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Policy Brief # 9

Behind the Big Numbers: Improving the Reach and Quality of Agent Networks in India

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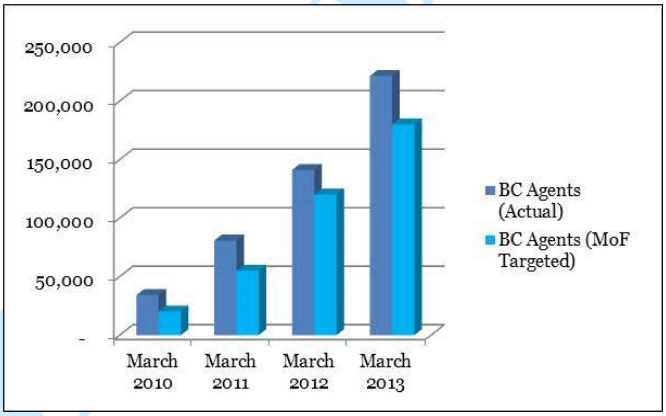
According to the World Bank Findex Survey, only 35% of Indian adults have access to a formal bank account and 8% borrowed formally in the last 12 months.[1] Only 2% of adults used an account to receive money from a family member living in another area and 4% used an account to receive payment from the government. As of March 2013, around four lakh villages remain without any banking presence.

In an effort to confront this daunting financial exclusion challenge, the RBI has long permitted banks to enlist business correspondent (BC) agents for the delivery of financial services outside bank branches. This has led to a dramatic increase in banking agents. In his keynote speech "Financial Inclusion – Issues in Measurement and Analysis" in Kuala Lumpur on November 5, 2012, RBI Deputy Governor Dr. K. C. Chakrabarty noted that the number of BC agents had increased from 34,532 to 120,098 between March 2010 and June 2012. The Ministry of Finance noted in its Overview of Financial Inclusion Efforts that the number of agents had risen to 152,000 as of December 2012. And, in his speech "Revving up the Growth Engine through Financial Inclusion," Dr. K. C. Chakrabarty noted that the number of BC agents had reached 221,341 by March 2013.



This is an extraordinary increase in BC agents in a very short period leading to a headline-grabbing "big number" that exceeds the Ministry of Finance's targets for BC expansion (see graph). And yet, in *MicroSave*'s work in hundreds of villages across India, it is often hard to locate a functioning BC agent that can actually conduct a transaction. Indeed, a sizable proportion of "listed" BC agents in India are no longer offering services, suffer from chronic system downtime, or lack the necessary cash to facilitate disbursements.

While growth in BC agents is important to expand physical access to banking services, a poorly functioning BC network can do significant damage to the reputation of the underlying service. Indeed, if a beneficiary has been promised a direct benefit transfer (DBT) into her bank account, but is unable to access her funds at the designated BC, then she will lose faith in the underlying DBT scheme. Similarly, she will be reluctant to ever put her cash into a BC system if she is not confident she can access her funds when she needs them.

In this Policy Brief, we describe the true reach and quality of India's BC networks, the design features of successful agent networks, and the policy and regulatory interventions that could help catalyse the roll-out of denser, higher-quality agent networks in poor communities across India.

A. So what is the true reach and quality of India's BC networks?

To better understand the quality and reach of India's BC networks, CGAP partnered with the RBI College of Agricultural Banking (CAB) to conduct a survey of 1,030 BCs across 11 states. The 2012 survey (which will be repeated annually) found that there were severe deficiencies across India's BC networks. Indeed, out of the 1,030 BCs in the sample, only 860 could be surveyed. Ninety one (8.9%) were unwilling to answer questions as they had either stopped being agents or were too unhappy about being a BC to respond. Seventy nine

[1] World Bank (2012), "Measuring Financial Inclusion: The Global Financial Inclusion Indicators," World Bank Policy Research Working Paper #6025.

(7.7%) were unreachable as the phone number was wrong or was not answered … suggesting that these too had stopped their BC business, but they were still listed as a BC agent on banks' websites and in the RBI and Ministry of Finance figures quoted above. Among the 860 who could be surveyed, 25% were not in a position to process transactions at the time of survey because they had no equipment, inadequate cash to meet customers' withdrawal requests, or had simply stopped offering BC services altogether. This 25% was in addition to the 170 CSPs who could not be contacted with the advertised contact information or were not functional. This suggests a 37% effective dormancy rate – in line the 22-43% self-reported dormancy rate from *MicroSave*'s own 2012 survey of Business Correspondent Network Managers.

A key problem is that India's agents do not earn enough money to incentivise them to offer reasonable quality of service. The survey found that over 58% of agents earn less than Rs.3,000 (then $54) per month – well below the $125-200 per month break-even point *MicroSave* has seen in markets with high-quality agent networks, such as Kenya, Tanzania, and Bangladesh. The median agent in the Indian survey indicated that they would need to earn at least Rs.6,500 ($118) per month to be willing to offer the service over the long-run.

Rural agents are in a particularly precarious situation. Until the DBT programme reaches scale, they are essentially dependent on opening and servicing no frills accounts.[2] Driven by government mandates, 109.9 million of these accounts have been opened between March 2010 to March 2013 - an impressive achievement. But once the accounts are opened and the mandate has been achieved, banks are scarcely paying agents to service the accounts on an ongoing basis … and so the vast majority of these accounts have lapsed into dormancy. As a result, rural agents are typically conducting a limited number of transactions, and making losses as can be seen from the CGAP-CAB survey and *MicroSave*'s Policy Brief # 6 Assessing Agent Profitability. If India is to achieve financial inclusion and to deliver DBT transfers to beneficiaries in a convenient, accessible manner, it will be essential to revisit the design and remuneration of the BC networks as well as the RBI's account opening (rather than account activity) mandates.

B. So what are design features of successful agent networks?

There are eight key requirements for an effective and thriving agent network.

1. **One or two anchor products to grow the business and build trust in the agent network**
At the outset, it is essential to offer one or two "anchor" products that are simple and easy to communicate and can drive volumes. In most countries, these are person to person (P2P) remittances and/or government to person (G2P) payments. These offer the best anchor products as they are inter-spatial transfers that can be confirmed either by receiving the money or by calling the recipient to confirm receipt. This instant confirmation helps build trust in the system and the agents that run it. Clearly with its burgeoning agent-based remittance industry and ambitious DBT schemes, India is well placed to fuel the growth of BC networks by marketing P2P and G2P anchor products.

2. **Careful selection of agents to ensure trust and convenience.**
In their rush to meet the RBI's account opening targets, banks and their BC partners have enlisted large numbers of agents while paying little attention to the agents' ability to provide sustained quality of service beyond account opening. This is a pity because we have found that all successful agent networks globally have followed structured and systematic agent selection processes. Selection criteria should reflect many aspects key to the viability of the business, such as the capacity to scale up and the ability to manage cash. However, end customer preferences for agent attributes – such as the agent's reputation in the community - are the most important considerations, since these will determine a user's willingness to conduct transactions through an agent.

3. **Effective and regular training of both agents and local bank staff.**
The knowledge and efficiency of agents is a key determinant of both customers' trust in, and use of, the system. Some Indian BCs receive adequate training in how to market and promote their new services, how to manage customer complaints effectively, how to deploy working capital most efficiently, and how to operate the underlying technology. But most agents in India do not. Their banks or BC network managers either do not offer such training, or agents cannot take time away from their other businesses, or the distance is too far and the cost is too high. However, these BCs are the extensions of banks and the onus of training agents rests with them and their BC network managers. Ongoing agent training is essential in order to provide customers with the experience that they need (and indeed deserve) and to build their trust in the BC as a banking channel.

[2] No Frills Accounts are meant to have been upgraded to Basic Savings Bank Deposit (BSBD) account as per an announcement of August 2012 – but have only been rechristened for reporting purposes. Per policy the new BSBD accounts should be fully interoperable and be provided with ATM/debit card, but this has hardly happened in reality.

4. Appropriate commission structures.
The success of the BC model is dependent on agents receiving adequate compensation. As demonstrated by the CGAP-CAB survey, few BC agents in India are making enough money to warrant serious investment in providing quality customer service. Until banks realise the broader business opportunities offered by the channel, it will be essential for government to offer adequate commission to banks and BCs to conduct the basic anchor product transactions. This will require revisiting the commissions offered by government for processing DBT transfers, and a prescription of the division of that enhanced commission between the bank, the BC network manager (if any) and the front-line BC agents.[3] This is addressed in the **policy and regulatory interventions** section below. In addition, these commissions need to be transparent, easily understood by the BCs, and paid on a regular and prompt basis. In too many cases, BCs have to wait six to seven months before they receive commission income from their bank partner.

5. Regular marketing support and monitoring from the banks.
BC-based banking is not an easy sell initially - a lesson that has emerged from agent based deployments across the world. If banks want the new system of BC agents to work, they will have to persuade hesitant customers that this alternative is not only secure and trustworthy, but in fact a preferable option for them. A small SBI bank sticker in an agent's shop will not accomplish this. Instead, banks will need to develop protocols and processes to not just refer customers to the bank's BC agents, but also to actively market and build trust in the channel. They must also monitor their BCs to ensure consistent quality of service (including the adequacy of liquidity balances with the agent), branding and point-of-sale marketing. This can either be done by bank staff (as practiced by Equity Bank in Kenya) or can be outsourced to a specialist agency (as done by M-PESA in Kenya).

6. Assistance with liquidity management.
As the DBT programmes take off, agents will start handling very large sums of money. In a recent study of DBT in Andhra Pradesh, *MicroSave* found many agents handling more than Rs. 700,000 in cash on peak disbursement days. These amounts are welcome as they drive volumes, but clearly also represent a risk to the bank and indeed to the security of the agent. Banks and BC network managers will have to work hard to manage the liquidity challenges faced by agents.

7. Integration of BC technology platforms into banks' mainstream banking platforms.
MicroSave research shows that the rural poor want banking facilities and features (delivered through BCs) at par with mainstream savings account holders. In the absence of adequate integration of BC technology platforms into banks' mainstream banking platforms, they cannot access many of the services they need or aspire to. This lack of integration often precludes services such as P2P remittances (where both the sender and receiver end have to be on the same banking platform) as well as G2P transfers. This is a major cost and inconvenience for consumers. It also reflects the mind-set that the poor will welcome banking services that are inferior and will be grateful for the access provided. Sadly, the experience of many millions of dormant 'No Frills Accounts' tells us otherwise. The poor want, need and deserve banking services at par with what is available to the rest of us and that requires adequate integration of BC technology platforms into India's mainstream financial system.

8. A diverse product/service range with direct access to the core banking system.
Once the basic trust in the system has been established through the anchor products described above, banks should introduce additional products to increase the revenue stream of agents. Ultimately the BC model should be seen as a "distributed banking model" rather than as a "financial inclusion drive" to meet regulatory compulsions or social objectives. The entire retail banking product suite (subject to regulatory restrictions or strategic considerations) should be made available over the BC platform. Indeed, the most successful BC agents *MicroSave* has seen in India operate as branch extension agents, typically offering "kiosk-banking" with direct access to their bank's core banking system, allowing them to sell as well as service a wide range of savings, insurance and loan products.

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[3] *MicroSave*/CGAP/BFA research into G2P payments in AP has shown that even when the State Government and banks are paying 2.0% commission, the BC managers are pocketing 1.5% to 1.75% and the front-line BC only gets 0.25%, or at best 0.5%, despite doing all the heavy lifting. This translates into a monthly earning of Rs.500 to Rs 1,000 even with quite extensive flows of DBTs – hardly a recipe for reducing churn and dormancy.

C. What are the policy and regulatory interventions that could help catalyse the roll-out of denser, higher-quality agent networks in poor communities in India?

MicroSave believes that addressing eight key policy/regulatory issues would result in denser, higher quality agent networks across the country. A more detailed analysis (including of operational issues) can be found in *MicroSave* Policy Brief # 8 "What Will It Take To Deliver 'Direct Benefits / Cash Transfer' Programmes Successfully?"

1. ***Implement the recommended 3.14% minimum commission per transaction.***
With the exception of some urban-based agents who specialise in remittance services, BC network managers and agents are largely unviable, in part because they are paid inadequate commissions by banks for delivery of DBT payments and in part because the channel has been unable to build the required transactional volumes. This has resulted in high levels of agent churn and agent dormancy. Indirect incentives, such as reimbursement of agent training costs by NABARD or of micro-ATMs by UIDAI, have not worked. There should be a policy directive establishing a minimum commission per transaction to be divided between banks, BC network managers and agents for delivery of DBT payments and minimum monthly commission for agents.[4] A benchmark fee for DBT transactions has been calculated by the UIDAI led inter-ministerial task force to be 3.14%, with a maximum of Rs.20 per transaction. This is in line with global standards and considerably less than the savings arising from weeding out ghost and duplicate beneficiaries anticipated by the Planning Commission and others. While banks should be able to freely determine the commission structure for *non*-DBT transactions, the directives for DBT transactions can offer a template for commissions on other BC-related activities. Implementing the 3.14% commissions on DBT transactions will provide the banks with a credible business case and impetus to build out high quality agent networks, on to which they can then add on additional services.

2. ***Establish service standards.***
Given the challenges with recruitment, training and support outlined above, it is clearly time to develop service level standards[5] for agents and banks – and to hold them accountable for service delivery in line with these standards. This will go a long way towards building the trust of the underbanked population. A system for random auditing of agents either through RBI's Department of Banking Supervision or through third party auditors should also be developed and implemented.

3. ***Focus on account activity rates.***
RBI (and the Ministry of Finance - Department of Financial Services) have always focused on outreach targets rather than agent and account activity rates. Consequently, over 75% of accounts opened and over 25% of agents are now dormant. In order to encourage account activity and agent viability, DFS (as the controlling department for banks) should establish incentives and/or directives which focus on account activity rates rather than account registrations.

4. ***Remove the confusion over the need to withdraw all benefits credited.***
The policy directives that beneficiaries must withdraw the full amount credited to their account were in conflict with the government's financial inclusion goals. It is good that a circular has been issued rescinding this requirement, but this has still not been translated into action in the field. Complete withdrawal of benefits increases costs for banks and BC network managers – some of which even created shadow accounts to allow beneficiaries to withdraw from their DBT account and then put the money into their savings account. Furthermore, this policy minimises float and thus further reduces the incentive for banks to participate and provide quality agent infrastructure. The Planning Commission, Ministry of Finance, and State Governments need to further clarify that beneficiaries are not required to withdraw all the benefits credited to their account, and that their accounts can be operated in the same way as any other bank account.

5. ***Scrap (most of) the cluster-based approach.***
The DFS notification on strategy and guidelines for financial inclusion introduced a monopolistic structure under which a single BC network managers would be the sole service provider for DBT delivery to all banks in an entire cluster (typically the size of a large state). This crowds-out healthy competition

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[4] It will also be necessary to further define the division of the 3.14% fee between banks, BC network managers and agents to ensure that the current practice of under-paying the front-line agents is eradicated. In its Policy Brief # 8 *MicroSave* has recommended that at least 50% (ideally 75%) should be paid to the front-line agents. In addition, clear guidelines on the monthly minimum that an agent should receive (with classification according to 'cost of living' in tier V/VI towns and villages >5,000, 2,000-5,000 and <2,000 population) is likely to be necessary.

[5] Examples of such service standards might include: minimum number of days agent would be available in the village; maximum time to open a new account and to issue an account number (with the ATM/debit card/smart card according to the delivery model); a working consumer and agent helpline in the local language; monthly reporting to RBI on resolution of complaints on the helpline etc.

and forces banks to depend on a single institution that might not have the capacity or incentive to deliver at such a large scale. Most of the cluster-based approach needs to be rescinded to encourage competition amongst BC network managers as well as banks. Fortunately, few, if any, banks have implemented the cluster-based approach to date. Hence, the under-bid contracts can, and should, be set-aside. At the same time, some of the good practices proposed as part of the cluster approach should be retained. For example, the recommendation that service providers offer multiple products through BC channels and integrate their BC platforms with their CBS should be retained. For a full analysis of these issues please see *MicroSave* Policy Brief #7 Is The Business Correspondent Model In Policy Paralysis?

6. ***Introduce standards for integration and interoperability.***
   Historically ATMs and credit or debit card payment systems using POS terminals have witnessed exponential growth and adoption due to uniformity of standards. While market forces eventually determine the success of a standard, policy makers and the regulator need to make concerted efforts and provide direction to enable greater standardisation and prevent the proliferation of non-inter-operable technology options. The on-going, un-coordinated, and somewhat redundant efforts for standardisation by various bodies need to be better coordinated. Existing proven standards that bring in economies of scale and scope need be leveraged instead of reinventing them. Standardisation should, to a large extent, be driven by market forces, with necessary interventions to set the broad direction. At the same time the roadmap for standardisation needs to protect historical investments as well as consumer interest.

7. ***Relax the 30km rule.***
   The July 2013 RBI master circular on branch authorisation again restricts the operational area for agents to within a 30km radius of a rural branch to which the agents are linked (for account opening, KYC, etc.). This effectively limits the establishment of large-scale agent networks to public sector banks that have large branch networks, while precluding smaller, more nimble and hungry banks. The 30km rule should be relaxed to enable smaller, more nimble banks to build widespread agent networks. Ultra-small-branches can also be considered a substitute for main branches for the purpose of meeting the 30 km requirement. As long as RBI is able to hold banks accountable for the fiduciary conduct and service quality of their agents, the 30km rule is not necessary and simply inhibits competition. The 30km rule can be and should be relaxed for outreach in unbanked and under-banked areas.

8. ***Allow Mobile Network Operators to act as issuers of e-money with proportionate supervision.***
   The Policy Guidelines for issuance and operation of Prepaid Payment Instruments restricts issuance of open loop prepaid instruments to banks. Banks in developing countries have struggled to build agent networks in poor and rural communities. This is in part because effectively serving poor customers requires banks to radically re-work their traditional "float-based" business models. And because non-banks cannot offer e-money services, there is little healthy competition to prod banks into serving poor and unbanked households. India needs regulation that distinguishes between the risks posed by payments from those posed by issuing credit. Accepting funds from the public and placing 100% of those funds in pooled accounts at supervised banks does not create prudential or liquidity risks. If the Government of India and the RBI really wanted to turbo charge financial inclusion and the use of Aadhaar-enabled accounts, it would allow MNOs to act as issuers of e-money with proportionate supervision, as advocated by CGAP and practiced in Malaysia, Kenya, the Philippines, Peru, Rwanda, Sri Lanka, Tanzania, Uganda, Zambia, and the eight countries of the West African Monetary Union. This would allow MNOs to use their experience and inherent advantage to build effective agent networks (Safaricom's M-PESA network in Kenya remains unrivalled in terms of reach, reliability and efficiency) and encourage banks to work alongside them as partners, as has happened in Kenya, Pakistan, Tanzania, and Uganda.

D. Conclusion

Achieving financial inclusion in a diverse country like India will not be easy, but the massive *Aadhaar*-enabled DBT programme provides a tremendous platform and anchor product to do so and to drive adequate volumes to remunerate agents in the villages. India thus has a tremendous opportunity to ensure that every poor household has access to a high-quality banking access point. While the impressive growth in the number of agents is an important step forward, it is by no means adequate as most of the agents are still of very poor quality or dormant, thus damaging trust in an agent-based system for DBT distribution and financial inclusion. This needs immediate remedial action by policy/regulatory actors, as well as commercial players, to make a concerted push to resolve the remaining barriers – before the complete break-down in the agent system, and the loss of the trust of India's masses, become a lasting impediment.