

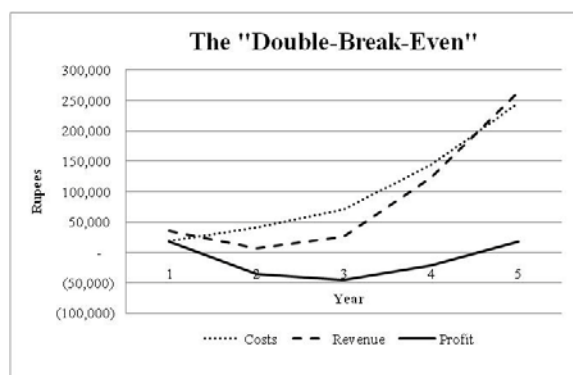
MicroSave India Focus Note 32

Making Business Correspondence Work - Crossing the Second 'Break-Even'

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A recent report on business correspondence (BC) in India¹ found that 95% of the nation's 600,000 villages have no bank branch. At the same time, RBI is opening the door for BCs to charge "reasonable" fees directly to clients, and expanding the categories of actors who may serve as BCs – both major steps towards a viable model.

An earlier *MicroSave* India Focus Note² argued that BCs must cross two independent break-even points before they achieve sustained profitability (see indicative chart, based on an actual business planning exercise, below). The first break-even, which is achieved when the BC or agent(s) sign up large numbers of villagers and earn enrolment fees from the bank, can be achieved in year 1. Agents can enrol customers in pauses between other business activities, and often postpone the technology investments needed to process later transactions.



Hitting the Second Break-Even

The second break-even takes longer, requires serious investment and is far less certain. This may explain why there are now 25 million 'no frills' accounts in India, of which less than 3 million (11%) are active.³

Based on *MicroSave's* business planning activities with various BCs, this Focus Note explores the path to second break-even. It focuses on the currently dominant 'transaction-based' model (in which banks compensate BCs based on transaction volumes).

Hitting the second break-even is a two-part process.

1. To win customer trust by shaping a sound governance regime for transactions.
2. To build impetus by accelerating the scale and scope of product adoption.

¹ Kochhar, Sameer, "Speeding Financial Inclusion", *Skoch Development Foundation*, 2009, p. 40.

² 'Making Business Correspondence Work in India'. *India Focus Note #24, MicroSave*, 2009.

³ Kochhar, p. vii.

⁴ "[A] governance structure is ... an institutional framework in which the integrity of a transaction, or related set of transactions, is decided", Williamson, Oliver E., "The Mechanisms of Governance", *Oxford University Press*, New York, 1996, p. 11.

Establishing Good Governance

Widespread account dormancy signals a failure in the governance of the transactions offered.⁴ For clients, trust can be shattered by experiences like:

- delays of months in receiving account opening clearance from correspondent banks;
- similar delays in receiving smart cards from technology companies;
- coming to withdraw funds and not receiving them;
- difficulty understanding point of sale materials due to low literacy, leading to unrealistic expectations;
- inability to check or confirm balances; and
- other disappointments, such as expecting account statements but not receiving them.

For agents, this failure can mean experiences like the following (all of which can be especially costly for enthusiastic agents who risk investing too quickly):

- delays of months in receiving compensation;
- similar delays in receipt of equipment deliveries;
- lack of back-up support when needed to resolve client problems; and
- delays resulting from irregular/erratic connectivity for data up-loading and processing.

This can lead agents to refuse to provide further service to clients, rather than risk damaging client confidence in other aspects of a business relationship.

BC Companies

For BCs, controlling governance problems requires large investments in:

- A carefully process mapped and adequately staffed service delivery system;
- Monitoring systems to ensure that service quality is rigorously and continuously controlled;
- adequate incentives for client account use; and
- Adequate training and incentives for agents to support clients in the habits of account usage.

If the BC is relying on an alliance or joint venture for distribution it must still monitor agent incentives closely, and be ready to pull out if it is losing control of quality or quantity of service delivery. This may require investment in a network of regional branches or 'super-agents'.

BC Agents

BCs must treat agents as key partners in success. This may mean helping them with business planning, and providing 'step-up' performance incentives. BC business planning models⁵ must fully account for:

- the time and working capital agents invest, and the opportunity cost of these resources;
- the dormant account ratio, and how it is impacted by different BC investments/initiatives;
- time and cost to break-even, and implicit cost of start-up financing; and
- the hard costs to agents of hiring new staff, and the opportunity cost of *their* time.

Accelerating Product Adoption

Once the governance systems are in place it is possible to deliver a profitable suite of services. The market segment is composed of high volume, low balance users.⁶ Experience elsewhere has found that payments and fund transfers are the key to this business.⁷

For example, there are many inter-state migrants in India, and remittances offer a direct and compelling value proposition. M-PESA, a unit of Kenyan telco Safaricom, attracted 6 million customers in 2 years through strong branding and a simple tagline: "send money home".⁸ Remittances are large enough to attract bank commissions that cover service delivery costs.

Cheque deposits, aligned with government payment schemes like the National Rural Employment Guarantee Scheme and aligned with the needs of small traders and merchants, can play a similar role. The BC need not offer cash on the spot initially. Handling these instruments for payment by the bank after clearance is a solid first step.

The faster a BC can facilitate local payment options such as utilities and purchases in local shops, the better. This may require a loan programme to help leading local merchants to purchase POS machines or mobile phone-based solutions.

In more remote rural areas mobile service delivery should be considered. A sales force of agents travelling fixed routes according to a regular schedule and equipped with POS machines will be able to sign on a large number of clients quickly. More frequent schedules will build client trust and product use faster, reduce BC problems with cash security. Well trained and motivated

agents will quickly increase client product use by providing timely, appropriate advice.

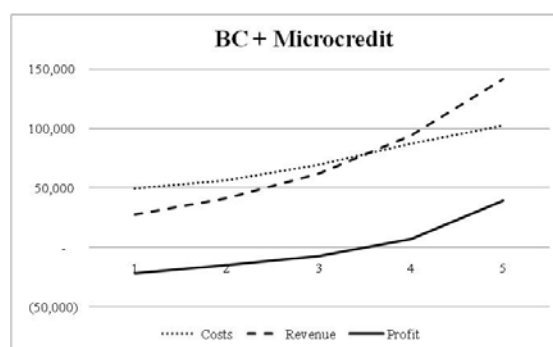
Microcredit delivery can also offer a relatively quick path to profitability. The risk of this 'add-on' is that it may distract BCs from more slowly incubating services. However Drishtee, a BC operating in Uttar Pradesh and Assam, has addressed this issue by linking the delivery of all products under an integrated monitoring and control system. In this way, the marginal cost faced by the agent in delivering slower maturing products can be sharply reduced.

Effective branding is another critical dimension of success. Branding can be discrete in the case of mobile agents, but it should be integrated unmistakably through features in the agent's clothing, the design of POS machines, receipts, passbook stamps, etc. For BCs with many illiterate clients, product take-up can be accelerated by 'user friendly' point of sale materials and transaction forms.

Whatever approach is used, client needs must be clearly understood first. There is no substitute for market research, prototype testing and piloting in advance of large-scale roll-out.

Conclusion

BC can be a profitable business, but the focus must be on getting governance right first. An integrated approach will involve early investments by both the BC and the agent. These cause the first break-even, along with its disappointed client expectations and dormant accounts, to vanish like the mirage that it has always been.



The second break-even is the real one, and it is reached at an earlier date, based on a clearer understanding of client needs, as depicted by the indicative path above.

⁵ *MicroSave* has developed a business modelling template for BCs that links pro forma analysis at agent and BC level, and supports integrated planning for both.

⁶ The salient characteristic of financial activity recently demonstrated (again) in **Collins et. al.**, "Portfolios of the Poor", *Princeton University Press*, Princeton, New Jersey, 2009.

⁷ **Pickens**, Mark et. al., "Scenarios for Branchless Banking in 2020", *CGAP & DFID*, 2009, pp. 4-5.

⁸ **Mas**, Ignacio and Olga Morawczynski, "Designing Mobile Money Services: Lessons from M-PESA", *Innovations*, Spring, 2009, p. 79.