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The Internet Potential

Any sound practice is obviously based on equally sound theoretical foundations. It is quite common to hear from seminar participants that they are practitioners and that the theoretical presentations are not of much relevance when it comes to solving so-called practical problems. The fact is that in the financial services sector, most of the practices have a sound legal and, perhaps, even a sounder economic basis. We may not be made constantly aware of it, but for the management to ignore the basics would be a colossal mistake. This is amply borne out by the professed ignorance of senior executives about the products, which were being originated and distributed by their own organizations. To blame the dealers and their indulgent bosses is of no use at all. The fact remains that every one was a party to these decisions and that the aim was to secure maximum bonus possible.

This chapter is an attempt at analyzing the economic values created by the internet and how to use it appropriately.

This chapter has been divided into two parts. Part 1 briefly reviews the management objectives for the massive technology upgrades and the expenses involved in introducing the new technology. Although the internet has been in use in the financial system of advanced countries for quite sometime, there is a feeling that the full potential is not being realized even there. In India, one is led to believe that this upgradation has been more a result of introduction of core banking solutions rather than a conscious decision arrived at because the banks and financial institutions wanted to achieve a given set of objectives or met a genuine customer need. This is clear when one looks at the nebulous objectives like 'Anytime Anywhere banking'. Therefore, this chapter begins with an

analysis of the stated objectives. Unfortunately, the data required for quantitative assessment is not available and we are not able to verify how far the stated objectives have been achieved.

The objectives:

- The main thrust of the banks and financial institutions, in the initial stages, was on meeting the competition from a few banks like HDFC, Citibank and HSBC, which had started offering these services. Therefore, internet-banking facilities were offered to retain and, possibly, to attract the technology savvy customers from the growing IT sector in the country. Some banks in the cooperative sector are even now trying to entice the younger customers by these means.
- Many banks had offered voluntary retirement schemes and were looking for ways to harness the technology support for handling the increased workload or even in handling the existing workload.
- In many public sector banks, the costs of routine transactions like cash receipts and payments, were unusually high because of the staff costs and they had to minimize these to ensure that the customers took to meeting their transaction needs through the ATMs and internet. It was pretty obvious that transaction costs were far too low when the internet was made use of.
- Branch expansion was a costly proposition and efforts had to be made to see that the existing premises were put to proper use while avoiding over crowding.
- Last but not the least, was the convenience offered to customers. The customers who opted for such facilities had the comfort of transacting from anywhere.

The Internet Economics

At one time, exaggerated claims were made and some theoreticians went to the extent of saying that all that was taught at management courses under subjects like 'managerial economics' was made redundant by the technology developments. There were also tall claims made that bank branches would be closed down and that most banking needs would be met through electronic transactions. The hope was that a few corner shops or kiosks in super markets could meet the needs of 80–90 per cent of the customers. However, the hopes raised by the early success of stand-alone e-banks were soon proved too exaggerated. Soon leading journals began to focus on the failure of these entities. There was a quick transition by

established entities to a new business model viz. 'brick and click' model. This model is currently being followed by most of the banks and financial institutions. They would have to strain to ensure migration of customers to the electronic medium.

In this chapter standard micro economic concepts have been used to examine how value is created on the internet and how this value can be captured. The internet creates value by vastly reducing the costs of transferring information, on a one-to-one, one-to-many or even many-to-many basis. In cases where the product itself is information, the potential for value creation is enormous. In financial services no physical products are involved. Hence, the product or service has significant value content.

It is important to make a comparison between different forms of interaction: personal and internet. This is particularly relevant in a branch setting. It is true that internet interaction is less personal than human interaction., yet it has several characteristics that make it potentially much more valuable in many cases.

- A lot of information can be provided at low cost. Investors can have access to live or recorded interviews with executive officials of an organization, a review of the reports filed with various statutory authorities, and so on. The economies of scale for providing the content, almost globally, make it entirely different from other modes of information transmission.
- The internet allows considerable flexibility in dealing with information. There is a far greater interactivity and search capability than any catalogue or brochure.
- Information access can take place at any time the investor desires and is very useful in differing time zones.
- Value can be created with internet communication either through reduced costs (the supply side) or on the demand side by improving the match between the buyer preference and the goods he may need or want.
- Information about goods comes from the availability of material through various catalogues, histories of consumer purchases comparisons and through aggregators. Customers get annoyed if unsolicited offers are made to them.

It is important to focus on some basic questions like the changing nature of the firm and the intangible products. The previously separate activities of telecommunication, informatics and audio-visual media are crumbling,

and there is a considerable overlap. Time honoured distinctions between home and work place, and intermediate goods and finished products are getting blurred. The intangible economy follows the rules of fuzzy logic of overlap rather than the exclusivity of binary logic.

The aforementioned changes have profoundly affected the production relationships, as also the asymmetry between producers and consumers. The customer, unlike in the past, is no longer ignorant. His decisions are based on information and he has not merely a wide choice but also sufficient guidance in reaching at conclusions. It further facilitates the process of unbundling production and assembly processes. The classic example of such unbundling is the drive in counters at McDonalds. The orders may appear to have been received at a given location, but actually, they are recorded some hundreds of miles away and are supplied in slightly lesser time than if they were received at the given location.

The intangible economy further changes, not only the fundamental nature of economic value, but also the value discovery and capture process. Neither production costs (full cost) nor marginal cost can be used as a guide (conventional economic theory models). It must be noted that, given the ease of replication, purchase does not equal consumption. The number of 'free riders' far exceeds the number of paying consumers. Another problem comes in because of what Stiglitz calls the 'infinite regress'—it is impossible to determine the value of a given piece of information without having this information. Traditionally the pricing of intangibles was a function of the support. The price of a book was determined by the quality of printing, number of pages, and so on. The content can now be priced separately from the support. There is considerable scope for price discrimination. The range of intangible pricing is getting broader and more complex. We are, at this stage, not looking at the pricing of internet services as such, the attention has veered round to pricing of services offered.

However, it appears that the financial services industry in India is not paying much attention to the pricing of these services. In spite of the cost advantages, banks and broking houses have not paid much attention to the charges levied. In fact, the normal method of marketing products is selling the software at almost negligible price and then charging for add-ons or selling a machine cheap and the contents to be priced in a manner that the costs of both are adequately recovered.

Banks are somewhat deficient in informing (some would say, training) their customers about the true state of affairs and more particularly the risk aspects of some newer products in which the banks were trading or offering to their clients. They were to say the least economical with truth. They

could certainly use the channel to increase the awareness about complex products. Further, they could also use the medium for educating the customers about the care that needs to be taken while using internet services. Merely sending out complex printed documents could perhaps absolve the financial institutions, but would it not be better to use more interesting methods to bring home the same message?

It must be pointed out that in a crisis situation sending messages about the solvency of the organization would and has, actually, fuelled more worries than dousing the panic fires. A bank CEOs' views on the current financial crisis would be viewed with greater interest and attention if they are transmitted in the right manner.

Equally important for a large number of customers is the need for a clear and authentic account of the nature of cyber crimes. Such incidents have a more telling effect than some complex instruction booklet. The bank could make the advisories free and charge suitably for the services rendered.

To conclude, it can be said that there is a need for the management to clearly spell out what it expects from the migration of customers to the internet. It also needs to spell out the basis for pricing decisions. The members of the staff who are to operate and market these services are many a time not aware of the rationale and do not take the required initiatives to publicize and market these facilities.