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   NEED/IMPORTANCE OF THE STUDY

   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

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INNOVATION IN FINANCIAL SERVICES: A STUDY OF FINANCIAL INSTITUTIONS

AMANDEEP KAUR SHAHI
ASST. PROFESSOR
RAYAT INSTITUTE OF MANAGEMENT
RAILMAJRA

KRITI AVASTHI
ASST. PROFESSOR
RAYAT INSTITUTE OF MANAGEMENT
RAILMAJRA

ABSTRACT

Innovation will be a major competitive battleground in the financial services industry. Innovation is more challenging for financial services firms than for other companies mostly because of short term financial pressure. The financial institutions- insurance, banking and financial services firms have a track record of innovative practices result in business success. Financial Institutions and the financial services industry are key to sustainability as they raise, allocate and price capital and provide risk coverage, influencing access to financing and risk protection and determining which government, business or individual activities get financed or protected against risks. The aim of the paper is to study the different types of financial services, to identify the importance and organizing of innovation in financial services of financial institutions and to find the various challenges of innovation in financial services faced by financial institutions. Exploratory design is to be used for research purpose. The study comprises 50 executives through questionnaire from banks, insurance companies and other financial Institutions of Chandigarh, Ropar and S.B.S. Nagar. The findings of the study are product innovation in financial services firms is most important and expect a growing role for business model innovation.

KEYWORDS

Business model, Challenges, Financial Institutions, Financial services, Innovative practices, Sustainability.

INTRODUCTION

Financial innovation as the act of creating and then popularizing new financial instruments, technologies, institutions, markets, processes and business models – including the new application of existing ideas in a different market context. It includes innovations across the financial world, whether their source is a regulated institution, a member of the wider financial community or shadow banking sector, or an individual inventor. However, no definition can quite capture the complexity of innovation in financial services where a single new product might bring together innovative features in terms of function, marketing and customer segment, and the supporting infrastructure. Another way to think about financial innovation is in terms of its function. Economists say that the overall function of financial innovation is to reduce financial market imperfections.Financial services innovation is important for the performance of the financial institutions. The financial institutions- insurance, banking and financial services firms have a track record of innovative practices that result in business success. The finance industry encompasses a broad range of organizations that deal with the management of money. They are a part of financial system consisting of financial institutions, financial markets, financial instruments and services that facilitate the transfer of funds. All four are interrelated. Among these organizations are banks, credit card companies, insurance companies, consumer finance companies, stock brokerages, investment funds and some government sponsored enterprises. For example, merchant bankers provide services for issuing financial products such as equity shares, bonds and debentures, while stock brokers provide services to the investors in the buying and selling of securities in stock exchanges.

Financial services firms have traditionally paid little attention to the poor because by definition the poor have limited assets. Informality, insufficient information, inadequate infrastructure and other barriers have reinforced the belief that serving the poor cannot be commercially viable, much less a driver of innovation. New, Lower cost business models have begun to challenge this conclusion, relying for instance on innovations in technology and utilization of existing retail channels. A wide range of examples shows the power of information and communications technology to reduce distribution and customer service costs, including the village ATM's of Citi bank and ICICI bank in India and the mobile transaction services of Wizzit and MTN banking in South Africa, Smart Communications and Globe Telecom in the Philippines, Celpay in Zambia and the Democratic republic of Congo and Vodafone and Safaricom in Kenya. Interestingly Wizzit and Globe Telecom provide financial services without associating with a bank or other financial institution, thus eliminating the need for the poor to hold bank accounts in order to pay bills, transfer funds and deposit or withdraw cash (Sutton and Jenkins 2007).

TABLE 1: FUNCTIONS OF FINANCIAL INNOVATION

Functions	Examples
To provide ways of clearing and settling payments to facilitate trade	Credit and debit cards, PayPal, stock exchanges
To provide mechanisms for the pooling of resources and for the subdividing of shares in various enterprises	Mutual funds, securitization
To provide ways to transfer economic resources through time, across borders and among industries	Savings accounts, loans
To provide ways of managing risk	Insurance, many derivatives
To provide price information to help coordinate decentralized decision-making in various sectors of the economy	Contracting by venture capital firms
To provide ways of dealing with the incentive problem created when one party to a transaction has information that the other party does not or when one party acts as agent for another	Price signals, extracting default probabilities from credit default swaps (CDS)

Source - Merton 1995

TYPES OF FINANCIAL INNOVATION

Several of the articles suggest and use typologies of what is included in the concept "innovation" in service firms. Some of these typologies specify in what part of the service firm innovation takes place. Hipp et al. (2000) make a distinction between three types of innovations:

1 Service Innovations, which include innovation in the service offer per se in the form of introductions of new or significantly improved services;

2 Process Innovations, which include new and improved work methods in the process by which a specific service is produced; and

3 Organizational Innovations, which is not limited to the individual service production process but includes significant improvements in wider organizational structures or processes.

According to OECD (2005) the types of innovation are as:

i. Product innovation

ii. Process innovation

iii. Marketing innovation

iv. Organizational innovation

Importantly, in relation to the focus on financial services, the manual's definition embraces innovative services as well as physical products and technologies, and includes significant improvements to existing products and services as well as truly revolutionary ideas.

"A product innovation is the introduction of a good or service that is new or significantly improved with respect to its characteristics or intended uses. This includes significant improvements in technical specifications, components and materials, incorporated software, user friendliness or other functional characteristics. Product innovations can utilise new knowledge or technologies, or can be based on new uses or combinations of existing knowledge or technologies. The term "product" is used to cover both goods and services."

• "A process innovation is the implementation of a new or significantly improved production or delivery method. This includes significant changes in techniques, equipment and/or software. Process innovations can be intended to decrease unit costs of production or delivery, to increase quality, or to produce or deliver new or significantly improved products."

• "A marketing innovation is the implementation of a new marketing method involving significant changes in product design or packaging, product placement, product promotion or pricing. Marketing innovations are aimed at better addressing customer needs, opening up new markets, or newly positioning a firm's product on the market, with the objective of increasing the firm's sales."

• "An organizational innovation is the implementation of a new organizational method in the firm's business practices, workplace organization or external relations. Organizational innovations can be intended to increase a firm's performance by reducing administrative costs or transaction costs, improving workplace satisfaction (and thus labour productivity), gaining access to non-tradable assets (such as non-codified external knowledge) or reducing costs of supplies."

LITERATURE REVIEW

Verghese (1990) identified the lessons of financial change and innovation in foreign markets offer to countries like India in shaping our future financial policies. There has been a proliferation of new financial products and techniques. Financial products with complex interlink ages between foreign exchange markets, money markets, capital markets and equity markets are being incessantly created, sophisticated and discarded. The distinction between different sectors of the market and different types of financial institutions has eroded. Banks are increasingly taking on non-banking financial activities while banking activities are being undertaken by non-banking financial institutions. Non-financial corporate entities are offering a wide variety of financial services and earnings from financial engineering are contributing a growing share of their profit. Harker and Zenios (2000) explained the efficiency of financial markets, the efficient operation of financial intermediaries – banks, insurance, pension fund firms, government agencies and so on has been instrumental for the efficient functioning of the financial system. Federal Reserve Bank of Philadelphia (2002) stated that rapid innovation is changing the array of financial services and payment options available to customers. The study also examined the driving forces behind the surge of innovation and the adoption of new technology. Goerge and Prabhu (2003) defined developmental financial institutions in emerging economies regularly assess new technology platforms to support their investments in new ventures, established firms, and technology institutions. Their financing decisions are guided by national priorities such as achieving technological self-reliance. By providing attractive financing options and related support, Developmental Financial Institutions are well placed to consciously channel finance into designated priority technology areas. The study suggested that governments in emerging economies actively use their Developmental Financial Institutions as technology policy instruments to encourage investment in priority technology areas. Developmental Financial Institutions need to develop higher levels of expertise in understanding macro-level technology priorities to enable them to contribute to developing national innovative capacity. Cainelli *et al.* (2004) explored the relationship between innovation and financial performance in service firms. The study shows that innovating firms out-perform non-innovating firms in terms of productivity levels and economic growth. Productivity was also found to be linked to the amount of innovation expenditure. White and Frame (2006) examined that financial innovation is defined as a new product or service, a novel organizational form, or new processes that reduce costs or risks or that improve quality. Rapid innovation, they emphasize contributes to the dynamic efficiency of the financial sector, which ultimately affects the overall growth of the economy. Delimatsis (2008) found that issues raised by the nature of and the trade in RECs which can be of concern for the General Agreement on Trade in Services (GATS) and the multilateral regulation of trade in financial services, notably in the case where World Trade Organization (WTO) members undertook sweeping commitments in financial services which equally apply to trade in RECs..

RESEARCH METHODOLOGY

The study entitled, "Innovation in Financial services: A Study of Financial Institutions" is Descriptive in design. The study is based on primary data and secondary data. The Primary data was collected though questionnaire from the banks and financial institutions of the Chandigarh, Roapr and S.B.S. Nagar. The sample size of study was 50 executives. Secondary data were obtained from the published reports, journals, magazines, books and related websites. Tabular analysis technique was used to present the findings. Percentages and Charts were worked out to present the innovation in financial institutions.

ANALYSIS AND INTERPRETATION

FIGURE 1: IMPORTANCE OF INNOVATION

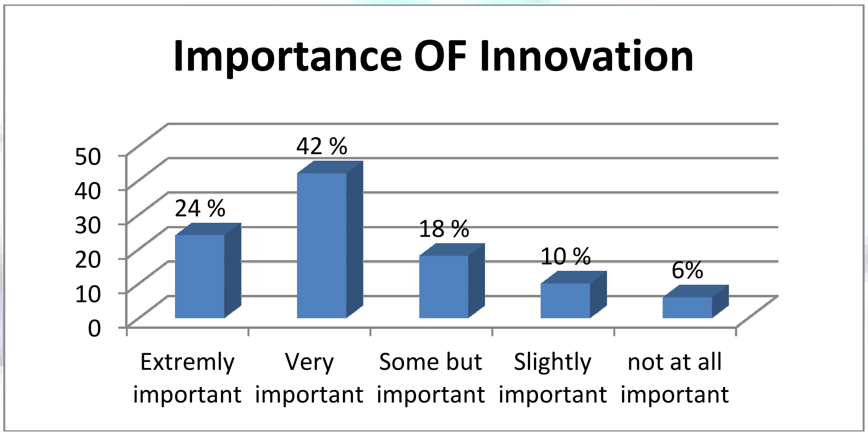

Figure 1 represents that 42 percent of executives said that innovation has been extremely important to the ability of their company to meet the profit. 24 percent executives said that innovation has been very important for the financial services companies. 18 percent executives say that it is important to some extent for the revenue generation of the companies. 10 percent respondents said that it is very slightly important and 6 percent executives said that there is not any importance of innovation in the financial services companies.

FIGURE 2: DISTRIBUTION OF INNOVATION ACTIVITY AND INVESTMENT

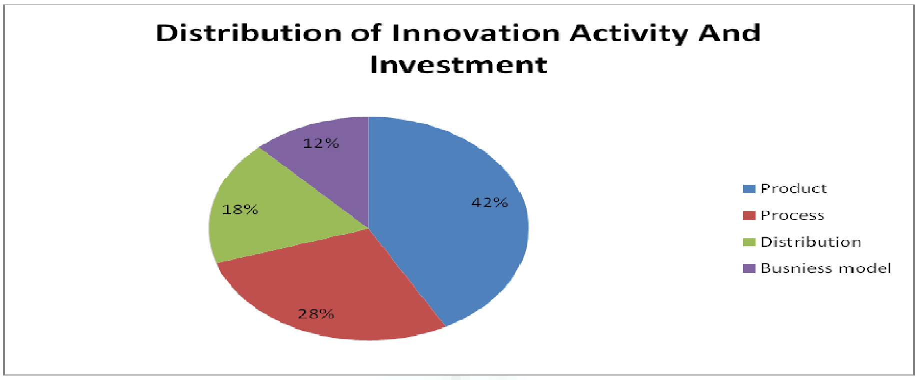

Figure 2 explains that 42 percent respondents said that they are spending money in product innovation, which will attract more consumers and compete with competitors with the variety of products. 28 percent executives spend in process activities, 18 percent executives invest in distribution activities for expand their services broader. 12 percent respondents invest in business model innovation, which expects a growing role in financial services innovation.

FIGURE 3: CHALLENGES FOR FINANCIAL SERVICES INSTITUTIONS

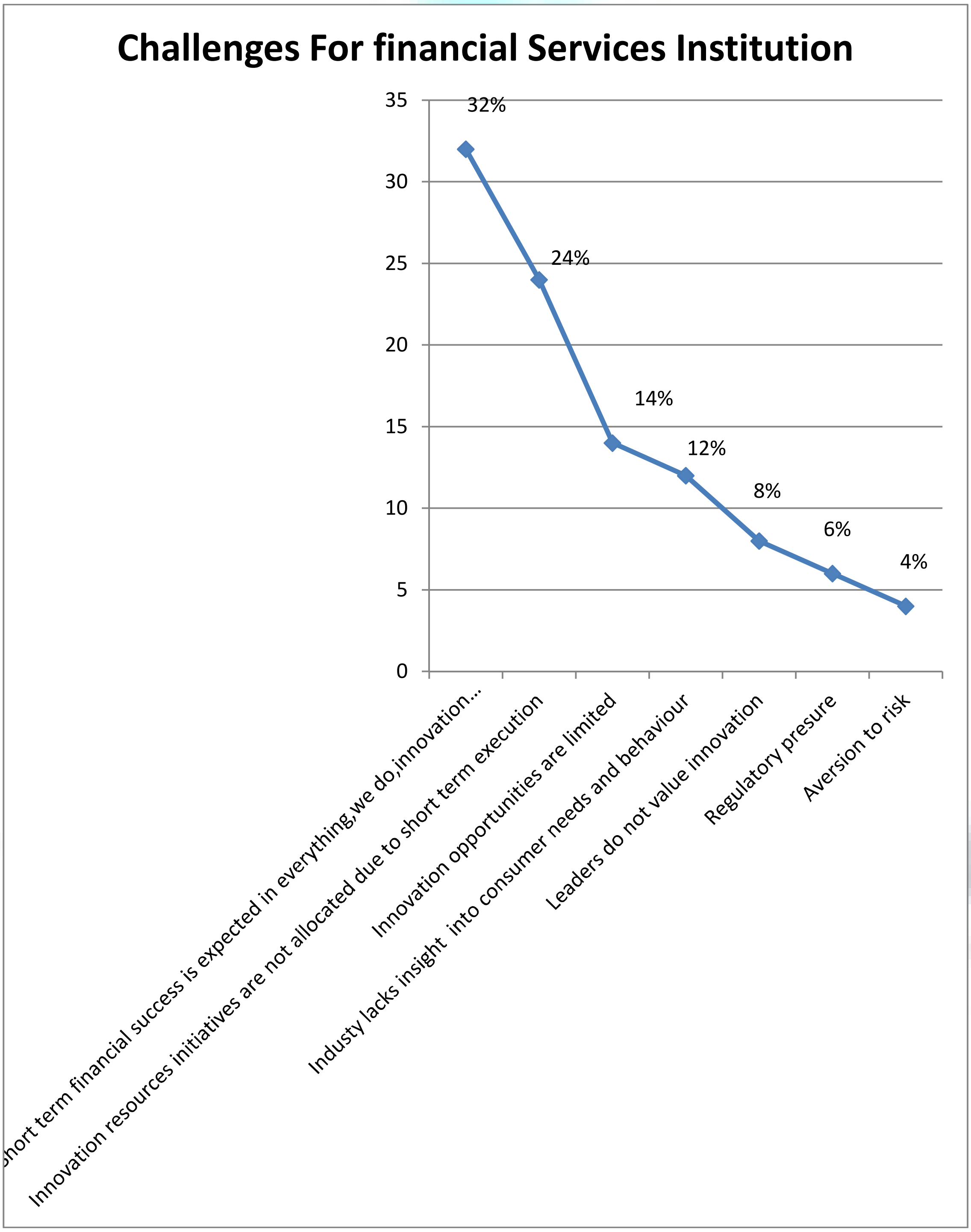

Figure 3 defines that innovation is more challenging for financial institutions than for other organizations mostly because of short term financial pressure. 32 percent executives say that financial services innovations are more challenging due to short term financial success is expected in everything we do; innovation initiatives often result in short term losses. 24 percent respondents said that the resources needed to pursue innovation initiatives are not allocated because these resources are critical to short term execution. 14 percent executives said that financial services innovations are challenging due to limited innovative opportunities, 12 percent executives said that industry lacks insight into consumer needs and behavior. 8 percent respondents said that financial services innovation are challenging because of leaders do not value \innovation, 6 percent said that it is challenging due to regulatory pressure and 4 percent say due to aversion of risk.

FIGURE 4: SOURCES OF IDEAS

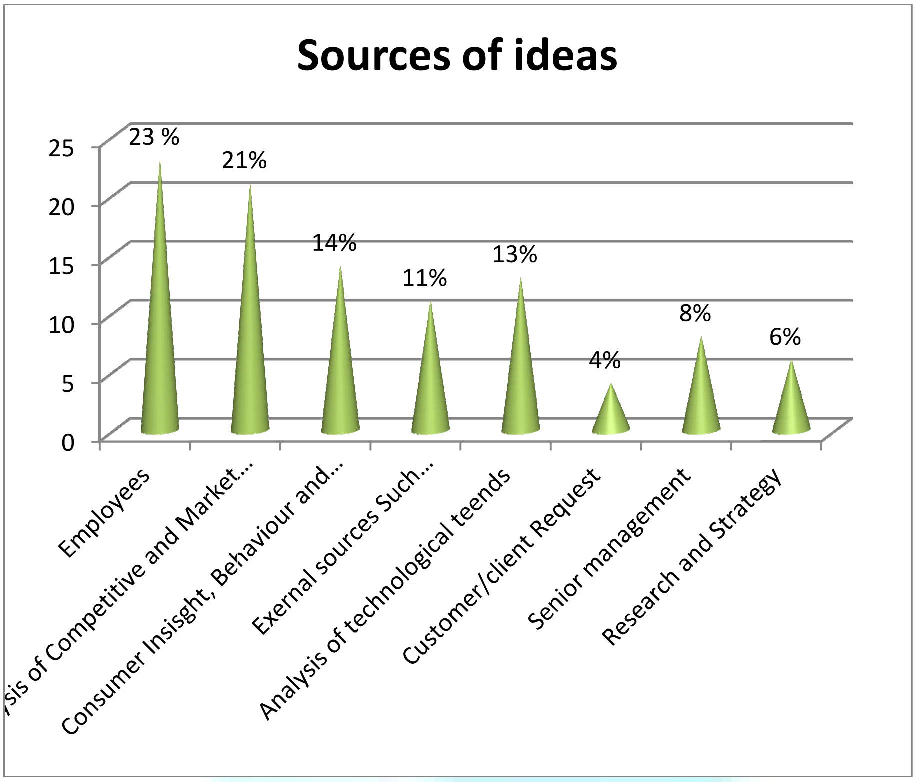

Figure 4 explains that when we asked the executives to select the most frequent sources of new ideas in their company 23 percent executives said that employees are the main source of innovative ideas.21 percent executives said reply that innovative ideas collected through analysis of competitive and market dynamics. 14 percent respondents said that consumer insights, behavior and trends are also a source of innovative idea. 11 percent said that external sources like partnerships, joint ventures or research institutions are source of innovative ideas. 13 percent executive said that technological trends are also source of innovative ideas. 8 percent respondents said that ideas are generated from senior management and CEO of the financial services companies.

FIGURE 5: ORGANIZING FOR INNOVATION

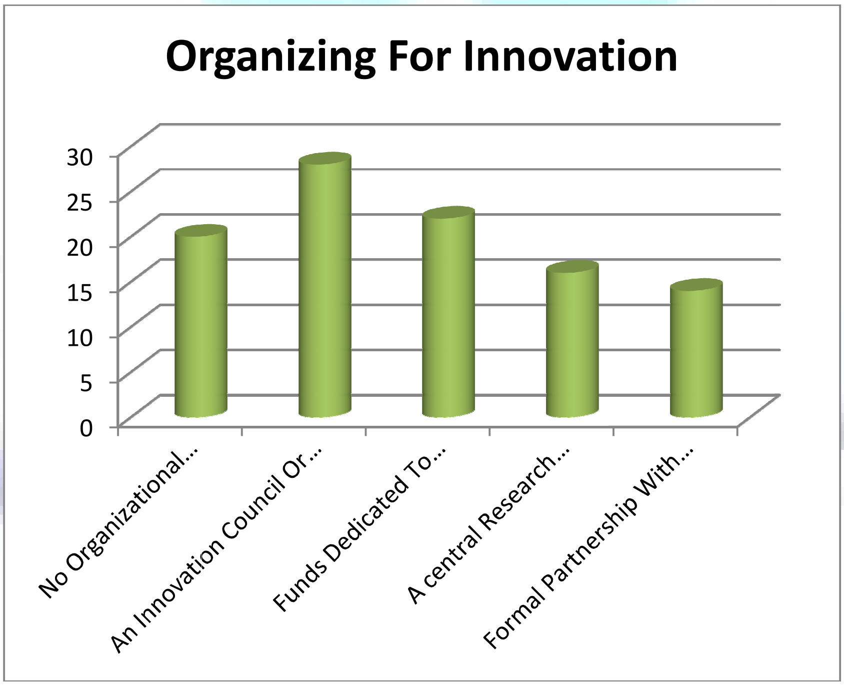

Figure 5 shows that executives indicate, that their companies have inadequate formal innovation structures. When asked to identify the barriers they face to commercializing innovations 20 percent respondents said that there are no organizational innovative mechanisms in their company, 28 percent executives felt that an innovative committee or council that reviews initiatives and their progress, 22 percent respondents replied that their companies have funds dedicated to innovation initiatives. 16 percent executives said that ideas suggested by other central research department or innovation center and 14 percent say that their companies have formal partnership with research centre and academics.

FIGURE 6: THE PERFORMANCE GAP

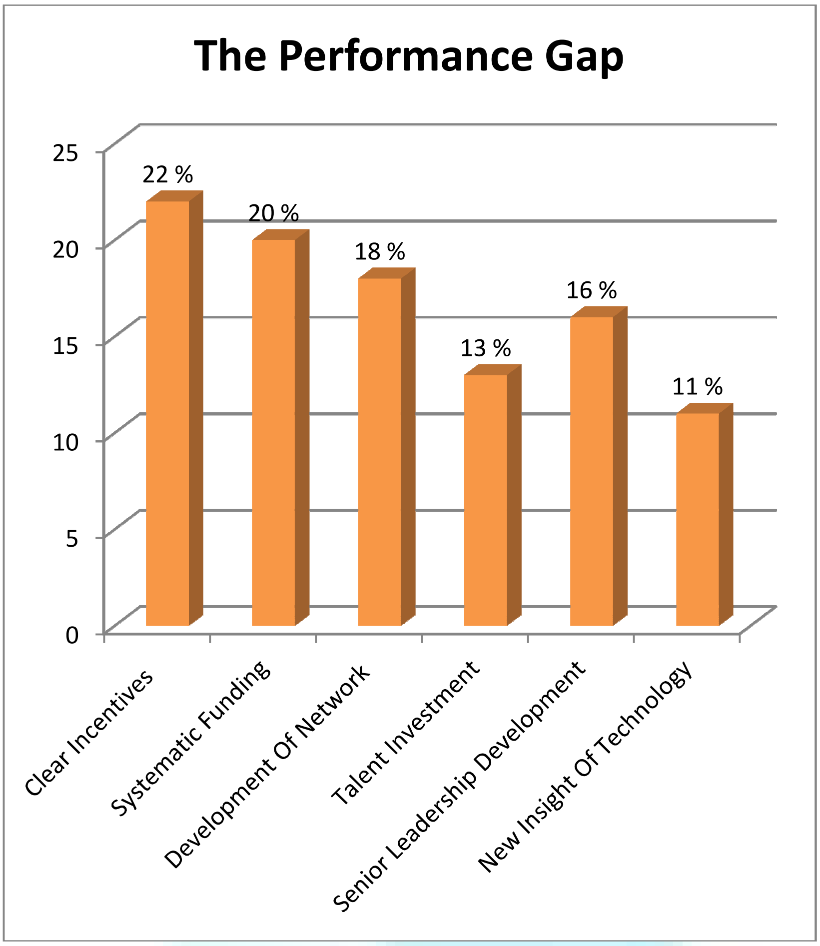

Figure 6 defines most executives see substantial opportunity for their company to improve performance in practices that most industries regard as vital for successful innovation. 22 percent executives said that they have focus on clear incentives and targets to innovate, 20 percent executives focused on systematic funding and innovation projects. 18 percent said that there is development of network of external partners to generate new ideas in their companies. 13 percent said about talent investment, 16 percent executives said about senior leadership development and 11 percent respondents focused on new insights of technology.

FINDINGS OF THE STUDY

Financial services executives said that innovation has been extremely important to the ability of their company to meet the profit. The study findings suggest that innovation will be a major competitive battleground in the financial services industry. Respondents who represent public and private firms in investment banking, insurance and other financial institutions conduct product innovation in financial services firms is most important and expects a growing role for business model innovation. The study finds that spending money in product innovation will attract more consumers and compete with competitors with the variety of products. Employees are the main source of innovative ideas. Innovative ideas collected through analysis of competitive and market dynamics. Innovative committee or council that reviews initiatives and progress of financial institutions which are helpful for organizing innovation. Most executives see substantial opportunity for their company to improve performance in practices that most industries regard as vital for successful innovation.

CONCLUSION

Innovative can have positive effects on service firms' performance. In the financial-services industry innovation as very important to the ability of their company to meet short- and long-term performance targets. The survey found a clear correlation between perceived importance and performance as more of the respondents who rated innovation as extremely or very important to their company believed they are more innovative than their competitors and peers. Innovation will be a major competitive battleground in the financial-services industry.

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