purposes and preparing financial statements. The annual depreciation is given by:

D = (C-S) / n

Where,
D is annual depreciation
C is original cost,
S is salvage value (value that property may fetch at the end of useful life)
n is life of building in years

Written Down Value (WDV) Method or Declining Balance Method

In this method, it is assumed that the property will lose value by a constant percentage of its value at the beginning of the year. Thus, the amount of depreciation goes on reducing every year because while depreciation is charged at fixed percentage, the capital value of asset decreases by depreciation charged every year. The WDV of an asset can be found out by the formula :

WDV = C(1-p)^n

Where,
C being original cost
n being life in years
p being the percentage at which depreciation is charged

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ALL THE VERY BEST FOR YOUR EXAMS

SHORT NOTES FOR

CAIIB

RETAIL BANKING

Though we had taken enough care to go through the notes provided here, we shall not be responsible for any loss or damage, resulting from any action taken on the basis of the contents. Creation of these short notes is the efforts of so many persons. First of all we thank all of them for their valuable contribution. We request everyone to go through the Macmillan book and update yourself with the latest information through RBI website and other authenticated sources. In case you find any incorrect/doubtful information, kindly update us also (along with the source link/reference for the correct information).

K Murugan, MCA MBA CAIIB