Understanding Agent Banking Strategy

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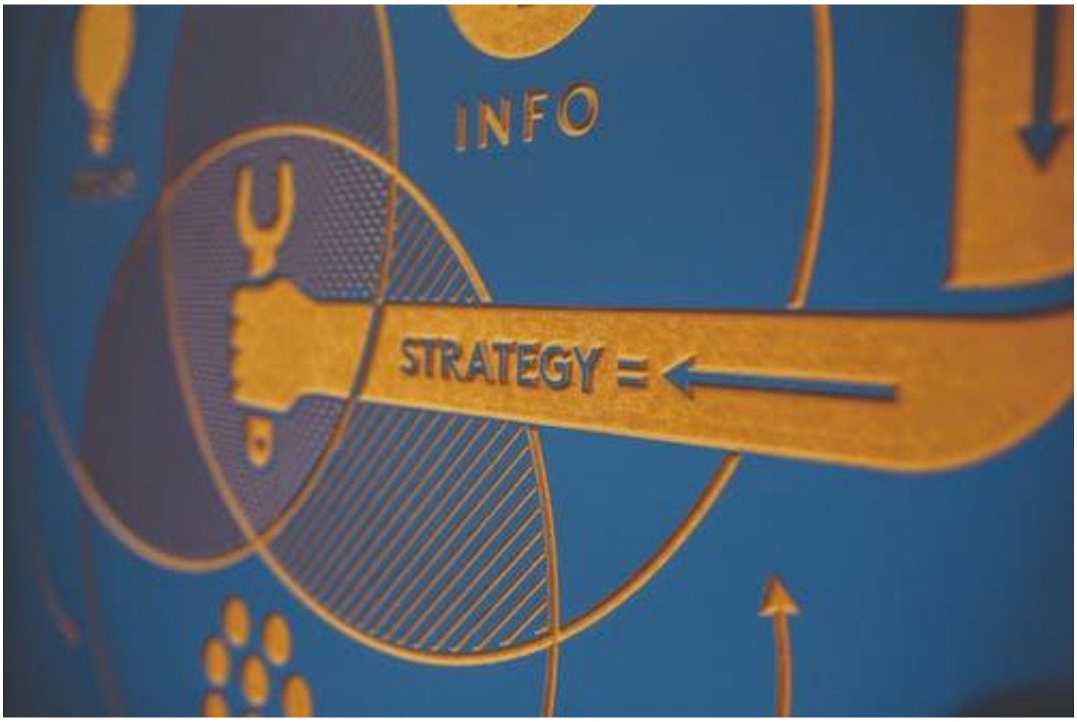

Agent banking has transformed financial access for millions in Africa and Asia, but despite this – many financial institutions are yet to exploit the potential of agency to provide better financial access for their customers. This blog has been written to help executives and boards understand agent banking strategy.

Changing landscape: Agent banking is a key component of the digital revolution in financial services. It represents the next evolution, for much of Africa and Asia, in retail banking channels, which can be traced from the issuance of cards in the 1950s, the launch of ATMs in 1969 and the microfinance movement of the 1990s onwards. Whilst financial institutions can process transactions digitally, much of the economy in Africa and Asia remains informal where 'cash is king' – this means in moving towards 'cash lite' economies - intermediaries are required to transition clients towards digital finance, through providing cash-in and cash out (CICO) services. Hence the importance of agent banking and mobile money.

Misconceptions: Whilst accepting the systemic importance of agent banking, many financial institutions either fail to implement agent banking, or have done so with limited success. This can be due to common misconceptions of agent banking, which lead a poorly implemented strategy.

a) Channel profitability: Agent banking is a low-cost channel, as such in the context of the bank as a channel, it neither makes nor loses significant funds. A focus on direct channel profitability will lead to an under-investment in the channel.

b) Channel strategy: Neither is agent banking a product – it is a channel that provides points of service and cash in and cash out to support a range of products and services. Therefore, product and marketing strategies are required to drive value and transactions through the channel.

Strategy formulation:

It is important to customise the agent banking strategy to the meet aspirations of the institution and the needs of its clients. This implies that banks servicing the mass retail market will implement agent banking differently from a bank focused on servicing a particular market segment, or a corporate finance bank.

i. Retail vs. corporate banking: Historically retail and corporate banking have been well defined and have operated distinct offering. With the digital finance revolution – it is possible to service many of the retail needs of corporate customers, and the business needs of retail customers.

ii. Customer acquisition: The rollout of digital identity is key to the viability of agent banking as it facilitates customer acquisition through agents. With the rollout of digital identity in Uganda, Centenary Bank acquired 400,000 new accounts within 9 months of launching agent banking[1].

iii. Product evolution: A range of products are serviced through agency channels, the strategy should outline the products which are expected to launch on the channel and how it is anticipated that products will evolve that use the channel.

iv. Channel evolution: Agent banking facilitates new ways to construct channels either in terms of reducing physical presence, or in opening services where establishing a branch would be uneconomic.

v. Transition to digital: Over time and with the development of additional products supported by digital channels, customers can be transitioned to digital channels where agents are used to support cash in and cash out, but other transactions happen through apps. Equity Bank Kenya now carries out 97% of its transactions digitally, with more than 600 million transactions in 2018 on their award-winning app[2].

Inter-related strategies

i. Institutional strategy: Agent banking must support the core institutional strategy, at least at inception, this ensures that agent banking is given a central position by the leaders of the institution and the requisite staffing and financial resources required for success. Over time agent banking may influence institutional strategy through supporting opportunities that did not exist earlier.

ii. Agent strategy: The agent strategy sets the distribution and nature of agents, whether agents will be owned by the bank – 'On Us', or to third parties or agent banking

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[1] Discussions with the author

[2] Investor briefs

platforms[3]- ‘Off Us’ or a combination of both. The agent strategy establishes agent qualification criteria, rollout rates, commission structures, agent support structures, and training.

iii. Marketing and communications strategy: Marketing messages and communications are set for the institution, and for delivery through agents. The strategy establishes outlet branding, signage, collaterals, distribution, and usage of collaterals. Messaging becomes important as local marketing and customer service is through the agent network.

iv. Product strategy: A standard launch offering focuses on cash in cash out, and a mobile app that facilitates bill payment and airtime top up. However, agent banking supports a range of products and services that drive transaction volumes or values. For example, supporting cash in and cash out for nano credit loans; or for providing locations for e-commerce deliveries; or for handling cash for FMCG distributors; or for providing solutions for agents themselves.

Financial modelling

Strategies are expressed in numbers. However, financial modelling for agent banking is unlike other forms of modelling a bank may use in two respects. Firstly, it relies upon understanding and modelling consumer behaviour to model transactions – given that this generates the commissions that supports the agent network. Modelling consumer behaviour implies a) understanding consumer behaviour can have a direct impact on product design and development and b) that the bank can influence customer behaviour through investing in deliberate activities, for example agent training. Secondly, it relies upon modelling the direct and indirect benefits derived from the channel. Typically, the business case for agent banking is derived mainly from indirect – not direct benefits.

Modelling: Direct Benefits

Direct benefits are calculated from the fee incomes less costs earned from the channel. This calculation is volume centric, and only returns significant profits at high volume. Typically, customers pay for withdrawing money, for airtime top-ups and for transfers.

Modelling: Indirect Benefits

Indirect benefits are derived to the bank rather than the channel in terms of cost savings, in deposit mobilisation, in supporting products which may not exist without the CICO channel and in terms of customer acquisition. Over time, the biggest benefit to the bank is likely to be in encouraging customers to move towards digital finance, secure in the knowledge that it is convenient to withdraw cash at any time.

i. Cost savings: Reducing cash handling – given that much of the cash in the agent system comes from the agents’ own businesses. Banks can rationalise branch infrastructure – given that many rural transactions can be handled through agents. Stanbic Bank Uganda were able to downsize rural branches whilst improving service levels through using agency to remove banking hall transactions. Agent banking is further critical in supporting large numbers of low value accounts which were earlier uneconomic.

[3] For example in Uganda the existence of the ABC agent banking platform enables banks to share agents.

ii. Products: Agent banking supports a range of products which rely upon CICO. These products should be modelled, not only for transaction income for the channel but to estimate the benefits to the bank of those products.

iii. Deposit mobilisation: Agency facilitates deposit mobilisation. Centenary Bank in Uganda were able to retire 75% of its fixed deposits within nine months of launching agent banking, through largely rural deposits raised through the channel.

iv. Account opening: As a low-cost channel agent banking supports large volumes of lower income customers. E-KYC enables agents to open accounts, to earn account opening commissions, and enables the bank to acquire customers at low cost. In 2018, Centenary Bank in Uganda opened 400,000 new accounts – a record for the bank – with many accounts opened through the agent channel.

Indirect benefits usually accrue to different functions within the bank, and not directly to the agent banking channel. The income from nano loans accrues to the loan department. Investment income from deposits accrues to the Treasury function. So its important that the model represents the benefit to the bank, and potentially establishes a transfer pricing structure which supports decisions on the channel over the longer term.

This blog is one of a series of blogs, should you wish to sign up to receive additional blogs, please write to David Cracknell at david@firstprinciples.consulting

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