

# Strategic Diversification : A Case of a National Bank

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## Abstract

Profit is essential for survival of any organization, which depends on a number of sector-specific factors. The present case related to National Bank, which felt the impact on profitability, on account of over dependence on corporate sector for its business. Alarmed with diminishing profitability, the bank undertook a slew of measures under "Project Akash" for increasing retail credit. These measures included establishing specialized retail centres and marketing setup for processing of retail loans, tie-ups with auto dealers, builders, and educational institutes along with promotion campaigns. The project did not deliver the results as anticipated by the management of the bank. When the management got into the nitty gritty of affairs, it realized that the project launched with a single objective had many ramifications, which needed to be probed further. These included customer service, human resources, marketing setup, operations, and many others. The management of the bank resolved to make the project successful.

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The MD & CEO of National Bank, Mr. Deepak Bhat was finding difficulty in answering questions posed by the analysts regarding the performance of the bank for the financial Year 2016-2017. The bank was in news for all the wrong reasons during the year. In its 77 years of existence, the bank suffered a net loss for the first time in any quarter, which occurred in the second quarter of FY 2016-2017. The bank posted a net loss of ₹ 520 crores. The MD & CEO then stated to the press that it was a transient phase, and the bank would return to black in the very next quarter. The analyst referred to the same statement of Mr. Bhat, for which he had no satisfactory answer, as the bank's net loss increased to ₹ 1076 crores in third quarter and ₹ 2345 crores in the last quarter [1].

## Brief Profile of National Bank

National Bank was founded on March 2, 1940 by a group of traders in Surat with a paid up capital of ₹ 20 lakhs and 30 employees. The bank made rapid progress touching new milestones. The present strength of workforce as on March 2017 was 43528 and business mix of the bank was ₹ 8.50 lakh crores (Deposits ₹ 5.20 lakh crores &

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[1] This case is based on a hypothetical strategic problem facing a bank, which is very relevant as banks face various types of risks in course of their business, one of which is concentration risk, that is, depending on a particular segment for its growth in business or profits.

Advances of ₹ 3.30 lakh crores). The bank was later nationalized in the year 1969. Starting from Surat, the bank went on an expansion spree as all things worked well for the bank . The total count of the branches crossed the magical figure of 6000 to 6013 in FY 2016-2017, including 33 branches abroad. The prime focus of the bank was corporate as reflected in its punch line starting with, “The Preferred Bank for Corporates” (1940), “Good Bank for Corporates” (1962).

Gradually, the bank's management realized that the bank cannot survive catering to the need of one niche. This was reflected well in punch line “The Bank for All,” which was coined during the tenure of Mr. Harsh Malya, predecessor to Mr. Bhat in 2010.

## The Problem

The over dependence on corporates for both deposits & advances took a toll on the profitability of the bank impacting the NIM (net interest margin) due to cut throat competition for business in this sector. NIM is a measure of difference between interest income generated and paid relative to the amount of interest income generating assets. The bank, in order to protect its image as a leader in corporate lending, aggressively pursued this sector. This factor coupled with rapid expansion and increasing operating expenses lead to a dent in profitability. The impact on profitability can be seen from the trends over the years as depicted in Table 1.

**Table 1. Profitability Trend from 2009 - 2017 of National Bank**

Financial Year	Operating Profit (Amt in ₹ Crores)	Net Profit (Amt in ₹ Crores)
2009-2010	8345	3482
2010-2011	7326	2890
2011-2012	7110	2532
2012-2013	7030	2276
2013-2014	6983	2123
2014-2015	6542	1854
2015-2016	6384	1756
2016-2017	5987	-3669

Note : Hypothetical figures developed for the case study

The heat of competition in the corporate sector was felt by the bank as corporates engage banks in competition for rates in bulk loans and deposits. The bank was exposed to concentration risk on account of over dependence on the corporate sector. The NPAs (non performing assets) in the corporate sector were rising as the economy was passing through a recessionary phase. The maximum exposure of the bank was in infrastructure, which was under stress due to stalled projects awaiting clearances from government authorities.

The over dependence of the bank on corporate lending was recognized by Mr. Harsh Malya, who launched Project Akash with much fanfare. The objective of Project Akash was to gradually reduce the percentage of corporate in total advances from 60% (FY 2009-2010) to 40%, with a simultaneous increase in core retail from 8% (FY 2009-2010) to 25% by March 2017.

## Potential of Retail

As opposed to the corporate sector, the retail sector is burgeoning and offers many advantages on account of the following reasons :

**(1)** The disposable income in India is rising, leading to an increase in spending on vehicles, housing, consumer durables, etc. The number of households with double income is increasing, thus increasing scope for retail lending.

**(2)** The general perception towards loans is changing. Earlier, people used to be credit averse and believed in living by their means. Now, they believe in consumption for which they are eager to borrow. The trend on spending and saving can be better understood in words of Mr. Rajesh Iyer, Branch Manager of TT Nagar Branch of National Bank..., "When I enquire from a typical gen Y working customer about current banking facilities, he/she tells about all the loans he/she has availed, but when asked about savings, he/she says it is nominal."

**(3)** The perception to own a house has undergone a drastic change. Earlier, people used to think about owning a house at the fag end of their service or after retirement, investing all retirement benefits to own a house ; whereas, now, a person starts thinking about owning a house from the day he/she gets a job.

**(4)** There are many reasons for growth of housing loans like rising rental income, prompting people to purchase a house for saving rentals or getting rental income. This coupled with the feeling of owning an asset resulted in rapid growth of housing loans. There are tax benefits also on principal as well as the interest component.

**(5)** Retail loans also offer an opportunity for building long term relationships with customers. For example, a student who avails an education loan is likely to give the same account number for salary when he/she gets employed and is a potential customer to avail other loans later.

**(6)** Retail loans also offer an opportunity for cross selling. Cross selling is offering one product with another. For example, selling life insurance along with housing loan, which covers the loan liability. There are many advantages of cross selling like low transaction costs and augmentation of non interest income. Non interest income is income earned other than what is earned from credit. National Bank has tie-up with Sterling Insurance Ltd. for selling their insurance products.

**(7)** Retail lending leads to diversification of risk as it involves a small quantum of loan to a large number of customers as compared to corporate lending. National Bank was already grappling with rising NPAs in the corporate sector and was trying to reduce overall exposure in it.

**(8)** Retail lending is a profitable venture as customers lack bargaining power ; so, margins are better as compared to what they are in corporate lending.

## **Project Akash**

**(1)** The project was undertaken to increase the share of retail credit in total advances of the bank. A number of initiatives were taken under the project such as :

**(i)** Setting up of retail loan centers at major centres where processing of retail loans was centralized. The sanctioning and documentation part of retail loans for cluster of branches at these centres was done by these retail centres. These centres dealt with housing loan, vehicle loan, education loan, and mortgage loan. The branches other than those covered by these centres sanctioned retail loans at their level.

**(ii)** Setting up of the marketing team exclusively for retail loans at retail loan centres. The role of marketing staff envisaged under the project was to generate new leads. The marketing staff had to submit weekly sales reports on

business generated to the marketing head at the regional office of the bank.

**(iii)** Tie up with builders, auto dealers, educational institutes for retail loans. The objective of this initiative was lead generation for housing loan, vehicle loan, and education loan for conversion to actual sales by the marketing staff.

**(iv)** Aggressive promotional campaigns highlighting low TAT (turn around time – time for sanction / processing of loan).

**(v)** Aggressive promotional campaign in print and on TV highlighting low TAT.

**(2) Performance Under Project Akash :** The performance under the project was a total debacle as the performance was not as envisaged under the project. While analyzing the performance, the core retail as percentage of total advances was 12%, that is, not even half of what was projected for 2016-2017. The initiatives under this project did not deliver the results as per the management's expectations. The feedback received by the management regarding performance of the marketing staff was also not encouraging as the branches complained about reporting of business generated by them being reported by the marketing staff in their weekly sales reports. Feedback on retail centres received with regard to processes regarding the business, that is, tie - up arrangement with builders, auto dealers, and educational institutes was also minuscule.

**(3) Reasons for Failure of Project Akash :** When the management tried to ascertain the reasons for failure of the project, the following findings emerged :

**(i)** The retail centres set up by the bank for specialization in processing of retail were perceived as too mechanical by the customers. The warmth and relationship enjoyed by the customers at the branches was felt lacking by them. As stated by Mr. Jagdish Sharma, a customer of Janpath branch in Delhi, who shared his experience with the retail centre. "It was like shifting my account to a new bank and starting my relationship afresh." The branch was supposed to collect documents from the customers and send it to the retail centres ; whereas, a majority of the branches performed the role of traffic police directing customers to the retail centres. After the sanction of loans, the customers had to come to these centres for documentation, which caused inconvenience to far away customers.

**(ii)** The role envisaged under the project for marketing staff was new lead generation ; whereas, they reported the business referred by the branches in their sales report. Their role was to generate lead collect documents from customers and carry out pre-sanction inspection. The marketing staff had no decision-making authority regarding the loan.

This set up created bone of contention between the marketing and processing staff. As in the words of Mr. Ashok Chauhan, processing officer at retail centre in Pune, "The stuff brought by the marketing staff is useless, which is rejected by other banks."

**(iii)** The tie up arrangement with auto dealers and builders proved to be a total debacle as most of the private sector players offered commission on volume of business generated by them. The quantum of business generated through this channel was insignificant .

**(iv)** The management of National Bank mooted an incentive scheme for marketing staff to motivate and bring competitiveness, but this was vehemently opposed by the officer and clerical staff unions.

**(v)** The campaigns run on TV, FM radio, & print media highlighted the turn around time for sanctioning/processing of retail loans. One of the commercials showed a person fed up of not being able to get into the bus on account of rush, and the customer just walks into a branch of the bank and is approved a vehicle loan instantly. Whereas, the real time customer experience regarding TAT in most of the branches and some of the retail centres was just the opposite. This was on account of the fear psychosis developed across the rank and file of the bank as the bank grappled with large slippages and punished the staff for minor lapses in credit proposals.

**(vi)** The dependence on corporate business affected the pricing of retail products as approximately 40% of the total deposits (5.20 lakh crores) consisted of bulk deposits mobilized from corporates above the card rate (normal rate).

**(vii)** The marketing staff was drawn from the branches serviced by the retail centres. The names of the marketing staff were given by the branches, who took this opportunity to shunt their non performing / troublesome staff.

## **Challenges**

There were a number of challenges to be addressed by the management of National Bank.

**(i)** The first and foremost challenge was to select the right person with aptitude for marketing.

**(ii)** The other issue was of motivating marketing and branch staff for business mobilization.

**(iii)** There was annual performance review, but business performance was given less weight, and more emphasis was given to conduct of the employees. There was scope for appraiser to give good evaluation to appraisee even when the business performance was poor. This led to pleasing the boss culture instead of performance culture.

**(iv)** The other challenge identified was the removal of fear psychosis developed in the bank staff on account of harsh punishment served for minor lapses as the bank was grappled with rising NPAs.

**(v)** The other issue was upgrading skills of staff so that they can handle customer queries confidently and mobilize business for the bank.

**(vi)** Develop performance culture as the present system of appraisal did not distinguish between performer and non - performer. The non performance of staff could be masked under conduct related evaluation parameters.

**(vii)** Effective customer service at branches and retail centres was needed.

**(viii)** Improving TAT (turn around time).

**(ix)** There were other issues like effective monitoring of marketing staff and changing perception of customers about retail centres.

**(x)** Another important issue was how to match customer expectations formed on the basis of corporate communication with actual service delivery.

## The Road Ahead

After a hectic analysis, Mr. Bhat was in a reflective mood in his cozy chamber about what went wrong - whether it was strategy and planning part or implementation part. Suddenly, a sense of confidence crept into his thoughts that when a bank having a legacy of 77 years starting with paid up capital of ₹ 20 lakhs survived facing challenges posed by the environment, it could rise again now also. He resolved that he would prove analysts wrong and immediately called a meeting of all the General Managers to let the Project Akash kiss the sky.

## Questions/ Issues

- (i) Identify the main issues in the case.
- (ii) Prioritize the problems faced by the National Bank.
- (iii) Whether the initiatives taken under Project Akash by National Bank are sufficient or else what additional initiatives are to be undertaken by the bank?
- (iv) What corrective measures should the bank undertake to make Project Akash successful?

## Managerial Implications

The present case study highlights the importance of spade work in terms of strategic planning and its execution. It also brings forth concentration risk, that is, depending upon one sector for business and profitability can be disastrous. Profit is essential for survival and growth of any organization and it should protect its margins according to changes in its environment, for which it must continuously adapt its strategy. For planning and implementing strategy, the organization must carefully evaluate the present position and the desired outcomes and the means to achieve them. This planning must include all aspects like market research, available resources, monitoring mechanism, involvement of all stakeholders, customer feedback to name a few. Execution of a strategy without proper planning will only lead to a fiasco.

## Teaching Notes

**(1) Synopsis :** Profit is essential for survival of any organization, which depends upon a number of sector-specific factors. The present case relates to National Bank, which felt the impact on profitability, on account of over dependence on corporate sector for its business. Alarmed with diminishing profitability, the bank undertook a slew of measures under “Project Akash” for increasing retail credit. These measures included establishing specialized retail centres and marketing setup for processing of retail loans, tie-ups with auto dealers, builders, and educational institutes along with promotion campaigns. The project did not deliver the results as anticipated by the management of the bank. When the management got into the nitty-gritty of affairs, it realized that the project launched with a single objective had many ramifications, which needed to be probed further. These included customer service, human resources, marketing setup, operations, and many others. The management of the bank resolved to make the project successful.

**(2) Learning Objectives :** This case study may seem to focus on a particular problem of profitability, however, it encompasses all aspects of management. At the end of this exercise, the participants should have an understanding

of the following issues :

- (i) Importance of involving all stakeholders in strategy formulation.
- (ii) Importance of feedback from customers.
- (iii) The importance of performance appraisal and its role in developing performance culture.
- (iv) Resolution of conflict of interest among different departments.
- (v) The importance selecting the right person with right aptitude for the task.
- (vi) The need to match customer expectation formed on the basis of corporate communication and actual service delivery.

**(3) Teaching Plan :** The following are the questions or issues that can be used for discussion of the case along with tentative time slot for each .

- (i) Identify the main issues in the case (15 minutes).
- (ii) Prioritize the problems faced by the National Bank (15 minutes).
- (iii) Whether the initiatives taken under Project Akash by National Bank are sufficient or what according to you would be the additional initiatives to be taken by the bank (20 minutes).
- (iv) What corrective measures should the bank undertake to make Project Akash successful (30 minutes).

This may include specific questions like :

- (i) What could be the measures to reduce TAT ?
- (ii) What operational changes should be made in functioning of retail centres ?
- (iii) How performance culture can be developed in the bank?
- (iv) What criteria should the bank consider for selection of marketing staff?

- (i) **Relevant Programs:** Strategic Management, Risk Management, Retail Banking
- (ii) **Courses :** Strategic planning and implementation ; banking risk and mitigants.

## **Suggestive Readings**

- (i) Gopinath, M. N. (2014). *Banking principles and operations*. Mumbai : Snow White Publications.
- (ii) Agarwal, O.P. (2016). *Retail banking in India*. New Delhi : Skylark Publications.

## **Disclaimer**

This case was prepared by the author for the sole purpose of aiding classroom discussion. Cases are not intended to serve as endorsements, or sources of data, or illustrations of effective or ineffective management. This case is

based on a hypothetical strategic problem facing a bank, which is very relevant as banks face various types of risks in the course of their business, one of which is concentration risk, that is, depending on a particular segment for its growth in business or profits.

### **About the Author**

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