AGENCY BANKING AND OPERATIONAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

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DECLARATION

I declare that this Research project is my original work and has not been presented in any other institution of higher learning.

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D61/84442/2013

This research project has been submitted for examination with my approval as the University Supervisor.

Signature: ______________________________ Date: ________________

MR.AKELO ERNEST

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DEDICATION

This work is dedicated to my entire family, my Dad Joseph, my Mum Ruth and to my dearest Kihuni for being a source of positive influence and inspiration in my life. Without their love and support this project would not have been made possible.

ABSTRACT

Agency banking roll-out in Kenya was meant to address the low financial inclusion in Kenya. As per the 2009 National financial access survey, 32% Kenyas bankable population is still totally out of the financial services orbit. Difficulties in accessing financial services main drivers are; long distance to banking channels and relative high costs of accessing financial services. In a bid to bridge the financial access divide and improve its access among the most vulnerable sections of the society, the Kenya government through the central bank amended the finance Act 2009 to facilitate use of third parties by banks to provide banking services. This study sought to establish the contribution of agency banking to operational performance of commercial banks in Kenya. The researcher was guided by objectives; to establish the impact of agency banking to operational performance of commercial banks in Kenya; to determine the operational challenges facing agency banking in Kenya and to establish the factors leading to the growth of agency banking. The researcher reviewed relevant literature and conducted a descriptive research design survey study to find out the effect of agency banking to operational performance of commercial banks. Data was collected by use of questionnaire. Data was analyzed and presented using descriptive statistical tools. In addition, advanced statistical technique was also used. SPSS (Statistical package for social sciences) model was also used in data analysis. The results were presented in a continuous prose form. The study showed that liquidity availability in the outlets affected banks performance in addition to leading to frustrated customers. The study also found out that agency infrastructure cost and security was a major influence to banks performance. The study therefore recommends that, banks should give more attention to security and find better ways of vetting their agents to ensure that large cash transaction are handled effectively. The study also recommends that agents should be more financially included to handle many transactions, like converting cheques into cash, deal with foreign currency exchange among others.

TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

LIST OF ABBREVIATIONS AND ACRONYMS

PIN	Personal Identification Number
POS	point-Of-Sale
KBA	Kenya Bankers Association
KCB	Kenya Commercial Bank
MFI	Micro Finance Institutions
NGO	Nonprofit Organizations
SPSS	Statistical Packages for Social Sciences
CBK	Central Bank of Kenya
CGAP	Consultative Group to Assist the Poor
FSD	Foundation for Sustainable Development
PSV	Public Service Vehicle
DTB	Diamond Trust Bank
EFINA	Enhancing Financial Innovation and Access
FSA	Financial Services Authority

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Getanga (2011), notes that an agency bank is an organization that acts on behalf of another bank or organization, this mean an agent accept deposits or extend loans facility using its own name; it only acts on behalf of the parent bank. It is a retail outlet contracted by a financial institution or a mobile network operator to process client's transactions. Rather than a branch teller, 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 (Central Bank of Kenya, 2011).

Developing countries like Kenya, Ghana and Nigeria are increasingly supporting agency banking as a mode of delivering banking services to many unreached people especially low-income households. Difficulties in accessing financial main drivers are; long distance to banking channels and relatively high costs of accessing financial services. Early experiences have shown that branchless banking through agency's can significantly reduce 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, 2009)

Brazil is probably the most developed market where agency banking has significantly increased financial system structure (Bloodgood, 2011). Agency banking has enabled bank customers to access the basic banking service such as; deposits, withdrawals, disbursement and repayment of loans, payment of bills, transfer of funds, balance enquiry, generation and issuance of mini bank statements, collection of documents in relation to account opening, loan application, credit and debit card applications, agency mobile phone banking services among others (CBK, 2011).

1.1.1 The Concept of Agency Banking

Lyman *et al*. (2008) defined a banking agent as a retail outlet contracted by a financial institution to process clients' transactions. Ignacio (2008) states that rather than a bank branch teller, 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 even get direct deposit from their employer. Globally, these retailers are increasingly utilized as important distribution channels for financial institutions.

Technology can enable banks and their customers to interact remotely in a trusted way through existing local retail outlets. Customers can be issued bank cards with appropriate personal identification number (PIN)-based or biometric security features, and the local store—the "banking agent"—can be equipped with a point-of-sale (POS) device controlled by and connected to the bank using a phone line or wireless or satellite technology. Infrastructure requirements can be further reduced by using mobile phones both to hold "virtual cards" for customers and as a POS device at the store (Ivatury *et al.*, 2008)

If a customer wishes to make a deposit at a store, swiping a bank-issued card puts the customer in direct communication with the bank. The bank automatically withdraws the equivalent amount from the banking agent's bank account to fund the deposit and issues a paper receipt to the customer through the POS device. The agent keeps the cash in compensation for the amount taken out of its bank account. If a customer wishes to make cash withdrawal, the opposite happens: the agent provides cash from the till, but is compensated by an equivalent increase in its bank account (Ivatury *et al.,* 2008)

Banks usually provide their agents with an interest-free overdraft that can be used only to fund banking agent transactions. In this case, the store's POS authorizes transactions as long as the store's account balance at the bank does not go below the amount of the overdraft. The store manager can increase the volume of agent business it can handle by depositing its own funds into the same account. The overdraft is a form of credit extension strictly between the bank and the retail outlet (Lyman *et al.,* 2008). It is the bank's business to ensure it is repaid; the customer will not know whether its banking transactions are being cleared with the support of an overdraft or not. Thus, in the event 13 of default by the store on an overdraft, there should be no claim back to the customers whose banking transactions were enabled through the use of the overdraft.

1.1.2 Operational Performance

Operational performance is a measure against standard or prescribed indicators of effectiveness, efficiency, and environmental responsibility such as, cycle time, productivity, waste reduction, and regulatory compliance (Sullivan, 2011).

Achieving and sustaining operational performance is more important than ever in today's challenging economic environment. Cost pressures, changing customer expectations, stronger competitors and other industry and market disruptions are collectively causing a tremendous strain on operational capabilities and performance. Operational performance excellence is no longer a desired end state but a near-term requirement for any successful company.

Banks' operational performance contributes to the operation and growth of an economy through various roles, including that of intermediary and provides of payment settlement facilities. Banks must also execute these roles faultless in order to promote confidence and stability in the system. The traditional role of banks has been that of intermediary, that is, the bringing together of borrowers and lenders. This can only be done successfully and for sustainable period with the careful management of credit, liquidity and risk factor essentially, because a bank is funded primarily by depositors, it has an obligation to ensure that the risks which depositor's funds are exposed to is minimized (Johnson & Susan, 2012).

Additionally banks facilitate business through the settlement of funds and the provision of credit to customers, provide 24 hour access to funds and facilities to save/invest with safety. Banks must continually upgrade their technologies, products and services in order to facilitate economic transactions and economic growth while maintaining its focus on the minimization and management of risk (CGAP, 2009)

The government looks towards banks in addressing the socio-economic needs of the citizens, notably the provision of banking services to the previously unbanked, as well as assisting in the financial education of the public. Therefore the sound management and regulation of all banks in the system is crucial. Any modern financial system contributes to economic development and the improvement in living standards by providing various services to the rest of the economy. These include clearing and settlement systems to facilitate trade, channeling financial resources between savers and borrowers, and various products to deal with risk and uncertainty (FSD, 2009).

1.1.3 Commercial Banks in Kenya

A commercial bank a is financial institution and a financial intermediary that accepts deposits and channels those deposits into lending activities, either directly by loaning or indirectly through capital markets. A bank is the connection between customers that have capital deficits and customers with capital surpluses. The Kenyan banking industry is one of the broadest and most developed in sub-Saharan Africa with 49 financial institutions, comprising 43 commercial banks, 1 mortgage finance company and five deposit-taking microfinance institutions (CBK 2012).

Agency banking took effect in Kenya in May 2011 after the publication of prudential guidelines by the Central Bank of Kenya. Agency banking has been practiced in a number of countries such as Brazil, Columba, Pakistan, South Africa and Indonesia. In April 28th 2012 Equity Bank unveiled an integrated financial system aimed at widening financial access and financial inclusion. 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. . There has been a shift from stable, non – volatile and predictable business environment to one which is quite volatile, unpredictable and competitive.

Globalization has spearheaded the integration of the Kenya 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 (CGAP, 2003). However, according to (FSAK, 2009) the Kenyan banking sector has demonstrated a solid growth over the past few years. The industry continues to offer significant profit opportunities for the major participants.

1.2 Research Problem

Banking agents are the backbone of agency banking, especially in remote and rural locations, where cash is still the most important way to make deposits and withdrawals. Agency banking was introduced to expand access to financial services, especially in remote areas where it has been expensive for banks to maintain a presence, owing to smaller volumes (Beck, Cull, Fuchs & Getanga, 2011). Other previous studies include; Abreu and Mendes (2002), Almogbil (2005), who did a study on banking the unbanked focusing on technology's role in delivering accessible financial services to the poor.

The agency banking service is dependent on banking agents to enable clients to effectively use the service (Siedek, 2008). Previous studies by have shown that branchless or agency banking through agents can significantly reduce set-up and delivery costs (Ivatury *et al*., 2008; Ignacio, 2008). Agents can offer cash deposits and withdrawal services alone or a broader range of financial services such as utility bill payments to customers who are more comfortable transacting at their local merchants than at traditional bank branches.

Despite the relevance of the agency banking in the commercial banks gaining competitiveness and enhancing operational performance, there has been limited research conducted locally specifically on the contribution of agency banking on commercial banks' financial performance. Most of the studies reviewed were done abroad and according to Aosa (1992), it's not right to import the wholesome results of a research without taking into account the contextual differences and hence the need to carry out local research.

Many studies attempting to shade some light on the subject under study are more general or have failed to give detailed insights and analysis on contribution of agency banking on the operational performance of banks in Kenya. In his study, Kirika (2013) investigated the challenges facing commercial banks in implementing agency banking. The study found out that some of the main challenges facing commercial banks in implementing agency banking include; limit in maximum amount to deposit and withdraw, slow speed of customer adoption, ease of losing money to fraud, delays on transactions due to network failures, lack of enough agents for some areas especially rural areas, across banks transactions not available, lack of infrastructure and agents not having enough float (money).

Mwai (2013) investigated the effect of agency banking on the financial performance of commercial banks; his study found out that agency banking has been implemented to a large extent in terms of products offered to its clients, through the agents and in terms of overall penetration throughout the country. Agency banking has had positive impact to financial performance of commercial banks in Kenya in terms of profitability, reduced employment costs and establishing branches. However, the finding of the study indicates that the concept of agency banking faces challenges that include: Difficulty in converting outlets into what would be comfortably being called outsourced banks.

Although the study attained its objectives, it did not examine the contribution of agency banking to the operational performance of banks in Kenya. There is little published work on the contribution of agency banking on the operational performance, particularly in the context of developing countries in the dynamic African region and specifically in Kenya. It is this knowledge gap the study intends to bridge. The study seeks to answer the following question; What is the contribution of agency banking to the operational performance of the commercial banks in Kenya?

1.3 Research Objectives

The general objective of the study was to evaluate the contribution of agency banking to the operational performance of commercial banks in Kenya.

1.3.1The specific objectives of the study are:

i. To determine the impact of agency banking to operational performance of commercial banks in Kenya.
ii. To determine the operational challenges facing agency banking in Kenya.
iii. To establish the factors leading to the growth of agency banking.

1.4 Value of the Study

Many financial institutions in Kenya (Equity bank, chase bank, KCB and Cooperative bank, post bank, consolidated) have turned to branchless banking methods such as agency banking in their efforts to increase their operational performance over their rivals. The study will show how agent banking has helped to enhance financial inclusion by reaching the frontiers that wouldn't have been reached had it not for agent banking. This will increase and build on the existing theory and knowledge and update this theory on the changes that agent banking is going through as it develops by the day. The study will also look at other services that can be best delivered to customers through agency banking for example insurance services, cashless PSV services mobile phone services in the case of Equity bank.

The study will also be important in policy formulation. It was of great interest and importance's to the government since it will help in the formulation and modification of the various policies to assist remove any outstanding hindrances to contribution of agency banking on operational performance of commercial banks.

The study is expected to be of help to commercial bank policy makers in identifying the key challenges involved in agent banking operations and coming up with strategies that will lead to improved operational performance.

In practice, this study was of importance to the banks because they will know how much they are gaining in through agency banking by reaching that extra person they would not have reached had they not engaged agents to help on agent banking in terms of operational performance. The study will provide information to the public and all players; the agent, customers, banks, the regulator (CBK) on the impact of agent banking on reaching the unreached segments of the international society.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviewed the literature on the contribution of agency banking adoption on the operational performance of banks in Kenya. The review covered both the theoretical and empirical reviews of the existing literature. The theoretical review helped in comprehending the current body of knowledge on the research topic while the empirical review helped in understanding what other related studies have found and suggested.

help in understanding what other related studies have found and suggested.

2.2 Theoretical Review

This section will review the interplay between operational performance, agent banking and commercial banks. . This is henceforth undertaken in the sections hereunder:

2.2.1 Agency Theory

Agency theory postulates that the firm consists of a contract between the owners of economic resources (principals) and managers (agents) who are charged with using and controlling those resources. Furthermore, agency theory is based on the premise that agents have more information than principals and that this information asymmetry, adversely affects the principals ability to effectively monitor whether their interests are being properly served by the agents. It also assumes that principals and agents act rationally and that they will use the contracting process to maximize their wealth. This means that because agents have self-seeking motives they are likely to take the opportunity to act against the interests of the owners of the firm, for example allocating themselves huge pay perks.

The theory of agency was first explicitly modeled by Jenses and Meckling (1976) in their study of structure of the firm. Agency theory addresses all exchanges involving cooperative effort and delegation of work and decision making by one party (principal), to another party called agent. Jensen & Meckling describe an agency relationship as a contract (implicit or explicit) in which one or more persons, the principal(s) engage another person, the agents, to take actions on their behalf. It thus involves delegation of some decision making authority to the agent. It is taken as unquestionable that an informed principal can benefit from this delegation to an informed agent and that it is in fact optimal for an uninformed principal to do so given their lack of skills, knowledge and experience.

The notion of agency is widely used in economics, legal and social sciences albeit with different comparable meaning. Human agents autonomously choose to engage relations with principals presumably because doing so promotes or does not conflict with their own interest. By engaging in agency banking relationship, however, an agent is bound to moral and legal rights that protect the interests of the principal through a legally enforceable contract entered into by both the principal and the agent. Agency theory seeks to determine the most efficient contract governing the two parties, given its assumption about the parties, organization and its formation. In agency banking, the contracting bank is the principal while the retail outlet or shops are the agents.

2.2.2 Bank-Focused Theory

The bank-focused theory emerges when a traditional bank uses non-traditional low-cost delivery channels to provide banking services to its existing customers. Examples range from use of ATMs to internet banking, mobile phone banking or agent banking to provide certain limited banking services to banks customers. This model is additive in nature and may be seen as a modest extension of conventional branch-based banking.

Banks must address the challenges posed by agency banking. Those factors as stated under research problem include agent networks, security, customer education and consumer trust. Banks must be extra careful about the agents they hire, and ensure that they uphold the required standards of delivery and conduct.

2.2.3 Bank-led Theory

In the most basic version of the bank led theory of branchless banking, a licensed bank institution (typically a bank) delivers financial services through a retail agent. It is composed of a sequence of three main entities; the bank, the retail agent, and the customer. That is, the bank develops financial products and services, but distributes them through retail agents who handle all or most customer interaction. In this model, the bank must carry out an audit of its agents to ensure that the agents operate within the generally accepted rules and regulations in order to safeguard the interests of the bank, agents and the customers.

2.3 Agency Banking Adoption

In the recent past, there has been a flow of empirical studies that document the striking level of adoption of agency banking by the commercial banks to reach mostly the rural areas. Surveys and other empirical studies find that the lack of financial access depends foremost on background conditions where, not surprisingly, the institutional variable is crucial in providing information and solving agency problems. Empirical studies show that the solution for the poor is to rely on informal financial services which are more expensive than formal financial and often times unsafe (Coyle, 2007; Donner, 2007). By filling a financial vacuum for the poor it offers the possibility of gaining access to savings, micro-credits and receiving remittances.

From literature reviewed, the major reason for the introduction of agency banking in many nations of the world is that, it is seen as a way of reaching the unbanked. The unbanked can simply be described as those individuals that do not have any form of account with a bank. Anderson (2007) defined the unbanked as "diverse group of individuals who remain outside the banking mainstream for many reasons.

Guatam (2008) stated that Africa has about 230 million unbanked households. In the same vein, Ladipo (2008) revealed a survey carried out by EFINA that cuts across all the states of Nigeria over a five year period and with a sample based on national integrated survey of households, that 74% (which is equivalent to 64 million people) of the adult population in the country have never been banked.

Anderson (2007) also noted that, a way of reducing the number of unbanked people is through the adoption of advanced electronic technology (which leads to non-dependence on branches for financial services). The objectives of agency banking are achieved through "non-traditional banking channel". These include delivery points (which are not distinct buildings). Among these channels are mobile phones and POS (Point of Sale Devices).

The benefits of agency banking cannot be overemphasized. Through all these delivery channels, banks will increase their outreach to the unbanked, provision of banking services will not be limited to working hours and weekdays, long queues that are rampant in banking halls was reduced, and loss of customer due to relocation of the customers from one area to another was averted. Many other benefits can be derived from agency banking (Mwirigi, 2011).

2.4 Agent Banking Operations

A banking agent is a retail or postal outlet contracted by a financial institution or a mobile network operator to process client's transactions. Rather than a branch teller, 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. Banking agents can be pharmacies, supermarkets, convenience stores, lottery outlets, post offices and many more (Kumar et al., 2006).

In Brazil, private and state owned banks deliver financial services through retail agents including small supermarkets and pharmacies, post offices, and lottery kiosks (Kumar et al., 2006). These agents are called banking correspondents. In January 2006, India's central bank issued a circular permitting banks to use post offices and specializes micro finance institutions (MFI), including nonprofit organizations (NGO), cooperatives, and for profit companies as retail agents.

The circular calls these agents business correspondents. Harper *et al. (2006*) in South Africa, branchless banking through retail agents is permitted only for licensed financial institutions. In Kenya the most basic version of agent banking is whereby a licensed financial institution typically a bank delivers financial services through a retail agent. The bank develops financial products and services but distributes them through retail agents who handle most customer interaction.

2.4.1 Shortcoming of Agency Banking

Liquidity is one of the biggest challenges in rolling out banking agencies in the establishment and the effectiveness of the agent network. Agents are the touch- points where the subscribers of the service can get money into and out of the system. In instances where a subscriber arrives at an agent with the need to withdraw a large amount it does happen that the agent do not have enough cash to satisfy the cash-out request. This leads to frustration and is one of the reasons why take-up of these systems are slower than what is expected. This problem is referred to as the agent liquidity problem- how to ensure that the agent has sufficient cash available to satisfy the need of the system (Central Bank of Brazil, 2007).

Security is one of shortcoming of most of today's branchless banking system is that they provide security at the network layer only and do not implement any application –layer cryptography. An important shortcoming typical of informal financial services is lack of reliability and continuity in the long run. Evidence from the four country studies suggests that technical failures (e.g., equipment malfunctioning and other errors occurring during a transaction) are not a major issue in branchless banking. Similarly, research on consumer experience in Brazil shows that less than 5 percent of users have made a mistake and paid the wrong bill at an agent, sent money to the wrong account, or noticed that a payment or a deposit was never processed or received (Collins, 2011).

Physical security is another common concern of regulators. In Brazil, for example, agents must deposit the cash received from clients in a bank branch no more than every other business day. This intended to limit cash accumulation that can lead to robbery by third parties or even by the agent itself. Regulators should avoid setting physical security standards similar to those imposed on bank branches, however, since this could have severe consequences for the viability of the service and hence access (Stephens & Kevin, 1998).

Policy and regulation is a challenge beyond agent banking. This is regulation and legislation of Agent Banking. The Policy makers and regulators have been facing challenges finding a way to safe development of branchless banking and operation with increased levels of financial access. Lyman and Staschem (2006) indicate that protecting client funds is priority for many financial regulators, as loss of funds can have serious consequences for customers, as well as for public confidence in financial systems.

2.5 Operational Performance

The use of the agent banking model by banks in Kenya has continued to improve access to banking services and has also increased financial deepening in the country since it was launched in 2011. Since the beginning of agency banking, the financial sector has recorded an increased growth with most Kenyans accessing finances at their convenience. According to the Central Bank of Kenya report dubbed Development in the Kenyan Banking Sector for the Quarter ended 30th June, CBK had authorized 13 commercial banks to offer banking services through third parties (agents). Since 2011, a total of 19,649 agents had been contracted facilitating over 58.6 million transactions valued at Ksh. 310.5 billion. This was an increase from 11 banks that had contracted 18,082 active agents facilitating over 48.4 million transactions valued at Ksh. 250.1 billion in March 2013, banking survey (2013). The increase could be as a result of agency banking adoption.

Ignacio (2008), agency banking strategies rely on agents that operate outside of bank branches. Agent banking is undoubtedly a necessity in Kenya. However, in comparison to Brazil and Colombia, Kenya suffers the following disadvantages; poor fixed line infrastructure, high incidence of fraud, insecurity-robberies, theft, carjacking, hijacking, level of technological literacy in rural areas still low, low financial education, poor transport system, few branches in rural areas, insufficient cash flow in rural areas some areas may lack agents who meet financial qualifications, low penetration of credit and debit cards, low volumes of utility payment bills for electricity, water, telephone and other pressing social concerns such as poverty, drought, famine, banditry, diseases, unemployment. It is however noteworthy that these challenges are surmountable and once due attention is given to them, agent banking can still be implemented (CBK, 2009).

Therefore the only cost the bank incurs is marketing materials and branding, as the agents outlets have to be branded and look like small branches. 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 (Hamblen, 2008).

2.6 Summary of Literature Review

This is a summarizes of the findings that have emerged as a result of empirical work on the study of the contribution of agency banking adoption on the operational performance of commercial banks in Kenya; the concept is fairly new in Kenya having been introduced in May 2011, it has however gained interest by banks and scholars are also gaining interest in the field. There are challenges and a factor affecting its adoption but the benefits are much more.

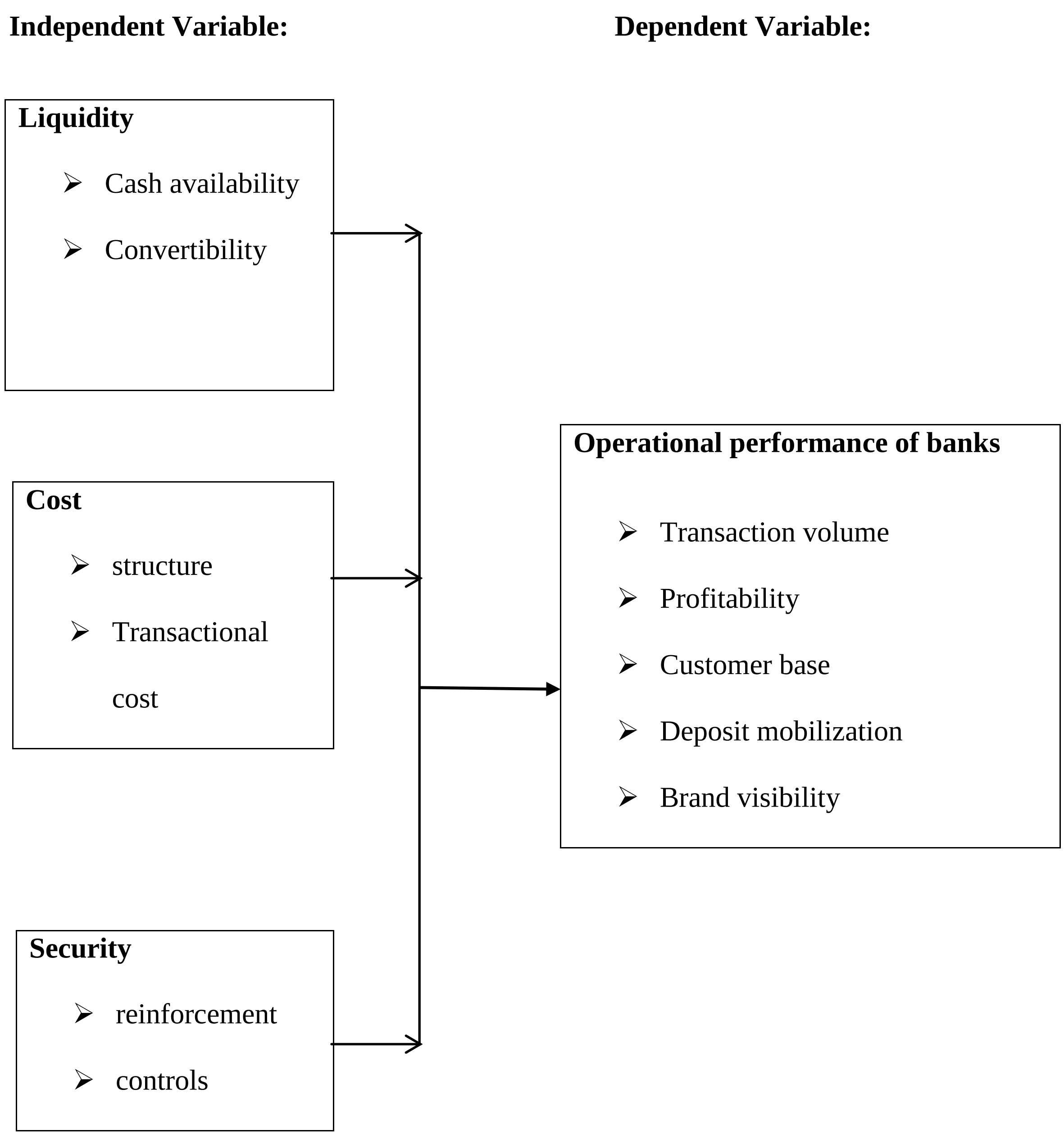
However, there has been little interest in study that seeks to find out the operational performance of the model hence this study seeks to bridge the gap. The ability to offer financial transactions online has also created new players in the financial services industry such as agency banking, online banks, online brokers and wealth managers who offer personalized services, although such players still account for a tiny percentage of the industry (Lyman, 2008).

Ignacio (2008) profound that successful branchless business models must work not only for providers and end clients, but also for agents. Providers depend on the energy of agents for customer acquisition and for managing liquidity so as to support cash withdrawals and deposits. Successful providers therefore view their agents as an important category of customer, rather than a passive channel.

2.7 Conceptual Model

The conceptual attempted to examine and explain factors that have affected and hence influenced provision of agency banking service in commercial banks in Kenya. These factors include, the cost of agency transactions, security and liquidity. These factors influence the banks on either to offer or not to offer agency service. While the independent factors are internal to business. The study determined the effects of independent variables on the dependent variable in order to access the contribution of agency banking to operational performance of banks in Kenya.

Figure 1: Conceptual Framework



Source: Researcher (2014)

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter sets out various stages and phases that was followed in completing the study. It involves a blueprint for the collection, measurement and analysis of data. In this stage, most decisions about how research was executed and how a respondent was approached, as well as when, where and how the research are completed. These included presents details of the research design, target population, sample design, data collection procedures and data analysis techniques.

3.2 Research Design

A research design describes plan, structure and strategy of investigation to obtain answers to research questions and control variance Ogula (2005). This study adopted a survey research design. This research design as defined by Orodho (2003) is a method of collecting information by interviewing or administering a questionnaire to a sample of individuals.

3.3 Target Population

The target population is the specific population about which information is desired. Ngechu (2004), a population is a well defined set of people, services, elements, event, and group of things or households that are being investigated. This definition ensures that population of interest is homogeneous. The target population of this study included 8 commercial banks in Kenya that offered agency banking services.

3.4 Data Collection

Data in is a set of values of qualitative or quantitative variables. Primary data was collected by use of questionnaire with both open and closed ended questions. The close end questions were more preferred since they are easier and quicker for respondents to answer and the answers of different respondents can be are easier to compare .While the open end questions are used as they permit an unlimited number of possible answers and respondents can answer in detail and can qualify and clarify responses.

The questionnaire was chosen as an instrument for the study since its practical to the research problem and the size of the population. Also large amounts of information can be collected from a large number of people in a short period of time and in a relatively cost effective way (Mugenda & Mugenda, 2003).

3.5 Data Analysis

Data collected was analyzed using descriptive statistics. The descriptive statistical tools such as frequencies, percentages, mean and standard deviation helps the researcher to describe the data. Data collected was coded, tabulated and presented according to each independent and dependent variable. The data was checked for completeness and consistency. Responses were analyzed using content analysis. Multiple regression models was used to analyze the data on operational performance. Multiple regressions is a statistical technique used to examine the way a number of independent variables relate to one dependent variable. This analysis was done with an aid of SPSS software.

3.5.1 Regression Model

$Y = ß_0 + ß_1X_1 + ß_2X_2 + ß_3X_3 + e$

Y- Operational performance of banks

$ß_0$ - the constant

$ß_1$, $ß_3$, $ß_2$, $ß_3$, $ß_4$, – are regression coefficients or change induced in Y by each X variable

X_1 – Liquidity

X_2 – Cost

X_3 – Security

e – Error term

Independent

variables

CHAPTER FOUR
DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presented the research findings in a study of agency banking to operational performance of commercial banks in Kenya. The analysis was focused on answering the research questions. The data was gathered exclusively from questionnaire as the research instrument. The study targeted 26 respondents comprising of agency manager and operation manager. Some of the respondents could not be accessed due to work commitment while others were on leave.

4.2 Response Rate

The response rate was fairly good because out of 26 questionnaires distributed, 19 were returned answered giving a response rate of 73.1%. According to Mugenda and Mugenda (2003) a 50% response rate is adequate, 60% good and above 70% rated very good. This also concurs with Kothari (2004) assertion that a response rate of 50% is adequate, while a response rate greater than 73.1% is very good. This implies that based on this assertions; the response rate in this case of 73.1% is very good. This commendable response rate was made possible after the researcher personally administered the questionnaires and made visits to remind the respondents to fill in the questionnaires.

4.3 Analysis of Demographic Data

This was a general analysis on the demographic data obtained from the respondents which included: - Job category, work duration in the bank, gender, number of years bank has offered agency banking and service offered.

4.3.1 Job Category

Table 4.1: Job Category

Job category	**Frequency**	**Percentage**
High Management	8	37%
Middle Level	10	48%
Low level	3	15%
Total	**21**	**100**

Source: Research Data (2014)

The study sought to find out the job category of the respondents. From the findings, 48% of the respondents who were the majority indicated that they were in middle management, 37% of the respondents indicated that they were in top management**,** 15% of the respondents indicated that they were low level management.

4.3.2 Work Duration

The respondents were asked to how long they have worked with the bank. From the findings, 43% of the respondents who were the majority indicated that they have worked for 6-10 year, 21% indicated that they have worked for 11-15 years, 17% indicated that they have worked for over 20 years, 14% indicated that they have worked for 16 – 20 years and 55 have worked below 5 Years.

Table 4.2: Work Duration

Work duration	Frequency	Percentage
Over 20 years	4	17%
16 – 20 years	3	14%
11 – 15 years	4	21%
6 – 10	9	43%
Below 5 years	1	5%
Total	**21**	**100%**

Source: Research Data (2014)

4.3.3 Distribution of the Respondents in terms of Gender

The study sought to determine the gender of the respondent and therefore requested the respondent to indicate their gender. The study found out that majority of the respondent were male by 63% whereas 37% of the respondent were female, this is an indication that both genders were involved in this study and thus the finding of the study did not suffer from gender bias.

4.3.4 Age Distribution of the Respondent

Table 4.3: Age Distribution

Age of Distribution	Frequency	Percentage
Above 50 yrs	1	6%
40 - 50 yrs	6	29%
36 – 40 yrs	8	35%
30 – 35 yrs	5	24%
26 – 30 Yrs	1	6%
21 – 25 Yrs	0	0%
Below 20 Yrs	0	0%
Total	**21**	**100%**

Source: Research Data (2014)

The study sought to establish the age distribution of the respondents. From the findings; 35% indicated they were between 36 – 40 years, 29 % were between 40 – 50 years, 24 % were between 30 – 35 years, 6% between 26 – 30 years, 6% were above 50 years and none below 20 years and between 12 – 25 years.

4.3.5 Duration of Agency Banking

Table 4.4: Duration of Agency Banking

Duration of Agency Banking	Frequency	Percentage
Above 2 years	13	65%
Above 12 months	3	12%
6 – 9 months	4	17%
More than 6 months	1	6%
Total	**21**	**100%**

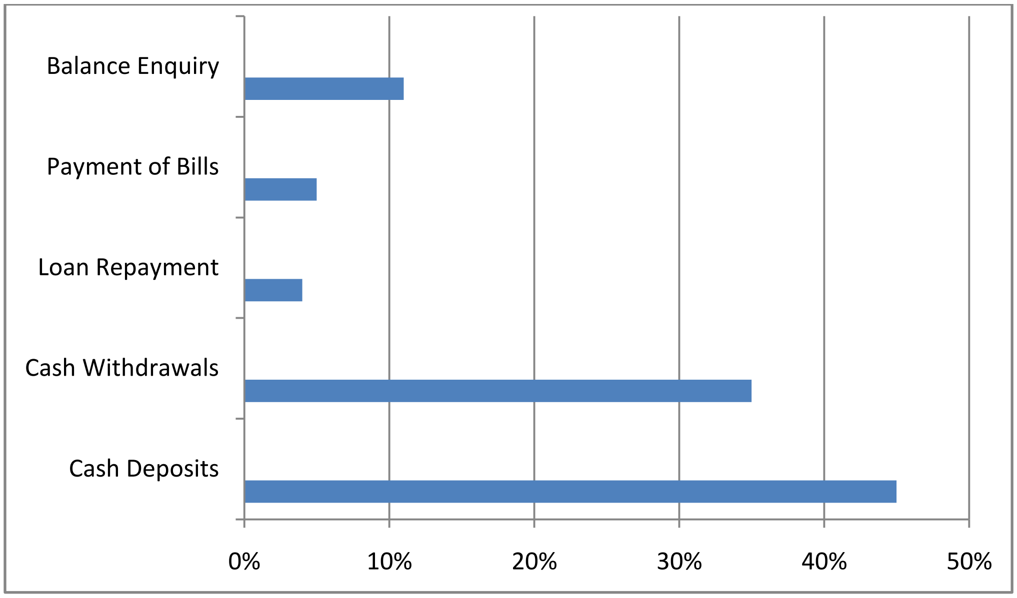
Source: Research Data (2014)

The study sought to find out for how long has the bank been offering agency banking. From the findings , 65% of the respondents who were the majority indicated that the bank have been offering agency banking for above 2 years, 17% have been offering agency banking for 3- 9 months, 12% have been offering for 9 – 12 months, and 6% have been offering agency banking for less than 3 months.

These results are consistent with the findings by Mwai (2013) in a study on the effect of agency banking on the financial performance of commercial banks. His study found out that agency banking has been implemented to a large extent in not more than 5 years. This mean is still a new product in the market.

4.3.6 Services Offered in Agency Banking

Figure 4.1: Services offered in agency banking



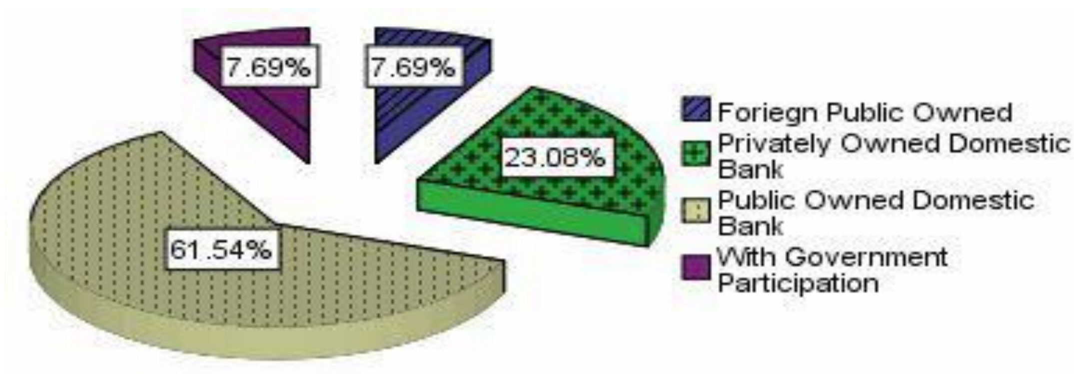
Source: Research Data (2014)

The study sought to establish the services that are offered in agency banking and from the findings 5% of the respondents indicated that they offered payment of bills, 4% they offered loan payments, 45% offered cash deposits , 11% offered balance enquiry and 35% that they offered cash withdrawals.

These results are different from the findings by Musau (2010) in a study on analysis of the utilization of agency banking on performance of selected banks in nairobi. Musau (2010) working with a sample of 40 and found out the services that are offered in agency banking and from his findings 35 % of the respondents indicated that they offered payment of bills, 24% they offered loan payments, 17% offered cash deposits , 12% offered balance enquiry and 12% that they offered cash withdrawals. This indicates that agency banking was not fully utilized during its inception period. These results are consistent with the findings by Siedek, (2008). The study found out that agency banking service is dependent on banking agents to enable clients to effectively use the service (Siedek, 2008). Previous studies by have shown that branchless or agency banking through agents can significantly reduce set-up and delivery costs (Ivatury *et al*., 2008; Ignacio, 2008).

4.3.7: Ownership Structure of the Bank.

Figure 4.2: Ownership structure of the bank



Source: Research Data (2014)

From the chart above, it is clear that 62% were Public Owned Domestic Banks,

23% were Privately Owned Domestic Banks, 8% were owned with Government participation and another 8% were Foreign Public Owned. Public Owned Domestic Banks are the majority at embracing agency banking.

4.4 Performance of Commercial Banks

4.4.1 Number of Agents for the Bank

Table 4.5: Number of Agents for the Bank

Number of Agents	Frequency	Percentage
Less than 500	2	9
500-1000 agents	4	19
1000-2000 agents	5	24
Over 2000 agents	10	48
Total	**21**	**100%**

Source: Research Data (2014)

From the chart above, 24% have 1000-2000 agents, 48% of the banks have over 2000 agents, 19 % have 500-1000 agents and 9% have less than 500 agents. This implied that pioneered into agency banking have numerous agency outlets and those that are joining the foray are fast catching up.

The findings are consistent with those by Ndiema (2013) From the findings, 33 % have 1000-2000 agents, 28% of the banks have over 2000 agents, 19% have 500-1000 agents, 14 % have100-500 agents and 4 % have less than 100 agents.

4.4.2 Reason for bank to venture into agent banking

Table 4.6: Reason for bank to venture into agent banking

Reason for bank to venture into Agent Banking	Frequency	Percentage
Increase territorial coverage	3	14%
Decongest branches	4	19%
Reach the poor marginalized unbanked	13	62%
Increase customer base	1	5%
Total	**21**	**100%**

Source: Research Data (2014)

From the findings, 19% of the respondents who were the majority indicated the main reason for venturing into agency banking was to decongest branches, 62% indicated to reach the poor marginalized unbanked, 14% indicated to Increase territorial coverage and 5% indicated to increase customer base.

The findings are consistent with those by Anderson (2007) and found out that the unbanked was a diverse group of individuals who remain outside the banking mainstream for many reasons and the major reason for the introduction of agency banking in many nations of the world is that, it is seen as a way of reaching the unbanked. The unbanked can simply be described as those individuals that do not have any form of account with a bank. Anderson (2007) also noted that, a way of reducing the number of unbanked people is through the adoption of advanced electronic technology, which leads to non-dependence on branches for financial services.

4.4.3 Impact of Agency Banking on Banks Performance

Table 4.7: Impact of Agency Banking on Banks Performance

Banks Performance		**Mean**	**Std Deviation**
Transaction volume	Increasing the turnaround in transactions	3.69	1.26
	Change of measures of transactions	4.25	0.93
Profitability	Payment of low commission to the agents	4.13	0.08
	Improving the quality of service	3.86	1.31
Customer base	Increasing customer base	3.77	1.47
	Customer segmentation	3.68	1.49

Source: Research Data (2014)

From the table it is observed that change of transaction measure in transactions to a very great extent affected performance of banks as evidenced by a mean score of 4.25, improving turn around in transactions was to a very great extent as shown by a mean score of 3.69, improving the quality of service was to a very great extent as shown by a mean score of 3.87, increasing customer base was to a very great extent as shown by a mean score of 3.78 and customer segmentation was to a moderate extent as shown by a mean score of 3.69 and also increasing the turn around a transaction was to moderate extent of 3.69.

4.5 Security on Performance

4.5.1 Security Services that Protect Client Information

Table 4.8: Security Services

Security Services	Frequency	Percentage
Very strong	9	41%
Strong	6	28%
Moderate	5	24%
Weak	1	7%
Very weak	0	0%
Total	**21**	**100%**

Source: Research Data (2014)

From the findings, 41% of the respondents who were the majority indicated that security services were very strong, 28% indicated that they were strong, 24% indicated that they were moderate and 6% indicated that they were weak while none of them indicated that they were very weak.

4.5.2 Risk Encountered by Operating Agency Banking.

Table 4.9: Agency risks

Agency risks	Frequency	Percentage
Operational risk	9	41%
Liquidity risk	6	28%
Reputational risk	5	24%
Legal risk	1	7%
TOTAL	**21**	**100%**

Source: Research Data (2014)

From the findings, 41% of the respondents who were the majority indicated that operational risk affected the operation of agency, 28% indicated liquidity risk, 24% indicated reputational risk and 6% indicated legal risk.

4.5.3 Preparing Agents to Perform Banking Duties

The study sought to determine how the bank was involved in preparing agents to perform their duties; therefore the respondents were requested to indicate with a Yes or No answer. The study found that majority of the respondent 76% indicated a Yes whereas 24% of the respondents were indicated No, this is an indication that the banks were involved in preparing agents to perform their duties

4.5.4 Challenges Encountered by Agents in Operating Agent Banking

Table 4.10: Challenges Encountered by Agents

Challenges	Frequency	Percentage
Untrained staff	12	57%
Inadequate cash in the agents	3	14%
System failures	4	19%
Data loss	2	10%
Total	21	**100%**

Source: Research Data (2014)

From the table above, it is clear that 57% indicated the main challenge was untrained staff 19% was System failures, 14% was inadequate cash in the agents and another 10% indicated Data loss.

The results are consistent with the findings by Kirika (2013) in a study on challenges facing commercial banks in implementing agency banking. This study deviated slightly and found out that some of the main challenges facing commercial banks in implementing agency banking include; limit in maximum amount to deposit and withdraw, slow speed of customer adoption, ease of losing money to fraud, delays on transactions due to network failures, lack of enough agents for some areas especially rural areas, across banks transactions not available, lack of infrastructure and agents not having enough float (money).

4.6 Effects of Agency Costs on Performance

4.6.1 Effect of Operational Cost on Bank Performance

Table 4.11: Effect of Operational Cost

Effects of agency costs	Frequency	Percentage
To a very great extent	10	46%
To a great extent	6	27%
To a moderate extent	4	21%
To a low extent	1	6%
To no extent at all	0	0%
Total	21	100%

Source: Research Data (2014)

From the above findings 46% of the respondents who were the majority indicated that cost affect performance to a very great extent, 27% to a great extent, 21% a moderate extent while 6% was to a low extent and none of the respondents indicated that it was to no extent.

4.6.2 Areas of Cost Influence on Performance of Banks

Table 4.12: Agency cost influence on performance of banks

Cost Influence	Mean	Std Deviation
Transactional cost	3.89	5.70
Infrastructural cost	2.74	1.54

Source: Research Data (2014)

From the findings, respondents indicated that infrastructure cost was to a very great as shown by a mean score of 3.89 and transaction cost was to a moderate extent as shown by a mean score of 2.74.

4.7 Liquidity on Performance

4.7.1 Frequency of Liquidity Challenge

Table 4.13: Frequency of Liquidity Challenge

Frequency of liquidity	Frequency	Percentages
Very often	4	20%
Often	12	55%
Rarely	2	10%
Never	3	15%
Total	**21**	**100%**

Source: Research Data (2014)

The study sought to find out how often respondents experienced liquidity challenge in their business. From the findings, 55% who were the majority indicated that they experience liquidity challenge often, 20% indicated that they very often experience liquidity challenge, 15% indicated that they never experience liquidity challenge and 10% indicated that they rarely experience liquidity challenge.

4.7.2 Effects of Liquidity Availability on Performance

Table 4.14: Effects of Liquidity Availability on Performance

Effects of Liquidity	Frequency	Percentages
To a very great extent	8	40%
To a great extent	5	26%
To a moderate extent	6	27%
To a low extent	2	7%
To no extent at all	0	0%
Total	**21**	100%

Source: Research Data (2014)

From the above findings 40% indicated that liquidity availability affects performance of bank to a very great extent, 28% indicate the effect was to a great extent and 7% indicated that the effect was to a low extent and none of the respondents indicated that it was to no extent.

4.7.3 How the respondents planned to cope with liquidity issues

The study sought to find out how the respondents were planning to cope with liquidity issues. From the findings, most of the respondents indicated that, they wish to increase their presence in limited geographical distance, so that one agent can act as a rescue for the other in case of liquidity problem. They also indicated that the problems are seasonal tending to be major during end month and weekends and hence plans were underway for most of them to address the problem.

4.8 Descriptive Statistics

Table 4.15: Performance of Agency banking as per number of agents, number of transactions per agent and volume of money flowing through the agents as per 2013

Commercial Banks	Number of Agents	Number of Transactions per agent	Volume of money flowing through the agents	ROA	Mean	Std Deviation
Kenya Commercial Bank	2,000	3600	7,200,000	42.7	2.67	0. 47
Equity bank	6,000	6790	40,740,000	50.4	1.98	0.48
Co-operative Bank of Kenya	4,000	5090	20,360,000	38.4	2.06	0.09
Family Bank	100	0	0	25.5	0	0
Diamond Trust bank	100	4299	429,900	25.9	3.12	0. 90
ECO bank	1000	0	0	26.5	0	0
Post bank	1,000	1389	1,389,000	22.2	3.60	0.68
Total	**53,677**	**21,426**	**209,430,845**	**41.2**	**2.51**	**0.45**

Source*: Computed by researcher using data extracted from annual reports of banks (2013)*

From the findings Equity Bank registered highest (6,000) number of agents as per the year 2012, followed by Co-operative Bank, Kenya Commercial Bank and Post Bank as indicated by 4,000, 2,000 and 1,000 respectively. Further the study indicates that equity bank registered the highest number of transactions per agent, followed by co-operative bank and Kenya commercial bank as indicated by 6790, 5090 and 3600 respectively.

This implies that banks have continuously performed significantly in agency banking leading to improved financial performance. However, as far as ECO Bank and family bank registered 1000 and 100 respectively, none was in operational. This study finding is in line with Mwangi (2011) who evaluated the role of agency banking in the performance of commercial banks in Kenya. The study was done on four banks offering agency banking services using questionnaires distributed to the banks' branch managers. The study established that infrastructure cost and security influence the performance of commercial banks attributable to agency banking to a very great extent. The study recommends that agency banking should be given more attention on security measures including risk-based approach and that the banks should find better ways of screening their agents to ensure that the large cash transactions handling is effectively carried out on their behalf; secure operating systems capable of carrying out real time transactions, generating an audit trail, and protecting data confidentiality and integrity.

Table 4.16: Evaluation of Commercial Banks Agency Banking 2011-2013 (Operational Performance)

Commercial Banks	2011	2012	2013	Overall Index Evaluation
Kenya Commercial Bank	3.28	3.38	4.11	3.98
Equity bank	4.08	4.45	4.66	4.63
Co-operative Bank of Kenya	3.42	3.58	4.22	4.16
Family Bank	3.08	3.45	4.08	3.02
NIC Bank	2.08	2.45	3.08	3.63
Diamond Trust bank	2.08	2.45	3.08	3.64
ECO bank	2.11	2.16	2.22	2.18
Post bank	2.22	3.22	3.922	2.637
Yearly Performance	20%	30%	35%	100%

***Source**: computed by researcher using data extracted from annual reports of banks (2013)*

The findings in Table 4.16 indicates that out of a total of 43 banks, 8 have rolled out the agency banking service with Equity bank, Co-operative bank and Kenya Commercial Bank showing significance performance index as shown by the overall evaluation of 4.63, 4.16 and 3.98 respectively.

However other banks that have rolled up the service (Family Bank, NIC Bank, Diamond Trust Bank, Eco-Bank and Post Bank) did not show much significance performance index. The findings further showed that yearly performance improved significantly from the year 2011 as shown by, 20% (2011), 30 % (2012) and 35 % (2013) respectively. This implies that agency banking is continuously improving leading to significance increased financial performance in those banks that have rolled up the service due to its convenience and efficiency in operation.

The finding is in line with Kithuka (2012) who sought to establish the factors influencing growth of agency banking in Kenya. The study sampled 100 Equity Bank agencies doing bank focused, bank led and non-bank led transactions in Kwale County. The study established that convenience of the money transfer technology plus its accessibility, cost, support and security influence the use of agency banking.

4.9 Relationship between Agency Banking and Operational Performance

Under the advance analysis, correlation analysis was first used to measure the degree of association between different variables under consideration. While the regression analysis was used to determine the impact of the agency banking on operational performance of rolled up commercial banks, the Chi-square test statistics was used to ascertain whether there is a significant difference in the agency banking and operational performance.

Finally, the t-test statistics was also used to find out if a significant difference occurred in the performance of banks with agency banking and those without agency banking.

4.10 Correlation Matrix

In this section, the study measured the degree of association between the agency banking functions and operational performance i.e. if the agency banking services (number of agents, number of transactions per agent and volume of money flowing through the agents) will increase operational performance of commercial banks.

From the a priori stated in the previous chapter, a positive relationship is expected between the measures of agency banking and operational performance. Table 4.3 and 4.4 presents the correlation coefficients for all the services considered in this study.

Table 4.17: Pearson's Correlation Coefficients Matrix for the Model (Operational Performance)

Agents Transactions	**Correlation**	**Number of Agents**	**Number of Transactions per Agent**	**Volume of Money Flowing**	**Operational Performance**
Number of Agents	Pearson Correlation	1			
	Sig. (2-tailed)				
	N	53,677			
Number of transaction per Agent	Pearson Correlation	0.68(**)	1		
	Sig. (2-tailed)	0			
	N	53,677	53,677		
Volume of money flowing through the agent	Pearson Correlation	0.486(**)	.409(**)	1	
	Sig. (2-tailed)	0	0.001		
	N	53,677	53,677	53,677	
Operational performance	Pearson Correlation	0.539(**)	0.596(**)	0.625	1
	Sig. (2-tailed)	0	0	0.076	
	N	53,677	53,677	53,677	53,677

** Correlation is significant at the 0.01 level (2-tailed).

***Source**: computed by researcher using data extracted from annual reports of banks(2013)*

From the correlation result for model, volume of money flowing through the agents has a strong positive correlation of 0.625 with operational performance which is significant at 1% and 5%. This implies that volume of money flowing through the agents have a positive effect on the level of operational performance in Kenyan banks due to increased profitability. Number of agents and the number of the transactions per agent also showed significant contribution to operational performance. The outcome from the statistics is consistent with earlier studies by Lipton and Lorsch (1992); Jensen (1993); Yermack (1996); Bennedsen et al (2006); Harris and Raviv (2005). They all argued that larger volume of transactions leads to improved operational performance.

Table 4.18: Two-Sample Assuming Equal Variances Banks rolled Up Agency Banking Service and Banks Not Rolled up Agency Banking Service

Variance	**(Banks rolled up agency banking service)**	**(Banks not rolled up agency banking service)**
Mean	0.06	0.024
Variance	0.002	1.000
Observations	8	4
Hypothesized Mean Difference	0	
Df	7	
t Stat	2.96	
P(T<=t) one-tail	0.005	
t Critical one-tail	1.77	
P(T<=t) two-tail	0.01	
t Critical two-tail	2.16	
Mean	0.06	0.024

Source: *Computed by the researcher from annual reports banks (2013)*

From table 4.18, the efficient rolled up agency banking recorded a mean of 0.06while the non-efficient banks recorded a mean of 0.024. However, the variance for the efficient banks and the no-efficient banks are 0.002 and 1.38 respectively. Furthermore, at two-tailed, the t- calculated of 2.96 is seen greater than the t-tabulated of 2.16.

Further the study carried out the hypothesis testing between agency banking and operational performance. The study findings are as shown below.

4.11 The significance of Agency Banking on Operation performance

Regression analysis was used to derive determinant of coefficient, analysis of variance and the significance of the explanatory on the dependent variable. Determinant of coefficient shows the percentage of the total variation on performance of commercial banks which is attributed to the changes in agency banking. Analysis of variance will be used to test if the sample mean are drawn from the same population and also to test if the model is fit for the estimation. Regression coefficient will be used to determine if agency banking and the control variables are statistically significant in causing the changes in operational performance of commercial banks.

4.11.1 Analysis of Variance

Analysis of Variance's (ANOVA) F-test was used to make simultaneous comparisons between two or more means; thus, testing whether a significant relation exists between variables (dependent and independent variables); thus, helping in bringing out the significance of the regression model. Since the value ($p=0.0024$) was below 0.05, it can be concluded that the regression model was significant and fit for estimation.

Table 4.19: Analysis of Variance

Model		Sum of Squares	df	Mean Square	F	p.
1	Regression	0.004	4	3.00	0.023	0.00
	Residual	0.01	10	36.00		
	Total	0.02	14	39.00		

4.11.2 Model Summary

Table 4.20: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.81	0.73	0.66	0.02	1.98

R-square values present proportion of the variation in operation performance of banks is attributed to the changes in the explanatory variables. From the adjusted determination coefficients, generally moderately strong linear relationships were established between dependent and independent variables. Their R-squared value of 73.901% was established and this implies that 73.01 % of the variation in operation performance of banks is attributed to the changes in the independent variables.

The study also used Durbin Watson (DW) test to check that the residuals of the models were not autocorrelated since independence of the residuals is one of the basic hypotheses of regression analysis. Being that the DW statistic (1.98) was close to the prescribed value of 2.0 for residual independence, it can be concluded that there was no autocorrelation.

4.11.3 Regression Coefficients

Table 4.21: Regression Coefficients

Independent variables	**Coef.**	**Std.Error**	**t**	**P>|t|**
LQD	2.01	0.00	0	0.998
COST	0.001	0.003	-0.38	0.709
SEC	0.17	0.05	3.19	0.003
_cons	0.16	0.009	18.79	0

From the regression analysis, only security and constant average is statistically significant at 5% level of significance. That is for security ($t = 3.19$, $p=0.003$, $p<0.05$) hence security is significant determinant of operation performance of commercial banks in agency banking. The regression coefficient result has also established that liquidity and cost are not significant factors in operation performance of commercial banks. Liquidity reported $t= 1.78$ and $p = 0.99$while cost reported $t =-0.38$ and $p = 0.71$.

From the analytical model, the estimated model becomes:

$$Y = 0.16 + 2.01LQD + 0.001COST+ 0.17SEC$$

Liquidity is positively related to operation performance of banks and a unit increase in liquidity will lead to 2.01 units increase in operation performance. The regression result established positive association with operation performance of banks. A unit increase in cost will lead to 0.001 units increase in operation performance of the bank and a unit increase in security will lead to 0.17 increases in operation performance of banks.

4.12 Discussion of the Research Findings

In summary, the findings indicates that out of a total of 43 banks, 8 have rolled out the agency banking service with Equity Bank, Co-Operative Bank and Kenya Commercial Bank showing significance performance index. However other banks that have rolled up the service (Family Bank, NIC Bank, Diamond Trust bank, ECO bank and Post bank) did not show much significance performance index. The findings further showed that yearly performance improved significantly from 2008 to 2012. This implies that agency banking is continuously improving leading to significance increased financial performance in those banks that have rolled up the service due to its convenience and efficiency in operation.

From the findings Equity Bank registered the highest number of agents as per the year 2012, followed by Co-operative bank, Kenya Commercial Bank and Family Bank. Further, the study indicates that equity bank registered the highest number of transactions per agent, followed by co-operative bank and Kenya commercial bank respectively. This implies that banks have continuously performed significantly in agency banking leading to improved operational performance. From the correlation result for model, volume of money flowing through the agents has a strong negative correlation of with operational performance. This implies that volume of money flowing through the agents have a positive effect on the level of operational performance in Kenyan banks due to increased profitability. Number of agents and the number of the transactions per agent also showed significant contribution to operational performance.

The study established that volume of money flowing through the agents has a strong positive correlation with operational performance. Number of agents registered by commercial banks had a moderately strong positive correlation with the banks' operational performance. Number of transactions per agents of commercial banks had a moderately strong positive correlation with the banks' operational performance. This owes to the fact that high-transaction though with low-balance accounts are common among the poor which brings about economies of scale (Podpiera, 2008). Commercial banks have branches that are not close to the customer, thus, the customer is less likely to use and transact. Commercial banks penetration in Kenya is very low and client interaction with the network is driven by mobile phone use and so controlled by telecom firms. Besides, other bank-based delivery channels such as branches have high costs inherent in these traditional banking methods. Thus, agency banking is an apt model used in delivering services in remote place or areas where bank branches are not in existence (Soares & Melo Sobrinho, 2007).

The findings show that commercial banks that had rolled up agency banking were more effect based on the number of agent signed by the commercial bank. Commercial banks provide cash deposit and withdrawal, balance enquiry, collection of documents in relation to account opening, loan application, credit and debit card application, collection of debit and credit cards, cheque book request and collection for their customers through agency banking. However, on deposits and withdrawals, the amount transacted is restricted by the ‘float’ accorded to the agent. Thus, low volume transactions are conducted at the agency banks. Security risky transactions like electronic fund transfer, disbursement of loans are rarely handled by agency banks.

The agents, given close supervision by the commercial banks, provide services consisted with what is in the service charter and CBK guideline. Thus, it was established that they mostly provide quality service to customers. Lyman, Ivatury and Staschen (2006) found that retail agents also handle all account opening procedures and identify and service loan customers. Generally, the study’s findings indicate a strong, significant, positive relationship between agency banking and operational performance.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATION

5.1 Introduction

This chapter summarizes the study and makes conclusion based on the results. The implications from the findings and areas for further research are also presented. This section presents the findings from the study in comparison to what other scholars have said as noted under literature review.

5.2 Summary

The study aimed to establish the status of agency banking in the country and the operational performance of the banks that have rolled up the agency banking service. The findings indicates that out of a total of 43 banks, 8 have rolled out the agency banking service with Equity bank, Co-operative bank and Kenya commercial bank showing significance performance index. However other banks that have rolled up the service (Family Bank, NIC Bank, Diamond Trust bank, ECO bank and Post bank) did not show much significance performance index. The findings further showed that yearly performance improved significantly from 2011 to 2013.

This implies that agency banking is continuously improving leading to significance increased operational performance in those banks that have rolled up the service due to its convenience and efficiency in operation. From the findings Equity bank registered the highest number of agents as per the year 2013, followed by Co-operative bank, Kenya commercial bank and family bank. Further the study indicates that equity bank registered the highest number of transactions per agent, followed by co-operative bank and Kenya commercial bank respectively. This implies that banks have continuously performed significantly in agency banking leading to improved operational performance. From the correlation result for model, volume of money flowing through the agents has a strong negative correlation of with performance. This implies that volume of money flowing through the agents have a positive effect on the level of operational performance in Kenyan banks due to increased profitability. Number of agents and the number of the transactions per agent also showed significant contribution to operational performance. They all argued that larger volume of transactions leads to improved operational performance. From the t-test result, the efficient rolled up agency banking banks recorded a higher mean while the non-efficient banks recorded a slightly lower mean. However, the variance for the efficient banks and the no-efficient banks also varied significantly.

5.3 Conclusion

From the findings above, it can be concluded that majority of the banks in the country have not embraced agency banking with only few 11 out of the 43 licensed and only 8 out of the licensed rolled up with the agency banking service. It can further be concluded from the findings that Equity Bank is the most performing commercial bank as far as agency banking is concerned followed by Cooperative Bank and Kenya Commercial Bank. Agency banking has positively and significantly influenced performance of commercial banks.

Banking agents enable commercial banks to divert existing customers from crowded branches providing a “complementary”, often more convenient channel. They use agents to reach an “additional” client segment or geography. Otherwise, reaching poor clients in rural areas is prohibitively expensive for banks since transaction numbers and volumes do not cover the cost of a branch. Banking agents that piggy back on existing retail infrastructure – and lower set up and running cost - play a vital role in offering many low-income people access to a range of financial services. Also, low-income clients often feel more comfortable banking at their local store than walking into a marble branch which increases the commercial banks' revenue.

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. It also cuts on human resource expenses. The banks do not have to employ new staff to manage the agency and the cost of training if any is to the bare minimum. It further, saves on equipment like furniture and computers. Additionally, the convenience of access to banking services and the extended hours that the banking agencies work is attractive features to the customer. This also helps increase banks' revenue will minimizing costs.

5.4 Recommendation for Research, Policy and Procedure

The study recommends that the government reduces the period of obtaining the legal documents in adopting agency banking. The government should support the program more often and reduce the high compliance costs, bureaucracy in registration and high cost of taxation. Other areas that the study recommends include the government dealing with the cumbersome laws and regulations, corruption and illegal permits and licenses. The study recommends that regulations be efficient to enable more banks to embrace agency banking service.

The study further recommends that commercial banks should fully embrace agency banking through adoption of improved technology for information security to make it more reliable to the customers. This will increase volume of transactions which will lead to financial performance. Based on the findings and conclusions presented above, the study recommends that banks should cushion their agents from certain costs such as insurance costs, cash in-transit or premise setup costs. This will enhance performance of banking agents. Besides, capacity of agents banking in providing services can be enhanced by banks ensuring that agents have enough float that can serve more client in order to mitigate clients disappointment and increase the number of customers. They can do this by advancing credit to their agents. In addition, banks should educate and regulate their agents to ensure uniformity in service delivery so as to enhance customer confidence in agents.

The study recommends that customers should be enlightened on the operation of agency banking in order to enhance their confidentiality. Additionally, the study recommended that agent frequently trained on the operation process and policies to eradicate occurrence of error and mistake that are highly hindering penetration of agency banking.

5.5 Limitations of the Study

The researcher encountered various limitations that may have affected the findings of this study. For instance, the study relied on secondary data sources. Secondary data can, however, be unreliable as they were intended for other purposes. This could include convincing external stakeholders that the business performs well. To curb this, the study sought audited financial results.

The sample for this study might have been small. Small samples have the drop-back of not being representative of the population reality. However, the researcher carried the study on all commercial banks engaged in agency banking hence it was fully inclusive.

Further, the performance of commercial banks is influenced by other factors other than contributions from banks agents. Thus, establishing the relationship between the two variables might be erroneous. The study tested the significance of the relationship established to mitigate this.

5.6 Suggestions for Further Studies

There is need for further research undertaken which may include studies on the factors affecting the financial performance of the agent banks; the role of the government or regulatory framework in supporting the adoption of agency banking and the impact of agency banking to the financial sector deepening or financial inclusion and other related studies. This would help establish effect of agency banking regulations on agents performance and answer the question: Does regulation (from banks and CBK) stifle agency banking or otherwise?

It is further suggested that further research should be done on the challenges facing implementation of agency banking. Studies can also be conducted on the effectiveness of agency banking on banking outreach/penetration in Kenya. It is also recommended that, as roadmap to agency banking development in Kenya, further studies can be done on customer perception of agency banking so as to determine what affect banking agents' performance from the demand side. Moreover, studies can be done on the economic impact of agency banking model performance in Kenya.

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Appendix II: Questionnaire

Section A: Bio Data

This questionnaire is designed to collect data on **Agency banking and operational performance of commercial banks in Kenya.** The questionnaire requires you to give demoghaphics.The research is strictly for academic purpose and your response was treated with utmost confidentiality. The respondent is highly encouraged and persuaded to respond to the statement in the most truthful and objective way possible.

Instructions: please tick inside the space provided or fill where appropriate.

1. Bank..

2. Branch...

3. State your job category

a) High level management [ ]

b) Middle level management [ ]

c) Low level management [ ]

4. How long have you worked with this bank?

a) Below 5 years [ ]

b) 6-10 years [ ]

c) 16-20 years [ ]

d) Over 20 years [ ]

5. Gender

a) Male [ ]

d) Female [ ]

6. How long has this bank been offering agency banking?

a) 0-6 Months [ ]

b) 7-12 Months [ ]

c) 13-18 Months [ ]

d) 18-24 Months [ ]

e) Over 2 Years [ ]

7. What services does this bank offer in agency banking?

a) Cash deposits [ ]

b) Cash withdrawals [ ]

c) Loan repayments [ ]

d) Payment of bills [ ]

e) Balance [ ]

8. What is the Ownership structure of the Bank?

a) Foreign Owned Private Bank [ ]

b) Foreign Public Owned [ ]

c) Privately Owned Domestic Bank [ ]

d) Public Owned Domestic Bank [ ]

e) With Government Participation [ ]

<u>Section B:</u> PERFORMANCE OF COMMERCIAL BANKS

9. How many agents do you have?

a) Less than 100 Agents [ ]

b) 100-500 Agents [ ]

c) 500-1000 Agents [ ]

d) 1000-2000 Agents [ ]

e) Over 2000 Agents [ ]

10. What caused your bank to venture into agent banking?

a) Increase territorial coverage [ ]

b) Decongest branches [ ]

c) Reach the poor marginalized unbanked [ ]

d) increase customer base.

11. It has been argued that agency banking has had an impact on the performance of commercial banks. Kindly rate the extent to which use of agency banking has impacted on the performance of your bank using the indicated performance measures. Use a scale of 1-5 where; 5 Very great extend, 4great extend, 3 Moderate extend, 2 little extend, No extend.

	1	2	3	4	5
Increasing customer base					
Low transactional cost					
Closer proximity by customer					
Increased branch productivity by reducing congestion					

<u>Section C</u>: SECURITY ON PERFORMANCE

12. How can you rate the security services that protect client information in the agent services?

a) Very weak [ ]

b) Weak [ ]

c) Moderate [ ]

d) Strong [ ]

e) Very strong [ ]

13. Which of the following risks does your bank encounter because of operating agent banking? Use a scale of 1 – 4 where 1 is very important, 2 is fairly important, 3 is important, 4 is not important.

	1	2	3	4
Operational risk				
Liquidity risk				
Reputational risk				
Legal risk				
Others (specify)				

14. Has your bank been involved in preparing agents to perform banking duties?

a) Yes [ ]

b) No [ ]

15. What challenges do the agents encounter in operating agent banking? Use a scale of 1 – 4 where 1 is very important, 2 is fairly important, 3 is important, 4 is not important,

	1	**2**	**3**	**4**
Untrained staff				
Inadequate cash in the agents till				
System failures				
Data loss				

<u>Section D</u>: EFFECTS OF COST ON PERFORMANCE

16. To what extent does operational cost by banking affect the operational performance of your bank?

a) To a very great extent [ ]

b) To a great extent [ ]

c) To a moderate extent [ ]

d) To a low extent [ ]

e) To no extent at all [ ]

17. To what extent do the following facts of agency banking influence the performance of your bank. Use a scale of 1-5 where; 5 Very extent, 4 Great extent, 3 Moderate extent, 2 little extent, 1 No extent.

	1	**2**	**3**	**4**	**5**
Transactional cost					
Infrastructural cost					

<u>Section E</u>: LIQUIDITY ON PERFORMANCE

18. In your opinion how often do agents experience liquidity challenges as they offer agency banking service?

a) Very often [ ]

b) Often [ ]

c) Rarely [ ]

e) Never [ ]

19.To what extent then does liquidity availability in agency outlets affect the performance of your bank?

a) To a very great extent [ ]

b) To a great extent [ ]

c) To a moderate extent [ ]

e) To a low extent [ ]

f) To no extent at all [ ]

20. How do you plan as a bank to cope with liquidity issues facing agency banking?

……………………………………………………………………………………………

……………………………………………………………………………………………

……………………………………………………………………………………………

……………………………………………………………………………………………

Thank you