THE IMPACT OF BRANCHLESS BANKING TO BUSINESS PERFORMANCE: CASE STUDY AT BSN

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ABSTRACT

The aim of this research is to study the impact of branchless banking to business performance. Branchless banking has great potential to extend the distribution of financial services to poor people who are not reached by traditional bank branch networks. It lowers the cost of delivery, including costs both banks of building and maintaining a delivery channel and to customers of accessing services. Branchless banking helps Bank Simpanan Nasional to improve their business performance since the introduction. This study is conducted by using qualitative method which is interview.

Keywords: business performance, branchless banking, agent banking

ABSTRAK

Tujuan kajian ini adalah untuk mengkaji kesan perbankan tanpa cawangan kepada prestasi perniagaan. Perbankan tanpa cawangan mempunyai potensi yang besar untuk mengembangkan rangkaian perkhidmatan kewangan kepada penduduk berpendapatan rendah yang tinggal jauh dari rangkaian cawangan bank. Ia mampu menjimatkan kos penghantaran, termasuk kos pembukaan cawangan. Perbankan tanpa cawangan juga mampu mengekalkan saluran penghantaran untuk membolehkan pelanggan mengakses perkhidmatan. Perbankan tanpa cawangan membantu Bank Simpanan Nasional untuk meningkatkan prestasi perniagaan mereka sejak ianya diperkenalkan. Kajian ini dijalankan dengan menggunakan kaedah kualitatif iaitu temubual.

Kata kunci: prestasi perniagaan, perbankan tanpa cawangan, ejen bank.

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CHAPTER 1

INTRODUCTION

1.0 INTRODUCTION

This chapter is separated into eight sections to explain about the study. It consist of problem background, the problem statement, research objectives, research questions, theoretical framework and hypotheses development, scope, significant of study, and expected result. All the sections will be discussed and elaborated.

1.1 PROBLEM BACKGROUND

Banking can be defined as the business activity of accepting and safeguarding money owned by other individuals and entities, and then lending out this money in order to earn a profit (Rajesh, 2012). Because of the improvement and increasing demand on banking services, many companies grew as a banking company. A banking company means any company which transacts the business of banking (Rahmatullah , n.d.)

However, as the time passed by, the activities covered by banking business have widened and now various other services are also offered by banks. Rajesh (2012) also said that the banking services these days include issuance of debit and credit cards, providing safe custody of valuable items, lockers, ATM services and online transfer of funds across the country.

Banking sector are the simple looking method with an activity that encourages the flow of the money into investment and productive use, has help in economic growth. That is to say, greater financial development is associated with higher long-run economic growth (Rousseau and Wachtel, 2011).

Banking sector also affect productive and investment. The primary purpose of bank is to mobilize otherwise idle resources for use in productive investment (Caroline, 1998). Caroline (1998) also said that banking function increase the share of resources targeted to productive investment.

As the banking sector become more important to people around the world, education system based on banking is established. More professional needed in banking sector as it growing bigger.

Nowadays, people are handling matters with helping of technology, such as internet, machine, and mobile phone. Technology has been an important driver in facilitating branchless banking because it enables banks to link with customers through a card-based, mobile phone-based, or other ICT-based device in real-time at affordable prices (Chemonics International Inc, 2010)

The banking sector has evolved into modern service which is branchless banking. Branchless banking is the delivery of financial services outside conventional bank branches using information and communications technologies and non-bank retail agents (Zamani , 2009).

According to Daniel and Matteo (n.d.) branchless banking has been booming in the last few years and it has the potential to provide financial services to low-income households who are not reached by traditional bank networks.

Branchless banking has made people life easier and avoids time wasting. Branchless banking enables clients to store, send, and receive electronic money through local agents, rather than traveling to the nearest bank branch (Ignacio , 2009).

However, there are still millions of people in this world were unbanked. According to Chala (2009), 2.5 billion adults, just over half of world's adult population, do not use formal financial services to save or borrow. Chala also said 62% of adults, nearly 2.2 billion, living in Asia, Africa, Latin America and the Middle East are unserved.

During this decade starting 2000, mobile has advanced from mere providing basic text messaging services to that of pseudo Internet Banking while customer could not only view the Balances, set up multiple types of alerts, but also transact activities such as fund transfer, instruct payroll based transactions, redeem loyalty coupon, deposit the check over mobile (Shripad, 2011). Mobile banking is the use of a smartphone or other cellular device to perform any online banking away from your computer. You will manage to complete some banking task such monitoring account balances, transferring funds, between accounts, bill payment and locating an ATM.

Mobile banking brings the users to interact with financial institution in different way and even shaping the financial industry itself. Mobile banking is easily implemented solution with a huge impact on growth, improving customer service, and increasing user retention and acquisition (Mobilearth, 2013).

A demand for mobile technology has risen nowadays, and more people are inspired to use it instead of going to the branch itself. Users enjoy the convenience of mobile banking so much, financial institutions continue to observe steady declines in branch transactions and accompanying foot traffic, while mobile access steadily climbs (Mobilearth, 2013).

1.2 PROBLEM STATEMENT

There are many people in this world who still do not have their own financial account. It is because some of them might be living in very small towns, or poor people who live far away from areas of larger population and cannot make the drive to the locations whenever they need to use banking services.

According to Dermish (2012), about 2.6 billion people in the world do not have access to formal financial services the role of finance then is to help the poor maintain a household and plan certain investment, such as in shelter, education, or enhanced productivity. In principle, the poorer the household, the more they need financial instruments to manage their lives.

Branchless banking has been considered an important alternative to extend the distribution of financial services to poor and remote areas, usually undeserved by traditional bank branch networks (Ivatury and Mas 2008).
In fact, there is an opportunity for banking technology to connect lower income citizens at reduces cost and bring millions of consumer to the formal financial marketplace through electronic channels (Wessbourd 2002). So branchless banking is really needed in rural area as it will become a medium for poor person to get financial services.

Branchless and mobile banking have a great potential to provide a range of affordable, and secure banking services to poor people in developing countries (CGAP, 2010). 1.7 billion of unbanked customer were estimated to have access to mobile phone. As the technology keeps expanding, the poor will enable to make financial transactions that are accessible and reliable.

1.3 RESEARCH OBJECTIVES

Generally, this research's main objective is to determine the impact of branchless banking to the business performance of BSN. Three objectives in these studies which are:

1. to identify what is branchless banking technology
2. to find impact of branchless banking technology to the business performance
3. to examine the level of the utilization of branchless banking technology by BSN

1.4 RESEARCH QUESTION

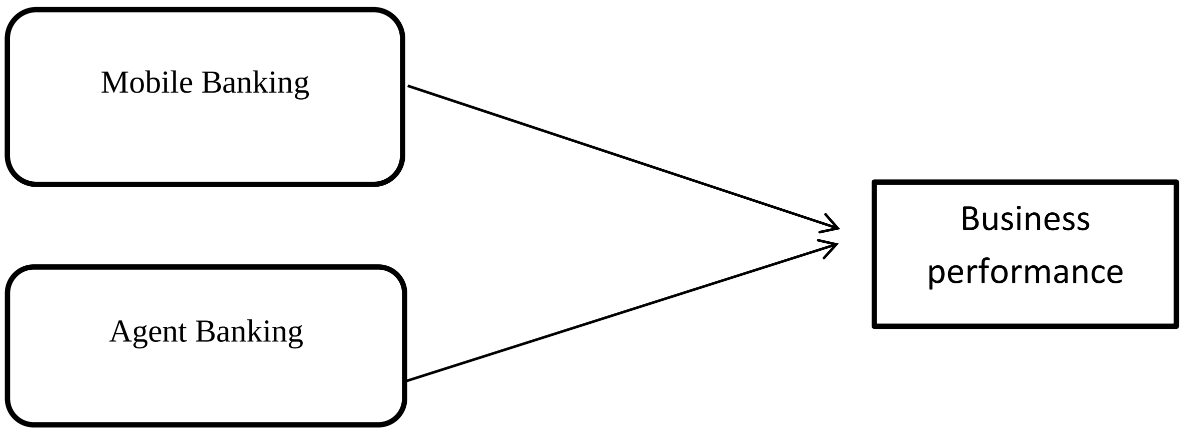
Based on the research objectives above, research questions are formulated as follows:

1. what is the branchless banking technology
2. what is the impact of branchless banking technology to the business performance
3. what is the level of the utilization of branchless banking technology by BSN

1.5 CONCEPTUAL FRAMEWORK

Figure shows the relationship between independent variables (type of branchless banking) and the dependent variable (business performance).

Branchless Banking



1.6 RESEARCH SCOPES

This study will carry out a careful study based on face-to-face interview. The scope of study will focus on the employee and branch manager of BSN Kuantan and also with group numbers of retail banking agent around Kuantan areas.

1.7 SIGNIFICANT OF STUDY

Hopefully the results of this research will be both theoretically and practically beneficial. In theoretical aspect, this research would help other researchers to prove the theory and also support the future research, generating food ideas and also provides better understanding.

Next, this research will help the branchless banking services to expand to other rural areas which are not yet covered by this service. Moreover, this research will also help the poor people to get their own financial account which seems extremely important in this era.

Besides, this research also will help to improve business performance and competitive advantage between bank and by that, our banking services will improve in many aspects.

Lastly, this research will benefit other students to understand the relationship between the branchless banking with business performance and could guide other researcher who interested to further study on this topic.

1.8 OPERATIONAL DEFINITION

1.8.1 Branchless Banking

According to Sarah (2012) branchless banking makes financial services available outside of traditional bank branches through the use of available technologies. These new business models rely on a widespread network of agents often retail locations, where customer can go to transact.

Branchless banking is a milestone to substantially increase the financial services outreach to the un-banked communities. Besides that, it also might be define as a distribution channel strategy used for delivering financial services without relying on bank branches. It is a cheaper alternative to conventional branch-based banking that allows financial institutions and other commercial actors to offer financial services outside traditional bank premises by using delivery channel like retail agents, mobile phone, post office, and grocery store.

1.8.2 **Retail Agent**

Gautam (2006) said that retail agent is payment services through postal and retail outlets, including grocery stores, and gas stations. A banking agent is a retail outlet that been offer a contract by a financial institution or mobile network operator in order to process clients' transactions.

Banking agents can be pharmacies, supermarkets, grocery stores, lottery outlets and post offices. Compare to a branch teller, it is the owner of the outlet that conducts the customer transaction and lets client to deposit, withdraw, and transfer funds. They also can pay their bills, inquire about an account balance, or receive government benefits or a direct deposit from their employer.

Agent may be able to play role in a broad range of services, including account opening, cash-in and cash-out, payment and transfer service, and perhaps even credit underwriting (CGAP, 2011). The cash-in and cash-out including cash disbursement of bank-approved loans and repayment collection.

1.8.3 **Rural Area**

Rural area is an open swath of land that has few homes or other buildings, and not very many people. A rural areas population density is very low. Many people live in a city, or urban area. Geographically, rural area is the area that where the population, housing, and territory is located outside cities and towns. Rural areas typically have a low population density and small settlements.

Rural areas commonly are agricultural areas, forest area, and mountains area where people who lived there normally are farmer, miner and stock farmers. Rural area does not have traffic problem, less air pollution, and also free from noisy air.

1.8.4 **Mobile Banking**

Wong (2002) defined mobile banking as the system comprises a mobile banking unit and a data processing centre which may be the mainframe computer of the bank responsible for processing banking transaction and data storage.

Mobile banking also can be defined as a system that allows client or customer of any financial institution to conduct a number of financial transactions through mobile phone and personal digital assistant.

Tiwari (2004) has defined mobile banking as a opportunity for banks to retain their existing, technology-savvy customer base by offering value-added, innovative services and to attract new customers from corresponding sections of the society.

1.8.5 **Business Performance**

The level of performance of a business over a specified period of time, expressed in terms of overall profits and losses during that time.

1.9 EXPECTED RESULTS

In this study, the result is expected to be positive relationship between the types of branchless banking towards business performance. According to some research on impact of branchless banking to business performance, shown that there are impressive outcome on the business performance.

The branchless banking has risen up the business performance of the bank. Sadiq (n.d.) in his research said that in only 7 years, First Direct became the fastest growing bank in the Britain. He also provides a table shows that the number of customer increase rapidly during the first 7 years. Hence, after this study, it is expected that the branchless banking, are positively co-related with the business performance of Bank Simpanan Nasional (BSN).

CHAPTER 2

LITERATURE REVIEW

2.0 INTRODUCTION

There is two main scope to focus on while doing literature reviews to ensure that the studies to be conducted successfully. Branchless banking plays an important role in this study where either it will give an impact on business performance or not.

An understanding of the branchless banking also play an important and need to be focus on. How these branchless banking process or model are capable to give impact into business performance. A challenge that may arise in this study is to provide a clear data on the number of people who using this service and data for BSN performance.

2.1 Definition of Branchless Banking

According to the Moorthi (2008), said Branchless Banking (BB) represents a significantly cheaper alternative to conventional branch-based banking that allows financial institutions and other commercial actors to offer financial services outside traditional bank premises.

Consultative Group to Assist the Poor (n.d.) defined branchless banking as a use of technology, such as payment cards or mobile phones, to identify customers and record transactions electronically and, in some cases, allow customers to initiate transactions remotely.

Consultative Group to Assist the Poor (n.d.) also said that branchless banking as a use of outlets such as post offices and small retailers, that act as agents for financial services providers and that enable customer to perform functions such as cash handling for account opening.

Besides that, branchless banking is a type of banking that takes place where the customer does not need to visit the location of the bank, but the business may be completed through technological services (Miller, 2003).
Peter and Reginal (2009) classified the minimum criteria for what constitutes branchless banking are:

i) Non-bank retail outlets are used as customer touch-points, at least for cashing in or out of the accounts
ii) Technology such as payment cards or mobile phones, is used to identify customers and authorize transactions as their own
iii) Transaction can be processed against an electronic store of value
iv) Accounts are issued by institutions recognized and explicitly or implicitly authorized by the banking regulator.

2.2 Historical Background of Branchless Banking

Peter (1997) said that in the mid-eighties, Midland Bank, the fourth largest bank in the UK with 2000 branches, began looking at ways how to attract more affluent customer. Then, Midland Bank has established First Direct, as their independent division (Sadiq, n.d.).

The first branchless banking and retail telephone banking service is UK's company which is First Direct (Sadiq, n.d.). First Direct also became the fastest growing bank in the Britain in only 7 years (Delphine, 1997).

First Direct operated from a central location could be accessed by customer via telephone 24 hours a day, 7 days a week, and 365 days a year (Sadiq, n.d.).

Date	Total number of customers	Total number of accounts	Calls/day	Staff
Apr-96	641,000	1,100,000	32,000	2,400
Dec-95	586,000	800,000	26,000	2,300
Dec-94	476,000	700,000	21,000	1,900
Dec-93	361,000	500,000	16,000	1,500
Dec-92	241,000	350,000	11,000	1,000
Dec-91	136,000	200,000	7,000	500
Dec-90	66,000	105,000	3,000	300
Dec-89	11,000	N/A	N/A	250

Source: "First Direct: Branchless Banking" INSTEAD, Fontainebleau, France, 1997.

2.3 Branchless Banking Model

2.3.1 Permissible Models

Mansoor et al., (2011) said only bank-led model of branchless banking is allowed which may be implemented in different ways. The bank-led model offers a distinct alternative to conventional branch-based banking, through which a customer conducts financial transactions at a whole range of retail agents (or through mobile phone) instead of at bank branches or through bank employees.

Firstly, it can be implemented either by using agency arrangement or by creating a JV between Bank and Telco/non-bank. Further, the mobile phone banking which make up for large part of branchless banking can be implemented by using one-to-one, one-to-many, and many-to-many models. From this journal, it categorizes permissible models into three type which are:

2.3.1.1 One-to-one (1-1) model

This model offers mobile phone banking services in collaboration with a specific Telco. The services may only be offered to customer that using mobile connection of that specific telco. This model can be either JV-based or also can be implemented through specific agreement between telco and the bank.

Mansoor et al., (2011) also added that this model offers greater customization, good service standards, chances of co-branding and co-marketing. But unfortunately on the other hand, it lacks in outreach as it is limited to the customers of one telco only.

One-to-one model does not necessarily high-class or require exclusivity. One bank can have several one-to-one arrangements with many telcos or one telco can have several one-to-one arrangements with many banks.

2.3.1.2 One-to-many (1-∞) Model

Different from one-to-one model, this model offers mobile phone banking services to customers using mobile connection of any Telcos. This model offers the possibility to reach to any bankable customer who has a mobile phone connection.

Unfortunately, Mansoor et al., (2011) said this model has several limitations in that all telcos may not be ready to offer the bank a priority SMS pipe to enable it to provide quick services which are essence in mobile phone banking.

Besides that, another serious drawback if this model is that it may require the bank to rely upon its own branch network for product distribution and cash cash-out services.

2.3.1.3 Many-to-many (∞ - ∞) Model

Many-to-many model provides many banks and many telcos to join hands to off services to virtually all bankable customers. “Third Party Service Provider” (TPSP) is necessitated under this system. It must be controlled by an FI or by a subsidiary owned and controlled by an FI or a group of FIs. Besides it also should be controlled by a third party under proper agency agreement with Financial Institutions.

2.4 Retail Agent Model

Agent have been used on an experimental basis since the introduction of the enabling regulation in 2006 (Ernesto, Denise, & Klaus , 2008). For poor people, “branchless banking” through retail agents may be far more convenient and efficient than going to a bank branch (Gautam, Timothy, & Stefan, 2006). Gautam, Timothy, & Stefan (2006) also said that for many poor customers, it will be the first time they have access to any formal financial services, and formal services are usually significantly safer and cheaper than informal alternatives.

For banks, branchless banking through retail agents is used to reduce cost of delievering financial services (potentially radically), relieve crowds in bank branches, and established a presence in new areas (Timothy, Gautam, & Stefan, 2008).

Ernesto, Denise, & Klaus (2008) said that two models of branchless banking, bank based and nonbank-based can be distinguished. Both use retail agents such as merchants, supermarkets, or post offices, to deliver financial services outside traditional bank branches. From this journal, it categorizes retail agent models into two types which are:

2.4.1Bank-based-model

This model allows every customer to have a direct, contractual relationship with prudentially licensed and supervised financial institution. Whether involving an account or a one-off transaction. The customer may deal with a retail agent who is equipped to communicate directly with the bank using either a mobile phone or a point-of-sale.

Retail agents have to face-to-face interaction with customers and perform cash in and cash-out functions. In some countries, retail agents also handle all account opening procedures and, in some cases, even identify and service loan customers (Timothy, Gautam, & Stefan, 2008).

Once an account is approved, the customer goes to retail agent to conduct any financial transaction, and then the agent will check the customer's identification documentation and process the transactions.

Figure 1 The Bank-Led Model

CUSTOMER	RETAIL AGENT	BANK
Step 1: Customer requests financial service.	**Step 2: Retail agent** checks **customer's** ID and processes transaction, either directly through **bank's** infrastructure (POS) or through **payment processing agent.**	**Step 3: Bank** credits and debits bank accounts of customer and other party to the transaction.
Examples of Services Offered: Deposits and with-drawals; money transfers; loan/bill/tax payments; loan application and disbursal; account opening and credit card application acceptance.	**Examples of Retail Agents:** Retail outlets (grocery stores, lottery outlets, pharmacies, etc.); socially motivated organizations (NGOs, MFIs, etc.); post offices.	**Examples of Other Parties:** Includes **retail agent** (for deposits or withdrawals) and recipients of money transfers (other customers, utility companies, tax authorities, etc.).

2.4.2 Nonbank-based-model

In the nonbank-based model, customers have no direct contractual relationship with a fully prudentially licensed and supervised financial institution. Instead the customer exchanges cash at a retail agent, in return for an electronic record of value. This virtual account is stored on the server of a nonbank, such as a mobile operator or an issuer of stored-value cards. The balance in the account can be used for storing funds for future use, or converting stored value back to cash at agents.

A more limited version of the nonbank-based model can be found in payment networks, which involve a technology provider or other nonbank institution offering a network of payment points where a customer can make payments to third parties of governmental entity can make payments to beneficiaries.

In the typical nonbank-led model of branchless banking, customers do not deal with a bank, nor do they maintain a bank account, or the bank may not be involved at all (Timothy, Gautam, & Stefan, 2008).

Timothy, Gautam, & Stefan (2008) also added that customer exchange their cash for e-money stored in a virtual e-money account on the nonbank's server, which is not linked to a bank account in the individual name.

Figure 2 The Nonbank-Led Model

CUSTOMER	RETAIL AGENT	NONBANK	BANK
Step 1: Customer requests sale or financial services using either cell phone or smart card. **Examples of Services Offered:** Deposits to and withdrawals from customer's e-money account (cash-in and cash-out); item purchases*; money transfers*; loan disbursal/repayment*; bill/tax payments*. * These services may also be accessible directly via cell phone without visiting a **retail agent**.	**Step 2: Retail agent** checks **customer's** ID and processes transaction on behalf of **nonbank**, using either cell phone or smart card reader. **Examples of Retail Agents:** Airtime vendors; department stores; supermarkets; other commercial enterprises.	**Step 3: Nonbank** registers transaction, updates the (virtual) e-money accounts belonging to the **customer** and the other party to the transaction. **Nonbank** manages individual **customer** accounts. **Examples of Other Parties:** Includes **retail agent** (for deposits, withdrawals, or item purchases); recipients of money transfers (other customers, utility companies, tax authorities, etc.).	**Step 4: Bank** (generally)† holds net funds from the nonbank's issuance of e-money on behalf of **nonbank. Bank** does not have a relationship with **customer** or **retail agent**. †This is the practice of mobile phone operators in the Philippines and Kenya, as a simple matter of business prudence, although not required by regulatory authorities in either country.

2.5 Agent Banking Regulations

There are several countries that also implement branchless banking into their financial institutions. Every country has their own branchless banking regulations.

2.5.1 Colombia

Since the adoption of the National Development Plan 2006-2010, the Colombian government has shown commitment to increasing financial access and has undertaken a number of regulatory reforms. Oxford Policy Management (OPM) has handled some case study on the regulations of many country that implement branchless banking. Oxford Policy Management (2011) said that Colombia's financial system is regulated by three institutions which are the Financial Superintendence of Colombia, the Congress and the Ministry of Finance. In this journal, said that recent regulatory reforms include:

i) The creation of a relatively open regulatory framework for financial institutions to use agents.
ii) The use of financial incentives for bank to offer low-value savings accounts
iii) Regulation of electronic and mobile bank accounts.
iv) Exemptions from the financial transaction tax imposed on bank customers
v) Improvements to the regulatory definition of microcredit.

In 2006, the government created Banca de las Oportunidades (BDO). This policy aims to enhance access to financial services by:

i) Promoting regulatory changes
ii) Coordinating financial capability initiatives.
iii) Providing incentives for financial institution to meet the unmet demand for banking services.

In Colombia, agents are called 'non-bank correspondents'. These are commercial businesses that can provide financial services on behalf of formal financial institutions.

Any type of legal entity or individual can become agent, but that person must conduct some business activity. Agents must be approved by the regulator, which reserves the right to establish conditions (Oxford Policy Management, 2011).

2.5.2 Brazil

The government's policy for financial inclusion in Brazil has two delivery mechanisms: microfinance and retail agents (Oxford Policy Management, 2011).

All Central Bank of Brazil (CBB)-licensed institutions are permitted to offer various services such as deposits, withdrawals, and transfers through legal entities functioning as agents (Consultative Group to Assist the Poor, 2010). Consultative Group to Assist the Poor (CGAP) has detail about the key points which are:

i) CBB is responsible for setting and enforcing anti-money laundering/combating the financing of terrorism rules applicable to CBB-supervised entities.
ii) Collecting, intermediating, or investing funds from third parties is reserved for CBB licensed, regulated and supervised entities.
iii) All deposit-taking entities are subject to licensing and supervision.
iv) The Payment System Law gives CBB a clear mandate to supervise the National Payment System.
v) There is no legal or regulatory provision that specifically addresses the provision of money transfer services.
vi) There is no specialized financial consumer protection body, but an active network of government entities enforces the Consumer Protection Code in the financial sector.
vii) The Civil Code provides for recognition of electronic signatures.

In Brazil, there is no specific definition of an agent provided. The following entities can act as agents: companies, entrepreneurs, and associations (Oxford Policy Management, 2011).

Agents are used to distribute welfare payments and other public services, and services such as pre-approved credit lines, simplified current accounts, and international remittances (Alliances for Final Inclusion, 2011). Agents can carry out the following activities:

i) Receiving, reviewing, and forwarding applications to open bank accounts;
ii) Acceptance of funds;
iii) Payments and money transfers;
iv) Effecting payment orders;

v) Receiving and forwarding applications for loans, or credit cards;

vi) Loan collection;

vii) Prepaid mobile phone top-ups and

viii) Certain foreign exchange activities with maximum of US$3,000 per transactions.

2.5.3 India

Consultative Group to Assist the Poor (2010) said Reserve Bank of India issued a circular in 2006 that allowed bank to use third-party business correspondents to deliver financial services outside bank branches. Then, a 2009 revision to the circular removed key restrictions. RBI had issued the guidelines in October 2008 which are:

i) Only banks licensed and supervised in India and with a physical presence in India can offer mobile banking to customers.

ii) Mobile banking services are limited to existing customers of banks.

iii) Cross-border and foreign currency remittances are not allowed.

iv) Services must be interoperable across mobile network providers within six months of offering.

v) Daily transactions are limited to approximately USD 110 for transfers and approximately USD 220 for purchases involving goods and services.

vi) Banks offering mobile banking services must obtain a one-time prior approval of RBI.

Oxford Policy Management (2011) stated that a definition of agent is not provided in the regulations and approval of agent by the regulator is not required.

The 2006 circular (Financial Inclusion by Extension of Banking Services - Use of Business Facilitators and Correspondents, 2006) states that agents can offer the following financial services on behalf of principals:

i) Identification of borrowers