EFFECTS OF AGENCY BANKING ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

BY

SIMBOLEY BRENDA CHEMUTAI

UNITED STATES INTERNATIONAL UNIVERSITY AFRICA

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A Report Submitted to the Chandaria School of Business in Partial Fulfillment of the Requirement for the Degree of Masters in Business Administration (MBA)

UNITED STATES INTERNATIONAL UNIVERSITY AFRICA

SPRING 2017
DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the United States International University in Nairobi for academic credit.

Signed:  _____________________  
Date:  _____________________

Brenda Chemutai (ID 633425)

This project has been presented for examination with my approval as the appointed supervisor.

Signed:  _____________________  
Date:  _____________________

Mr. Kepha Oyaro

Signed:  _____________________  
Date:  _____________________

Dean, Chandaria School of Business
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ACKNOWLEDGEMENT

My appreciation goes to my family for the support and encouragement. My mother for pushing me to take this step into furthering my education.

I thank my supervisor, Kepha Oyaro, whose relentless support and encouragement saw me through this research report.

I would also like to appreciate the respondents. I extend my sincere gratitude to for taking time and filling the questionnaires.
Access to financial services especially in rural areas was not always an easy task in Kenya. The cost of travelling to a bank was often higher than the cost of making a transaction in a brick and motor institution. Since 2010, the banking sector has been making strides towards greater financial inclusion through the introduction of agency banking. Rather than using bank branches and their own field officers, they offer banking and payment services through retail outlets, including grocery stores, pharmacies, retail shops, gas stations among others. This study sought to investigate the effect of agency banking on the financial performance of commercial banks in Kenya. The study had three specific objectives: determining the effect of agency banking on customer growth, determining the effect of agency banking on deposit growth and to determine the effect of agency banking on cost reduction.

The study employed a descriptive research design. The study sampled 120 agents and 12 middle managers from the banks that have rolled out agency banking. Primary data was collected with the use of questionnaires. Data analysis was done using SPSS and Microsoft Excel to generate quantitative reports. The collected data was analyzed and presented in the form of tabulations and percentages.

The study established that there was a significant growth in customers as a result of agency banking. It also established that there was a positive correlation between most of the services offered by agents and customer growth. It also determined that a significant amount of accounts are opened on a daily basis by agents. The study concluded that agency banking has to a great extent influenced and improved financial inclusion. On deposit growth, the study established that agents contributed significantly to the overall deposits collected by banks. Middle managers agreed that they rely on agents to bring in a significant portion of deposits for the overall performance of banks.

On cost reduction, the study determined that agency banking reduced the costs that would be incurred in building the brick and motor institutions and banking halls. However, the study also established that there were significant costs that would hinder agency services such as security and transaction costs. The study established that there was a positive correlation between transaction, infrastructure costs and cost reduction. An increase in transaction and infrastructure costs would bring about an increase in the overall cost of agency banking. Some
of the measures highlighted by the study to curb these costs included, improving technology, reducing transaction costs as well as improving customer care. The study recommends that customer care needs to be improved as services are being relayed to customers. There is also the need to develop new products and services so as to reach more customers. The study further recommends increased awareness of the service offerings as well as reduced charges for cash deposits so as to increase the volume of transactions being carried out via agents. This study recommends the streamlining of operational costs involved in providing financial services. Improved network coverage through technologically advanced equipment is another step through which agents can provide timely and efficient services.
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<tr>
<td>AFS</td>
<td>Agency Financial Services</td>
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<tr>
<td>ATM</td>
<td>Automatic Teller Machine</td>
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<td>CICO</td>
<td>Cash In Cash Out</td>
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<td>CBK</td>
<td>Central Bank of Kenya</td>
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<td>ID</td>
<td>Identification</td>
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<td>IFC</td>
<td>International Financial Corporation</td>
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<tr>
<td>OTC</td>
<td>Over the Counter</td>
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<tr>
<td>POS</td>
<td>Point of sale</td>
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<tr>
<td>PIN</td>
<td>Personal Identification Number</td>
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<tr>
<td>ROA</td>
<td>Return on Assets</td>
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<td>ROE</td>
<td>Return on Equity</td>
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<td>ROC</td>
<td>Return on Capital</td>
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<td>ROI</td>
<td>Return on Investment</td>
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<tr>
<td>SACCOS</td>
<td>Savings and Credit Cooperative Societies</td>
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<td>SPSS</td>
<td>Statistical Package for the Social Science</td>
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CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the study

Access to financial services is one of the keys to alleviating poverty and achieving sustainable economic growth. Two billion people worldwide still lack access to regulated financial services (Grandolini, 2015). Anything that bars access to financial services undermines an individual’s or household’s ability to take responsibility for their own financial security, in turn potentially damaging their well-being. Access to financial services is recognized globally as important to financial stability and the integrity of markets (Collard, Coppack, Lowe, & Sarkar, 2016). A large percentage of these underserved population are domiciled in developing countries where they live in remote areas where there are no bank branches making it difficult and costly to access financial services.

Access related impediments are owed to the high cost inherent in the traditional brick and mortar approach that characterizes normal bank branches. Poor households have needs for financial services; inaccessibility to credit from formal system leads them to borrow from money lenders to or from friends and relatives at a much higher and unsustainable rate of interest. Many countries especially in developing nations are increasingly embracing branchless banking as a viable means of extending basic financial services to reach out to under-served urban and rural population. It significantly reduces set-up and delivery costs, offering cash-in/cash-out operations only or a broader range of financial services to customers who usually feel more comfortable banking at their local merchants than at traditional bank branches (Lozano & Mandrile, 2010).

The revolution of information technology has influenced almost every facet of life, among them is the banking sector. Service delivery in banks has greatly transitioned from visiting banking halls to making transactions without even being in the bank. The need to reach customers in low income areas gave rise to agency banking. The development of agency banking services is aimed at decongesting banking halls, reduce the incidences of long queues in banking halls as well as providing services at a personal level in residential estates and even rural areas (Kwabena, 2013).
Agency banking is defined as the provision of banking services by a third-party agency to customers on behalf of a licensed, prudentially-regulated financial institution, such as a bank or any other deposit taking commercial bank (Kerich, 2015). An agent, in this case, is a retail outlet contracted by a financial institution to process client transactions. It is the owner or an employee of the retail outlet who conducts the transaction and lets clients deposit, withdraw, and transfer funds, pay their bills, inquire about an account balance, or receive government benefits or a direct deposit from their employer (Wanyoike, 2014).

Banking agents can be pharmacies, supermarkets, convenience stores, lottery outlets, post offices, and many more. In Kenya, these agents are increasingly utilized as important distribution channels for financial institutions. The scope of offered services may include facilities to conduct bank and stock market transactions, account transfers, balance inquiries, bill payments, and stop-payment requests (Vutsengwa & Ngugi, 2013). Banking agents are usually equipped with a combination of point of sale (POS) card reader, mobile phone, barcode scanner to scan bills for bill payment transactions, Personal Identification Number (PIN) pads, and sometimes Personal computers (PCs) that connect with the bank’s server using personal dial up or other data connection. Clients that transact at the agent use a magnetic stripe bank card or their mobile phone to access their bank account (Wanyoike, 2014).

Agency banking was first developed in Brazil in 1999 and has gained popularity in developing countries. It is said to have tremendously impacted the financial performance of banks in Africa and the world over. However, agency banking is a fairly new concept in Africa with it being highly implemented in Kenya and South Africa (Agalla, 2014). Agency banking took effect in Kenya in May 2010 after the publication of prudential guidelines by the Central Bank of Kenya. Central Bank of Kenya is the regulating authority with 45 banking institutions whereby 44 are commercial banks and 1 is a mortgage finance company. As at June 30, 2015, Central Bank of Kenya had authorized 17 commercial banks to offer banking services through third parties (agents). Since 2010 to June 2015, a total of 38,297 agents had been contracted by the 17 banks. These agents had undertaken over 175.4 million transactions valued at KShs. 930.1 billion (CBK, 2015).

The agency banking retail approach is designed to help banks increase their outreach without incurring additional costs of setting up. The banks have come together under Kenya Bankers
Association (KBA), which serves as a lobby for the banks interests and addresses issues affecting member institutions. The commercial banks and non-banking financial institutions offer corporate and retail banking services but a small number, mainly comprises the large banks, offer other services including investment banking (Orita, 2015).

Banks are continuously seeking to automate and optimize their operations into productive and customer friendly processes. Therefore the transition from traditional branch banking to agency banking has caused banks to develop strategies that will attract new customers and retain existing ones. The desire to reduce both operational and administrative costs has resulted in adoption of agency banking. For this reason, the banking industry has become increasingly competitive and it is therefore paramount for banks to make the transition to agency banking to remain relevant. A decline in the financial performance of the commercial banks will therefore have a significant implication on the economic growth of the country (Kombe & Wafula, 2015)

Commercial banks in Kenya are profit making institutions and thus profit can be termed as the measure of financial performance. Financial performance is the degree in which financial objectives are being accomplished in an organization. Several financial ratios have been developed to measure profitability. They include Return on Asset (ROA), Return on Capital (ROC), Return on Investment (ROI) and Return on Equity (ROE). Bank regulators and analysts have used ROA and ROE to assess industry performance and forecast trends in market structure as inputs in statistical models to predict bank failures and mergers and for a variety of other purposes where a measure of profitability is desired (Arisa & Muturi, 2015). Return on assets is the ratio of annual net income to average total assets during a financial year. It measures efficiency of the business in using its assets to generate net income. ROA is derived by dividing annual net income by average total assets. Average total assets are derived by dividing the sum of total assets at the beginning and at the end of the financial year by two. Return on owner's equity (ROE) ratio is calculated as net profit after tax divided by the total shareholders’ equity. This ratio measures the shareholders rate of return on their investment in the company (Gold, 2016).
1.2 Statement of the Problem

Access to banking services especially in rural areas in Kenya was often a rigorous endeavor. It required customers to travel long distances and make queues at banking halls to receive services from banks. For this reason, commercial banks sought to move closer to customers by developing agents within local towns. (Mwende, Bichanga and Mosoti, 2015). Agency banking has created greater access to formal banking services and it represents a cheaper alternative to conventional branch based banking through the use of delivery channels like retail outlets, mobile phones, internet and automated teller machines (ATMs). In a bid to take advantage of the cost-saving and accessibility brought about by the agency banking model, Kenyan financial institutions have over the last five years embarked on an aggressive entry into this segment.

According to the CBK, 17 commercial banks had contracted 39,871 agents as at September 2015. (Ngigi, 2016) Some of the banks that have rolled out the agency model include, Post bank (Benki yangu), Equity bank (Equity Mashinani), KCB bank (KCB Mtaani), Co-op bank (Co-op Kwa Jirani) and Family bank (Pesa pap). The rationale for adopting agency banking was to enable Kenyan financial institutions to take advantage of the cost saving and accessibility brought about by the agency banking model. (Mwirigi, 2013). According to the (CBK 2014), there was significant growth in retail deposits amongst commercial banks that had embraced agency banking. However, the correlation between the performance of commercial banks and agency banking has yet to be clearly documented.

Several studies have been done for instance, Kamau, (2012), undertook a study on the relationship between agency banking and financial performance of banks in Kenya and established negative and weak correlation between the two. Mwangi, (2011) sought to establish role of agency banking in the performance of commercial banks in Kenya and established that cost effectiveness (infrastructure, human resource and security cost) associated with agency banks positively influence banks financial performance. Kithuka (2012), studied factors influencing growth of agency banking in Kenya and established that convenience of its technology, accessibility and cost has influenced its use. The issue which arises is to whether the agency banking has succeeded in achieving the set objectives of the commercial banks. The queues in the banking halls may have reduced considerably, more accounts opened by the targeted populace and general financial services availed to the unbanked but have these agents
significantly affected the performance of commercial banks? This study will be aimed at bridging the existing knowledge gap and giving more insight on the role of agency banking in the financial performance of commercial banks in Kenya,

The specific objectives of the study were; to assess the effects of agency banking on customer growth, to determine the effects of agency banking on deposit growth, to evaluate the effects of agency banking on cost reduction

1.3 General Objective
The general objective of this study was to analyze the effects of agency banking on the financial performance of commercial banks in Kenya.

1.4 Specific Objectives

1.4.1 To determine the effect of agency banking on customer growth in commercial banks

1.4.2 To determine the effect of agency banking on deposit growth in commercial banks’

1.4.3 To determine the effect of agency banking on cost reduction in commercial banks

1.5 Importance/Significance of the Study

1.5.1 Financial Institutions
The study will be of great importance to financial institutions as they will evaluate their performance/profitability in relation to agency banking. It will also provide banks who are yet to venture into agency banking valuable insight on the significant impact that agency banking has on the financial performance; in a bid to guide them into adopting and managing their agency banking channels.

1.5.2 Government Policy Makers
The findings of this study would be important to policy makers in government especially the central bank to reduce the regulations and policies that do affect the performance of agents such as float restrictions hence lowering the overall performance of banks.
1.5.3 Academicians and Researchers
The study would contribute to the existing body of knowledge on agency banking and be of use by academicians. The findings would further be of use as a reference point in further research in this area.

1.6 Scope of the Study
The study was conducted in Nairobi County with the population focus being 12 commercial banks that have rolled out agency banking services. The study targeted bank agents as well as middle managers of the respective banks. The study was conducted within the month of September to November.

1.7 Definition of Terms

1.7.1 Agency Banking
Agent banking means providing banking services to the bank customers through the engaged agents under a valid agency agreement, rather than a teller/cashier. It is the owner of an outlet, who conducts banking transactions on behalf of the concerned bank (Ferdous, Mosharafa & Farzana 2015).

1.7.2 Bank Agent
Refers to any third party acting on behalf of a bank (or other principal), whether pursuant to an agency agreement, service agreement, or other similar arrangement (Lauer, Dias, & Tarazi, 2011).

1.7.3 Commercial Bank
A financial institution that provides banking and other financial services to their customers. A bank is generally understood as an institution which provides fundamental banking services such as accepting deposits and providing loans (Sundaram & Sriram, 2015).

1.7.4 Financial Inclusion
The process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost. It can also be referred to universal access to a wide range of financial services at a reasonable cost. These include not only banking products but also other financial services such as insurance and equity products (Malik, 2014)
1.7.5 Financial Performance
It is the process of measuring the results of a firm's policies and operations in monetary terms. It is used to measure firm's overall financial health over a given period of time (Eshna, 2012).

1.7.6 Customer Growth
It is defined as successfully guiding customers through adoption, retention, expansion and advocacy (Wojno, 2016).

1.7.7 Deposits
Deposits consist of money placed into banking institutions for safekeeping. These deposits are made to deposit accounts such as savings accounts, checking accounts and money market accounts. The account holder has the right to withdraw deposited funds, as set forth in the terms and conditions governing the account agreement (Investopedia, 2017).

1.7.8 Cost Reduction
It is defined as the process of used to save the unit cost of the product without compromising its quality by using new and improved methods (Surbhi, 2015).

1.8 Chapter Summary
This chapter has discussed the background of the problem and therefore giving a brief introduction into what agency banking is. The statement of the problem to be researched and the purpose of this study has been given. The significance of the study to different stake holders and scope of the study have been discussed together with the definition of important terms in the study within this chapter.

The next chapter would give a literature review of the effects of agency banking; it would look at the literature in the area in great detail so as to understand previous works on the same. Chapter three is going to explain the methodology of the research to be done. It would give the research design which includes the methods that would be used to obtain information among other details. Chapter four presents the data collected from the field, its analysis, and finally the interpretation of the findings. The data is presented in form of tables. Chapter five gives the discussion of findings, conclusions and recommendations. It also gives the recommendations for further studies.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction
This chapter reviews the literature on the contribution of agency banking on the financial performance of commercial banks in Kenya. The following areas are captured customer turnover, deposits, costs and income growth.

2.2 Effects of Agency Banking on Customer Growth
The ultimate goal for banks is to maintain a certain level of customers that will enable them generate profits. Therefore the aim is to retain existing and gain new customers. By so doing, customer growth becomes a paramount objective for the banks. Banks are realizing that revenue growth cannot be taken for granted anymore, and that survival will not simply be a question of turning revenues into reasonable profits, but to actively secure that flow of revenues in the first place (Ruttoh, 2013).

In other words, banks must shift their focus away from the singular obsession with efficiency of recent years, and return their gaze to revenue growth, market share, and put back in the center of attention the very source of that revenue: the customer. The consumer marketplace is continuing to fragment into smaller subsets of needs and behaviors, which is affecting the way banks and other financial institutions market products and services Approaching new customer segments as a potential source of additional revenue – mainly lower, but secured income segments - retired people and public institutions employees (e.g. teachers) as potential target groups for simple and low volume loan products (cash loan, credit card) can expand the revenues of the bank (Ruttoh, 2013).

The products and services of most commercial banks in Kenya can be targeted to meet the financial needs of the households as well as their income generating activities; many commercial banks in Kenya are beginning to examine retail banking as an opportunity to explore and are even changing their operations from corporate banking to retail banking. This is because there is stiff competition in the banking industry that has forced them to diversify into new markets. Customer growth begins with customer acquisition and retention. Acquisition refers to the initial commencement of a business relationship when a venture
brings a customer on board. Customer growth can be attributed to accessibility, convenience and financial inclusion.

2.2.1 Accessibility
Financial inclusion has been on the low and this can be attributed to the long distance customers, in rural areas especially, have to walk to access financial services. Sometimes, the amount of money someone wants to withdraw from the bank is equivalent, or even less than the transportation cost, while others find the new ultra-modern banking halls intimidating. Thus they avoid formal financial services and opt for informal financial services which are readily accessible in rural areas (Wainaina, 2011). Access to finance is critical for sustainable economic growth and social development. Financial inclusion empowers low income people and marginalized sectors of society to actively participate in the economy, which leads to increasing employment and decreasing poverty levels (Bold, 2011).

Banking agencies help financial institutions to divert existing customers from crowded branches providing a “complementary” often more convenient channel. Other financial institutions especially in developing markets use agents to reach an “additional” client segment or geography. Reaching poor clients in rural areas is often prohibitively expensive for financial institutions since transaction numbers and volumes do not cover the cost of a branch. In such environments, banking agents that piggy back on existing retail infrastructure – and lower set up and running cost- can play a vital role in offering many low income people their first-time access to range of financial services. Also, low – income clients often feel more comfortable banking at their local store than walking into a brick and mortar structure. Taking the bank to the community has not only widened and deepened the financial market but it has also enhanced customer loyalty to respective banks. This has continued to create committed entrepreneur-clients. Agency banking has enabled bank customer to access the banking services within the comfort of their neighbor-hood (Jaldesa, Muturi & Sumba 2015)

2.2.2 Convenience
Agency banking was introduced to aid increasing convenience in banking for customers especially for those based in rural areas as the agents operating hours are more since some agents open as early as 0:600 hours and close as late as 01:00 hours. Through agency banking, customers can deposit at free or low costs and withdraw at a cost that would have previously
included transport. In addition, agency banking is deemed more convenient as they open for longer hours compared to formal banks, there are shorter queues to access services, more accessible for illiterates and the very poor who might feel intimidated in branches. Therefore customers save on time they have to travel to a bank branch, and the time they have to wait in line to be served (Mwangi & Wanyoike, 2012). Banks are now providing special services, value-added services, by way of increasing convenience, tapping a broader market, increasing service channels and lowering cost in accessing their services. When there is a great demand for these services like school opening times, month end and other prime times the long queues lead to disservice to customers, who in today’s Kenyan market have a choice of going to competitors reducing revenues therefore taking away the business (Jaldesa, Muturi & Sumba, 2015).

2.2.3 Financial Inclusion

Financial inclusion means much more than just banking to the unbanked. It now refers to the convergence of various bank and non-bank players to provide financial services at lower costs, wider reach and greater convenience to all end consumers of financial services, unbanked otherwise (Finacle, 2012). Fact that if poor are not connected to our formal financial system, their growth and improvement will not take place and as the country grows they will still be poor without access to basic necessities. Secondly due to lack of financial system awareness they can be lured to enter in fraud money saving schemes and can be looted. They lack awareness of investing and will risk the future of their children.

Unrestrained access to public goods and services is the sine qua non of an open and efficient society. As banking services are in the nature of public good, it is essential that availability of banking and payment services to the entire population without discrimination is the prime objective of the public policy. Importance of financial inclusion can be summarized as below: If customer is financially educated, he will make better financial choices. It will help in improving overall growth of the country. Access to financial services at an affordable cost will improve life of the poor (Damodaran, 2013). Consumers’ adoption of multiple channels has fueled their expectation of true multi-channel banking, which allows them to transition seamlessly between touch points as they fulfil several, or even a single transaction. Agency banking, an important channel innovation that has improved banking penetration in
underserved areas in the past, can help banks top into other segments, by becoming an integrated component of multi-channel banking (Finacle, 2012). Financial inclusion empowers low income people and marginalized sectors of society to actively participate in the economy, which leads to increasing employment and decreasing poverty levels (Bold, 2011).

Companies are always looking to expand their share of the market, in addition to trying to grow the size of the total market by appealing to larger demographics, lowering prices, or through advertising. In addition, when financial agent banks do not have branches that are close to the customer, the customer is less likely to use and transact with their service. However, the emergence of new delivery models as a way to drastically change the economics of banking the poor. By using retail points as agent banking other providers can offer saving services in a commercially viable way by reducing fixed costs and encouraging entrepreneurs to use the service more often, thereby providing access to additional revenue sources (Aduda, Kiragu & Ndwiga 2013).

The Global Findex Database 2014 said seventy five per cent, or eight out of every ten Kenyan adults, is banked through bank and mobile money accounts. Kenya’s banked population is above the global average of sixty two per cent. Kenya’s high financial inclusion rate to the success of mobile money in making banking services available to hitherto unbanked populations especially the rural poor, women and illiterate communities and expanding the scope of services offered through mobile cash platforms as well as bank agents (East African, 2015).

2.3 Effects of Agency Banking on Deposit Growth

Commercial banks are institutions that engage in two distinct types of activities, one on each side of the balance sheet deposit-taking and lending. Commercial Banks deposits are dependent on depositor’s money as a source of funds (Werner, 2014). Bank deposits represent the most significant components of the money supply used by the public, and changes in money growth are highly correlated with changes in the prices of goods and services in the economy (Mashamba, Magweva, & Gumbo, 2014). Bank deposits are made to deposit accounts at a banking institution, such as savings accounts, checking accounts, time deposit accounts and money market accounts. The account holder has the right to withdraw any deposited funds, as set forth in the terms and conditions of the account. The "deposit" itself is a liability owed by
the bank to the depositor (the person or entity that made the deposit), and refers to this liability rather than to the actual funds that are deposited (Adem, 2015). Consumers deposit their money in banks as a safety measure, for ease of access and the possibility of returns. The motive is to keep the money in safety for future use.

Bank deposits represent the most significant components of the money supply used by the public, and changes in money growth are highly correlated with changes in the prices of goods and services in the economy. Deposits provide most of the raw materials for bank loans and thus represent the ultimate source of the bank’s profits and growth. Banks make profit by using their deposits, therefore it is said that depositors can disciple banks (Gemedu, 2012). Commercial banks are critical to the development process. By granting loans in areas such as agriculture, manufacturing, services, construction and energy sectors, banks contribute to the development of the country. Bank loan portfolio including volume, tenor and structure may be generally influenced by their expectations of the performance of economy both in terms of stability and level of performance. As cited by banks make out more loans during periods of boom and reduced level of macroeconomic uncertainty and curtail lending when the economy is in recession (Churchill, 2014).

2.3.1 Accessibility

There is a positive correlation between bank deposits and financial service expansion. Since it’s costly to build banking halls in every town, banks opted to increase their service provision through agents. These agents not only influence deposits but agency banking is also influenced by the level of deposits in a certain area. It is expected that banks expand their facilities and service provision by considering factors such as competition, deposit potential, regional income and existence to infrastructure. Thus deposits can also be a factor to consider when in need of an agency banking expansion strategy. By creating greater access to financial services, agency banking has in turn increased the level of deposits for banks. Providing the “un-banked” access to safer and cheaper financial services has led to banks recording more deposits than ever before. Equity bank attributes two thirds of the income from agency banking as a result of deposits and the remainder on withdrawals (Bankelele, 2015).

Han and Melecky (2013), found that a broader access to and use of bank deposits can significantly mitigate bank deposit withdrawals or growth slowdowns in times of financial
stress. Where a large share of population still lacks access to bank deposits, trust in banks is yet to be firmly established, and the integration in global financial flows is growing. In addition to the access and use of deposits, bank stability and the dummy for the occurrence of banking crises are the most significant explanatory variables in our regressions. The results hold even when accounting for the possible leverage effects of outliers. The main message is that countries should recognize that policies to promote a broader use of bank deposits could improve resilience of bank funding. Such policies can thus enhance overall financial stability and complement the mainstream macro-prudential policies to foster stability of the financial system (Han, et al., 2013).

2.3.2 Deposit Mobilization in Banking

Financial institutions provide a system through which savers deposit their money and borrowers can access those funds. The process by which deposits are transformed by the banking sector into real productive capital is at the core of financial intermediation (Abel, 2013).

Deposit mobilization is defined as the process of encouraging customers to deposit with the bank or persuading new clients to open accounts with the bank. The motivation for mobilizing savings is in the lower cost compared to other sources of funds. Deposits are mobilized to meet the required liquidity for loans. Deposit mobilization is the collection of cash or funds by a financial institution from the public through its current, savings, fixed, recurring accounts and other specialized schemes (Banson, Sey, & Sakoe, 2013). To enhance profitability, banks seek to minimize their expenditure and are forced to mobilize low cost deposits. Thus the amount of deposits are important. The deposit size largely decide the banks capability to lend money to borrowers; the higher the deposits, the higher will be the funds at the disposal of a bank to lend and earn profits. However deposit growth is profitable only if the commercial bank does not incur additional expenses to obtain and retain cash (Adem, 2015).

Banks simply cannot function without deposits from savers in the economy. Many developing countries suffer from low domestic savings rates. Domestic deposits traditionally provide a cheap and reliable source of funds for development, which is of great value to developing countries, especially when the economy has difficulty raising capital in international markets. Banks generally fund more of their loan books with customer deposits in order to stand more
robustly against liquidity squeezes and contribute to the stability of the banking system. Any decline in the amount of deposits at the banks raises important questions about whether the banks will be able to remain successful and meet the credit needs of the economy (Abel, 2013).

Mobilization of deposits is one of the important functions of banking business. It is an important source of working fund for the bank. Deposit mobilization is an indispensable factor to increase the sources of the banks to serve effectively. Mobilization of deposit plays an important role in providing satisfactory service to different sectors of the economy. The commercial banks must tap deposits from urban and rural areas. This helps the banks to provide large amount of funds to priority sectors for development. The success of the banking greatly lies on the deposit mobilization. Performances of the bank depend on deposits, as the deposits are normally considered as a cost effective source of working fund. Mobilization of rural savings is one of the important objectives of the Commercial Banks. It helps to expand banking operations (Shettar, 2014).

2.3.3 Deposit Interest Rate

The other most important consideration regarding demand for particular deposit is the expected rate of interest on deposits. This implies that demand for a particular deposit is positively related to expected rate of interest on deposits. The higher the rate of interest, the more money will be saved, since at higher interest rates people will be more willing to forgo present consumption. With increase in interest rate, people are encouraged to save more income and consume less in order to earn more return on bank deposits in the long run (Awole, 2016).

According to Wubitu (2012), deposit interest rate has a positive insignificant impact with bank deposit growth. He found that holding other things constant, a percentage increase in deposit interest rate will lead to an 11.2 percent increase in bank deposit growth at an insignificant level of more than 10 percent. The positive sign suggests that the substitution effect outweighs the income effect. Economic theory suggests that a rise in interest rate can have either positive or negative effect on bank deposit growth. Awole (2016), agreed that interest rate in the banking system is held as investment cost from the investor’s point of view and opportunity cost from the depositor’s point of view. Thus, capital market forces balance interest rates. In other words, the just and correct interest rate should be determined through market mechanism, that is, interest rate is balanced in supply and demand conditions in proportion with the inflation.
rate. Deposits are more interest rate sensitive and banks may choose to increase investments in interest rate sensitive assets and to decrease investments in loans. That is commercial bank deposits are interest rate sensitive, therefore as the interest rate changes the deposit of the commercial banks will change (Awole, 2016).

It is known that depositors bring money to the bank which the bank in turn lends it to borrowers. The gross earnings of the bank are determined by the volume and composition of loanable funds and the rates at which they are loaned. After losses and expenses of operation are deducted, the net earnings provide a margin out of which interest on 24 deposits can be paid. Because of the competition for these funds among bankers who desire to loan them at a profit, a bank must pay interest or lose deposits to a competitor. The payment of interest on deposits is explained in this wise, like any other interest rate (Awole, 2016).

Opuku (2011) argued that high discount rates reduce returns on loans from firms and individuals who borrow from the banks, deposits and consequently savers will offer fewer deposits to banks. Lower discount rate allows banks to borrow more and extend more loans to borrowers as well as reducing possible moral hazards and adverse selection. It further facilitates loan repayments and increase returns to depositors. This facilitates deposit mobilization by commercial banks and all things being equal more deposits will be received.

2.4 Effects of Agency Banking on Cost Reduction

The high costs inherent in traditional banking is considered as one of the impediments to providing financial services to the society and most especially to the “un-banked” population. The minimum deposit amounts for opening bank accounts had previously led to customers shying away from banking. The amount of money expended to serve a poor customer with a small balance and conducting small transaction is too great to make the accounts viable (Veniard, 2010). However, through agency banking, the delivery of services has moved from the traditional way towards a more efficient and customer friendly service. Agency banking radically reduces the cost of setting up points of contact with customers, allowing agents, to reach out into areas where building branches would be too expensive. Banks expansion is usually limited due to the high initial cost of opening a branch and in many areas due to the low economic status of the people living in these areas. The set up costs incurred by banks when opening branches takes several years to translate into profits and this leads to limited
expansion. Banks are now partnering with already established businesses across the country in order to take services closer to the people. (Kipng'etich, 2014). The bank does not incur cost of recruiting new employees because the agent that is approved by bank is the one who hires or carries out the transactions himself. Agents purchase the POS machines and mobile phones. Systems are installed in the mobile phones to allow the agents to transact and send the data to the central processing center where the information is captured and data reconciled. Therefore the only cost the bank incurs is branding the outlets. The bank saves costs in terms of advertising and hiring sales personnel. This is the work of the agent as he is paid according to the number of transactions and accounts opened therefore the agent makes sure there is traffic in his outlet in order to earn more (Watiri, 2013). This in turn will lead to increased customer base and thus the market share, increased coverage with low cost solution, increased revenue from improved indirect productivity by reducing congestion in existing branches. Customers will in turn benefit from agency services since the cost of travelling distances has been reduced considerably with the service being at close proximity.

According to Veniard (2010), agency banking systems were found to be up to three times cheaper to operate than branches for two reasons. First, agent banking minimizes fixed costs by leveraging existing retail outlets and reducing the need for financial service providers to invest in their own infrastructure. Although agent banking incurs higher variable costs from commissions to agents and communications, fixed costs per transaction for branches are significantly higher.

2.4.1 Low Transaction Costs
Since agency banking is targeted towards financial inclusion, transaction costs related to the financial services have to also reduce considerably. This is because the segments targeted are often customers with low balances but with frequent transactions. Banking agents should be the lowest cost channel for cash transactions, and the charges for using them should reflect that. Transaction charges should be lower on deposit than on withdrawal, reflecting the additional revenue deposits. This may seem at odds with the higher commission the bank might pay the agent for a deposit, but this reflects that the bank stands to gain far more from a deposit than from a withdrawal. So the bank should aim to recover more of its costs when the money is on its way in, not out. As is expected, most commercial banks that have rolled out agency
banking have put in place a transaction cost model on withdrawals and no fees for cash deposits. This is expected to increase the volume of deposits into the bank, making money available for loans and other investment opportunities. Agent banking systems are most cost effective for transactional accounts with low balances and frequent transactions (Veniard, 2010).

Gardeva and Rhynea (2011), in a survey report on opportunities and obstacles to financial inclusion observes that, product cost-structures and branching costs were ranked 7th and 12th respectively viewed as significant obstacles to financial inclusion, especially by providers, high branching costs in rural areas are associated with poor physical infrastructure roads, electricity et cetera. That branchless banking is able to leapfrog. Such infrastructure barriers ranked surprisingly high, at 9th on the obstacles list. Agent banking drastically reduces the cost of setting up points of contact with customers, allowing MFIs, banks and other providers to reach out into areas where building branches would be too expensive. Through partnerships with businesses across the country, banks will take their services closer to the people in areas with potentially less number and volume of transactions (Ahmed, 2015).

Customer’s visiting the general store will benefit from lower transaction costs as it is closer home and hence no need to travel 150 km to a bank, longer banking hours as the agents will operate for longer hours and shorter queues than in branches. Barriers for poor people to access appropriate financial services include socio-economic factors (e.g., education, gender and age, low and irregular income and geography), regulatory factors (e.g. provision of identity documentation) and product design factors (e.g., minimum account balances). Some major barriers financial service providers experience when expanding appropriate services to poor people are the cost of providing those services and finding the regulatory space to innovate (Afande & Mbugua, 2015).

As a general rule, transaction costs do not vary in direct proportion to a transaction’s size. Thus serving the poor with small value services is simply not viable using conventional retail banking or insurance. It is well documented that access to savings accounts, insurance and other financial services is crucial to allow poor people to invest in their homes and small businesses, weather the impact of economic shocks, build up savings as financial cushions against unexpected events, and manage uneven cash flows and seasonal incomes. Yet, an
estimated 2.5 billion people over half the world’s adult population – do not have access to formal financial services, representing a huge untapped potential for economic and social development. 2.2 billion Of these unserved adults live in Africa, Asia Latin America, and the Middle East.

There are multiple barriers to expanding financial inclusion that vary from country to country (Ofunya & Mbugua, 2015). Key barriers include the high transaction costs of delivering small-scale financial services across large geographic distances, infrastructure constraints such as lack of roads, fixed telephone lines, and ID systems, and insufficient information amongst both providers and consumers. The lack of data on the state of financial inclusion is another main constraint, both to advance financial inclusion and to evaluate the impact of policies aimed at improving access (AFI, 2012).

2.4.2 Low Operating Costs

Fixed operating costs from facility and equipment maintenance, electricity, heating, etc. do not incur to the bank. In addition, equipment maintenance and supplies for POS devices, such as repair service and paper, might be provided by the bank. Evidence confirms that agents administer loan funds more quickly and receive customer payments faster than branches. This might also result from agent recognition and lower transaction concentration at agent locations.

In any case, it reduces operating costs from client management for the bank and reduces portfolio risk (Ledgerwood, Earne, & Nelson, 2013). In a branch channel, salaries for employees are a source of fixed operating costs. The agent, in contrast, receives variable commission instead of a fixed salary. Commission depends on revenue streams and reduces economic risk for the bank. This cost might reduce if the agent derives high intrinsic benefit from ensuring service quality and bank regulation standards In comparison with a built branch, investment costs decrease. One of the major fixed operating costs from ABCs is float management (Ledgerwood et al., 2013).

The agent has to maintain sufficient cash float and e-money float to meet CICO transaction requirements at business times. Businesses employed as agents might leverage excess cash from their own turnover and profits to provide the required float for CICO transactions (Haas, 2015). In that overview, the agent needs to settle float as frequently as every four days due to the dominance of cash-in transactions from customer savings. In cases where the bank focusses
on savings, transmittances, and payments to meet the specific needs of low-income and unbanked populations), cash-in transactions result in a positive cumulative net cash flow at the agent in early stages, so that the he has to settle excess cash for e-money. Once savings accounts are built up, cash-out transactions may dominate. For a consistent customer experience and in order not to discourage customers, adequate float management has to ensure sufficient float to meet cash-out requirements at business times (Ledgerwood, 2013).

Operating costs from float management can amount to 35 to 60 percent of the overall costs for ABCs (Ledgerwood, 2013). However, as other costs decrease, the proportional share of float management cost increases. In comparison, traditional branch channels are limited to areas that ensure larger average transaction sums and sufficient turnover to cover their costs from float management. In summary for float management, the agent manages CICO transactions, which reduces operating costs and mitigates risk for the bank, as compared to a branch. Operating costs from float management incur to either the agent, specialized master agents or the bank.

In case of a branch channel, these costs incur to the bank. However, the settlement frequency and the number of cash transports might be higher for ABCs than for branch channels (Haas, 2015). In summary for operating costs, expenses from employing facilities, equipment, and personnel are reduced for ABCs as compared to branch channels, as the agent business’ infrastructure, personnel, and possibly the agent’s and customers’ mobile phones are leveraged. Operating costs from float management and particularly from cash transports can tip the scales for or against the profitability of ABCs; costs and risk could be mitigated through outsourcing to the agent or to specialized float management agents. Operating costs and risk incur to the agent business. The bank should carefully assess whether the agent meets the required qualification to cope with costs and risks (Haas, 2015).

### 2.4.3 Low Infrastructure Costs

Agent banking systems are up to three times cheaper to operate than branches for two reasons. First, agent banking minimizes fixed costs by leveraging existing retail outlets and reducing the need for financial service providers to invest in their own infrastructure. Although agent banking incurs higher variable costs from commissions to agents and communications, fixed costs per transaction for branches are significantly higher (Veniard, 2010).
Some of the benefits that commercial banks gain from agency banking are: huge savings on cost of construction of bank premises and leasing costs when banks are using the agency premises; human resource expenses have reduced as banks do not have to employ new staff to manage the agency and the cost of training if any is to the bare minimum; savings on equipment like furniture and computers (Chepkulei, 2015). Formal approval for each branch opening is required in 78 percent of developing countries. In several countries, such as in Kenya, physical inspection from a central bank representative is required as part of the approval process, which may substantially delay a branch opening in remote areas. In several countries, such as in India, regulating authorities limit the number of branches in geographical areas. Whether a branch opens and when a branch opens therefore depends on administrative processes. These regulations impose restrictions to efficient branch installation, thus may substantially affect investment costs and the profitability of branches (Mas, 2011). The construction and facilities of bank branches are subject to regulation and therefore cause substantial investment costs.

Regulated security requirements come at particularly high costs. Regulators commonly specify the following construction characteristics for branches (Mas, 2011): 1. Minimum size of the building 2. Building characteristics, such as thickness of glass between tellers and customers 3. Physical layout, such as characteristics of the vault and cameras. The specifications, which assume one concept of a branch, unrelated to the location and volume of business, often cause inefficiencies that result in additional costs and prevent innovation (Mas, 2011). Investment costs from agents incur as much as the bank needs to provide additional tangible and intangible resources. These depend on the qualifications of the agent and resource requirements for the provision of services for the agent. When delivering through agents, the bank primarily enhances existing infrastructure rather than investing in new infrastructure and reduces investment costs, compared to deliverance through branch channels (Kendall, Machoka, Veniard, & Maurer, 2011). Outsourcing agent recruitment and equipment purchase to specialized and scaling ANIs further reduce investment costs to the bank.

Besides, financial performance results in a deepening of the market and creates economies of scale. It assists in bringing the cost of financial services down and allows for greater financial sector development. Banks have reduced need to invest in new infrastructure and lower acquisition costs for mobile-enabled agents and mobile wallets. In addition to reaching the
unbanked masses, the agency banks are also increasing employment opportunities across the country. Agency banks also improves banks performance as it reduces huge savings on cost of construction of bank premises and leasing costs than when banks are using the agency premises (Aduda et al., 2013).

2.5 Chapter Summary

Agency banking is not new in the world and it has been applied successfully in Brazil and other parts of Asia. Since its inception in 2010, banks in Kenya have been keen to take advantage of the cost-saving and accessibility brought about by the agency banking. As a result, many studies have been conducted to evaluate the effect of agency banking on to the performance of these banks in Kenya with all of them finding a positive relationship between banks financial performance and agency banking.

This chapter has given a review on the literature on the effects of agency banking on deposit growth, customer growth and cost reduction. Chapter three provides research methodology which outlines the methods used to collect that data, research design and how data was analyzed.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction

This chapter gives the methodology that was used in the study. It includes the following subsections: Research Design, Population and Sampling Design, Data Collection Methods, Research Procedures, Data Analysis Methods and the Chapter Summary.

3.2 Research Design

This study applied a descriptive research design. Descriptive research gathers quantifiable information that can be used for statistical inference on your target audience through data analysis. Descriptive research designs help provide answers to the questions of who, what, when, where, and how associated with a particular research problem; a descriptive study cannot conclusively ascertain answers to why. Descriptive research is used to obtain information concerning the current status of the phenomena and to describe "what exists" with respect to variables or conditions in a situation. (Eugene & Lynn 2016). This study involved an investigation on the effects of agency banking on the financial performance commercial banks. The dependent variable was financial performance while the independent variables included cost reduction, deposit growth and customer growth.

3.3 Population and Sampling Design

3.3.1 Population

Target population refers to the entire group of individuals or objects to which researchers are interested in generalizing the conclusions. (Hassan, 2016). The target population for this study was 40,592 commercial banks as well as 25,408 middle managers from the 17 that have rolled out agency banking as of 2015 (CBK, 2015). Due to gaps in agency banking research, there was no way of accurately measuring the size of this population.

3.3.2 Sampling Design

Sampling ensures that some elements of a population are selected as riding representative of the population.
3.3.2.1 Sampling Frame
A sampling frame is defined as a list of all the units of the population of interest (Lehan, 2016). This study majorly focused on the bank agents and middle level managers from each of the bank in question.

3.3.2.2 Sampling Technique
Stratified random sample is a random sample in which members of the population are first divided into strata, then are randomly selected to be a part of the sample (Williams, 2016). It was employed due to the heterogeneous nature of the population. The criteria was based on the agents and the middle level managers. A simple random sampling technique was used to select firms to be included into the survey.

3.3.2.3 Sample Size
A sample size is defined as a subset of a population selected for measurement, observation or questioning, to provide statistical information about the population. (Boundless, 2016). A sample size of 120 agents (at least 10 from each bank) and at least 12 middle managers was selected from the total population.

3.4 Data Collection Methods
Data was primarily be collected through questionnaires. The questionnaires were semi structured in line with the research questions. It was divided into four sections: Section A contained demographic information, Section B contained questions on customer relations with the bank, Section C sought data on deposits and section D was based on costs. A five point Likert scale was used for closed ended questions.

The questionnaires consisted of both open ended and closed questions covering all the variables of study. The questionnaires also used the Likert scale type of questions. Open ended questions allow free responses from the respondents without providing or suggesting any structure for the responses. The Likert scale types of questions were used to determine the respondent’s attitudes or feelings about a given subject.

3.5 Research Procedures
In line with the research design, the study adopted the use of the questionnaire as the data collection tool. A pre-test of data collection was conducted to evaluate the reliability of the
document. A few questionnaires were administered to a few agents before the actual data collection exercise. The questionnaires were reviewed and revised to highlight the issues recorded during the pilot test.

The drop and pick later method was employed when receiving the questionnaires from the respondents. Personal administration was chosen upon so as to ensure that a high response rate was achieved.

3.6 Data Analysis Methods
In this study, the researcher collected both quantitative and qualitative data. Descriptive statistics was employed to analyze quantitative data using percentages, and tables. Frequencies were converted to percentages so as to ease interpretation, analysis of the data and presentation of the findings of the research. Content analysis was employed to analyze qualitative data.

Before processing the responses, data preparation was done on the completed questionnaires by editing, coding, entering and cleaning the data. Data collected was analyzed using descriptive statistics. The descriptive statistical tools aided in describing the data and determining the respondents’ degree of agreement with the various statements under each objective. The data analysis tool used was Statistical package for Social Sciences (SPSS) and Microsoft Excel to generate quantitative reports. The analyzed data was presented in the form of tables and figures.

3.7 Chapter Summary
Chapter 3 enumerated the research methodology and design. It has given a detailed analysis of the research design, population and the sampling process that was used in collecting the research data. Stratified sampling technique was used. This was done to ensure the results are more representative and also give all segments a chance to participate in the study. Data analysis was done using the Statistical Package for Social Sciences. The next chapter focused on data analysis and findings of the research. These were obtained from the collected data in the filled out questionnaires.
CHAPTER FOUR

4.0 RESULTS AND FINDINGS

4.1 Introduction
The purpose of this research was to analyze the effects of agency banking on the financial performance of commercial banks in Kenya. This chapter highlights the findings of the study as outlined in the research objectives and methodology.

4.2 Questionnaire Response Rate
The study sampled 12 out of the 17 banks that have rolled out agency banking. The study targeted 12 middle managers and 120 agents out of which 9 middle managers responded and 79 out of the 120 agents responded giving a response rate of 66%. Figure 4.1 highlights the findings.

![Figure 4.1 Response Rate](image)

4.3 General Information
The study targeted banks undertaking agency banking. Therefore, the results on demographic characteristics of these organization and the persons who filled in the questionnaires were investigated in the first section of the questionnaire. Findings are presented in this section under name of bank, years worked for the bank and or as an agent and the number of agents per bank. These are presented below.

4.3.1 Bank Representation
The questionnaire posed a question that required both the agents and the middle managers to highlight the bank they represent as agents and middle managers respectively. A middle
manager from each bank was selected to represent their bank in the study. As for the agents 18% from Co-operative and Chase Bank. 10% from National Bank and Kenya Commercial Bank. 8% from Standard Chartered Bank and Barclays Bank. 6% from both Jamii Bora and Equity Bank. 5% from K-Rep and Diamond Trust Bank. 4% from Equatorial Commercial Bank and 3% from NIC Bank. Table 4-1 highlights the bank representation for agents and middle managers

Table 4-1 Bank Representation

<table>
<thead>
<tr>
<th>Name of Bank</th>
<th>Agents Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>K-Rep</td>
<td>4</td>
<td>5%</td>
</tr>
<tr>
<td>Co-operate</td>
<td>13</td>
<td>18%</td>
</tr>
<tr>
<td>Chase</td>
<td>14</td>
<td>18%</td>
</tr>
<tr>
<td>SCB</td>
<td>6</td>
<td>8%</td>
</tr>
<tr>
<td>ECB</td>
<td>2</td>
<td>4%</td>
</tr>
<tr>
<td>Jamii Bora</td>
<td>5</td>
<td>6%</td>
</tr>
<tr>
<td>Equity</td>
<td>5</td>
<td>6%</td>
</tr>
<tr>
<td>NIC</td>
<td>2</td>
<td>3%</td>
</tr>
<tr>
<td>KCB</td>
<td>8</td>
<td>10%</td>
</tr>
<tr>
<td>Barclays</td>
<td>6</td>
<td>8%</td>
</tr>
<tr>
<td>DTB</td>
<td>4</td>
<td>5%</td>
</tr>
<tr>
<td>NBK</td>
<td>8</td>
<td>10%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>79</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.3.2 Years Worked for the Bank

The study sought to find out the period the respondents had worked for the bank. The findings were highlighted in table 4-2. 67% of the middle managers had been with the bank for more than 5 years while the rest had worked for a period of 2-3 years. As for the agents, 58% had been working for a period of 2-3 years, followed by 32% having worked for 3-5 years and the other 10% having worked for 1 year or less.
Table 4-2 Years Worked for the Bank

<table>
<thead>
<tr>
<th>Years</th>
<th>Middle Managers Frequency</th>
<th>Percentage</th>
<th>Agents Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 year or less</td>
<td>0</td>
<td>0%</td>
<td>8</td>
<td>10%</td>
</tr>
<tr>
<td>2-3 years</td>
<td>3</td>
<td>33%</td>
<td>46</td>
<td>58%</td>
</tr>
<tr>
<td>3-5 years</td>
<td>0</td>
<td>0%</td>
<td>25</td>
<td>32%</td>
</tr>
<tr>
<td>5-10 years</td>
<td>6</td>
<td>67%</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>Over 10 years</td>
<td>0</td>
<td>0%</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9</strong></td>
<td><strong>100%</strong></td>
<td><strong>79</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.3.3 Number of Agents per Bank

The study inquired the number of agents in operation within Nairobi county. Table 4-3 outlines their responses. 44% had 20 or less agents, 22% had between 21 and 40 agents and 33% had more than 100 agents operating.

Table 4-3 Number of Agents in Operation

<table>
<thead>
<tr>
<th>Number of agents</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>20</td>
<td>4</td>
<td>44%</td>
</tr>
<tr>
<td>21-40</td>
<td>2</td>
<td>22%</td>
</tr>
<tr>
<td>41-60</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>61-100</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>Above 100</td>
<td>3</td>
<td>33%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.4 Effects of Agency Banking on Customer Growth

The second section sought to identify if there was a significant growth in customers as a result of agency banking. From the findings, both the managers and agents agreed that there was an increase in customers as a result of agency banking. The findings in this section are presented under growth in customers, percentage of accounts opened by agency banking, influence of
agency banking on financial inclusion, accounts opened within a month, customer preference of agents over banking halls and financial services and agency banking.

4.4.1 Growth in Customers
The study sought to determine the growth in customers for each bank. 67% of the middle managers indicated a growth of between 200-500 customers while 33% of them indicated a growth of between 501 and 1000 customers. Table 4.4 presents the findings.

Table 4-4 Growth in Customers

<table>
<thead>
<tr>
<th>Customer Growth</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>200 – 500</td>
<td>6</td>
<td>67%</td>
</tr>
<tr>
<td>501 – 1000</td>
<td>3</td>
<td>33%</td>
</tr>
<tr>
<td>1001 – 5000</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>5001 – 10 000</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.4.2 Percentage of Accounts Opened attributed to Agency Banking
The respondents, middle managers, were required to indicate the percentage of accounts opened attributed to agency banking. 44% of the middle managers indicated between 26%-50%, 33% indicated 25% and below and 22% of them indicated 51%-75% accounts. Figure 4-11 presents the findings.
4.4.3 Influence of Agency Banking on Financial Inclusion

The respondents were required to indicate the extent to which agency banking has influenced financial inclusion. 78% of the respondents agreed that, to a great extent, agency banking influences financial inclusion. 22% of them indicated that agency banking has had no influence in financial inclusion. Table 4-5 presents the findings.

Table 4-5 Influence of Agency Banking on Financial Inclusion

<table>
<thead>
<tr>
<th>Response</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>To a very great extent</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>To a great extent</td>
<td>7</td>
<td>78%</td>
</tr>
<tr>
<td>To a very low extent</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>No extent at all</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>Nil</td>
<td>2</td>
<td>22%</td>
</tr>
<tr>
<td>Total</td>
<td>9</td>
<td>100%</td>
</tr>
</tbody>
</table>

4.4.4 Accounts opened by agents within a month

The respondents were required to indicate the average number of accounts they open in a month. 95% of the agents indicated that an average of 0-10 accounts are opened in a month,
4% indicated 11-20 accounts and 1% responded to not opening any in a month. Table 4-6 indicates the findings.

**Table 4-6 Account Opened in a Month-Agents**

<table>
<thead>
<tr>
<th>Response</th>
<th>Frequency</th>
<th>Percentages</th>
</tr>
</thead>
<tbody>
<tr>
<td>None</td>
<td>1</td>
<td>1%</td>
</tr>
<tr>
<td>0- 10</td>
<td>75</td>
<td>95%</td>
</tr>
<tr>
<td>11-20</td>
<td>3</td>
<td>4%</td>
</tr>
<tr>
<td>21-30</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>50- Above</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>79</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

**4.4.5 Customer Preference of Agents to Banking Halls**

The respondents were required to indicate whether customers preferred agents to visiting a banking hall. 52% of the respondents agreed that customers preferred agents, 25% neutral, 15% strongly agreed and 8% disagreed. Figure 4-3 indicates the findings.

**Figure 4-3 Preference of Agents to Banking Halls**
4.4.6 Extent levels of the Most Commonly used Services

The respondents were asked to indicate the extent levels of the most commonly used services. A five-point likert scale ranging from 1-5 where Not at all (1), To a little extent (2), To a moderate extent (3), To a great extent (4) and To a very great extent (5). Analysis was done by use of mean and standard deviation. From table 4-8, the findings gave a mean score of 3.5 and a standard deviation of 0.13 indicating that majority of the respondents agreed to a great extent that cash withdrawals are common. Agents offer cash withdrawals services at a fee depending on the amount withdrawn.

As for the bill payment, the findings gave a mean score of 2.99 and a standard deviation of 0.12 indicating that most respondents agreed to a moderate extent that bill payments is a commonly used service. The findings determined, with a mean score of 3.72 and standard deviation of 0.12 that cash deposits were to a great extent a commonly used service by customers. For the Account applications, the mean was 3.72 with a standard deviation 0.12 indication that to a great extent, it is a common service. The findings also determined that loan repayments at a mean score of 2.90 and standard deviation 0.12 was to a moderate extent a common service.

The respondents also felt that processing loan applications was to a moderate extent a commonly used service at a mean score of 2.89 and a standard deviation of 0.13. When it came to issuing bank statements, the respondents agreed that it was commonly used service to a moderate extent at a mean score of 2.6 and standard deviation of 0.10. The study determined that foreign exchange and dealing with customer complaints were to a moderate extent a commonly used service with a mean scores of 2.5 and 2.34 and standard deviations of 0.11 and 0.12 respectively.

Table 4-7 Extent levels of Commonly used Services

<table>
<thead>
<tr>
<th>Service</th>
<th>Mean</th>
<th>Std Dev</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash withdrawal</td>
<td>3.48</td>
<td>0.13</td>
</tr>
<tr>
<td>Bill payment</td>
<td>2.99</td>
<td>0.12</td>
</tr>
<tr>
<td>Cash deposits</td>
<td>3.72</td>
<td>0.12</td>
</tr>
<tr>
<td>Account applications</td>
<td>3.72</td>
<td>0.12</td>
</tr>
<tr>
<td>Service</td>
<td>Value 1</td>
<td>Value 2</td>
</tr>
<tr>
<td>----------------------------------------</td>
<td>---------</td>
<td>---------</td>
</tr>
<tr>
<td>Loan repayments</td>
<td>2.90</td>
<td>0.12</td>
</tr>
<tr>
<td>Processing loan applications</td>
<td>2.89</td>
<td>0.13</td>
</tr>
<tr>
<td>Issuing bank statements</td>
<td>2.59</td>
<td>0.10</td>
</tr>
<tr>
<td>Handling foreign exchange transactions</td>
<td>2.48</td>
<td>0.11</td>
</tr>
<tr>
<td>Dealing with customer complaints</td>
<td>2.34</td>
<td>0.12</td>
</tr>
</tbody>
</table>

4.4.7 Correlation Analysis

The researcher conducted a correlation analysis so as to analyze the extent levels of the most commonly used services and their overall effects on the customer growth for commercial banks in Kenya. Data on cash withdrawal, bill payment, cash deposits, account applications, loan repayments, processing loan applications, issuing bank statements and handling foreign exchange transactions were computed into single variables per variable by obtaining the averages of each variable. Pearson’s correlations analysis was then conducted at 95% confidence interval and 5% confidence level 2tailed. The table below indicates the correlation matrix between the aforementioned services and financial performance of the banks.

According to the table, there is a positive relationship between customer growth and cash withdrawals, cash deposits, loan repayments, processing loan applications; and issuing bank statements and bill payment 0.45, 0.45, 0.05, 0.03, 0.10 respectively. The positive relationship indicates that there is a correlation between customer growth and the services mentioned. This infers that cash deposits and cash withdrawals have the greatest effect to customer growth, followed by loan repayments, processing loan applications, and issuing bank statements respectively. It also infers that there is a negative relationship between customer growth and account applications, handling foreign exchange transactions and handling customer complaints -0.01, -0.16 and -0.26 respectively.
<table>
<thead>
<tr>
<th></th>
<th>Cash withdrawal</th>
<th>Bill payment</th>
<th>Cash deposits</th>
<th>Account applications</th>
<th>Loan repayments</th>
<th>Processing loan applications</th>
<th>Issuing bank statements</th>
<th>Handling foreign exchange</th>
<th>Dealing with customer complaints</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash withdrawal</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bill payment</td>
<td>0.45</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash deposits</td>
<td>0.45</td>
<td>0.40</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Account applications</td>
<td>-0.01</td>
<td>0.28</td>
<td>0.16</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loan repayments</td>
<td>0.05</td>
<td>0.11</td>
<td>0.16</td>
<td>0.00</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Processing loan applications</td>
<td>0.03</td>
<td>0.06</td>
<td>0.17</td>
<td>0.17</td>
<td>0.06</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Issuing bank statements</td>
<td>0.10</td>
<td>-0.13</td>
<td>0.20</td>
<td>0.08</td>
<td>-0.04</td>
<td>0.36</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Handling foreign exchange transactions</td>
<td>-0.16</td>
<td>-0.23</td>
<td>0.05</td>
<td>-0.26</td>
<td>0.02</td>
<td>0.11</td>
<td>0.59</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Dealing with customer complaints</td>
<td>-0.26</td>
<td>-0.51</td>
<td>0.09</td>
<td>0.06</td>
<td>-0.03</td>
<td>0.06</td>
<td>0.42</td>
<td>0.57</td>
<td>1</td>
</tr>
</tbody>
</table>
4.5 Agency Banking and Deposit Growth

The research study sought to find out the effect of agency banking on deposit growth. The respondents were required to indicate how much of the banks’ revenue comes from deposits. The respondents were also required to indicate the value of these deposits and their frequency. Findings are presented in this section under portion of income attributed to deposits, portion attributed to the agents, agreement of agency deposits on banks’ performance and the value of the deposits received.

4.5.1 Portion of Banks’ Income Attributed to Deposits

The respondents were required to indicate the portion of banks’ income that comes from deposits. 56% of the respondents agreed that deposits make about 20%-40% of the banks income, 33% agreed on 0-20% and the other 11% indicated that deposits attributed to 40-60% of their income. Table 4-10 highlights the findings.

**Table 4-9 Portion of Banks' Income Attributed to Deposits**

<table>
<thead>
<tr>
<th>Portion</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-20%</td>
<td>3</td>
<td>33%</td>
</tr>
<tr>
<td>20%-40%</td>
<td>5</td>
<td>56%</td>
</tr>
<tr>
<td>40%-60%</td>
<td>1</td>
<td>11%</td>
</tr>
<tr>
<td>60%-80%</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>80%-100%</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.5.2 Bank Deposits Attributed to Agency Banking

The respondents were asked to indicate the portion of deposits that came from their agents. Majority of the respondents indicated that more than 30% of deposits come from agents. Equatorial Commercial Bank indicated the highest portion of deposits as coming from agents while Standard Chartered Bank attributed only 15% of their deposits as coming from the agents. The average of the results was 33%. Figure 4-4 presents the findings.
4.5.3 Agreement of Agent-Related Deposits on Banks Financial Performance

The respondents were required to indicate whether agent-related deposits had an effect on the financial performance of banks. 78% of the respondents agreed while 22% were neutral to this assertion. Table 4-12 presents the findings.

<table>
<thead>
<tr>
<th>Agreement</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly Disagree</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>Disagree</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>Neutral</td>
<td>2</td>
<td>22%</td>
</tr>
<tr>
<td>Agree</td>
<td>7</td>
<td>78%</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.5.4 Value of the Agent-Related Deposits

The study sought to analyze the monetary value of the deposits coming from agents. The respondents were asked to identify the value of deposits made by customers in a day. 56% of
the respondents valued the deposits at 25,000 & below a day, 46% valued them at 25,000-50,000 per day and 3% at 50,000-75,000. Table 4-13 presents the findings below.

Table 4-11 Value of Agent-Related Deposits

<table>
<thead>
<tr>
<th>Value of Deposits</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>25,000 &amp; below</td>
<td>44</td>
<td>56%</td>
</tr>
<tr>
<td>25,000-50,000</td>
<td>33</td>
<td>42%</td>
</tr>
<tr>
<td>50,000-75,000</td>
<td>2</td>
<td>3%</td>
</tr>
<tr>
<td>75,000 and above</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>79</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.6 Agency Banking and Cost Reduction
The study sought to investigate the effects of agency banking on cost reduction. Findings are presented in this section under, costs incurred by agents, extent to which operational costs influence transaction costs and measures put in place to reduce operational costs.

4.6.1 Costs Incurred by Agents
The respondents were required to indicate the costs they incur. The responses were aggregated into security costs, transaction costs, infrastructure costs, airtime for communication, cash flow management, rent, miscellaneous and ATM delays. 27% of the respondents incurred security costs, 19% incurred transaction costs as well as airtime for communication with clients, 14% of the costs incurred were miscellaneous, 10% incurred infrastructure costs, 5% ATM delays, cash flow management costs accounted for 4% of the costs and 3% of the costs were rent costs. Table 4-14 presents the findings.

Table 4-12 Costs Incurred by Agents

<table>
<thead>
<tr>
<th>Cost</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Security costs</td>
<td>21</td>
<td>27%</td>
</tr>
<tr>
<td>Airtime for Communication</td>
<td>15</td>
<td>19%</td>
</tr>
<tr>
<td>Transaction Costs</td>
<td>15</td>
<td>19%</td>
</tr>
<tr>
<td>Infrastructure Costs</td>
<td>8</td>
<td>10%</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>11</td>
<td>14%</td>
</tr>
</tbody>
</table>
4.6.2 Operational Costs and Transaction Costs.

The study sought to identify the extent to which operational costs influence transaction costs. 89% of the respondents agreed that operational costs have an influence on transaction costs to a great extent while 11% indicated that the influence of operational costs on transaction costs was to a very great extent. Table 4-15 presents the findings.

Table 4-13 Operational Costs and Transaction Costs

<table>
<thead>
<tr>
<th>Extent</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>To a very great extent</td>
<td>1</td>
<td>11%</td>
</tr>
<tr>
<td>To a great extent</td>
<td>8</td>
<td>89%</td>
</tr>
<tr>
<td>To a very low extent</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td>No extent at all</td>
<td>0</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>9</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.6.3 Correlation between Operational, Transaction Costs and Cost Reduction

The researcher conducted a correlation analysis to determine the relationship between operational, transaction costs and their effect on cost reduction. Table 4-14 below indicated that transaction cost. This infers that both transaction and infrastructure cost have a positive relationship to cost reduction. Meaning that an increase in infrastructure costs results in an increase in agency costs.

Table 4-14 Correlation Matrix

<table>
<thead>
<tr>
<th></th>
<th>Transaction Cost</th>
<th>Infrastructure Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transaction Cost</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Infrastructure Cost</td>
<td>0.91</td>
<td>1</td>
</tr>
</tbody>
</table>
4.6.4 Measures to Reduce Operational Costs.

The respondents were asked to indicate the measures the bank could take in order to reduce operational costs. The responses were aggregated to, improve customer care, reduction of transaction fees, improving cash flow management, reducing ATM charges, reduce loan rates, improve network coverage, improving technology, better management practices and improving security to agents. 29% recommended the reduction of transaction fees, 19% indicated improved customer care, 13% of the respondents indicated improving technology in terms of internet banking and the relay of instant messaging as well as the reduction of loans/mortgages. 8% of the respondents suggested better management practices for back-end operations. 6% indicated improving cash flow management when it came to maintaining a substantial amount of float for transactions. 5% indicated improved network coverage as well as improving security for agents.

Table 4-15 Measures to Reduce Operation Costs

<table>
<thead>
<tr>
<th>Measures</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improve customer care</td>
<td>15</td>
<td>19%</td>
</tr>
<tr>
<td>Reduction of transaction fees</td>
<td>23</td>
<td>29%</td>
</tr>
<tr>
<td>Improving cash flow management</td>
<td>5</td>
<td>6%</td>
</tr>
<tr>
<td>Reducing ATM charges</td>
<td>2</td>
<td>3%</td>
</tr>
<tr>
<td>Reduce loan rates</td>
<td>10</td>
<td>13%</td>
</tr>
<tr>
<td>Improve network coverage</td>
<td>4</td>
<td>5%</td>
</tr>
<tr>
<td>Improving technology</td>
<td>10</td>
<td>13%</td>
</tr>
<tr>
<td>Better management practices</td>
<td>6</td>
<td>8%</td>
</tr>
<tr>
<td>Improving security to agents</td>
<td>4</td>
<td>5%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>79</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

4.7 Chapter Summary

In this chapter the results and finding of the study were presented. The researcher began by introducing the chapter and outlining the effects of agency banking on customer growth, on deposit growth and cost reduction. Chapter five will discuss the summary of the findings, discussion of key data findings, conclusion and recommendations.
CHAPTER FIVE

5.0 DISCUSSION, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction
The chapter presents a summary and discussions of the research findings on the effects of agency banking on the financial performance of commercial banks. It further gives the conclusions based on the findings in chapter four and recommendations on what measures the banks can put in place to improve agency banking services. The following discussions, conclusions and recommendations are made. The recommendations are based on the objectives of the study.

5.2 Summary
The study set out to analyze the effects of agency banking on the financial performance of commercial banks. The study was focused on three research objectives: determine the effects of agency banking on customer growth; determine the effects of agency banking on deposit growth; determine the effects of agency banking on cost reduction.

The study used a descriptive research design. Simple random sampling technique was used to select the sample firms in order to give each element of the population an equal chance of being included in the study. A representative sample of 12 banks was selected. Out of which 12 middle managers and 120 agents were selected using simple random sampling. Data was collected using questionnaires; both open and close ended questions were employed for the research. In addition a five point likert scale was also used to access agreement and extent levels. The questionnaires were checked for completeness, and data was entered into SPSS for further analysis. Descriptive statistics including mean and standard deviations were computed. The data was presented in the form of tables and figures.

The study established that agency banking had a positive influence on customer growth. Both the middle managers and agents agreed that agency banking had an impact on financial inclusion especially because of its convenience and ease of use. Agency banking has greatly increased the level of financial inclusion. It has enhanced efficiency by availing services to customers at lower costs. By so doing, banks have been able to increase customer outreach thereby increasing customer growth. The study also established that since agents are authorized
to open accounts for customers, the overall growth of customers has been positive with an average of between 0-10 accounts being opened in a month. The variety of services offered similar to those you find in banking halls has also encouraged the growth of customers.

On deposit growth, most banks have a free transaction cost policy for deposits. This has encouraged customers with huge cash flows to deposit their money at agents at no costs. This therefore signifies a positive influence of agency banking on deposit growth.

On cost reduction, agency banking has significantly reduced the costs it would take to build the brick and motor institutions. Agents are often pharmacies, general shops and even kiosks that have are in operation. They then offer financial services to customers. Operational costs are however slightly higher and in turn increase transaction costs. Since the premises is not owned by the bank, the other costs related to the agent are borne by the agents and not the bank. Thus reducing the overall costs of availing financial services in general.

5.3 Discussions

5.3.1 Effect of Agency Banking on Customer Growth

In Chapter 4 we established that there was a significant increase in customer growth. Increased access to financial services has encouraged the unbanked to seek financial services from agents all over Kenya. Financial services have in the past five years been availed to customers through agency banking. This has increased the number of transactions facilitated by bank agents (Kambua, 2015). This is largely attribute to increases in transactions relating to payment of bills, mini statement requests, cash withdrawals and cash deposits which in turn improves profitability of commercial banks (Kambua 2015).

Mas & Siedek (2008) argued that the lower operational cost the agent channel offers relative to other existing channels might induce banks to use this vehicle to cater to new customer segments that were previously not sufficiently economically attractive, for instance lower income customers in peri-urban areas. The banks would therefore need to reinvent their strategy in order to target new customer segments. Banking agencies help financial institutions to divert existing customers from crowded branches providing a “complementary” often more convenient channel. Other financial institutions especially in developing markets use agents to reach an “additional” client segment or geography (Afande and Mbugua, 2015).
Afande & Mbugua (2015) found that agency banking has made great strides in financial inclusion. Greater geographical coverage brought about by agent banking is the strongest predictor of financial inclusion. This is because services are brought closer to the people and thus saves a lot of time which would have been used to queue in banking halls or ATMs. They found that the strongest evidence to this effect was the fact that customers were willing to forego the extra cost charged at agent banking outlets to have their banking needs taken care of.

The study established that customers often aren’t aware of the offerings available at the agents. Customer awareness improves financial inclusion as supported by the findings of Muasya & Kerongo (2015) who agree that financial services awareness positively influences access to financial services. When people are aware of the available services, are provided with more accurate and up-to-date information on new developments in agency banking segment and know where to get the services, their access to financial services increases thus enhanced financial inclusion.

5.3.2 Effect of Agency Banking on Deposit Growth

Commercial banks in Kenya use various innovation delivery channels to recruit customers who deposit their savings. The innovation delivery channels that are used in Kenya when recruiting bank customers are, mobile banking, internet banking, credit cards, automated tellers machines and more recently the agency banking (Ngumi, 2013).

Ngumi (2013) argues that bank innovations, like the use of POS terminals have made access to financial services efficient. He further says that, the usage of POS terminals in Kenya has been on the rise since the year 2010 due to the introduction of agent banking. Agent banking has provided many customers the opportunity to access their bank accounts without having to travel to a physical branch. Those banks that were first movers in agent banking attracted a huge customer following and hence enabled access to deposits which eventually bolstered the funding mechanism of such banks. Kenyan bank customers are capable of accessing their bank accounts even from the rural and remote locations of the country. This has made the unbanked to also take their money to the bank and thus boosting the deposits of banks.
5.3.3 Effect of Agency Banking on Cost Reduction

One of the primary impediments to providing financial services to the poor through branches and other bank-based delivery channels is the high costs inherent in these traditional banking methods. The amount of money expended by financial service providers to serve a poor customer with a small balance and conducting small transactions is simply too great to make such accounts viable (Muasya & Kerongo, 2015).

Banks have used the agency model to reduce on costs that would have otherwise impacted the overall profitability of the bank. The study determined that majority of the operational costs are borne by the agents and thus have a positive influence on the performance of the bank. These findings are supported by those of Muasya and Kerongo (2015), who determined that contracting agent outlets has considerably reduced on the costs associated with accessing financial services both in terms of the structural barriers in opening bank accounts, transactional costs and costs associated with long distances covered to access mainstream retail bank branches. With such a reduction in costs, the rural poor who have remained unbanked for generations have warmed up to the idea of owning bank accounts through which they access financial services. Thus, cost is a correlate of access to financial services – the lower the cost the higher the level of access to financial services (Muasya & Kerongo, 2015).

5.4 Conclusions

5.4.1 Effect of Agency Banking on Customer Growth

The study sought to analyze the effect that agency banking has on customer growth. The study established that agency banking has a positive impact on customer growth. It has made access to financial services more convenient and in turn improved the financial performance of banking institutions. It has encouraged customers to seek other financial services like loan applications, bill payments, balance enquiry and issue of bank statements.

Agency banking has improved financial inclusion. Majority of the population is no longer unbanked due to the presence of agents in rural and semi-rural areas. The agents have been equipped with tools and the knowledge of bank products and have significantly led to the increase in customer awareness and ultimately the growth of customers for their respective banks.
5.4.2 Effect of Agency Banking on Deposit Growth

The study set to determine the effect of agency banking on deposit growth. The study determined that the low if no cost charge to deposit money has encouraged many customers with large sums of money to deposit at their convenience. The agents also sought to provide financial risk management services for clients with turnovers of over Kes 100, 000.

The advent of financial innovations such as POS terminals has also made access to financial services more efficient. The use of these devices has made the relay of information much easier and readily available to clients seeking information on their accounts. This has created a trust between customers and banks and as a result generated great revenues for banks as customers can make transactions at their convenience without worrying about risk.

Deposit mobilization positively affects the financial performance of commercial banks. Thus, deposits play a vital role in the financial performance and sustainability of a bank and it is an indispensable factor in which loan disbursements and revenue generations are based. (King’ang’ai et al., 2016).

5.4.3 Effect of Agency Banking on Cost Reduction

The study set out to determine the effect of agency banking on cost reduction. The study determined that operational costs of agency banking were fairly low. The overall cost of operating under the umbrella of agency banking is very low because there is no construction of a branch involved. The major costs are borne by the agent. These mostly include rent, security costs, infrastructure costs and airtime for communication especially when the network is off.

5.5 Recommendations

5.5.1 Recommendations for Improvement

5.5.1.1 Effect of Agency Banking on Customer Growth

The study established that since agency banking is a convenient channel to access financial services, there’s a lack of hospitality and customer care that comes with it. Customers often seek great service with a personal touch which is often not the case since the agent might be running several businesses in conjunction with the agency banking. The study therefore
recommends that customer care needs to be improved as services are being relayed to customers. There is also the need to develop new products and services so as to reach more customers especially in rural areas. Increased awareness of the products and services being offered by the bank is also a step into increasing the number of customers the bank intends to target.

5.5.1.2 Effect of Agency Banking on Deposit Growth
The study established that some banks charged a fee to make cash deposits with the bank. It also established that customers weren’t aware of the deposit limits that were set by the bank. Some of the banks have no limit when it comes to depositing cash and this might be a deterrent to customers seeking to make frequent deposits of large sums of money through agents. The study recommends increased awareness of the service offerings as well as reduced charges for cash deposits so as to increase the volume of transactions being carried out via agents.

5.5.1.3 Effect of Agency Banking on Cost Reduction
The study established that operational costs have a bearing on the transaction costs associated with agency banking. In addition, costs such as security are becoming a hindrance to the provision of financial services by agents. Network delays also resulted in additional costs for both the agents and customers. This study recommends the streamlining of operational costs involved in providing financial services. Some of these costs can be borne by the parent bank so as to ease the burden on the agents and eventually the consumer. Improved network coverage through technologically advanced equipment is another step through which agents can provide timely and efficient services.

5.5.1.4 Recommendations for Further Research
The study recommends that similar research be conducted in rural areas so as to determine if agency banking has in fact improved financial inclusion especially for the unbanked. This will aid in understanding the extent to which agency banking has improved the overall performance of commercial banks.
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Of Commercial Banks In Kenya; Survey Study Of Banks In Kenya. *International


APPENDICES

Appendix I: Questionnaire for Middle Managers

EFFECTS OF AGENCY BANKING ON THE FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

This information is being sought solely for academic purposes and will be treated with strict confidence. Kindly answer the questions by writing a brief statement or ticking the boxes provided as will be applicable. Please take a few minutes to complete this questionnaire. Kindly answer all questions.

SECTION A: Demographic Information

1. Name of the bank ________________________________________________
2. What is your position in the bank? ________________________________
3. What gender are you?
   a) Male □
   b) Female □
4. What is your level of Education?
   a) Post Graduate □
   b) Under Graduate □
   c) College □
   d) Others □
5. How many years have you worked in your bank? (Tick one)
   a) Below 1 year □
   b) 1- 4 years □
   c) 4- 7 years □
   d) Over 7 years □
6. Which department are you working currently? Please tick one
   a) Branch Management
   b) Operations
   c) Customer service
   d) Cash

7. How long has this bank been offering agency banking services?
   a) Less than 1 year
   b) 2 years
   c) More than 3 years

8. How many agents do you have currently?
   a) 0-20
   b) 21-40
   c) 41-60
   d) 61-100
   e) Above 100

SECTION B: Effects of Agency Banking on Customer Growth

9. Has there been growth of customers in your bank in the last 5 years?
   Yes [ ] No [ ]
   If yes, by how much?
   a) 200 – 500
   b) 501 – 1000
   c) 1001 – 5000
   d) 5001 – 10 000
10. To what extent has there been customer growth in your bank?
   
a) 5%  
b) 20%  
c) 40%  
d) 50%  
e) 100%

11. What percentage of accounts opened can you attribute to agent banking?
   
a) 25% and below  
b) 26% - 50%  
c) 51% - 75%  
d) 75% and above

12. To what extent would you rate the influence of agent banking on financial inclusion?
   
a) To a very great extent  
b) To a great extent  
c) To a very low extent  
d) No extent at all

13. In your opinion, what influences customer growth in commercial banks?
   
___________________________________________________________________________
   
___________________________________________________________________________
   
___________________________________________________________________________
   
___________________________________________________________________________

55
SECTION C: Effects of Agency Banking on Deposit Growth

14. What portion of the banks income would you say comes from deposits?
   a) 0-20%   
   b) 20%-40%  
   c) 40%-60%  
   d) 60%-80%  
   e) 80%-100% 

15. What portion of the banks’ deposits comes from agents (percentage)?
   ____________________________________________________________

16. Would you agree that the deposits from agents influence your banks’ performance?
   i. Strongly Disagree   
   ii. Disagree          
   iii. Neutral         
   iv. Agree            
   v. Strongly Agree   

SECTION D: Effects of Agency Banking on Cost Reduction

17. To what extent does operational cost of agency banking affect the transaction cost of financial services through agents at your bank?
   i. To a very great  
   ii. To a great extent 
   iii. To a very low extent 
   iv. No extent at all
18. How much does it cost to offer the following services through the following platforms?

<table>
<thead>
<tr>
<th></th>
<th>Cash Withdrawal</th>
<th>Cash Deposits</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Agent</td>
<td>A.T.M</td>
</tr>
<tr>
<td>2500 &amp; below</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2501-5000</td>
<td></td>
<td></td>
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<tr>
<td>20,001-35,000</td>
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<tr>
<td>35,000-50,000</td>
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</tbody>
</table>

19. Which measures have you put in place to reduce operational costs of agent banking so as to reduce transaction costs?

____________________________________________________________________________
____________________________________________________________________________
____________________________________________________________________________

20. To what extent do the following facts of agency banking influence the performance of your bank? Use the scale: Not at all (1), To a little extent (2), To a moderate extent (3), To a great extent (4) and To a very great extent (5).

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
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<tr>
<td>Transaction cost</td>
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<tr>
<td>Infrastructure cost</td>
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</table>

21. Apart from the ones named above which other costs does your bank incur in agency banking

____________________________________________________________________________
____________________________________________________________________________
____________________________________________________________________________
Appendix II: Agents Questionnaire

SECTION A: Demographic Information

1. Name of Agent _____________________________________________________________

2. For which bank/ banks are you an agent?
________________________________________________________________________
________________________________________________________________________
________________________________________________________________________

3. Date of registration________________________________________________________

4. How long have you been an agent?
   i. 1 year or less
   ii. 2-3 years
   iii. 3- 5 years
   iv. 5- 10 years
   v. Over 10 years

SECTION B: Effects of Agency Banking on Customer Growth

5. What is the average number of customers served daily?
   i. Less than 20 customers
   ii. 20- 50 customers
   iii. 50- 100 customers
   iv. 100 + customers

6. How many accounts are opened at this agency within a month?
   i. None
   ii. 0- 10
   iii. 11-20
7. To what extent do you agree with the statement that some customers prefer agents because they are closer to them as compared to the main bank?

i. Strongly Disagree

ii. Disagree

iii. Neutral

iv. Agree

v. Strongly Agree

8. On a scale of 1 to 5. Where: Not at all (1), To a little extent (2), To a moderate extent (3), To a great extent (4) and To a very great extent (5). Which is the most commonly used service among the ones listed below?

<table>
<thead>
<tr>
<th>SERVICE</th>
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<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
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</thead>
<tbody>
<tr>
<td>i. Cash withdrawal</td>
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<td>ii. Bill payment</td>
<td></td>
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<td>iii. Cash deposits</td>
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<td>iv. Account applications</td>
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<td></td>
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<tr>
<td>v. Loan repayments</td>
<td></td>
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<td>vi. Processing loan applications</td>
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<td>vii. Issuing bank statements</td>
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<td>viii. Handling foreign exchange transactions</td>
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<td>ix. Dealing with customer complaints</td>
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</tbody>
</table>

9. Is there a limit of how much a client can withdraw or deposit with the agents?

i. Yes

ii. If yes, which is the minimum and maximum a client can withdraw or deposit?
   Deposit _____________________
10. What measures has your bank taken in regard to pricing to enhance customer growth?

________________________________________________________
________________________________________________________

SECTION C: EFFECTS OF AGENCY BANKING ON DEPOSIT GROWTH
This section attempts to establish the effect of agency banking on deposit growth.

11. On average, how many deposits are made in a day?
   i. None
   ii. 0-10
   iii. 11-20
   iv. 21-30
   v. 50-Above

12. Of what value are these deposits?
   i. 25,000 & below
   ii. 25,000-50,000
   iii. 50,000-75,000
   iv. 75,000 and above

13. To what extent would you rate the influence of agent banking on financial inclusion?
   i. To a very great extent
   ii. To a great extent
   iii. To a very low extent
   iv. No extent
SECTION D: EFFECTS OF AGENCY BANKING ON COST REDUCTION

This section attempts to establish the effect of agency banking on cost reduction.

14. What costs do you incur as an agent?

__________________________________________________________________
__________________________________________________________________
__________________________________________________________________

15. Which measures would you recommend to be instituted by banks in order to increase number and volume of transactions to pull down agent costs?

__________________________________________________________________
__________________________________________________________________
__________________________________________________________________

16. Do you incur operational costs related with agent banking?
   i. Yes  [ ]  No  [ ]

   ii. If answer is yes, how do you reduce such costs?

       __________________________________________________________________
       __________________________________________________________________
       __________________________________________________________________