

MicroSave Briefing Note # 134

Term Deposits: Rural Clientele Ask For More

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Term deposits¹ are one of the most common means of investment in rural sub-districts of Java. A majority of rural clients prefer term deposits in commercial and rural banks² because of the perceived guaranteed safety and assured return. This therefore also offers an inadequately realised growth potential for rural banks.

Of late, the majority of rural banks, despite their huge market potential, have witnessed a decrease in deposit mobilisation. They have been losing business to competitors, mostly commercial banks. Sometimes other savings or investment options available to the client are more appropriate, or convenient, than the products offered by the rural banks. For example, in the absence of a suitable savings product, a rural client may prefer to hold his/her surpluses in land, durables, crop inventory, livestock and jewellery. While the recent loss of business can be attributed to a number of factors, *MicroSave* market research clearly demonstrates that the mismatch between demand and product offering is one of the most important.

Of late, a growing number of rural banks have made renewed efforts to revive their deposit portfolio. This Note highlights the experiences of rural banks in mobilising term deposits, the issues and challenges they face, and the strategies adopted by them to revive their portfolio and growth.

Term Deposit Product: Does It Meet Client Demand

A steady growth in the number and amount of deposits at a bank sustains capital adequacy, improves cross-selling opportunities and nurtures public confidence, and thus determines financial robustness of the institution. However, if growth falters it may indicate loss of faith in the bank, and eventually loss of clients and reduced profitability. *MicroSave*'s research studies have indicated that an increasing number of existing BPR customers have been either discontinuing or gradually reducing the volume of deposits they hold with rural banks.

MicroSave studies in Java region³ of Indonesia have revealed that the current deposit products offered by a

number of rural banks are not appropriate to address the banking and short term investment needs of a range of clients thereby driving them to their competitors in the formal and informal sectors. Moreover, products offered by some commercial banks are also facing service quality issues like long queues, cumbersome cash withdrawal processes, and penalties charged upon early deposit withdrawal.

Rural clients place deposits to compensate for uneven income streams, manage unforeseen events, social and religious obligations and for future consumption. Quick access to their deposits is crucial for them to respond to emergencies and unanticipated investment opportunities. Moreover, the transaction costs (i.e. the cost of making a deposit and of liquidating it, the cost of travelling to the financial institution, the opportunity cost, and cost of paperwork) can be so high that a seemingly positive real rate of return appears negative, and a rural depositor therefore turns to either a local MFI or an informal means of savings.

The demand for deposit products at a rural bank increases with the interest rate paid on those deposits. However rural clientele have their own mechanisms to compare rate of return with other informal means of arrangement. The interest on deposits paid by BPRs may seem attractive when compared to the interest paid on commercial banks' regular savings products. However, this benefit may be ignored as customers value the safety of the deposits more than anything else.

The age of a client has a big influence on his/her financial behaviour. In general, village youth prefers investment in assets and durables. Nonetheless, they may keep a small portion of their investment in a term deposit scheme to diversify their portfolio. But the pattern changes during retirement, when the investments allocated to term deposits rise significantly. Clients expect maximum return with security, ease of operation, and liquidity from the rural bank entrusted with these deposits. Many senior citizens also ask for quick personal loan facility against their deposits to

¹ 'Term Deposit' product refers to term deposits received by the bank for a fixed period withdrawable only after the end of the fixed period. These deposits can be withdrawable prematurely but on prior notice. It includes recurring deposit and fixed deposit scheme.

² The term rural bank or BPR (*Bank Perkreditan Rakyat*) represent secondary banks in Indonesia, which are regulated and supervised by the central bank. They usually operate at the sub-district level. BPRs are locally based and mostly privately owned rural banks. They cater to lower to middle income clients; they are not part of the payments system; they face strict branching restrictions; and they are subject to different regulations than commercial banks.

³ Java is an island of Indonesia. It is the world's most populous island, and one of the most densely-populated places on the globe. Java is the home of 60 percent of the Indonesian population. Java is divided into four provinces, West Java, Central Java, East Java, and Banten, and also two special districts, Jakarta and Yogyakarta. (Source: Wikipedia)

meet immediate requirements such as medical expenses.

It is rare to find a BPR that offers special rates and facilities for senior citizens. While some do offer negotiable interest rates on the deposits these do not necessarily meet client expectations.

Issues And Challenges Faced By A Rural Bank

MicroSave studies identified that, in recent times, commercial banks have generally been more successful than rural banks in mobilising term deposits. This is because of a combination of factors such as grandiose branch offices, brand equity, and an exclusive marketing team to drive deposit mobilisation. *MicroSave*'s research also found that most rural depositors (existing, as well as new) were unaware of many of the products and services offered by both commercial and rural banks. They chose a commercial bank based on its corporate image and local presence.

The following are the key issues and challenges faced by a rural bank seeking to mobilise term deposits:

Lack of Focus: Rural banks generally focus inadequately on building their deposit portfolio. Marketing and promotion efforts are minimised, and efforts are often only directed at staff members and their close relatives or acquaintances. This is because deposit mobilisation in rural areas is a high volume but resource intensive affair. Thus, while it supports the sustainability of the bank by providing stable funds, there is often a trade-off between the money that can be earned on these funds and the relatively high mobilisation costs involved.

KBPR Arta Kencana has vast experience in delivering deposit and savings services. In 2011, they opened a new branch in a new geography. KBPR sought *MicroSave* support to understand the market segment for term deposit products and help in setting up a marketing strategy to ensure sustained growth in coming years. *Inter alia* *MicroSave* helped KBPR to design a product brochure containing the range of products and services offered by the bank, and a section on future planning and banking. The section on future planning and social upliftment was included not only to create awareness, but also as an important strategy to market BPR in the long run.

Rural vs. Commercial Banks: BPRs are often compared with commercial banks on interest rates and services provided. In most cases rural banks offer higher interest rates than commercial banks. Customers expect service delivery of a similar standard from both commercial and rural banks. Savings in both types of banks are secured and guaranteed by the government (under *Lembaga Penjamin Simpanan*-Indonesia Deposit Insurance Corporation), but people perceive savings to be more secure with a commercial bank. This acts as a major challenge for rural banks as they lose existing clients and face difficulty in attracting new ones,

despite offering better interest rates (sometimes even negotiable interest rates), as well as the opportunity to win prizes through lottery schemes.

Inability to use a market segmentation strategy: Rural banks mostly do segmentation based on demographic parameters and ignore variables such as culture, socio-economic, behaviour, usage pattern, service need and benefits sought by the clients. They also face difficulty in targeting post segmentation, i.e. which segment to choose for growth and profit. Some even identify the market, but find it difficult to decide on product and services that will attract and retain clients. BPRs often waste their resources trying to mobilise deposits from clients for whom deposits are of little importance. For example, those involved in daily businesses compare the return on deposits to the return on their businesses, and conclude that investing surpluses in the business is more attractive than depositing in a financial institution.

Lack of adequate performance standards and incentive schemes: Rural banks that have been successful in deposit mobilisation are often characterised by clearly defined performance standards and incentive schemes to drive uptake.

Client segments are highly differentiated therefore it is important to identify them and develop specific strategies to target different groups. Segmentation of different groups allows a bank to adapt or refine products, services and communication/marketing to the requirements of each group – whether age, gender, livelihood, deposit size etc. In some cases this may require designing of new products for specific segments.

It is useful for rural banks to analyse their client databases in greater depth to more effectively orient marketing and cross selling efforts. *MicroSave* assisted a rural bank in dividing depositors into sub-segments such as:

- **Big depositors:** save in high volume, are more security conscious, compare interest rates offered, need facilities such as ATM, and prefer commercial banks.
- **Busy but regular depositor:** clients engaged fulltime in their business, prefer doorstep service.
- **Relationship:** a segment which depends on recommendations/suggestions from their close circle of friends. They typically prefer to stick to one institution rather than exploring possibilities elsewhere.

Conclusion: Rural banks can develop an edge over commercial banks to capture term deposits. BPRs offer higher interest rates, lower minimum deposits, usually do not charge penalties on early withdrawals, and have convenient local offices. However, to develop and maintain a competitive edge BPRs need to understand their target segments and fine tune their products, services, and marketing efforts. This calls for better market intelligence as well as committed and capable institutional resources.