# BIG BANKS & SMALL SAVERS: A new path to profitability[1]

***Can large banks make low-balance accounts viable and profitable?***

***What would make low- income clients more likely to use bank accounts to save?***

***How does the use of different channels influence the outcome for clients and banks?***

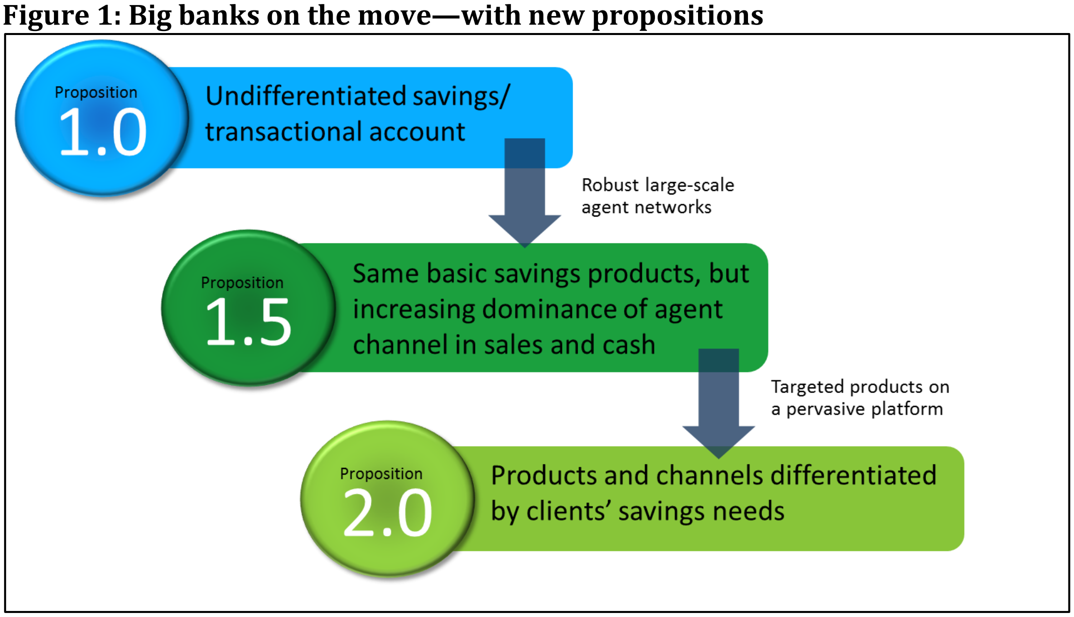
People with low and moderate incomes save in a variety of ways, as the seminal book, *Portfolios of the Poor,* has shown. One way is using a bank account. But the importance of a bank account in a personal or household savings portfolio varies greatly. Often, after some initial activity, clients let bank accounts go dormant; or even if a monthly inflow continues, the account holder makes one immediate withdrawal of all funds. Banks across the developing world encounter these profiles among the mass market of lower-income clients.

The Gateway to Financial Innovations for Savings (GAFIS) project—funded by the Bill & Melinda Gates Foundation, sponsored by Rockefeller Philanthropy Advisors and managed by Bankable Frontier Associates (BFA)—set out to answer how banks might change this dynamic by broadening their value proposition to appeal to poor savers while improving their own bottom line.

GAFIS worked with five leading banks to help design and deliver new "inclusive" products: Bancolombia's *Ahorro a la mano*, a mobile-only savings account with transactional features; BANSEFI (Mexico) and its account linked to conditional cash transfers from the Government; Equity Bank (Kenya) and its *Jijenge* and School Fees goal-driven savings accounts; ICICI Bank (India) and its *Apna* savings account, delivered through CASHPOR, a microfinance institution; and Standard Bank of South Africa and its *AccessSave* accounts.

Collectively, these five banks hold more than $250 billion in assets and serve more than 77 million customers. In total, more than 4 million new GAFIS-linked accounts have been opened during the 3-year project; of which 900,000 were demonstrating savings behavior in the account, including 550,000 who were "new, *poor* savers."

**Figure 1: Big banks on the move—with new propositions**




[1] This is an Executive Summary of the full GAFIS Public Report, written by BFA, available at www.gafis.net.

The GAFIS journey (from 2010 to 2013) is one mirrored in many banks around the world—a journey from traditional, old-fashioned and often *exclusive* banking practices, to 21st century, *inclusive* retail banking. We dub this the journey from banking Proposition 1.0 to Proposition 2.0 (see Figure 1). The most advanced GAFIS banks are, at best, halfway through the journey, but the GAFIS findings and commitment to change inspire optimism that these oft-perceived "lumbering giants" can compete head to head with more nimble, tech-savvy competitors and deliver new value to low-income clients, and shareholders.

***Traditional low-balance bank accounts (Proposition 1.0) are not close to profitable.*** Basic bank accounts are the workhorse product of mass market retail banking today, but they often don't work well for the bank or the customer. For the bank, more than 80% of these accounts typically have too low a balance to be profitable on their own; and as many as 50% lie dormant. Applying full costs, the "stylized" basic bank account with a $30 balance loses the bank as much as $2.79 each month. With current cost structures, banks can only make a profit on these accounts if the balances exceed $800, a virtually unreachable number across a large segment of lower-income clients. For example, the average balance in basic savings accounts at GAFIS banks ranged from $5 to $151; and the median was much lower, ranging from $2 to $20. Part of the low-balance problem is that customers find it inconvenient and costly to make small deposits or withdrawals through a bank branch structure, so most household money remains outside the banking system.

***Structural and business model change may need to precede product innovation.*** Initially framed as an issue of product innovation, improving the profitability of a basic account in fact demands innovation in service channels, internal structure and business model. Large banks foster strong internal competition for financial, human and IT resources. Marginal or experimental products aimed at inclusion are unlikely to succeed for long in the ongoing battle for resourcing without institutional buy-in. But external support from the GAFIS project helped to facilitate and buttress the development of new inclusive propositions for the GAFIS banks. Peer-learning, new analytical tools and external accountability all supported significant institutional shifts.

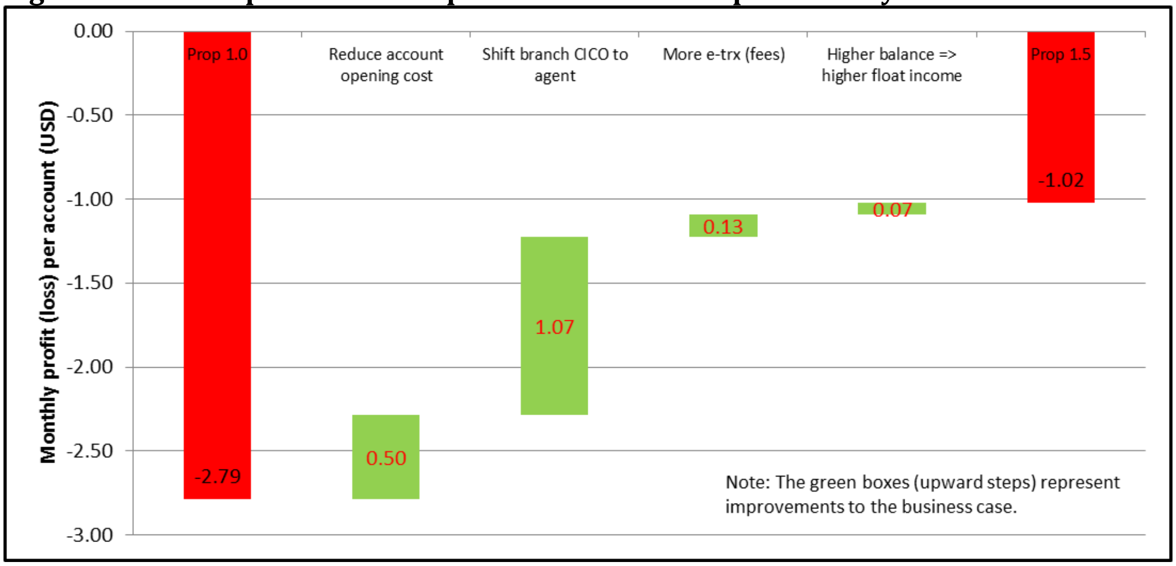
One indicator has been the creation of new inclusive banking divisions within two of GAFIS' large commercial banks, with bottom-line responsibility for clients in the inclusive segment. New products and channels are now managed in a more integrated fashion—with proactive CEO and board support.

Another indicator is change to costing methodologies. Realizing that existing cost allocations unduly burden its new mobile-based and agent-delivered products with unrelated expenses, one bank recalculated a lower monthly unit cost for accounts opened remotely and serviced (for cash in/out) off-site at agents or at an ATM without a card. This cost reduction enabled a positive business case for the new product.

***Development of an agent channel to originate and activate accounts (Proposition 1.5) sharply improves the business case.*** Even without changing the product offering, the deployment of agents who can originate new accounts and take deposits from clients radically improves the business case for banks—helping reduce the net loss per account per month from -$2.79 to -$1.02 (see Figure 2). The GAFIS banks now collectively report some 25,000 agents, almost 10 times the number at the start of the project, and five times the current number of their branches.

The new channel improves the business case by reducing costs. Agents reduce the cost of cash-handling transactions to as low as a fifth of that in the branch. Agents also reduce origination costs relative to branch-opened accounts. GAFIS observed variations in impact on the activation rate: aggressive selling by agents can lead to high dormancy, but the post-opening "high touch" by some agent models can improve activation and usage rates—as shown by the 70% active rate for one bank with a poor, rural client base (compared with less than 20% active ratios for typical G2P-driven bank account openings in that country).

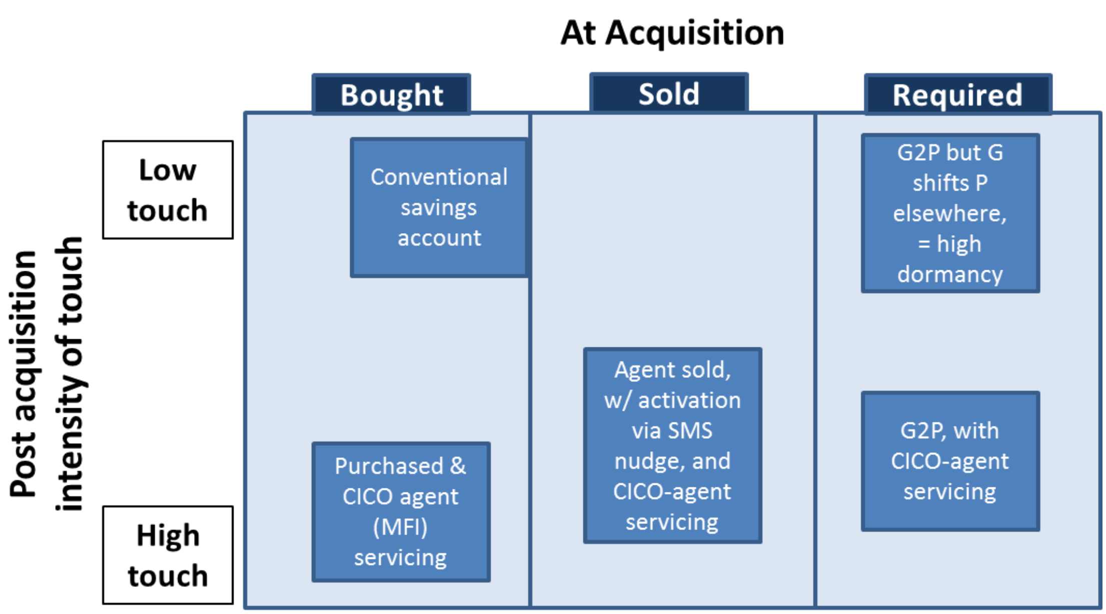
**Figure 2: How Proposition 1.5 improves account-level profitability**




On the income side, GAFIS banks provide evidence that an agent channel can play a significant role in deposit mobilization. For example, since early 2011, the number of agent transactions at one GAFIS bank now exceeds that through any other channel—with deposit value twice that of withdrawals.

In addition to the agent channel, GAFIS banks are also starting to use new communications channels to connect with customers post-opening, sending out SMS messages with reminders, information and offers. While use of SMS is still at an early stage, initial evidence suggests that **SMS messages can stimulate higher activation rates in newly opened accounts**, further improving the business case. At one GAFIS bank, sending a choreographed series of SMS messages to new account holders cut inactive ratios by around a third year-on-year; and engaging SMS messages at another are showing early payoff.

**Figure 3: Intensity of "touch" for bought, sold and required savings products**



At the same time, some of the banks are battling with mobile operators—which are rapidly emerging as competitors for both financial services and related agent channels—for what they consider fair access and pricing on channels used for transactional banking. One GAFIS bank faces a looming 600% increase in charges to access the mobile channel to facilitate mobile transactions, and another faces a doubling.

***The retail bank of the future (Proposition 2.0) offers new tailored and flexible products.*** A robust agent channel enables banks to focus on tailoring and targeting products to specific customer needs. GAFIS banks are starting to combine "big data" from their mass-market accounts with qualitative survey insights to better understand their low-income client bases. This analytics enables banks to better identify potentially active clients, which in turn increases the odds of not only marketing savings but cross-selling other products.

By analyzing bank data, complemented by surveys and financial diaries of clients, **GAFIS identified three different patterns of *savings* behavior—A) Spend down slowly; B) Accumulate; C) Preserve**, which are all different from *non*-savings patterns like "dump & pull". Low-income clients today typically use informal products to undertake different types of savings because suitable bank products have not been affordable or accessible. Broadening formal savings options to support such a range of different types of savings behavior is a way banks can improve their value proposition to low-income savers.

## IMPLICATIONS FOR OTHER BANKS

GAFIS banks and countries have unique features, but as a group they are quite typical of large commercial banks in emerging markets worldwide. For this wider group, the GAFIS learnings have at least three broad implications:

- Banks are competing with non-bank providers and other informal instruments to capture transactional accounts which show "spend down slowly" behavior;
- However, as more cash is converted to electronic value, the battle will shift to the payment system of the country. Depending on regulations, banks will likely compete with specialist providers—but may still retain the advantage if they hold the core account;
- To target offers and incentives for additional products on their electronic platforms, **financial providers need the capacity to collect, integrate, and analyze client data as never before**. The data is likely to come from their own or others' transactional "big data" bases and from ongoing, systematic client-level surveys, which add a qualitative perspective.

Achieving these changes inside large, complex organizations will require that **sufficient resources are allocated to the processes of change management**. The challenge for banks is not only about designing new products or rolling out new channels to serve a new segment. Beyond these, it involves catalyzing and managing the ripple effects of changes throughout existing structures, systems, knowledge bases and people.

The payoff? Banks that shift their R&D and operations toward Proposition 2.0 are more likely to endure and succeed as large retail banks in the future. The process of learning to serve low-income clients profitably with new, flexible and cost-effective products should enhance a bank's ability to serve its mid- and upper-income clients. Better serving small savers could in fact change the face of large 21st century commercial and retail banking.

**Please find the Full Report, written by project manager Bankable Frontier Associates, available for download at [www.gafis.net](http://www.gafis.net).**