Unit 8: Banking Systems

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Objectives

After studying this unit, you will be able to:

- Define Corporate Banking
- Classify Corporate Bank Customers
- Elaborate on Retail Banking
- Discuss significance and functions of Merchant Banking
- Describe Treasury Management

Introduction

Previous unit gave you an insight on loans and advances provided by banks whereas in this unit you will study about different banking systems such as corporate banking, retail banking, merchant banking and treasury management. Banking system can be defined as the structural network of institutions that render financial services within a nation. The members of the banking system and the functions they typically execute comprises of commercial banks that take deposits and make loans, investment banks which specialize in capital market issues and trading, and national central banks that issue currency and set monetary policy. Banking System is a chief mechanism through which the money supply of the country is ensured and controlled. The banking system enables us to understand Commercial Banks, Secondary Banks, Central

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Banks, Merchant Bank or Accepting Houses and Discount Houses but except saving banks and investment banks and other intermediaries.

8.1 Corporate Banking

Corporate banking includes products and services that are offered specially to corporations such as lending services that could be in the form of a secured or unsecured loan, financing, underwriting, cash management, issuing of stocks and bonds etc. Few of these transactions may include various banks and syndicates.

Corporate banking represents a wide range of banking and financial services provided to domestic and international operations of large local corporates and local operations of multinational corporations.

Services of corporate banking include the following:

- Access to commercial banking products, including working capital facilities such as domestic and international trade operations and funding,
- Channel financing, and overdrafts,
- Letters of guarantee, etc.
- Structured solutions both onshore and offshore,
- Term loans (including external commercial borrowings in foreign currency),
- Domestic and international payments,
- Support to client's worldwide operations, ensuring a full understanding of the company's business and financial needs.

Banks may classify their corporate customers into three segments on the basis of capital employed and sales volume: Large corporations, Mid-size companies, and Small and Medium business Enterprises (SMEs). Corporate customers can be further segmented into industry verticals, such as automobiles, aviation, tourism, etc. Banks develop long-term relationships with their corporate clients as a part of their marketing efforts. In a competitive market, building strong relationships with the customers help to retain customers and improve profitability. The communications and relationships between the banks and their corporate clients are affected by three factor groups – 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 growing to become a mutually beneficial 'partnership relationship' between the 'client' and the bank.

Did u know? Banking products are broadly classified into fund-based products and fee-based services.

Fund-based products are further subdivided 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.

Fee-based services can be further 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/ forfeiting, 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.

Banks need to deal with the changing requirements of their customers through new product development. However, financial products can be easily replicated.

The pricing of banking products directly affects customer acquisition and customer retention, in addition to profitability and long-run viability.

Caution Price is a mechanism to cover the costs of operations which comprises of production costs, distribution costs, promotion costs, and other operational expenses.

The pricing decision is influenced by many factors such as cost, competition, customers, and other constraints. With the advent of deregulation and the simultaneous rise in competition, many of the banks have acquired 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 credit-worthiness of the customer, stage of relationship, etc.

Notes New product development and innovation are considered essential for a bank's long term sustainability.

Corporate banking products are distributed mainly through a direct sales force or bank branches, supplemented by phone banking and online banking. Relationship officers are based at several branches of banks; they make frequent client visits to nurture relationships and to develop fresh business opportunities. Banks attempt to develop an optimal distribution mix using personal/ non-personal ways of delivery, in order to achieve various objectives such as superior customer service, operational efficiency, and profitability. Integrated banking software applications – usually referred to as Core Banking Solutions (CBS) — are essential 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 regarded 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 ignored this segment for a long run due to the high incidence of Non-performing Assets (NPA) and the lack of proper tools 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 several banks. This shift has been affected by the policy initiatives introduced by the Reserve Bank of India and the government in favour of SMEs. With big enterprises getting access to cheaper funds from other channels, their bargaining power has been increased with respect to the banks. This situation has also induced corporate bankers to look at SMEs as an avenue for profitable growth.

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Caselet

Corporate Banking Business of ICICI Bank

ICICI Bank provides innovative financial solutions to its corporate clients, tailored to meet their requirements, while diversifying its revenue streams and generating adequate return on risk capital through risk-based pricing models and proactive portfolio management. Its focus in the financial year 2003 is on technology-driven enhancement of delivery capabilities to offer improved service levels to clients. It set up centralized processing facilities for back office operations where technology is leveraged to benefit from economies of scale arising out of large transaction volumes. During the year it continued to expand the scope of its Web-based services. ICICI Bank provides corporate internet banking services through ICICIebusiness.com, a single point web-based interface for all corporate products. The portal enables clients to conduct their banking business with ICICI Bank through the Internet in a secure environment.

ICICI Bank offers online foreign exchange and debt securities trading services. A dedicated product and technology group develops and manages back-office processing and delivery systems. Dedicated relationship groups for corporate clients and the government sector focuses on expanding the range and depth of its relationships in these sectors. In the corporate segment, it focuses on leveraging its relationships to expand the range of products and services to channel finance, transaction banking and non-fund based products.

ICICI Bank has strong relationships with several large public sector companies and state governments and it is leveraging these relationships to expand the range of transaction banking services. It has already been empanelled for collection of sales tax in eight states. It continued to focus on corporate lending transactions including working capital finance to highly rated corporate, structured transactions and channel financing. It also focused on leveraging its skills in originating and structuring transactions as well as on its ability to take large exposures to adopt an originate-and-sell-down strategy.

This not only increased the risk-adjusted return on the capital employed but also enabled it to offer a comprehensive solution to its corporate clients. ICICI Bank's dedicated structured finance, credit and markets group, with expertise in financial structuring and related legal, accounting and tax issues, actively supports the business groups in designing financial products and solutions. This group is also responsible for managing the asset portfolio by structuring portfolio buy outs and sell-downs with a view to increase the risk-adjusted return on the capital. During fiscal 2003, ICICI Bank focused on the agri-financing segment and developed several innovative structures for agri-business, including dairy farming, farmer financing and warehouse-receipt-based financing.

It achieved robust growth in this segment and is working with state governments and agri-based corporate to evolve viable and sustainable systems for financing agriculture. It has also integrated its rural banking, micro-finance and agri-financing activity to offer integrated banking services in rural areas.

Source: www.icicibank.com/

The Global Relationship Management teams of the banks are tasked with understanding in depth the sectors in which clients operate with the aim of adding value through detailed industry knowledge and structured financial solutions.

Sector-based Client Service teams that combine relationship managers, product specialists and industry specialists to develop customized financial solutions service clients are engaged.

In today's global banking scene, Corporate Bankers are facing a series of unprecedented and sweeping challenges in the areas like Treasury Management, Trade Finance, Risk Management, Compliance Management, Electronic Trading and Derivatives Markets. Adding to this are the mounting complexities from ongoing regulatory changes, decreasing margins and fierce competition.

Self Assessment

State whether the following statements are true or false:

1. Banks develop short-term relationships with their corporate clients as a part of their marketing efforts.
2. The pricing decision is not influenced by such factors such as cost, competition, customers, and other constraints.
3. Every bank has to set its own Benchmark Prime Lending Rate (BPLR) to price its asset products.
4. The pricing of banking products directly affects customer acquisition and customer retention.

Fill in the blanks:

5. Cash inflows and outflows are checked by …………… manager.
6. It is the function of treasury management to minimize the …………….. .
7. The main function of treasury management is to maintain the ……………….. of business.

8.2 Retail Banking

The relationship between the bankers and the customers is not the same like before. The market has undergone a sea change. The customers have become more demanding today. The transition from sellers market to buyers market has compelled the bankers to understand the pulse and needs of the customers.

It may not be incorrect to say that the banking products and services today are designed by the customers. The luxury of discretion to design the products and services by the bankers is not any more available to the bankers.

Bankers today have no choice except to alter their product mix, delivery channels and corporate structure to serve their functional role. Some of the products which were shunned by the bankers and were treated as inflationary 20 years ago in nature like housing loan, consumer durables finance which otherwise were the prerogative of the bank employees have become targets of bank business and area of fierce competition and business mantra. Banks are vying with each other to sell across their ideas and products in the compelling hours of competition and the unexpected quarters say cooperative banks too have joined the fray.

Retail banking has wider connotation and is not the same as that of retail lending. Retail banking refers to the efforts of the bankers to reach up to the customers on both fronts of the balance sheet i.e., Liabilities side as well as Assets side. Under the liabilities side, we have deposits. Unless the banker designs the products according to the needs of the customers and facilitate better bargain to them in terms of rate interest, time and delivery channels, it is not easy for them to solicit business in this segment. The age of walk in deposits is gone. With interest deregulation in the sector of deposits with the sole exception of Savings Bank Account, where the apex monetary authority continues to decide the rate of interest, rest of the fields are open for competition.

In the Assets side, we have credit/loan schemes of the various banks. The job of the banker has become very difficult in this segment too. Bankers today are offering various sops to attract the potential customers. For instance, payment of free insurance premium by the bank comes along with the vehicle loan in respect of few banks. Some banks are prepared to offer total credit solutions along with housing loan, we mean here, they have enabled facility of consumer durables finance, vehicle finance in one go the customers who avail of housing loan from them.

This way, we understand retail banking includes designing delivery of customized products from both sides of the balance sheet.

The following channels are effectively utilized by the bankers to mobilize business from the potential clients:

- Premises banking or banking at doorsteps
- Automated Teller Machines
- Debit Cards and Credit Cards
- Telephone banking
- Internet Banking
- Mobile Banking
- Electronic Funds Transfer/Electronic Clearing System debit

8.2.1 Retail Banking – Retail Lending Schemes (Asset Focused Segment)

There has been a great heat of competition in selling ideas, products and services under this segment between one bank and the other. Retail lending, a departure from conventional advance, offers higher yield, quicker turn, the possibility of less incidence of the account going bad or non-performing if it is monitored on an ongoing basis. Monitoring of the account is easier in retail lending segment as compared to the conventional advances, for the reason that installments and repayment schedule have to be monitored in respect of retail lending.

Example: An advance to an industrial unit, security verification, conduct of the account by the borrower, compliances with statutory norms by the unit, submission of periodical returns like balance sheet, income tax assessment order and other regulatory ones from time to time.

While novel retail lending products are introduced by the banks to compete effectively in the market, the products which are prevalent in the industry and marketed by the banks are given below, as an illustration:

- Housing Finance.
- Consumer durable finance.
- Vehicle (two-wheelers and four-wheelers) finance
- Personal Loan
- Advance against future lease rentals
- Mortgage Loan
- Pension Loan etc.

Margin: The contribution brought in by the borrower is termed as margin. Margin requirements differ from one type of finance to others and they differ from one bank to the other. There is no standard capsule of margin in this segment.

Interest: The rate of interest has been deregulated by the apex monetary authority which suggests that the rate of interest offered by one bank for a retail lending scheme may not match with the one offered by the other bank. The rate of interest is decided by the individual banks.

Figure 8.1: Composition of Retail Lending (RBI report on Trend & Progress of Banks 2002-03)

1	Housing	₹ 34654 Crores	50%
2	Consumer durables	₹ 6904 Crores	10%
3	Loans to Individuals agt Shares etc.	₹ 1762 Crores	5%
4	Other Priority Sector/ Personal Loans	₹ 26089 Crores	35%
5	TOTAL	₹ 69409 Crores	100%

Source: Iyengar, G. Vijayaragavan, "*Introduction To Banking*" 2011, (P-307), Excel Books Pvt. Ltd.

8.2.2 Retail Banking – Liability Focused Segment (Deposit Accounts)

Saving Fund Account/Savings Bank Account

A saving fund account may be opened by a properly introduced individual singly or jointly, minors of the age of 10 years and above and minors under natural/legal guardianship.

Saving fund account cannot be opened in the name of any business concern whether proprietary/ company/partnership or association. Savings fund account cannot be opened in the name of:

- Panchayat Samitis
- Government departments
- State housing boards
- Water/Sewerage and Drainage Boards
- Housing Corporations/societies
- State Text Book Publishing Corporations
- Municipal corporations
- Industrial Development Authorities
- State Electricity Boards
- State Text Book Publishing Corporations
- Metropolitan Development Authority
- Any bank including land development banks

The following are the exceptions to the above. Saving Fund account can be opened in the name of the following:

- Any Government dept./body/agency in respect of grants/subsidies released for implementation of schemes sponsored by Central Government subject to production of an authorization from respective Govt. departments to open savings fund account, e.g., District Rural Development Agency, Member of Parliament Local Area Development Scheme, Khadi and Village Industries Board, Agriculture Produce Market Committee.
- Companies licensed under Section 25 of Companies Act, 1956, which are permitted not to add to their names the word "limited ", e.g., Indian Banks Association.

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- Societies Registered under Societies Registration Act 1860 or any other corresponding law
- Primary cooperative credit society being financed by the bank
- Any trust/institution whose entire income is exempted from payment of income tax
- Any other institution permitted by RBI on application made by the bank
- SF account in the name of Hindu Undivided Family (HUF) can be opened if it is not engaged in business activity
- Farmers Club
- Development of children and women in rural areas
- Self Help Groups
- Banks can also open SF account of state Govt. dept./bodies/agencies in respect of grants/ subsidies released for implementation of various State Government plans subject to obtaining an authorization that the department is authorized to open Savings Fund Account from the department itself.

Self Assessment

State whether the following statements are true or false:

8. Monitoring of the account is not easier in retail lending segment as compared to the conventional advances.
9. Margin requirements differ from one type of finance to others and further from one bank to the other.
10. Retail Banking has narrower connotation and is not the same as that of retail lending.
11. Bankers today have no choice except to alter their product mix, delivery channels and corporate structure to serve their functional role.

8.3 Merchant Banking

Merchant Banking is a combination of banking and consultancy services that banks provide to its customers. It renders consultancy, to its clients, for various matters such as financial, marketing, managerial and legal. Consultancy refers to provide advice, guidance and service for a fee. It helps a businessman in commencing a business. It helps to raise (collect) finance. It helps to modernize, expand and restructuring of the business. It helps to revive sick business units. It also helps companies to register, buy and sell shares at the stock exchange. In short, merchant banking provides a wide range of services for beginning, until running a business. It acts as Financial Engineer for a business.

"Merchant banking refers to a form of banking that both commercial and investment banks participate in. It involves trading unregistered securities including stock, bonds and private equity securities. Merchant banking serves large businesses, including international corporations, and some wealthy individuals. However, its role in the economy can affect consumers at all levels."

8.3.1 Significance of Merchant Banking

The very existence of merchant banking shows the need for specialized investment information. This is the main role of merchant banking. While many commercial banks may be satisfied with standard business plans and market research, the merchant bank is an active player in the field itself. The seasoned merchant banker knows exactly where strategic assets are situated, and which firms and strategies to fend off. With a merchant banker, a small business person is hiring a skilled partner with a long-term interest in the field. The real significance here is that using a merchant bank lowers the risks for a new firm.

8.3.2 Functions of Merchant Banking

Merchant banking is a service oriented industry. Merchant banks all over the world carry out the same set of services. In India, merchant banks carry out the following functions and services, specifically:

1. Corporate Counselling
2. Project Counselling
3. Pre-investment Studies
4. Capital Restructuring
5. Credit Syndication
6. Issue Management and Underwriting
7. Portfolio Management
8. Working Capital Finance
9. Acceptance Credit and Bill discounting
10. Mergers, Amalgamations and Takeovers
11. Venture Capital
12. Lease Financing
13. Foreign Currency Finance
14. Fixed Deposit Broking
15. Mutual Funds
16. Relief to Sick Industries
17. Project Appraisal

Each of these functions is detailed briefly below:

Corporate Counselling

Corporate counselling is the set of activities that is undertaken to ensure the efficient running of a corporate enterprise. It may include the rejuvenating of old line companies and ailing units, and directing the existing units in identifying the areas or activities for growth and diversification. The merchant banker directs the clients on various aspects like location factors, organizational size, operational scale, choice of product, market survey, cost analysis, cost reduction, allocation of resources, investment decision, capital management and expenditure control, pricing, etc.

Following are the activities which form part of corporate counselling:

1. Providing guidance in areas of diversification based on the Government's licensing and economic policies.

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2. Undertaking appraisal of product lines, analyzing their growth and profitability and forecasting future trends.
3. Rejuvenating old-line companies and ailing and sick units by appraising their technology and process assessing their requirements and restructuring their capital structure.
4. Commissioning of diagnostic studies.
5. Assessment of the revival prospects and planning for rehabilitation through modernization and diversification and revamping of the financial and organizational structure.
6. Arranging for the approval of the financial institutions/banks for schemes of rehabilitation involves financial relief, etc.
7. Providing assistance in getting soft loans from financial institutions for capital expenditure, and the requisite credit facilities from the bank.
8. Monitoring of rehabilitation schemes.
9. Exploring possibilities for takeover of sick units and providing assistance in making consequential arrangements and negotiations with financial institutions/banks and other interests/authorities involved.

Task Visit and organization which had recently had counselling and study various activities and methods of corporate counselling done by the concerned bank.

Project Counselling

Project counselling is a part of corporate counselling. It includes the study and analysis of the viability of a project and the steps required for its efficient and effective implementation are broadly the subject matter of project counselling.

Following are the activities that form a part of the project counselling:

1. Undertaking the general review of the project ideas/project profile.
2. Providing advice on procedural aspects of project implementation.
3. Conducting review of technical feasibility of the project on the basis of the report prepared by own experts or by outside consultants.
4. Assisting in the selection of a Technical Consultancy Organization (TCO) for preparing project reports and market surveys, or review of the project report or market survey reports prepared by TCO.
5. Assisting in the preparation of project report from a financial angle, and advising and acting on various procedural steps including obtaining government consents for implementation of the project.
6. Assisting in obtaining approvals/licenses/permissions/grants, etc. from government agencies in the form of letter of intent, industrial license, DGTD registration, and government approval for foreign collaboration.
7. Providing guidance to Indian entrepreneurs for making investment in Indian project in India and in Indian joint ventures overseas.
8. Identification of potential investment avenues.

9. Carrying out precise capital structuring and shaping the pattern of financing.
10. Arranging and negotiating foreign collaborations, amalgamations, mergers, and takeovers.

Pre-investment Studies

Pre-investment studies relate to the activities that are concerned with making a detailed feasibility exploration to evaluate alternative avenues of capital investment in terms of growth and profit prospects. Some of these activities are as follows:

1. Carrying out an in-depth investigation of environment and regulator factors, location of raw material supplies, demand projections and financial requirements in order to assess the financial and economic viability of a given project.
2. Helping the client in identifying and short-listing those projects which are built upon the client's inherent strength with a view to accentuate corporate profitability and growth in the long run.

Capital Restructuring Services

Merchant bankers assist the corporate enterprises in structuring their capital in such a way that it would minimize the cost of capital and maximize its return on capital invested.

Following are the services that are covered in capital restructuring:

1. Examining the capital structure of the client company to determine the extent of capitalization required.
2. Preparing a comprehensive memorandum for the controller of Capital issues, and securing consent where the capitalization takes place through issue of bonus shares.
3. Suggesting an alternative capital structure conforming to legal requirements, viz., extent of capitalization on reserve and quantum of disinvestments by 'offer for sale' and/or fresh issues of corporate securities such as equity share, and preference share in the case of FERA/FEMA companies.
4. Preparing a memorandum covering valuation of shares and justifying the level of premium applied for.

Credit Syndication

Activities connected with credit procurement and project financing, aimed at raising Indian and foreign currency loans from banks and financial institutions are collectively known as 'credit syndication'.

Activities that are covered under credit syndication are as follows:

1. Estimating the total cost of the project to be undertaken.
2. Drawing up a financing plan for the total project cost which conforms to the requirements of the promoters and their collaborators, financial institutions and banks, government agencies and underwriters.
3. Preparing loan application for financial assistance from term lenders/financial institutions/ banks, and monitoring their progress, including pre-sanction negotiations.
4. Selecting institutions and banks for participation for financing.

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Credit syndication services overlap with the activities of project finance and project counselling. But the loan syndication also includes the preparation of applications for financial assistance from financial institutions/banks.

Issue Management and Underwriting

Issue management and underwriting refers to the activities relating to the management of the public issues of corporate securities, viz. equity shares, preference shares, and debentures of bonds, and are aimed at mobilization of money from the capital market.

Following are some of the popular services provided by merchant bankers in this regard:

1. Preparation of an action plant.
2. Preparation of CCI application and assisting in obtaining consent/acknowledgement.
3. Preparation of budget for the local expenses for the issues.
4. Selection of issues Houses and advertising agencies for undertaking pre and post-issue publicity.
5. Obtaining the approval of institutional underwriters and stock exchanges for publication of the prospectus.
6. Drafting of prospectus
7. Selection of institutional and broker underwriters for syndicating/underwriting arrangements.

Portfolio Management

Portfolio management can be defined as making decisions for the investment of cash resources of a corporate enterprise in marketable securities by deciding the quantum, timing and the type of security to be bought.

The services covered are as follows:

1. Undertaking investment in securities.
2. Undertaking review of Provident fund investment, Trust investment, etc.
3. Undertaking investment for non-resident Indians, on both repatriation and non-repatriation basis.
4. Collecting and remitting interest and dividend on investment.
5. Carrying out a critical evaluation of investment portfolio.
6. Safe custody of securities in India and overseas.
7. Providing advice on selection of investments.

Working Capital Finance

The finance required for meeting the day-to-day expenses of an enterprise is known as 'Working Capital finance'.

1. Assessment of working capital requirements.
2. Preparing the necessary application to negotiations for the sanction of appropriate credit facilities.

3. Advising on the issue of debentures for augmenting long-term requirements of working capital.
4. Assisting, coordinating and expediting documentation and other formalities for disbursement.

Acceptance Credit and Bill Discounting

Acceptance credit and bill discounting connotes the activities relating to the acceptance and the discounting of bills of exchange, besides the advancement of loans to business concerns on the strength of such instruments, are collectively known as 'Acceptance Credit and Bill of discounting.

In order to the bill accepting and discounting takes place on sound lines, it is imperative that the firm involved commands a good reputation and financial standing.

Merger and Acquisition

This is a specialized service provided by the merchant banker who arranges for negotiating acquisitions and mergers by offering expert valuation regarding the quantum and the nature of considerations, and other related matters.

The various functions that form part of this activity are as follows:

1. Identifying organizations with matching characteristics.
2. Undertaking management audit to identify areas of corporate strength and weakness in order to help formulate guidelines and directions for future growth.
3. Obtaining approvals from shareholders, depositors, creditors, government, and other authorities.
4. Conducting exploratory studies on a global basis to locate overseas markets, foreign collaborations and prospective joint venture associates.
5. Monitoring the implementation of merger and amalgamation schemes.

Merchant bankers provide advice on acquisition propositions after careful examination of all aspects, viz, financial statements, articles of associations, provisions of companies act, rules and guidance of trade chambers, the issuing house associations, etc.

There are many reasons for the recent trend towards mergers and amalgamations, such as:

1. Existence of excess unused manufacturing capacity of the purchasing company, which can be utilized efficiently by taking over other units.
2. Lack of manufacturing space with the purchase company. The best solution may be to buy the controlling interest in another company having excessive manufacturing space or capacity.

Venture Financing

Venture capital is the equity financing for high-risk and high-reward projects. The concept of venture capital originated in the USA in the 1950s, when business magnates like Rockefeller financed new technology companies. The concept became more popular during the sixties and seventies, when several private enterprises undertook the financing of high-risk and high reward projects.

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Lease Financing

Leasing is an important alternative source of financing a capital outlay. It involves letting out assets on lease for use by the lessee for a particular period of time.

Following are the important services provided in regard to leasing:

1. Providing advice on the viability of leasing as an alternative source for financing capital investment projects.
2. Providing advice on the choice of a favourable rental structure.

In India, leasing is a non-banking financial activity. Commercial banks like State Bank of India and Canara Bank also provide lease financing by forming subsidiaries under the amended Banking Regulations Act of 1949.

Foreign Currency Financing

Foreign currency finance is the fund provided for foreign trade transactions. It may take the form of export-import trade finance, euro currency loans, Indian joint venture abroad or foreign collaborations. The main areas that are covered in this type of merchant activity are as follows:

1. Providing assistance for carrying out the study of turnkey and construction contract projects.
2. Providing guidance on forward cover for exchange risk.
3. Providing assistance in opening and operating banks accounts abroad.
4. Providing assistance in applications to working groups, liaison with RBI, ECGD and other institutions.
5. Providing assistance in obtaining export credit facilities from the EXIM bank for export of capital goods, and arranging for the necessary government approvals and clearance.
6. Assisting in arranging foreign currency guarantees and performance bonds for exporters.

Forms of Foreign Currency Loans

The various types of foreign currency loans are:

- Euro-currency Loans
- Financing Indian Joint Ventures abroad through:
  - Advice on the nature of client's investment.
  - Financial structuring of the project
  - Syndication of Euro loans
  - Bank guarantees
  - Procuring euro-currency facilities in the form of management and syndication of Euro-currency loans, bonds, Floating Rate Notes (FRNs), Floating Rate Certificates of Deposits (FRCDs), US commercial papers, with the assistance of International Treasury Management Limited (ITM).
  - Providing advice on currency swaps and interest rate swaps.
  - Arranging deferred term export finance to Indian entrepreneurs by maintaining a quick liaison with the export country's Export Credit Agencies who offer fixed rate

finance at concessionary interest rates, in particular export credit agencies in the UK (ECGD), USA (EXIM Bank), Japan, Italy, Norway, East Germany (HERMES), and who enjoy lines of credit from France (COFACE), Korea, Spain, Austria, Canada, Denmark, and India.

- Providing assistance in foreign collaborations through:
  - Helping locate foreign collaboration and joint venture partners abroad.
  - Providing advice on local laws, product risk, government regulations regarding shareholdings, exchange restrictions, taxation, dividends, incentives and subsidies, etc.

Brokering Fixed Deposits

Following are the services rendered by merchant bankers in this regard:

1. Computation of the amount that could be raised by a company in the form of deposits from the public and loans from shareholders.
2. Helping the company of observe all the rules and regulation in the connection.
3. Making arrangement for payment of interest amounts.
4. Drafting of advertisement for inviting deposits.
5. Filing a copy of advertisement with the Registrar of Companies for registration.
6. Providing advice to the company on the terms and conditions of fixed deposits, and deciding on the appropriate rate of interest, keeping in view the prevailing capital and money market conditions.

Mutual Funds

Mutual funds are institutions that mobilize the savings of innumerable investors for the purpose of channelling them into productive investments in a wide variety of corporate and other securities.

Some of the services rendered by mutual funds are as follows:

1. Mopping up public savings.
2. Investing the funds in a diversified portfolio of shares and debentures belonging to well managed and growing companies.
3. Earning investors a steady return on investments with an assurance of capital appreciation.

Relief to Sick Industries

Merchant bankers extend the following services as part of providing relief to sick industries:

1. Rejuvenating old-lines and ailing units by appraising their technology and process, assessing their requirements and restructuring their capital base.
2. Evolving rehabilitation packages which are acceptable to financial institutions and banks.
3. Exploring the possibilities of mergers/amalgamations, wherever called for.

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Project Appraisal

The evaluation of industrial projects in terms of alternative variants in technology, raw materials, production capacity and location of plant is known as 'Project Appraisal'.

Financial Appraisal

Financial appraisal involves assessing the feasibility of a new proposal for setting up a new project or the expansion of existing production facilities. Financial appraisal is undertaken through an analysis which takes into account the financial features of a project, including sources of finance. Financial analysis helps to trace the smooth operation of the project over its entire life cycle.

Technical Appraisal

Technical appraisal is primarily concerned with the project concept in terms of technology, design, scope and content of the plant, as well as inputs are infrastructure facilities envisaged for the project. Basically, the project should be able to deliver a marketable product from the resources deployed, at a cost which would leave a margin that would be adequate to service the investment, and also plough back a reasonable amount into the project to enable the enterprise to consolidate its positions.

Economic Appraisal

Economic appraisal of a project deals with the impact of the project on economic aggregates. These may be classified under two broad categories. The first deals with the effect of the project on employment and foreign exchange, and the second deals with the impact of the project on net social benefits or welfare.

Self Assessment

Fill in the blanks:

12. Venture capital is the ……………. financing for high-risk and high-reward projects.
13. Foreign currency finance is the fund provided for …………….. trade transactions.

8.4 Treasury Management

Treasury management can be described as the management of cash, funds, currency, bank and financial risk. That's why it is an imperative tool of finance. Cash inflows and outflows are checked by finance manager. The finance manager makes the list of all receivable amounts which will increase the treasure house of the company. He also keeps a track record of the dates in which he has to receive the fund from debtors. Under this management, he estimates all financial risk for the investment of cash. All investment is done on the basis of investment policy. Many organizations have separate treasury department. If company deals with foreign currency, then management of foreign currency risk is the duty of treasury department. Suppose, Google Inc. USA Company which is a MNC and it receives the fund from advertisers and shares with ad-sense publisher. A good treasury officer can give the advice to Google Inc. about when company should pay the bill of ad-sense publishers.

Example: There are 90, 00,000 ad-sense publishers and approximate US $100 which company has to pay to each Indian ad-sense publisher after one month. Now within 15 days, Google Inc. will choose that day when the price of dollar in Rupees will be minimum. Suppose, if company paid on 21st Feb. 2010 US $100 to one publisher when the price of dollar is ₹ 46.5 and pays ₹ 2139 and if the next day, price will decrease 0.5 dollar. Then, it means Google Inc. is in foreign currency loss ₹ 50 each publisher because, company has power to pay in next day and save ₹ 50 for each ad-sense publisher. If company has to pay US $100, then company can receive loss of ₹ 45 Crore due to foreign currency loss.

So, to manage and control foreign currency is the major project under treasury management. In government departments, fund management is under treasury management. Treasury department makes map to collect for govt. treasure and decide how to use it for welfare works. Finance manager creates good relationship for getting locker facility at cheap rates and company can keep its important documents in locker of banks. These documents and commercial papers can be sold by banks in money market and company can take part in money market by indirect way.

Notes Finance manager also do the duty to sell company's fixed assets at high price and he also acquire the properties for company at cheap rate for effective utilization of treasure of company.

8.4.1 Objectives of Treasury Management

Treasury management is done with the following objectives:

Risk Management Objectives

Following are the risk management objectives of treasury management:

- To ensure the stability of the boroughs financial position, by sound risk-management techniques;
- To constantly address the need to minimize risk and volatility whilst aiming
- To achieve the treasury management strategic objectives.

Borrowing Objectives

Following are the borrowing objectives of treasury management:

- To ensure that exposure to different types of borrowing instruments is at a prudent level relative to the Council's outstanding debt.
- To achieve the lowest level of interest paid on the Borough's debt as prudently possible while at the same time minimizing the potential volatility of the average rate of interest.
- To achieve an average rate of interest that falls within the best performing quarter of London Boroughs.
- To effect funding in any one year at optimum cost - having regard to future risks from movement in interest rates or variable rate borrowing.

Notes

- To manage the debt maturity profile, ensuring that in any one year repayments are no greater than 15% of the long term debt outstanding, with a restriction on 50% of debt maturing over the first five years of the portfolio.
- To ensure that the average maturity period of long-term loans outstanding is greater than 7 years.
- To take advantage of debt restructuring and debt repayment opportunities that may arise, for future revenue savings - taking into account the risks involved.

Investment Objectives

Following are the investment objectives of treasury management:

- To achieve an overall return on total deposits of at least one quarter of one per cent above the average seven day notice London Interbank Bid Rate (LIBID) - the rate at which a bank will bid to borrow money in the London money market with the minimum risk of capital loss.
- To achieve an average rate of interest that falls within the best performing quarter of the London Boroughs.

8.4.2 Functions of Treasury Management

The main functions of treasury management are as follows:

To Maintain the Liquidity of Business

The main function of treasury management is to maintain the liquidity of business. Without proper liquidity, it is very risky for business to operate smoothly. By using cash flow analysis and working capital management, treasury officer makes a good ratio of liquid assets and liquid liability.

To Minimize Currency Risk

In above example of Google Inc. business, it is already explained that it is the function of treasury management to minimize the currency risk. For this, treasury managers remain in touch with currency market of the world. They analyze the reason of crisis in currency market. Sometimes this crisis will be benefited for them because they have to pay less to other country for getting their service at cheap rates.

To Provide Quick Finance to Company

It is also function of treasury department to supply quick finance to company, when it needs the money. For this, a good network in financial market is required.

Self Assessment

Fill in the blanks:

14. A finance manager keeps a track record of the …………….. in which he has to receive the fund from debtors.
15. Finance manager creates a good relationship for getting locker facility at cheap rates and company can keep its important …………….. in locker of banks.

Notes

Case Study

Retail Banking Business of ICICI Bank

Mr. Bhargava Dasgupta heads the international business operations of ICICI bank and he has to travel a lot these days. He is busy in building the ICICI bank's next big platform-globalization. He feels that it is impossible to reach to the clients everywhere across the world physically for providing the financial services, so it will be strategically sound to leverage the relationships with other banks in serving the global consumer. The success of the bank in the domestic market is largely credited to the customer orientation, high quality of customer service, innovative financial product introductions and active involvement in serving the emerging and latent needs of the Indian consumer. They want to take their domestic market success to the global level. The recent spot of operations by the bank is an indicator of becoming a global financial service provider. ICICI bank has opened its first overseas branch in Singapore in 2003; in mid 2003, they opened the representative offices in London. They are close to acquire properties by the year 2003 end in Pundong and have already procured properties in East London to start their business operations including strategies to open offices in Toronto and Bahrain.

Retail banking is a key element of ICICI's growth strategy. With upward migration of household income levels, increasing affordability of retail finance and acceptance of use of credit to finance purchases, retail credit has emerged as a rapidly growing opportunity for banks that have the necessary skills and infrastructure to succeed in this business. ICICI Bank has capitalized on the growing retail opportunity in India and has emerged as a market leader in retail credit. The dimensions of the retail strategy include innovative products, parity pricing, customer convenience, strong processes and customer focus.

Cross-selling of the entire range of credit and investment products and banking services to customers is a critical aspect of ICICI's retail strategy. ICICI Bank offers a wide range of retail credit products. It has expanded the market significantly over the last few years by taking organized retail credit to a large number of high-potential markets in India, by penetrating deeper into existing markets and by offering customized solutions to meet the varying credit needs of the Indian consumer.

ICICI Bank is one of the leading providers of mortgage loans, two-wheeler loans, commercial vehicle loans and personal unsecured loans, and continues to maintain leadership in automobile finance. ICICI Bank's total retail disbursements in fiscal 2003 are approximately ₹ 200 billion. Retail credit constituted 18% of ICICI Bank's balance sheet at March 31, 2003, compared to only 6% at March 31, 2002. Cross selling has emerged as one of the significant drivers of retail credit growth. In fiscal 2003, cross selling accounted for about 20% of mortgage loans and auto loans and about 25% of credit cards issued. In May 2003, ICICI Bank acquired the entire paid-up capital of Transamerica Apple Distribution Finance Private Limited (TADFL), which is renamed as ICICI Distribution Finance Private Limited (IDFL). IDFL is primarily engaged in providing distribution financing in the two-wheeler segment. The acquisition is expected to supplement the Bank's retail franchise, especially in the two-wheeler segment.

Retail Deposits

During fiscal 2003, ICICI continued its focus on retail deposits. This has reduced its funding cost and has enabled it to create a stable funding base, with over 4.7 million deposit customers. Following a life stage segmentation strategy, ICICI Bank offers differentiated liability products to various categories of customers depending on their age group (Young

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Notes

Star Accounts for children below the age of 18 years, Student Banking Services for students, Salary Accounts for salaried employees, Roaming Current Accounts for businessmen, Private Banking for high net worth individuals and Senior Citizens Accounts for individuals above the age of 60 years). ICICI Bank has further micro-segmented various categories of customers in order to offer products catering to specific needs of each customer segment, like defence banking services for defence personnel. This strategy has contributed significantly to the rapid growth in the retail liability base.

Credit Cards

ICICI Bank is also the largest incremental issuer of cards (including both debit and credit cards) in India. At March 31, 2003, ICICI Bank had issued over 3.4 million debit cards and 1.0 million credit cards. Its multi-channel distribution strategy provides its customers 24%7 accesses to banking services. This distribution strategy not only offers enhanced convenience and mobility to the customer but also supports its customer acquisition and channel migration efforts.

Electronic Channels

During the year, ICICI has expanded its electronic channels and migrated large volumes of customer transactions to these channels. Seventy percent of customer induced transactions take place through electronic channels.

ATMs

During fiscal 2003, the Bank significantly strengthened its ATM network, taking the total number of ICICI Bank ATMs to 1,675. ICICI Bank has also pioneered the concept of mobile ATMs to reach out to remote/rural areas. Other facilities offered through multilingual screen ATMs include bill payments and prepaid mobile card recharge facility. ICICI bank is also planning to share the network with other key players in financial services market to give a wider access to its customers.

Internet Banking

ICICI Bank has about 3.4 million customers with Internet banking access, who can undertake all their banking transactions (other than physical cash transactions) on the Internet. ICICI Bank's Internet banking customers can also pay their bills for more than 45 billers and shop on 85 online shopping portals.

Phone Banking

ICICI Bank considers phone banking to be a key channel of service delivery and cross-sell. ICICI Bank's 1,750-seat call centre, the largest domestic call centre in India, can now be accessed by customers in over 355 cities across the country. The call centre handles more than 2.5 million customer contacts per month. The call centre services all retail customers across the ICICI group. The call centre uses state-of-the-art voice-over-Internet-protocol technology and cutting-edge desktop applications to provide a single view of the customer's relationship.

Mobile Banking

ICICI Bank's mobile banking services provide the latest information on account balances previous transactions, credit card outstanding and payment status and allow customers to request a cheque book or account statement. ICICI Bank has now extended its mobile banking services to all cellular service providers across the country and NRI customers in the United States, United Kingdom, Middle East and Singapore.

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Service Delivery through Multi-channel Distribution Network

With the foundation of a strong multi-channel distribution network, it has successfully developed a robust model for distribution of third party products like mutual funds, Reserve Bank of India (RBI) relief bonds, and insurance products, with market leadership in these areas. This model also allows it to meet all customer needs by offering the customer the complete basket of financial products, while leveraging its distribution capability to earn fee income from third parties.

Online Trading

ICICI direct (www.icicidirect.com) is the market leader in Internet based share trading, with complete end-to-end integration for seamless electronic trading on stock exchanges. ICICI direct has a rating of "TXA1" from CRISIL, indicating highest ability to service broking transactions. During the year, ICICI direct launched online trading in the derivatives segment of the NSE.

Question

1. What problem Mr. Bhargava Dasgupta is facing in this case?
2. What recommendations will you make to Mr. Bhargava Dasgupta? Should he go global? Give your reasons.

Source: www.icicibank.com/

8.5 Summary

- Corporate banking represents a wide range of banking and financial services provided to domestic and international operations of large local corporates and local operations of multinational corporations.
- Price is a mechanism to cover the costs of operations which comprises of production costs, distribution costs, promotion costs, and other operational expenses.
- The transition from sellers market to buyers market has compelled the bankers to understand the pulse and needs of the customers. With interest deregulation in the sector of deposits with the sole exception of Savings Bank Account, where the apex monetary authority continues to decide the rate of interest, rest of the fields are open for competition.
- Monitoring of the account is easier in retail lending segment as compared to the conventional advances, for the reason that installments and repayment schedule have to be monitored in respect of retail lending.
- The contribution brought in by the borrower is termed as margin. Margin requirements differ from one type of finance to others and they differ from one bank to the other.
- Merchant Banking is a combination of banking and consultancy services that banks provide to its customers.
- The concept of venture financing became more popular during the sixties and seventies, when several private enterprises undertook the financing of high-risk and high reward projects.
- Merchant bankers provide advice on acquisition propositions after careful examination of all aspects.

Notes

- Treasury management can be described as the management of cash, funds, currency, bank and financial risk. That's why it is an imperative tool of finance. Cash inflows and outflows are checked by finance manager.

8.6 Keywords

Benchmark Prime Lending Rate (BPLR): The BPLR is the interest rate that commercial banks charge their most credit-worthy customers.

Core Banking Solutions: Core banking is a term used to describe the services provided by a group of interconnected bank branches.

Export-Import Banks: It is the principal financial institution in the country for coordinating the working of institutions engaged in financing exports and imports.

Floating Rate Certificates of Deposits (FRCDs): A floating rate certificate of deposit issued by a bank that pays a monthly, quarterly, semi-annual, or annual coupon based on a floating interest rate.

Floating Rate Notes (FRN): A floating rate note, often called an FRN or "floater", is a debt instrument that pays a floating interest rate.

Lease: A lease is a contractual arrangement calling for the lessee (user) to pay the lessor (owner) for use of an asset.

London Interbank Bid Rate (LIB/D): The average interest rate which major London banks borrow Eurocurrency deposits from other banks.

Technical Consultancy Organization (TCO): Technical Consultancy Organisations (TCOs) were created for facilitating technical consultancy for industrial projects.

8.7 Review Questions

1. Write short note on corporate banking.
2. What kinds of services are offered by corporate banking?
3. What do you understand by retail lending schemes?
4. Briefly describe saving accounts.
5. Define merchant banking. Explain significance and its functions.
6. What type of loans is issued on foreign currency?
7. What do you mean by treasury management?
8. Write an essay on the objectives and functions of treasury management.
9. Describe portfolio management.
10. What activities are included in corporate counselling?

Answers: Self Assessment

1.	False	2.	False
3.	True	4.	True
5.	Finance	6.	currency risk
7.	liquidity	8.	False