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CONTRIBUTION OF AGENCY BANKING TO THE IMPROVEMENT OF FINANCIAL INCLUSION IN COMMERCIAL BANKS IN RWANDA: A CASE OF COMMERCIAL BANKS IN BUGESERA DISTRICT, RWANDA

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Abstract: **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 was carried out to examine the contribution of agency banking to the improvement in financial inclusion in Bugesera district, as this is a key pillar for Rwanda Vision 2020. The study adopted descriptive research design and focused on the activities of banks offering agency services within Bugesera district. The target population for the study was agents of commercial banks operating in Bugesera District. Simple random sampling was used and both primary and secondary data collected. The data was central-edited to account for analytical utility and the Statistical Package for Social Sciences (SPSS) used for analysis while Microsoft Excel was used for the listing and ranking of variables. Tools of classification of data was statistical tables, histograms, line charts and bar charts. For the qualitative data, simple listing of suggestions, factors and other itemized variables was adopted. After exploration and organization of the data, descriptive statistics was used. This study is expected to highlight the winning points from agency banking, which can further be exploited as Rwanda seeks to achieve its goal of financial inclusion for all, under the Vision 2020. Data collected was analyzed through SPSS version 21 and presented through percentages, means, standard deviations and frequencies. Descriptive statistical tools such as frequencies, percentages, mean and standard deviation helped the researcher to describe the data. Multiple regression models were used to analyze the data on financial performance. The study revealed that financial services accessibility by customers through baking agencies had a positive impact on financial performance of commercial banks in Rwanda. The study found that increased market share had a positive effect on the financial performance of commercial banks with many banking institutions indicating that increased market share allowed a company to achieve greater scale in its operations which generally improved its profitability. Multiple regression models were used to analyze the data on financial performance. The ANOVA results for regression coefficient indicate that the significance of the F is 0.00 which is less than 0.05. This implies that there is a positive significant relationship the effect of agency banking and performance of commercial banks in Rwanda and that the model is a good fit for the data.**

Keywords: **Financial services accessibility, customers, financial inclusion, commercial banks Bugesera district, Rwanda.**

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1. INTRODUCTION

1.1 Background:

Since 2012, there have been significant improvements in the banking sector with the introduction of agency banking in Rwanda, an innovative delivery channel that seeks to bring access to financial services much closer to entrepreneurs (BNR, 2014). This study sought to find out the role of agency banking in improving financial performance of commercial banks in Rwanda. In the last decade, there has been an explosion of different forms of remote access financial services, that is, beyond branches. These have been provided through a variety of different channels, including mobile phones, automatic teller machines (ATMs), and point-of-sale (POS) devices and banking correspondent (Podpiera, 2008).

In many countries, these branchless channels have made an important contribution to enhancing financial inclusion by reaching people that traditional, branch-based structure would have been unable to reach. One of the main obstacles to financial exclusion is cost: both the cost to banks involved in servicing low value accounts and extending physical infrastructure to remote rural areas, and the cost (in money and time) incurred by customers in remote areas to reach bank branches. These agents have also penetrated into rural areas where offering banking services could be expensive for banks.

In rural areas it is often prohibitively expensive for commercial banks since transaction numbers and volumes do not cover the cost of a branch (Kitaka, 2011). Also, low income clients often feel more comfortable banking at their local store than walking into a marble branch (Adiera, 2015).

Though the bank continues to invest in rolling out brick and mortar branches that are complimented by various channels, the challenge of access to formal financial services remains a big impediment to financial performance. Customers (especially in remote areas) are forced to travel long distance and spend huge amounts on transport in order to access a branch. In addition to the cost of transport is the time spent commuting to and fro that could have been spent more productively. To curb these challenges, the National Bank of Rwanda released a legislation that allows commercial banks to contract third party retail networks as agents. Aduda, (2013), the main objective of all commercial banks is to increase their profitability through expansion of their branch network in order to reach many of their potential and existing customers who are in remote places where access to banking services is limited. Besides this, agency banking also assists in decongesting banking halls by letting the customers receive banking services elsewhere. In an effort to achieve this, they have opted to use the existing business enterprises such as pharmacies, supermarkets and convenient stores. This is what is referred to as Agency banking.

1.1.1 Agency Banking:

Agency banking was first developed in Brazil in 1999. Although by 2000, only 1,600 municipalities in Brazil had bank branches, by 2010, some 170,000 agents cover all of the 5,500 municipalities, and nearly 12 million accounts have been opened at agents over the years. Brazil's experience has offered valuable lessons for countries where banks can contract an agent (McKay, 2011). The Banks Act allows a bank to contract agents to receive on (the banks) behalf from its clients any deposits, money due to it or applications for loans or advances, or to make payments to such clients on its behalf.

Agency banking refers to the services offered by retail or postal outlet contracted by financial

Institutions to process clients' transactions. Rather than a branch teller, it is the owner or an employee of the retail outlet who conducts the transaction and lets the client deposit, withdraw, and transfer funds, pay their bills, inquire about an account balance, or receive government benefits or a direct deposit from their employer (Ivatory & Layman, 2008).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, personal identification numbers(PIN) pads, and sometimes personal computers that connect with the bank's server using a personal dial-up or other data connection. Identification of customers is normally done through a PIN but could also involve biometrics. With regards to the verification, authorization, and settlement platform, banking agents are similar to any other remote bank channel (CGAP, 2006).

Local regulation determines if commercial banks are allowed to work through retail outlets. Regulators generally determine what kind of, if any, commercial banks are permitted to contract banking agents, what products can be offered at the retail outlets, how commercial banks have to handle cash transport, know your customer requirements, consumer protection, and other operational areas. Agency banking functions include; enabling customers to pay their bills, inquire about an account balance or receive government benefits or a direct benefit from their employer. It also helps bank customers to make payment of rent and insurance premium. Besides these, it accepts deposits from customers and allows withdrawals and transfer of funds (Ivatury, 2008)

1.1.2 Financial Performance:

Financial performance is conclusions drawn from financial analysis of a firm. Financial analysis is the selection, evaluation, and interpretation of financial data, along with other pertinent information, to assist in investment and financial decision-making. Financial analysis may be used internally to evaluate issues such as employee performance, the efficiency of operations, and credit policies, and externally to evaluate potential investments and credit-worthiness of borrowers, among other things (Drake, 2016). Financial performance is subjective of how well a firm uses its assets from its primary mode of business to generate revenue. This term is also a general measure of the firm's overall financial health over a given period of time and can be used to compare industries or sectors in aggregation (Hales, 2015).

Some of the key aspect that is looked at in financial performance is profitability, liquidity, solvency, financial efficiency and repayment capacity. Further analysis of financial performance uses methodologies such as financial ratio analysis, benchmarking, measuring performance against budget or a combination of these (Barnet et al, 2016). Dess and Robinson (1984) performed a study that compared subjective measures to objective measures of profitability. They used a three-step approach to test the correlation between objective and subjective measures of return on assets (ROA), sales growth, and overall financial performance. Both objective and subjective measures of the ROA and sales growth were used in addition to two measures of overall financial performance. The measures of overall financial performance were compared to the objective and subjective ROA and sales growth. Dess and Robinson (2014) found that a firm's subjective perceptions of how well it had done over a specific time period were in agreement with the objective measures of change in return on assets and sales. They were also in agreement with the firm's subjective evaluation of overall financial performance. Finally, it was stated that subjective performance measures were probably the most appropriate for examining relative performance within an industry (Dess & Robinson, 2014).

1.1.3 Agency Banking and Financial Performance:

A bank agent is a commercial entity that has been contracted by a commercial bank and approved by the National Bank of Rwanda to provide specific services on behalf of the bank. Agents are equipped with the skills necessary to provide basic banking services according to standards set by the banks with commercial bank key objective of offering the full range of banking services to their customers without them having to visit a branch. This provides the opportunity to access financial products and services at a location nearest to the customer, thus breaking down certain barriers to financial inclusion such as cost and accessibility.

Agency banking as a strategy of expansion depicts its concept from the branchless banking model into which the wordings are will use interchangeably. Branchless banking is a distribution channel strategy used for delivering financial services without relying on banks branches (Ivatury and Mars, 2008). 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). Agency banking is a type of branchless banking where third parties are involved in performing some of the activities that are traditionally performed in banking halls by bank personnel. Globally, retailers and post offices are increasingly utilized as important distribution channels for financial institutions. The points of service range from post offices in the Outback of Australia where clients from all banks can conduct their transactions, to rural France where the bank Credit Agricole uses corner stores to provide financial services, to small lottery outlets in Brazil at which clients can receive their social payments and access their bank accounts (Kumar et al, 2016).

In understanding agency, there are three parties to a transaction: the customer, the agent's employee who operates the POS (Point of Sale) device and the bank. Each party should authenticate themselves before initiating any transaction, preferably with two factors of security hence; the customer and the authorized employee of the agent each have a personal card plus a secret PIN. To avoid fraudulent POS terminals, a bank could also announce a unique secret key to each of its clients through which the bank identifies itself to its clients before each transaction (Ivatury, 2008). Financial performance is conclusion drawn from financial analysis of a firm. Financial analysis is the selection, evaluation, and interpretation of financial data, along with other pertinent information, to assist in investment and financial decision-making. Financial analysis may be will use internally to evaluate issues such as employee performance, the efficiency of operations, and credit policies, and externally to evaluate potential investments and the credit-worthiness of borrowers, among other things (Drake, 2006). Financial performance is a subjective measure of how well a firm uses its assets from its primary mode of business to generate revenue (Greenwood and Jovanovic 2014). This term is also a general measure of the firms overall financial health over a given period of time and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation (Hales, 2015).

Some of the key aspect that is looked at in financial performance is profitability, liquidity, solvency, financial efficiency and repayment capacity. Further analysis of financial performance uses methodologies such as financial ratio analysis, benchmarking, measuring performance against budget or a combination of these (Barnet et al, 2016). Profit is the ultimate goal of a firm. To measure the profitability, there are variety of ratios used of which Return on Asset, Return on Equity and Net Interest Margin are the major ones (Murthy and Sree, 2008). ROA is a major ratio that indicates the profitability of a bank. It is a ratio of income to its total assets (Khrawish, 2011). It measures the ability of an organization's management to generate income by utilizing company assets at their disposal.Net Interest Margin (NIM) is a measure of the difference between the interest income generated by banks and the amount of interest paid out to their lenders, relative to the amount assets. It is usually expressed as a percentage of what the financial institution earns on loans in a specific time period and other assets minus the interest paid on borrowed funds divided by the average amount of the assets on which it earned income in that time period (the average earning assets). ROE is a financial ratio that refers to how much profit a company earned compared to the total amount of shareholder equity invested or found on the balance sheet. ROE is what the shareholders look in return for their investment. Return on Assets (ROA) is the ratio of Net Income after Taxes divided by Total Assets. The ROA signifies managerial efficiency. In other words, it depicts how effective and efficient the management of banks has been as they seek to transform assets into earnings. A higher ratio indicates a higher performance of the banks. It is a useful tool for comparing profitability of one bank with other or the whole commercial banking system. Moreover, the ROE is said to measure the rate of return on the bank's shareholders equity and it is calculated by dividing banks net income after taxes by total equity capital which includes common and preferred stock, surplus, undivided profits, and capital reserves. This measure of profitability gives an indication of what the banks earns on the shareholder's investment; many researchers have presented ROA as an appropriate measure of bank profitability. Among them Rivard and Thomas (1977) who argued that bank profitability is best measured by ROA in the sense that, ROA cannot be distorted by high equity multiplier? However, Hassan and Bashir (2008) also claims that as ROA tend to be lower for financial intermediaries, most banks heavily utilize financial leverage to increase their ROE to competitive levels.

1.1.4 Commercial Banks in Rwanda:

Khambata (2016) defines a commercial bank as a financial institution that is capable of accepting deposits, making business loans, and offering basic investment products. According to the National Bank of Rwanda there are currently 17 commercial banks that are fully registered and operating in Rwanda. These are profit making financial institutions that play a significant role in the financial system of the country. Commercial banks play a number of roles in the financial stability and cash flow of the country's private sector. Commercial banks provide a number of import financial and trading documents such as letters of credit, performance bonds, standby letters of credit, security underwriting commitments and various other types of balance sheet guarantees. They also take the responsibility for safeguarding such documents and other valuables by providing safe deposit boxes. Currency exchange functions and the provision of unit trusts and commercial insurance are typically provided by the relevant departments in larger commercial banks. Commercial banks in Rwanda also play a very significant role as agents of monetary policy. The Central Bank of Rwanda largely depends on commercial banks in effecting its monetary policy. The banks also contribute a significant portion of the Country's Gross Domestic Product (GDP) (Rajan & Zingales, 2008). Despite the mentioned achievements, commercial banks in Rwanda have their share of challenges. One of the challenges faced by commercial banks is the stiff competition from both local and international players. The other challenge relates to increasing operational expenses and expanding non-performing loan portfolio that forces most commercial banks to use a significant portion of their profits to provide for non-performing loans. Commercial banks in Rwanda are also getting several challenges with rapid changes in technology that requires them to continue improving their existing systems to cope with dynamic business environments. The dynamic business environment in which commercial banks operate has made some of the banks to consider alternative ways in order to remain competitive in the market. One of strategies pursued by commercial banks is agency banking. Banking agents help commercial banks to divert existing customers from crowded branches providing a complimentary often more convenient channel. Other commercial banks, especially in developing markets, use agents to reach an additional client segment or geography. Banking agents are the backbone of mobile banking, i.e., performing transactions over a mobile device, most often a mobile phone. To enable clients to convert cash into electronic money and vice versa which can be sent over their mobile phone, clients will have to visit a branch, automated teller machine (ATM), or banking agent. Especially in remote and rural locations, where cash is still the most important way to pay and transact, a mobile banking service is dependent on banking agents to enable clients to effectively use the service.

Agency banking took effect in Rwanda in May 2012 after the publication of prudential guidelines by the National Bank of Rwanda. Agency banking has been practiced in a number of Countries such as Brazil, Kenya, Columbia, Pakistan, South Africa and Indonesia. The agency banking retail approach is designed to help banks increase their outreach without incurring additional costs of setting up. 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. Globalization has spearheaded the integration of the Rwanda economy with other world class economies such as Singapore, which is now part of the global village. The powers of information and technology, de-regulation, globalization of markets and stiff competition has made banks better educated, more inquisitive, sophisticated and deciding. The banking environment has changed tremendously thereby posing serious implications and challenges to the survival and profitability of banks. This is according to Consultative Group to Assist the Poor (CGAP, 2008). However Rwandan banking sector has demonstrated a solid growth over the past few years. The industry continues to offer significant profit opportunities to the major participants.

1.2 Statement of the Problem:

Initially access to banks will be not an easy thing for a common man in Rwanda as banking sector will be majorly targeting working class and the middle class/people with more disposable income. To move closer and access many customers, commercial banks started to allow other commercial outlets like shops and supermarkets to act in their capacity as formal banks and this will be formally launched by National Bank of Rwanda about five years ago, but just a handful of banks have so far taken up the option. So far KCB, Bank of Kigali, cogebanque and equity bank have launched their agent banking segment.

In Rwanda agent banking has seen dramatic expansion in very many countries all over the world including Rwanda. With agency banking, low-income people no longer need to use scarce time and financial resources to travel to distant bank branches. And since agency banking transactions cost far less to process than transactions at an automated teller machine (ATM) or branch, banks can make a profit handling even small money transfers and payments (Booz, 2013). The adoption of agency banking is mainly geared to improve on market share by attracting and retaining their customers, improving their financial performance and create variety of services. To this end, it is not clear whether the adoption has led to increase in market share and financial performance. This study therefore aimed at assessing the contribution of agency banking on financial performance of commercial banks in Rwanda.

The rationale for adopting agency banking is to enable Rwandan financial institutions to take advantage of the cost saving and accessibility brought about by the agency banking model. According to the (BNR 2013), there will be significant growth in retail deposits amongst commercial banks that had embraced agency banking. Unlike the past, today it is common to find one agent providing services of at least two commercial banks at the same outlet. The current study therefore seeks to bridge the gap between what has been previously studied by other researchers by carrying out a research on the impact of agency banking on the financial performance of commercial banks in Rwanda. Although customers have benefited a lot through the agency banking, it is not clear whether the financial performance of commercial banks have improved or not as a result of adopting agency banking. This study will attempt to answer the following research question: What is the contribution of agency banking to the improvement of financial inclusion of commercial banks in Bugesera district, Rwanda?

1.3 Objective of the Study:

1.3.1 General objective:

The general objective of the study was to examine the contribution of agency banking to the improvement of financial inclusion of commercial banks in Bugesera district, Rwanda.

1.3.2 Specific objectives:

The objectives of the study were:

1. To establish the contribution of financial services accessibility by customers on the improvement of financial inclusion of commercial banks in Bugesera district, Rwanda.

2. CONCEPTUAL FRAMEWORK

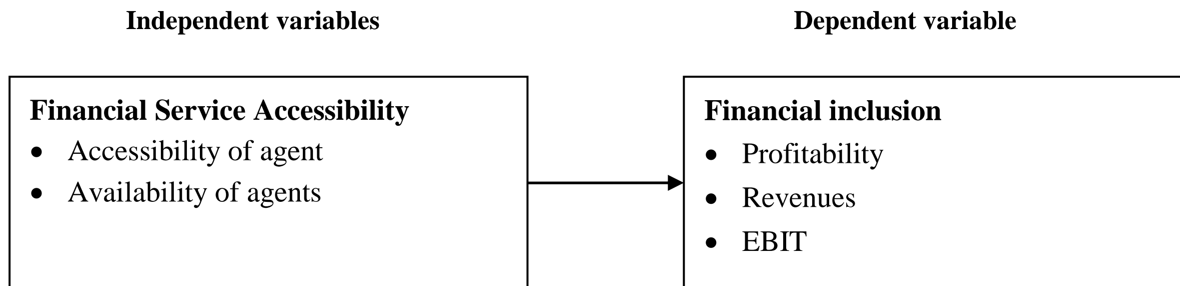

Figure 2.1: Conceptual framework

3. TARGET POPULATION

The population for this study is commercial banks in Rwanda specifically the agents of various banks in Bugesera District. According to National Bank of Rwanda (BNR, 2015), there are 60 agents of commercial banks in Rwanda which is the target population for this study. Mugenda and Mugenda, (2013), states that the target population should have some observable characteristics, to which the researcher intends to generalize the results of the study. Hence the target population was 60 agents of different banks in Bugesera District.

4. RESEARCH FINDINGS AND DISCUSSION

4.1 Financial Services Accessibility and Financial inclusion:

Table 1: Financial services accessibility through agency banking

	Frequency	Percentage
Yes	45	80
No	11	20
Total	56	100

The study sought to determine whether financial services accessibility through agency banking affects the improvement of financial inclusion of commercial banks in Bugesera district, Rwanda. From the findings the study established that, majority of the respondents agreed that financial services accessibility through agency banking affects the financial performance of commercial banks in Rwanda as shown by 80% where as 20% of the respondents were of contrary opinion. This implies that financial services accessibility through agency banking affects the improvement of financial inclusion of commercial banks in Bugesera district, Rwanda.

Table 2: Extent to which financial services accessibility affects the improvement of financial inclusion of commercial banks in Bugesera district, Rwanda

	Frequency	Percentage
To a very great extent	26	46
To a great extent	14	25
To a moderate extent	9	16
To a little extent	5	9
To no extent	2	4
Total	56	100

The study sought to determine the extent to which financial services accessibility through agency banking affects the financial performance of commercial banks in Rwanda. From the findings the study established that 46% of the respondents indicated to a very great extent, 25% of the respondents indicated to a great extent, 16% of the respondents indicated to a moderate extent, 9% of the respondents indicated to a little extent and finally 4% of the respondents indicated to a no extent at all. This implies that financial services accessibility through agency banking affects the financial performance of commercial banks in Rwanda to a great extent.

Table 3: Financial services accessibility

	Strongly agree	Agree	Moderate	Disagree	Strongly disagree	Mean	Std. Deviation
Agency banking adoption in banking systems has shown a great momentum and spread at an unbelievable pace across the world which has increased the accessibility of financial service	28 (50%)	14 (25%)	14 (25%)	0	0	1.71	0.38
There is great potential of using this in agent banking for provision of banking services to unbanked community	22 (39%)	26 (46%)	5 (9%)	3 (6%)		2.06	0.37
Agency banking has led to accessibility of financial service to many customer in remote areas	24 (43%)	14 (25%)	14(25%)	3 (6%)	1 (1%)	1.83	0.39
Accessibility of banking service through agency banking has led to profitability of commercial banks	26 (46%)	24(43%)	3(6%)	3 (6%)		1.91	0.38

The study sought to determine the level at which respondents agreed or disagreed with the above statements relating on effects of financial services accessibility through agency banking on financial performance of commercial banks in Rwanda. From the findings the study established that majority of the respondents agreed that; Agency banking adoption in banking systems has shown a great momentum and spread at an unbelievable pace across the world which has increased the accessibility of financial service as shown by mean of 1.71. Agency banking has led to accessibility of financial service to many customers in remote areas as shown by mean of 1.83. Accessibility of banking service through agency banking has led to profitability of commercial banks as shown by mean of 1.91 and finally there is great potential of using this in agent banking for provision of banking services to unbanked community as shown by mean of 2.06. The study further established that agency banking made it easier for commercial bank to reach out to many potential clients without investing so much in opening branches hence it's a cost effective measure. It also increased the ease of expansion hence outreach to far flung market pockets of bankable populations. Further it also increased distribution channels to offer financial services hence improving overall performance of the organizations.

5. CONCLUSIONS

The study further concludes that financial services accessibility by customers through banking agencies had a positive impact on financial performance of commercial banks in Rwanda with many of the banking institutions indicating that agency banking had made it easier for them to reach out to many potential clients without investing so much in opening branches hence it's a cost effective measure.

5.1 Recommendations:

The study recommends that the banking institutions should considered intensifying the agency banking network which will ensure services accessibility by customers and thus improving financial performance.

Finally, the study recommends that banking institutions should consider coming up with lock in strategies for the already captured market. This will award more power to the bank in controlling the prices and services it offers to its customers.

5.2 Areas for further research:

The study sought to determine the effects of agency banking on financial performance of commercial banks in Rwanda. The study recommends that a study should be done on the challenges facing the adoption of agency banks by commercial banks in Rwanda

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