



# G:ENESIS

The Study of the Emergence of  
Entry-level Bank Branches in  
South Africa

Final Report

July 2013

# **The Study of the Emergence of Low Cost Bank Branches in South Africa**

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**Attention: Mia Thom**

Dear Mia,

It is with great pleasure that we send to you the final report on the emergence of low-cost bank branches in South Africa.

Sincerely

Genesis-Analytics Team

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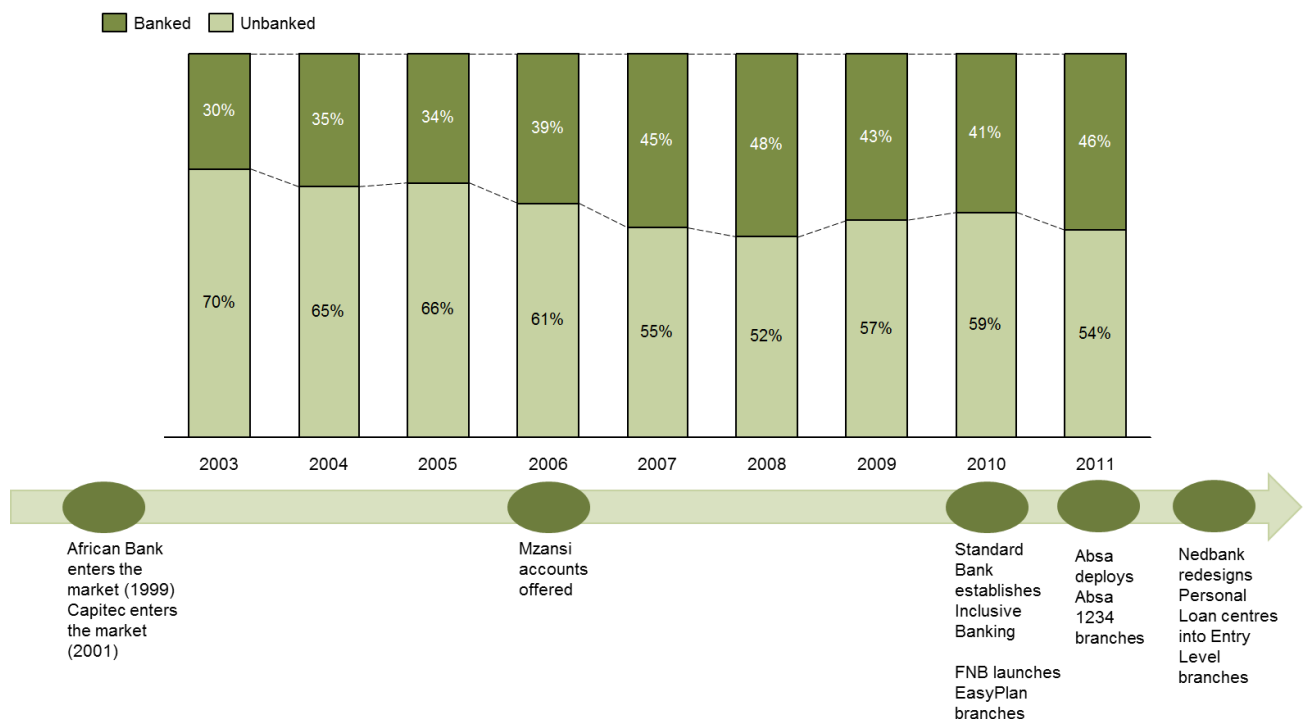
# EXECUTIVE SUMMARY

## 1. INTRODUCTION

Over the past two decades the financial sector in South Africa has seen a shift in the landscape for the provision of financial services to the lower income market. The result of which is access for millions of people who were previously financially excluded. Alternative distribution strategies and mobile provision have played their part, but banks themselves have changed their strategies to extend the reach of their offerings. Bank branch intermediation is generally regarded as better quality than many other forms of intermediation given access to face-to-face interaction with skilled staff across a wide range of services. However physical infrastructure and trained staff come at a cost which is often difficult to justify for low value transactions in the entry-level market.

There has been a substantial increase in the provision of bank accounts, from 30% in 2003 to 46% in 2011. This is potentially an indicator that banks are successfully adjusting their strategies to overcome these challenges, generally by rolling out low-cost, high volume branches (referred to in this study as entry-level branches) to meet the needs of this market segment. To gain a better understanding of this shifting landscape Cenfri on behalf of FinMark Trust commissioned Genesis-Analytics to review the landscape of entry-level branches and identify successful elements of an entry-level banking strategy in South Africa.

**Figure 1: Timeline of shifts in banking landscape from 2002-2011**



## 2. THE SHIFTING BANKING LANDSCAPE

Figure 1 above highlights that the shift has not been overnight and that various factors over many years have culminated in the current landscape of the banking sector in South Africa. These factors included the Mzansi account initiative, changing socio-economic conditions and the entry of the 'Disruptors'.

***Mzansi account uptake reflects market demand.*** In an effort to redistribute the concentration of wealth and extend large industry services to the previously excluded population in South Africa, the new democratic government negotiated industry charters that were designed to obtain commitment from traditional providers to extend their services into the underserved and unserved markets. The financial sector was no exception and in 2004 the agreements were reached that would shift the banking landscape in South Africa to extend their offerings to the previously excluded population. A key outcome of the directives was the development and implementation of a basic low-cost set of financial services to the entry-level market segment. It was believed that the complex and differing options from the banks caused confusion and made comparison for unsophisticated customers difficult. As such, the financial industry developed and introduced a set of standards in 2006 designated the Mzansi account initiative. The success of the Mzansi account initiative is debated, but what it did reveal was a demand in the entry-level-market for banking services beyond just a low-cost product offering.

***Socio-economic factors improve viability of entry-level accounts.*** The new opportunity that the banks were witnessing in the entry-level market converged with two socio-economic trends that were shaping the wider landscape of South Africa: rapid urbanization and formalization of the economy. Historically, the financially underserved or unserved markets were largely informal and in rural or remote areas. However, from 2002 to 2010 the urban population grew from 26.3 million to 30.8 million resulting in a higher concentration of entry-level customers in cities. Over the same period formal employment grew from under 8 million to over 9 million, meaning more customers in the entry-level market could qualify for unsecured personal loans. These two factors made previously excluded clients more accessible and viable for the banks.

***Disruptors demonstrate opportunity.*** Capitec Bank had been operating in the high margin unsecured credit market since its entrance into the banking sector in South Africa in 2001. Capitec was the first bank to enter the banking sector in 20 years, and along with African Bank and Ubank, disrupted the traditional model of the existing banks (the Incumbents - Absa, FNB, Nedbank and Standard Bank). The Disruptors (Capitec, African Bank and Ubank) demonstrated profitable opportunities in the low income market beyond the middle and upper income models which the Incumbent banks had been targeting until that point. Competition from the Disruptors played a substantial role in changing the banking strategies of the Incumbent banks.

The convergence of government pressure, a changing socio-economic environment and viability in high-margin unsecured credit created the incentives for banks to target



the lower income market and brought about a shift in the banking landscape in South Africa. The entrance into the new target market required a change in strategy to effectively service.

### 3. ENTRY-LEVEL BANKING STRATEGIES

***Changing strategies required to serve the new market.*** Serving the entry-level market required a focussed approach to reduce operational and capital expenditures as well as innovative means to acquire and effectively serve high volumes of clients in the new target market. Across the banks this translated into four changes in entry-level banking strategies: change in bank branches, change in composition of infrastructure, change in products and services and a shift in promotional activities.

***Banks adopt common strategies.*** Across the four changes adopted by banks, common strategies to serving the entry-level market emerged, that include:

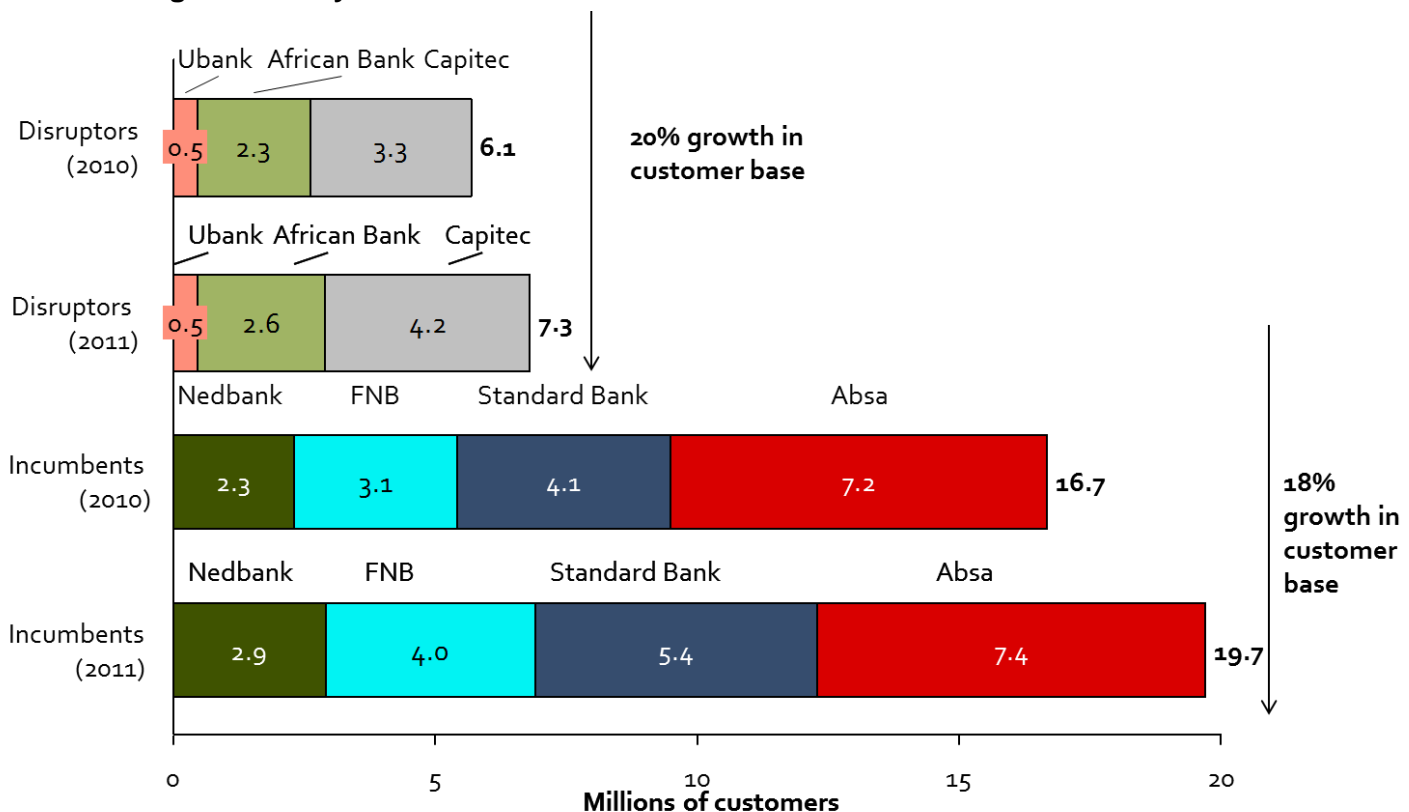
- Introduction of cashless bank branches that substantially reduces the cost of infrastructure and eliminates the cost of cash handling.
- Smarter staffing to reduce staff costs such as employing fewer staff with lower qualifications and offering a lower basic and high commission remuneration structure.
- Extending operating hours to serve commuters effectively.
- Establishing alternatives to branches to reduce capital costs, such as mobile offerings, carve outs/in-retailer models, 'access agents', self-service devices (cash accepting ATMs) and kiosks.
- Movement away from a credit only focus to an increased range of basic products covering all financial services (transactional, savings, credit and insurance, and transactional) to better serve the entry-level market.
- Adopting below-the-line marketing strategies to differentiate bank entry-level offerings from their traditional offerings and attract the entry-level market.

These new strategies have gone hand in hand with substantial infrastructure investment by banks and an increase in the number of entry-level customers served.

## 4. EMERGING TRENDS

**Substantial customer growth in the entry-level market.** The new strategies have paid off and the banking landscape has bared witness to an increase in the number of entry-level customers for both the Disruptors and the Incumbents. Figure 2 below indicates that from 2010 to 2011 the Incumbents entry-level customer base grew by 18% from 16.7 million to 19.7 million customers. During the same period the customer base for the Disruptors grew by 20% from 6.1 million to 7.3 million customers.

**Figure 2: Entry-level bank customers <sup>1</sup>**



**Incumbent bank branches more than doubled between 2010 and 2011.** Unlike the Disruptors, the Incumbent banks needed to tap into the appeal of the entry-level market and differentiate their new branches from their traditional ones. The result was investment in entry-level branches off a low-base and non-branch infrastructure to extend the reach of the banks. Figure 3 below shows that FNB and Nedbank had the largest growth in entry-level branches. Figure 4 shows that Standard Bank and Nedbank led the way in alternative infrastructure, which includes ATMs, bank shops, kiosks and bank agents. This is highlighted by Standard Bank's 'Access agents', who are local community members that act as ambassadors for Standard Bank in informal communities, assisting individuals in making wiser financial choices. Overall, Nedbank

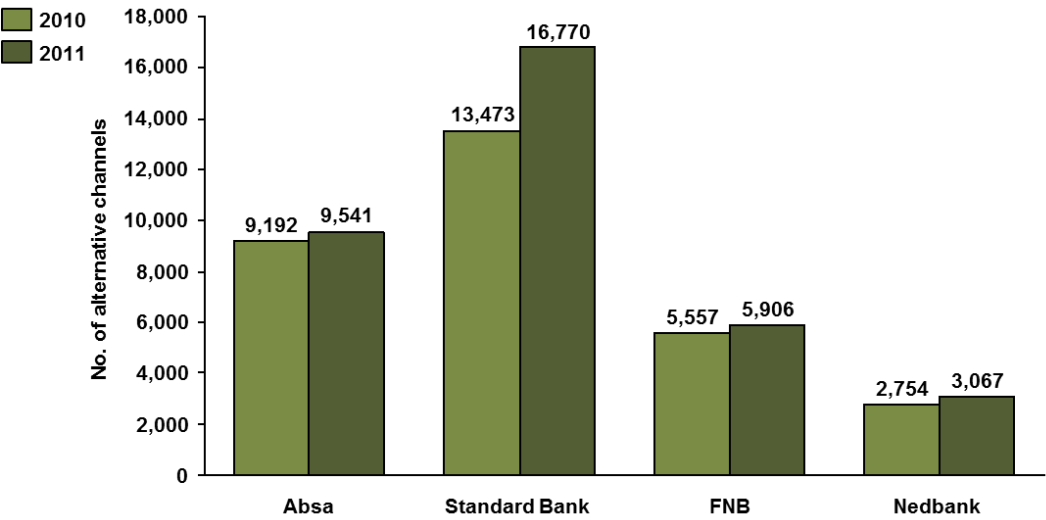
<sup>1</sup> The figure draws on the following sources: Absa integrated Annual Report, 2011; Standard Bank South Africa, Annual Report 2011; UBS, *Charting a new path to sustainable, profitable growth for Nedbank Retail*, 2011; MoneyWeb, *Capitec made FNB rethink its model*, 2011. The entry-level customer numbers were confirmed during interviews with the banks and bank definitions of entry-level clients were used, generally referring to clients below LSM 7.

had the most growth in alternative channels from 2010-2011 introducing over 100 new branches, as well as investing in personal loan kiosks, ATMs and their in-retailer model.

**Figure 3: Growth in entry-level branches 2010-2011 <sup>2</sup>**



**Figure 4: Growth in Non-Branch Infrastructure 2010-2011 <sup>3</sup>**



<sup>2</sup> Absa Integrated Annual Report, 2011; Standard Bank South Africa, Annual Report 2011; FNB Annual Report 2010-2011; Nedbank Annual Report 2011.

<sup>3</sup> *Ibid*

## 5. KEY FINDINGS: COMMON ELEMENTS OF AN ENTRY-LEVEL BANKING STRATEGY

The growth in the entry-level market highlights the emergence of entry-level banking as a critical component of any banks' strategy in South Africa. Operating in this market creates many challenges, the most critical of which is balancing a low-cost branch model with attracting high volumes of clients that have previously not been banked. This study identified common elements for a successful entry-level banking strategy that include:

***Innovation in attracting entry-level clients:*** Bank placement plays a critical role in attracting large volumes of customers into entry-level bank branches. However, it is not the only option. Banks have adopted a more aggressive approach to attracting new clients through a layered marketing approach: (i) promotional activities (ii) on-boarding (iii) education and (iv) personal interaction. At the branch, banks identify potential customers that need further education for understanding of the product and ensure that staff is fully equipped to deliver this education. Away from the branch such as in the case of Standard Bank, Access agents are tasked with on-boarding new customers in using the alternative channel offerings, such as directing a new customer to an AccessPoint (bank shop) and stepping them through their first transaction.

***Technology coupled with human interaction is key to the value proposition:*** Technology has played a critical role in enabling low-cost access to financial services. Capitec illustrated how a technology-driven business model can allow for the profitable extension of financial services to the entry-level market, by simplifying both the bank's processes and services offered to customers. The Incumbent banks followed such a model by implementing innovations such as smart ATMs (cash-accepting), self-servicing kiosks and cellphone banking. However, the drive to substitute over the counter services with technological equivalents needs to be complemented with a human interaction component to ensure adoption. The banks have done this by complementing the increase in access-enabling technology with a human education component to ensure customer acceptance and usage.

***Introduction of 'one-stop-shop' to deliver full-service banking to the entry-level segment:*** The riskiness in the high-margin unsecured lending market encouraged banks to extend their other retail banking offerings to the entry-level market. Banks have introduced a comprehensive set of simple products (credit, insurance, savings and transactional) and aim to provide a one-stop-shop for full-service banking. However, not all banks have adopted the same approach. Whereas FNB and Absa have opted to achieve full service through their entry-level branches, Standard Bank and Nedbank had opted to use a complementary approach between their branches and alternative infrastructure. Nedbank has adopted a hub and spoke model that translate into them viewing alternative channels, such as kiosks and in-retailer models as complementary to, rather than substitutes for branches. This is especially true in rural areas, where low customer volumes often do not warrant the high costs

associated with setting up branches and ATMs. Examples of this include Nedbank servicing its rural customers through its in-retailer presence in Boxer stores and Standard Bank through its Access points ('bank shops' in small spaza stores).

## 6. CONSIDERATIONS GOING FORWARD

***Diversification in product offerings beyond credit is key:*** The unsecured credit market is becoming saturated<sup>4</sup>, putting pressure on the performance of many banks whose strategies still depend largely on credit; such as Capitec and African Bank. Banks are growing their non-credit offerings to the entry-level market, but effective diversification away from credit remains challenging due to lower profit margins.

***Progress in rural areas, but still underserved:*** Rural communities have low customer volumes and are more costly to serve, limiting the extension of entry-level bank branches thus far. Ubank is the only bank currently with the majority of its operations in rural areas. Ubank has branches within mining communities and only 10% of their 500 000 customer base are urban. To access this market, the Incumbents and Disruptors alike are introducing mobile offerings and identifying opportunities to partner with entities that have a rural footprint. For example, Nedbank has partnered with Boxer stores to provide accessible banking services. Absa offers CashSend, FNB offers eWallet and Nedbank offers M-Pesa with Vodacom. FNB had around 580,000 eWallet customers in June 2011, with approximately R700m funds being transferred from 2010 to 2011. The extent to which this is rural is unknown.

***Increased competition and choice:*** The study highlights the move of the Incumbent Banks towards the entry-level market, but Capitec and African Bank are also moving into the middle-income markets looking for new customers. The result will most likely be a convergence, leading to increased competition, and may improve the range and appropriateness of financial services available to banking clients in South Africa.

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<sup>4</sup> Fitch Special Report on South Africa Banks, 2013. <http://www.bdlive.co.za/economy/2013/08/02/banks-improved-earnings-not-sustainable-says-fitch>

# 1. INTRODUCTION

The banking landscape in South Africa appears to be shifting, with the traditional big banks in the country changing their physical infrastructure to include branches geared towards the entry-level market. These new branches are indicative of a change in banking strategies towards the lower-income segments, expanding their possible target market. While there is a shift from some banks to entry-level branches, niche banks have already taken up a strong position in this market with customer products and service propositions well targeted for these consumers. To gain a better understanding of this shifting landscape Cenfri on behalf of FinMark Trust commissioned Genesis-Analytic to review the landscape of entry-level branches and identify successful elements of an entry-level banking strategy in South Africa.

This report looks at the shifting entry-level banking landscape, the strategies banks are adopting to serve the entry-level market and future considerations in serving this market.

## 2. METHODOLOGY

A number of research techniques were utilised in order to investigate the nature of entry-level bank branches. Within this report, we define a branch as the physical infrastructure of the bank, and specify the definition of an entry-level branch as one that serves the entry-level market. This is determined by the size, location and products offered at the branch. We define the entry-level market as those individuals within LSM 1-6, with an associated average income up to R7,500 per month, and are formally employed in low level positions (such as miners, service workers, teachers and nurses)<sup>5</sup>, and hence earn a steady income. Our approach includes a combination of desktop research, field research (by way of structured interviews and mystery shopping exercises) and analysis thereof. Through our desktop research we were able to gather existing research on entry-level bank branches as well as the perceptions and sentiments in the market.

The field research involved team members performing mystery shopping exercises at select entry-level branches, and interviews with the appropriate representatives of the banks. The mystery shopping exercise added another dimension to our data collection with a complete, unbiased customer experience. The structured interview discussions, formulated with the aid of supporting research, were conducted with key strategic figures at six chosen banks; namely Absa, African Bank, First National Bank, Nedbank, Standard Bank and Ubank<sup>6</sup>. The intent of these interviews was to extract the opinions, understandings and motivations of industry professionals that have observed and been involved in the strategic decisions making of the entry-level bank branch models. This report provides detail on the approach to entry-level bank

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<sup>5</sup> Genesis Analytics team analysis, 2013

<sup>6</sup> Capitec was not available for an interview

branches for Standard Bank, Absa Bank, First National Bank, Nedbank, Capitec Bank, African Bank and Ubank.

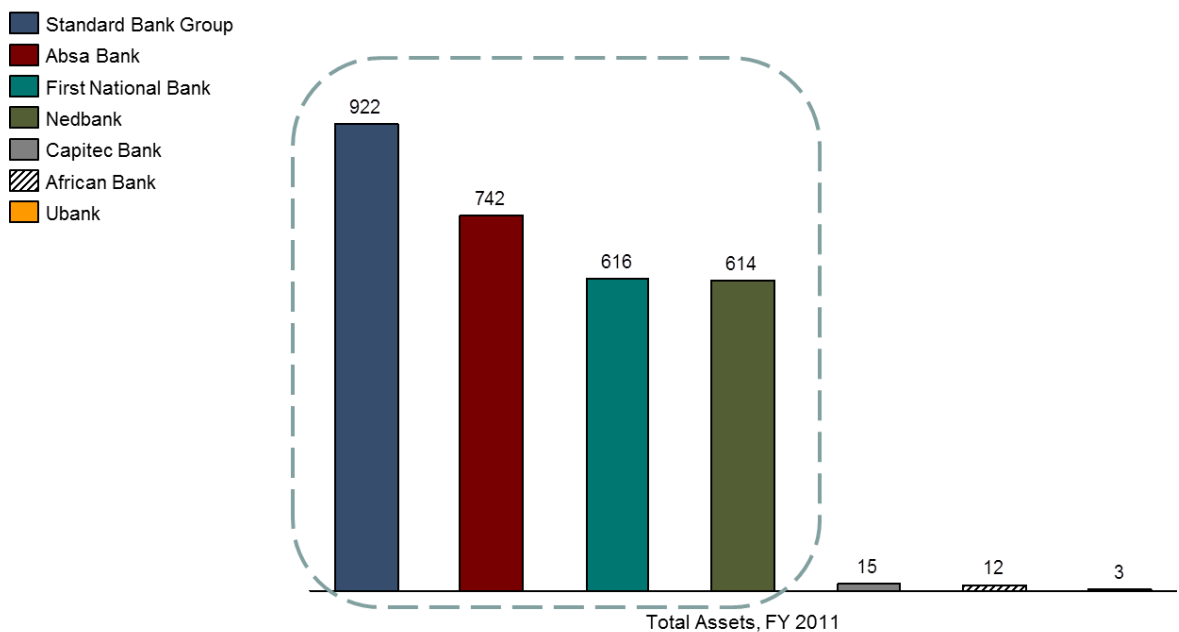
This report offers an overview of the available knowledge of entry-level branches in South Africa, based on the available public information. Where some specifics are excluded it constitutes sensitive information to the banks, however this has not impacted on the findings of our report. Estimates of senior management officers at the banks are used as theoretical benchmarks.

## 3. THE BANKING LANDSCAPE AS IT WAS

### 3.1. The Incumbents

In South Africa's banking system, the "Big Four" (Standard Bank, Absa, First National Bank and Nedbank) are established as the dominant players. Figure 5 shows that together these banks account for over 80% of South Africa's total banking assets<sup>7</sup>.

**Figure 5: Total assets of selected banks<sup>8</sup>**  
ZAR Billions, 2011



Established in 1862, Standard Bank is the largest bank in South Africa with respect to assets and market capitalisation. Standard Bank South Africa had a headline earnings of R9.5 billion and total assets to the value of R922 billion for the financial year 2011. Standard Bank employs over 28,000 employees and has more than 700 branches

<sup>7</sup> The Banking Association of South Africa, *Financial Cooperatives Indaba*, 2012

<sup>8</sup> Absa Integrated Annual Report, 2011; Standard Bank South Africa, Annual Report 2011; FNB Annual Report 2011; Nedbank Annual Report 2011.

and service centres, and around 7,000 ATMs. The bank serves a total of 9.8 million retail and business banking customers<sup>9</sup>.

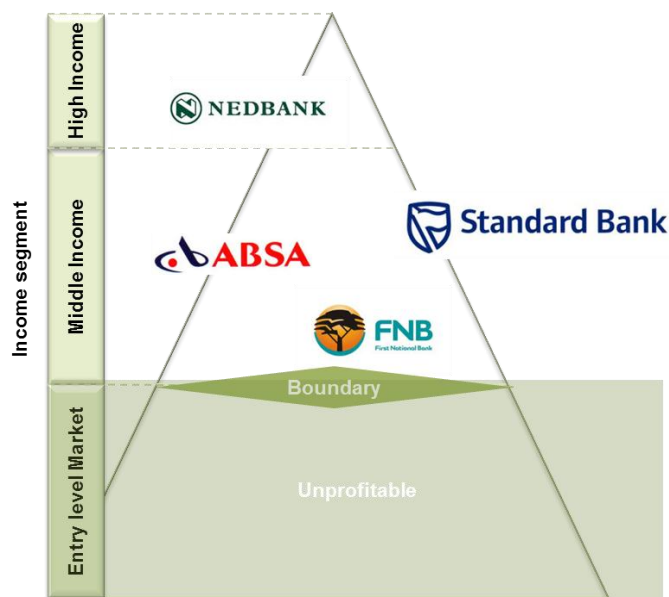
Absa Bank Ltd is the second largest bank in South Africa in terms of assets and is also South Africa's largest retail bank<sup>10</sup>. Absa serves 12 million customers with close to 1,000 outlets, and over 9,000 ATMs and other self-service terminals in 2011. It is first in the market in terms of customer base and physical infrastructure<sup>11</sup>. Absa Bank has total assets of R742 billion, with headline earnings of R4 billion in 2011<sup>12</sup>.

First National Bank was established in 1838 and is the oldest of the four banks. First National Bank South Africa has total assets to the value of R616 billion and headline earnings of R4.7 billion in the fiscal year 2011. FNB South Africa has close to 6,000 ATMs and 800 outlets/representation branches, serving around 8 million retail customers<sup>13</sup>.

Founded in 1888, Nedbank Ltd has close to 27,000 employees and around 500 branches and 2,500 ATMs in South Africa in 2011. Nedbank Limited has total assets of R614 billion, with headline earnings of R5.5 billion<sup>14</sup>. Nedbank Retail serves close to 5 million customers<sup>15</sup>.

### 3.2. The Traditional Target Market

Illustration 1: Traditional Customer Pyramid



Before the onset of democracy in South Africa, the Incumbent banks historically focused on banking the middle and upper-income groups. Bringing banking services to customers was seen as an expensive enterprise (as it required infrastructure investment), thus in order for the banks to remain profitable, they needed to target customers that would bring in sufficient revenue to cover these costs. These customers were of the middle and high-income segments, which could be targeted for non-interest income and product cross-selling (particularly large secured

<sup>9</sup> The Standard Bank of South Africa, *Annual Report*, 2011

<sup>10</sup> Absa Annual Report, 2011

<sup>11</sup> Absa Group Limited, *Annual Report*, 2011

<sup>12</sup> Absa Annual Report, 2011

<sup>13</sup> First Rand Annual Integrated Report, 2011

<sup>14</sup> Nedbank Limited Annual Report, 2011

<sup>15</sup> Nedbank Group Division Profile, 2011



debt products such as home loans), and provided adequate returns from fee and funds income to support the infrastructure of physical branches, as well as the development of electronic channels<sup>16</sup>.

The individuals who made up the low income market were not thought of as a profitable segment to target. Many in this segment were financially excluded as a legacy from the previous political system. The banks' existing service model meant low yields were earned from these low activities and low values, making it unprofitable for them to extend their infrastructure to serve this market's different transactional profile. Many of these customers lived in rural areas, which were difficult to serve for a bank given the logistics required (such as cash transportation), and generally did not represent sufficient potential revenue to warrant the construction of a branch. This dynamic meant many individuals in the country remained unbanked, with little or no access to affordable financial services.

With the changing political environment in the country since 1994, many individuals that had previously been excluded began to move into the formal economy. As such, the government began putting increasing pressure on banks to bring financial access to those who previously had none. This resulted in the Financial Sector Charter (FSC) that was brought into effect in 2004 with the purpose of driving financial inclusion and providing a globally competitive financial sector reflective of the South African demography<sup>17</sup>. This was to be achieved through providing greater availability of financial products and services to the financially underserved<sup>18</sup>. As such, the government, the Incumbents banks and Postbank launched the Mzansi account.

### 3.3. Mzansi Account

The FSC generated the Mzansi account in 2004, and it was officially launched by the banks in 2006. The Mzansi account was designed by the Incumbent banks as part of a government initiative for promoting inclusive financial products and services for the unbanked sector of the economy. The Mzansi product was aimed at LSM groups 1-5, and was intended to be both affordable and to deliver value to this segment<sup>19</sup>. The account offered customers a low cost debit card, with which customers could deposit and withdraw money, make balance enquiries, recharge cellphone airtime and make payments at POS devices.

**Illustration 2: Mzansi account cards**



Source: IOL

<sup>16</sup> Genesis Analytics team analysis, 2013

<sup>17</sup> Financial Sector Charter Council, 2013

<sup>18</sup> South African Banking Sector Overview, 2012

<sup>19</sup> Cenfri, *Insurance product standards to reach low-income consumers in South Africa*, 2011

It was believed that the complex and differing options from the competitors caused confusion and made comparison for unsophisticated consumers difficult, and as such banks would offer standardised Mzansi accounts. The banks were not allowed to compete on price, and the fees for the various transactions on the Mzansi account were the same across all the banks. However the standardisation of the product offering diminished the incentive for banks to competitively innovate within this market and restricted the banks from being able to differentiate the product and add value to the consumer.

Users of the Mzansi account were typically categorised with a high cash preference, with most of the funds in the accounts being withdrawn once-off, resulting in much less transactional activity than customers within other income segments. Utilisation, fee income and account balances were also significantly lower than similar traditional accounts of the four banks, making these Mzansi accounts unprofitable for the banks to offer and maintain. As a result, transaction fees charged by banks on the account progressively increased over time and many of the Mzansi account holders found that these accounts became too expensive. Subsequently, many of the 6 million Mzansi accounts that were initially opened became dormant, with holders moving to alternate entry-level accounts provided by banks. This yielded the opposite effect of the intended strategy behind the initiation of the account.

The Mzansi account is currently no longer marketed by the banks, while the number of existing account holders is in decline<sup>20</sup>. Customers are utilising other entry-level retail banking products affiliated with the bank at which they retained their Mzansi account (such as entry-level savings and credit products)<sup>21</sup>, where Mzansi accounts were shown to deliver less value. Other banking product innovations have developed from the Mzansi account concept, with banks creating new account offerings still aimed at the lower-income market but renamed and rebranded and exclusive to the banks (as opposed to being standardised as the Mzansi accounts were). Such products include FNB's Easy Plan initiative, Absa's Transact account, Standard Bank's Access account and Nedbank's Ke Yona account.

The failure of the Mzansi account is partly attributed to the account becoming a social responsibility rather than a profitable strategy for commercial banks<sup>22</sup>. Losses incurred by banks were a result of high origination, collection and servicing costs with a low utilisation by its account holders. The low utilisation of Mzansi accounts can partially be attributed to it being only a single product, rather than a full banking solution. Mzansi only looked at providing a low cost product, but in itself did not address the other issues faced by the entry-level market, such as ability to access bank branches, their comfort in using these branches as well their other banking needs. We see a decline in Mzansi account usage from 2010-2011, as is seen in Figure 6 below.

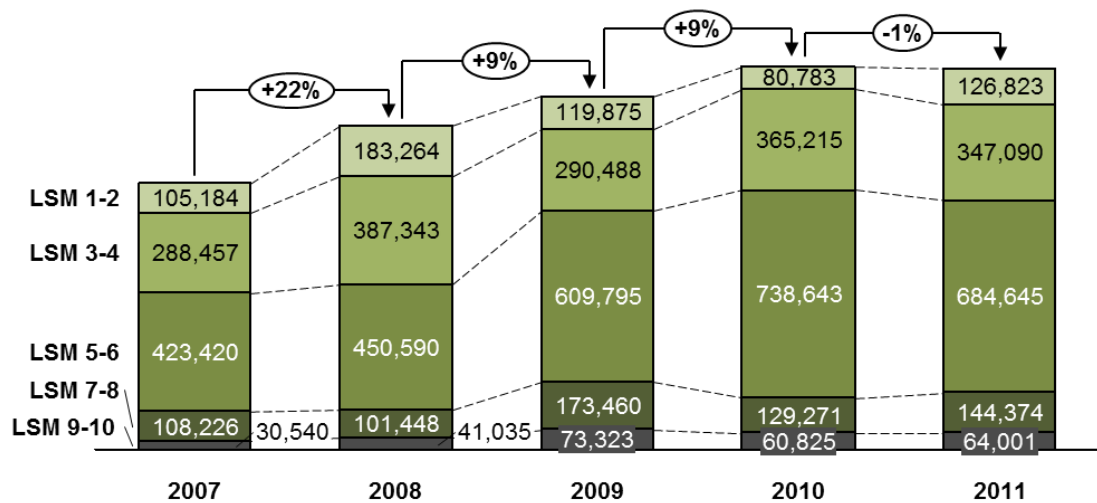
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<sup>20</sup> BASA, *Embedding Financial inclusion*, 2012

<sup>21</sup> Fin24, *Mzansi account flops*, 2010

<sup>22</sup> Mail and Guardian, *Mzansi accounts reach dead end*, 2012

**Figure 6: Mzansi account usage<sup>23</sup>**  
2007-2011



The Mzansi account also bred a sense of counterproductive discrimination in that some customers saw the account as a ‘poor person’s product’. Uptake of the Mzansi account has fallen dramatically over time with the average utilisation rates remaining flat. Some of the banks entry-level accounts that have resulted from the Mzansi account are even cheaper in fees than the Mzansi account, and offer a full service. This saw a gradual shift away from Mzansi accounts, which was predominately driven by regulatory requirements as opposed to profit potential, towards the banks’ entry-level product suite. This shift likely represents value to both the customer, who receives a more complete service offering, and the bank, which can differentiate its entry-level banking offering within the market.

#### 4. THE SHIFTING BANKING LANDSCAPE

Since the failure of Mzansi, the Incumbents have continued to adjust their models, increasing the range of their operations and their reach. Through the mystery shopping exercise as well as with the interviews with the various banks, a number of factors emerged which indicated that the banks have been adapting their operating models to reach a larger, more inclusive market. The evidence of the banking landscape changing was found around a number of aspects, including:

- A change in banks’ branches
- A change in the composition of banks physical infrastructure
- A change in the products and services offered
- A shift in promotional activities

Within each of these areas common trends between the banks were found, as well as differences in the models used by the banks.

<sup>23</sup> AMPS data, 2007-2011

While the Mzansi account provision by the big banks was driven by government initiatives, we find that the shift towards entry-level branches is a result of the economic viability of the market. We see that in general, these branches tend to be financially sustainable: where smaller premises, lower rental amounts and the removal of cash all lend to reducing the branch operation costs. The smaller fee revenue values are compensated by higher volumes of customers.

#### 4.1. The New Target Market

The Incumbents continue to enjoy the largest share of the overall market in South Africa supported by the largest infrastructural network. However, over the last number of years we have seen a broadening of these banks' target market. Competition amongst these banks in the low-income segment has intensified as banks shift their target down-market. While the banks still compete aggressively for the upper and middle-income segments, there has been an increase in the amount of focus placed on the lower-income, or entry-level market segment. Banks shifting more of their focus down market can be attributed to both the high saturation in the middle to upper-income segments, and to the recognition of a large potential market within the lower-income segments.

**Figure 7: Proportion banked per LSM group** <sup>24</sup>  
2004-2011

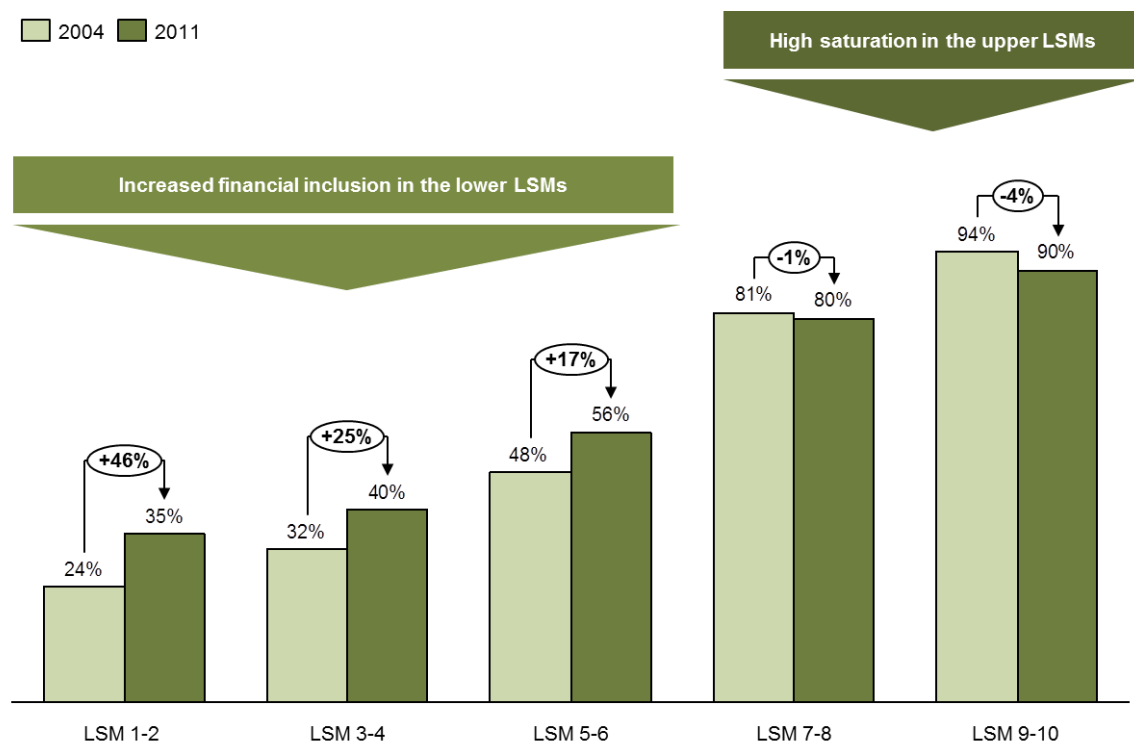


Figure 7 shows that the middle-to upper-income market is saturated in terms of banking product take-up, thus profit potential for the banks is limited to their ability to

<sup>24</sup> Finscope data, 2004-2011

take market share from competitors. In the lower-income market, banks see the opportunity to capture new, previously unbanked customers, driving up customer growth and revenues. In addition, the potential for higher margins on personal loans, given the enhanced risk profile of the lower-income market, was a compelling factor drawing the Incumbent banks to the lower-income market.

We define the entry-level target market as individuals earning up to R7500 p.m. (as is consistent with the banks' definition of the entry-level customer segment). This translates to those individuals who fall into LSM 1-6, which Figure 8 shows constitutes 65% of the total population.

**Figure 8: Proportion of population per LSM group<sup>25</sup>**  
*Adults, 2012*

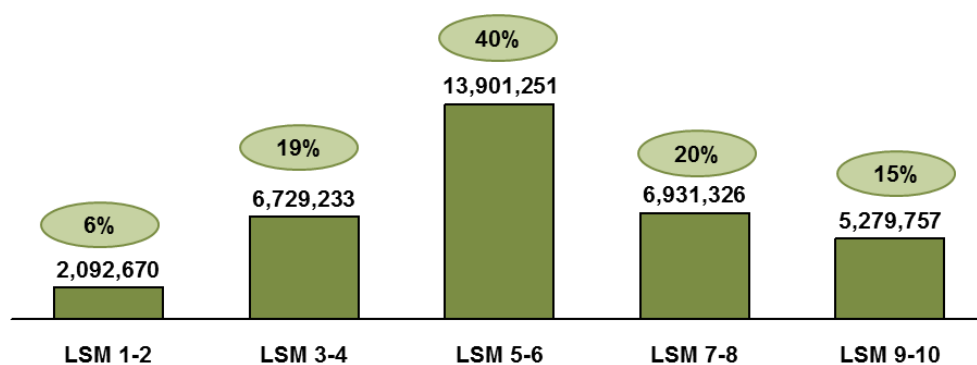


Figure 9 below shows that the lower-income market does however have a largely different transactional profile to that of the traditional market where both transaction values and volumes tend to be smaller.

<sup>25</sup> AMPS data, 2012

**Figure 9: Financial channel usage by LSM group** <sup>26</sup>  
*Adults, % usage, 2012*

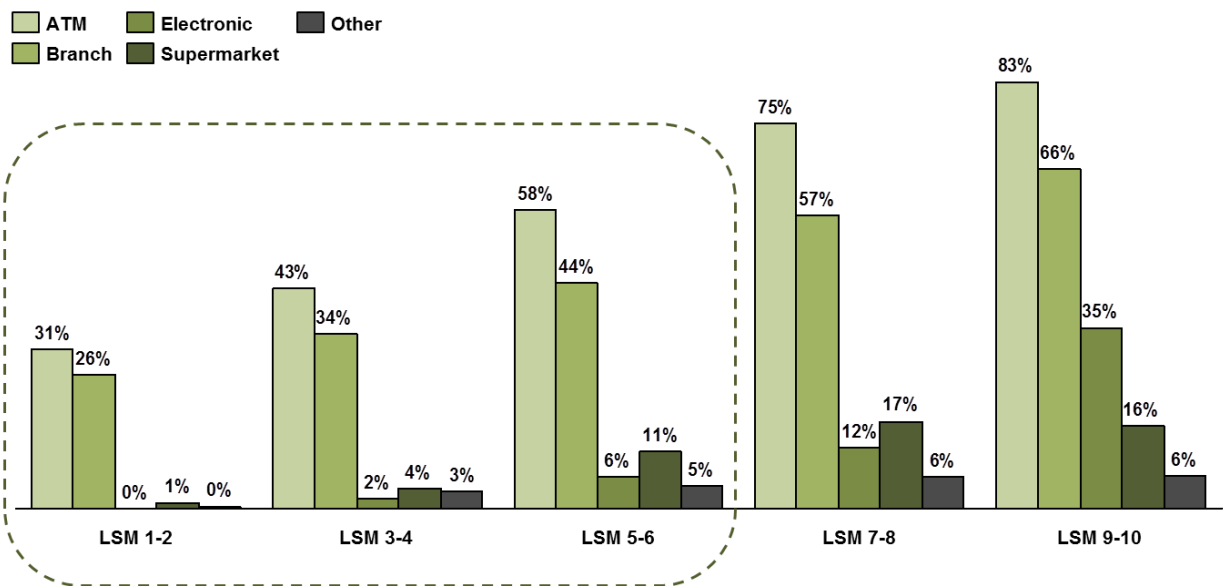


Figure 9 shows that within the lower LSMs, there is a much stronger prevalence towards using either an ATM or a branch, with very low usage of electronic channels (cellphone and internet banking) in comparison to the higher LSM groups. If the Incumbents were to reach the lower end of the market, they would need to focus on branches and ATMs. However within the lower-income customer segment, the cost to serve generally outweighs potential revenues given low transaction values and volumes. Hence, in order to effectively serve the lower-income market, lower cost branch models would need to be developed.

The cost to serve with branches is a challenge and there is a need to convert over the counter services with technological equivalents. The lack of understanding and familiarity amongst the entry-level market segment with electronic distribution channels requires an educational component to support their adoption. Several of the Incumbent banks have already adopted this strategy: complementing access-enabling technology with educational support provided in lower cost branches. The next section builds upon this with its exploration into how banks are effectively changing their branch layouts and physical infrastructure to lower cost models, and attracting new customers within the entry-level market.

## 4.2. Changing Bank Branches

Each of the Incumbents has over the last few years developed a strategy of deploying branches which have lower costs to operate. These branches are often referred to as low cost branches or entry-level branches and are serving an increasingly important role in the banks' segment strategies, as well as increasing financial access within

<sup>26</sup> *Ibid*

South Africa. These branches are differentiated from traditional branches by a range of characteristics, including the cost to set up and operate, the location of the branches, and the products and services offered within the branches.

A primary aim of an entry-level bank branch is to have significantly lower capital expenditure (capex) and operating expenditure (opex) than a traditional bank branch. One way for banks to decrease their capital cost is to reduce the size of the branches. Typically, the size of an entry-level bank branch lies within the range of 50 square meters to 100 square meters (a structure less than 50 square meters would be defined as a kiosk). These smaller branches also increase the flexibility banks have, as location requirements are no longer dictated by available rental space.

A balancing act emerges, and banks must guard against building a branch that is too big and expensive or too small and unprofitable. Most of the banks interviewed indicated that they assess the stand-alone economic viability of a branch, meaning that if a branch is unprofitable, it would inevitably be shut down. Along with the size, banks have also reconsidered the features (such as the furnishings) inside the branches, often making them cheaper and simpler. The average cost of building a traditional branch can be close to R6 million, depending on the aesthetics of the location of the branch. Branches that are and positioned in more affluent areas (e.g. Sandton and Melrose) can cost up to R8 million on average, and can be as high as R25 million. However, an entry-level bank branch can cost as little as R1.5 million to build depending on the size of the branch.

While reducing the size of branches has a significant impact on the affordability of the branch, the biggest cost savings comes from removing the cash from the branches, as this contributes up to between 30% - 50% of the branch costs. Removing the cash lowers the initial capex cost of the branch as the branch does not need to be fitted with bullet proof glass, security doors and other measures which are both expensive, and also increases the space required to build a branch. Along with the reduction in capex costs, the removal of cash reduces the opex costs significantly by avoiding the cash management fees and insurance costs. Furthermore, there are lower staffing costs as the bank does not need to employ tellers to handle over-the-counter transactions.

Often these entry-level branches, rather than handle cash, include self-service devices in the branch which can take cash deposits and in some cases can be used to make transfers. In many instances these devices are overseen by a staff member who is trained to explain the device to customers who are less technologically adept. Often staff who are chosen to explain the device are required to speak the local language in order to ensure the customers are comfortable when using it.

In entry-level branches the banks have reconsidered the amount of staff required branch and the responsibilities of staff members. Staff representatives in the entry-level bank branches are generally required to expedite quick service around a limited number of products (4 or 5 products on average). Though they may have some basic knowledge and training on some basic financial products, they are not required to

have extensive knowledge on the many products offered in traditional bank branches. This reduces the time and cost required to train the staff. Most of the entry-level bank branches make use of staff members with lower qualifications than of staff in traditional branches (often with a minimum of a matric qualification), as this translates to a lower cost for operating the branch. The remuneration structure of staff in entry-level bank branches (with the exception of the branch manager/supervisor) is generally that the staff receive a low fixed basic and a high variable commission based portion in their remuneration package (where in traditional branches staff are generally remunerated through a higher fixed basic as opposed to commission) which translates to lower fixed staffing costs to the banks. This different staff remuneration structure is adopted by the banks as it works as an effective incentive for staff to actively pursue sales. This is important where revenue in entry-level branches is substantiated through new sales. Some banks use the converse model where the remuneration structure includes a major fixed portion and a minor variable portion, dependent on whether they are constrained to adhering to a consistent remuneration structure across all branch types.

On average, there are usually five bank staff members and a branch manager servicing customers in an entry-level branch. Some staff members go out and seek potential customers as opposed to relying on the “feet through the door”. Permanently positioned members in the branch often include the branch manager and the service consultants who facilitate ATM transactions by customers at the branch.

In these entry-level branches there is also a large emphasis placed on the education of the customers using the branch. It is important for both the customer and bank to spend the required time and attention to ensure that a customer understands the product he is purchasing or the service he is making use of. Within customer interaction at the entry-level branch, face-to-face communication is a significant component of account procurement, problem resolution and customer education. This face-to-face component sanctions a service dimension that cannot be delivered by virtual banking facilities and applications. Demographically, the lower-income segment is for the most part made up of consumers who possess a lower level of education, in which case face-to-face interaction is essential in the description of products sold to customers as well as their associated ramifications (especially if this takes place in the customer’s home language).

Most of the banks researched have embarked on various customer education initiatives in their entry-level branches through face-face interaction, such as on-boarding of a new customer to ensure they understand the product suite available, or through promotional campaigns, such as prize giving associated with product explanations. One such common initiative by some of the banks includes community drives, with workshops held in the town halls of selected communities, with the aim of educating customers.



## 4.3. Changing Composition Of Banks' Physical Infrastructure

### 4.3.1. The Incumbents' Entry-level branch models

Entry-level branches have been rolled out in a large scale by the incumbent banks as they look to focus more on the low-income segment of the market. Along with these branches the banks are also making use of further channel options to reach the segment, such as mobile service offerings and direct sales agents. Evidence of the shift in banks' physical infrastructure is apparent in all of the Incumbents.

#### **Absa**

Absa is the leader in South Africa in terms of footprint, as it accounts for 37% of the all physical infrastructure (branches and ATMs)<sup>27</sup>.

Absa segments its branches into<sup>28</sup>:

- Affordable branches (including 1234 branches and loan centres) for entry-level customers;
- Transactional branches for mainstream customers; and
- Exclusive branches for the upper-end market.

Figure 10 shows the growth in Absa's physical infrastructure and indicates that Absa has seen steady growth in access points, especially entry level branches, with the number of Absa 1234 branches doubling from 2010 to 2011.

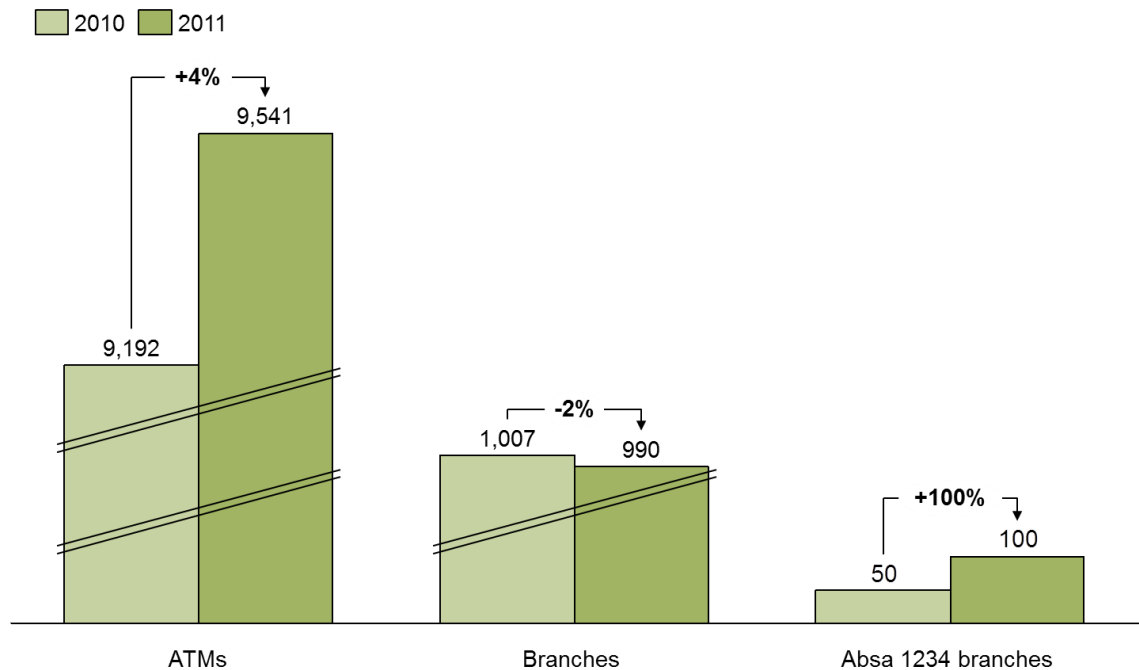
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<sup>27</sup> Genesis Analytics team analysis, 2012

<sup>28</sup> Absa Group Limited, *Integrated Annual Report*, 2011

**Figure 10: Absa's Physical Infrastructure<sup>29</sup>**

2010-2011



Absa decides how to locate these variant branches through a differentiated geographical zone approach. Within each zone different types of branches are set-up to serve the total customer base. Absa performs both internal analysis, looking at their existing customer base, and external analysis, determining their potential customer base, when deciding where to locate a branch. Generally, within a zone, Absa would locate both a traditional transactional branch and an entry-level branch, such that all customer segments within that zone are served. Absa looks to ensure that these zones are economically viable, such that there may be cross-subsidisation across branches within a specified zone.

Absa has also seen consistent growth of around 27% in entry-level customers, from a base of 7.2 million customers in 2010 to 7.4 million customers in 2011<sup>30</sup>. Absa notes that while all of the branches are geared towards service provision, its entry-level branches are strongly sales orientated.

<sup>29</sup> Absa Integrated Annual Report, 2011

<sup>30</sup> *Ibid*

Absa's 1234 branches are cashless and all are equipped with cash-accepting ATMs. There is a strong customer education component within these branches, which have dedicated 'educational zones'. This zone set has a touch-screen device whereby customers can obtain information on the product suite and how to transact. Further, there are also personnel that are situated in the branch to assist customers in using technology (such as the self-service devices and the ATMs), labeled 'educator migrators'. These branches offer Absa's trademark entry-level products, including a transactional account, a saving account, a loan and an investment product. The branch name stems from the simplified product offering, including; one transactional account (the Transact Debit account), two savings accounts (the MoneyBuilder and 32 Notice Deposit), three loan options (Personal loan, Micro loan and the Express loan) and four insurance options, which are four variations of a funeral Plan option<sup>31</sup>.

**Illustration 3: Absa's educational zone**



Source: Genesis Analytics team, 2013

Absa also serves the entry-level customer base at 'Affordable branches' and personal loan centres. Affordable branches are full service offering branches that deal with cash-handling, offer comprehensive customer service, and include a strong customer education element. This entails sales agents undertaking an extensive 'on-boarding' process, whereby customers are fully equipped with the necessary information when taking out new products. Absa's personal loan centres specifically focus on the sale of personal loans, with limited customer service and no cash-handling.

In order to motivate customers to migrate to more economical electronic channels, Absa has located a cash accepting ATM, a standard ATM and a self-service device (where customers can use the self-service to obtain statements, check balances and transfer money) within each branch. These are generally located within the branch to ensure customer safety when making use of the machines. By using an 'educator migrator' to educate customers in how to use the machines, Absa has seen consistent growth in usage and acceptance of this technology<sup>32</sup>.

Absa ensures that despite specific branches designed for entry-level customers all branches are enabled to service these customers. This occurs where staff will identify entry-level customers within a traditional branch and adopt the same on-boarding process that would occur within an entry-level branch. Further, Absa has carved out space in some of their traditional branches to increase Absa 1234 visibility and to serve the entry-level segment within this space<sup>33</sup>.

To further access to the entry-level market, Absa has rolled out an extensive Workplace banking programme, where Absa makes arrangements with an employer to offer financial services to the employee base. Absa also has direct sales agents

<sup>31</sup> Mystery Shopping exercise undertaken by the Genesis Analytics team, 2013

<sup>32</sup> Interview with Mike Bruwer (and team), Absa Sales and Service Distribution Type Specialist, 2013

<sup>33</sup> *Ibid*

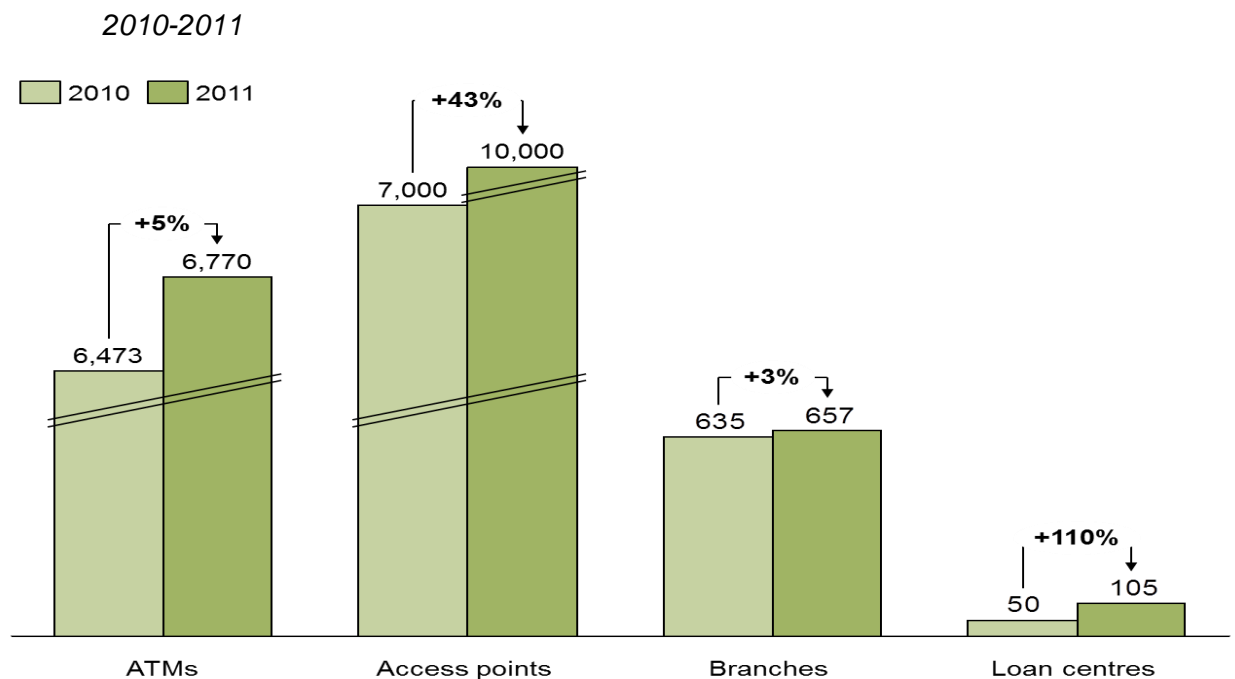
which go into communities to open new accounts (making use of tablet devices), and issue cards to customers. Further, Absa ensures cash access through more than 1,000 POS devices located within a wide-range of retailers, which provides a point of presence in areas which would have otherwise not been economically viable (such as deep rural areas)<sup>34</sup>.

Absa offers a mobile money transfer service called CashSend, whereby customers can transfer money using a cellphone, internet banking or an ATM. These funds can be accessed by a non-banked individual through an Absa ATM using their reference code. Absa is also linked to Western Union to facilitate remittances, which are offered within the entry-level branches. Western Union has a strong rural presence, hence the relationship has served to increase Absa's rural footprint. This service is most frequently used by migrant workers transferring funds across borders<sup>35</sup>.

### Standard Bank

Standard Bank's physical infrastructure share is second in the market, with 27% of South Africa's total number of all branches and ATMs<sup>36</sup>. In recent years, Standard Bank has shown immense growth in its entry-level offering, with a 43% increase in access points and a doubling in the loan centres, reflected in Figure 11 below.

**Figure 11: Standard Bank's Physical Infrastructure** <sup>37</sup>



Standard Bank established its Inclusive Banking unit in 2010, with the objective to deliver affordable banking to the entry-level market through access points in community retailers, loan centres and mobile banking. In 2011, Standard Bank acquired more than 1.3 million new customers in the entry-level market, bringing the

<sup>34</sup> Interview with Mike Bruwer (and team), Absa Sales and Service Distribution Type Specialist, 2013

<sup>35</sup> CityPress, *Western Union clinch a deal with Absa*, 2000

<sup>36</sup> Genesis Analytics team analysis, 2013

<sup>37</sup> Standard Bank South Africa annual reports, 2010-2011

total to around 5.4 million entry-level customers in 2011. This accounts for around 59% of Standard Bank's overall personal banking customer base<sup>38</sup>.

Standard Bank's entry-level distribution strategy comprises of Access Banking centres (previously Loan Centres), AccessPoints and Access agents. Standard Bank's loan centres were launched in 2010 and only sold personal loans, offering no transactability or cash-holdings. These are primarily located near branches and ATMs such that customers can still receive a full service, but with the primary objective of selling personal loans. Standard Bank is looking to provide further products and services within these loan centres, to enable transactional product sales alongside loans, and more importantly providing a full-service to customers.

These branches are now being relabeled as Access Banking centres, looking to offer customers more banking products. Unlike other banks' entry level branch models, these branches will accept cash deposits, however through a drop-box facility (where staff have no access to cash). These branches are set to offer a complete product offering, including transactional accounts, savings accounts (including group savings accounts), credit cards, loans (including Affordable Housing home loans) and insurance products. Within these Access Banking centres, Standard Bank is currently migrating all E-Plan, Mzansi accounts and Value accounts to Access accounts, to offer a more harmonized product offering.

Standard Bank's AccessPoints, or 'bank shops', are the cornerstone of Standard Bank's low-cost service delivery to the entry-level market. Customers can perform basic transactions within these bank shops, where the merchant makes use of a POS device to facilitate cash-in and cash-out (where limit amounts are set by the merchant). Customers can also perform cash transfers and balance enquiries. The cash transfer service is linked to Standard Bank's mobile service offering, where customers can transfer cash to another individual via a mobile phone (which can be performed at the AccessPoint), and that individuals can access the cash using the PIN, at any AccessPoint or Standard Bank ATM. Finally, customers can purchase airtime and electricity at AccessPoints.

Given that these AccessPoints represent no major set-up costs to the bank, Standard Bank is able to set-up AccessPoints in close proximity to the entry-level market, for example, at a spaza shop within a township area. Standard Bank does, however, invest in training the merchants in facilitating the transactions, which ensures that customers have a human touch point when transacting at AccessPoints. Further, since merchants are generally community members, this entrenches the sense of trust between the customer and the merchant. These AccessPoints provide a viable alternative where an ATM would have been unfeasible to operate (owing to heightened servicing costs and security risks)<sup>39</sup>.

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<sup>38</sup> Standard Bank South Africa, *Annual Report*, 2011

<sup>39</sup> Interview with Carolina Reddy: Head of Distribution Planning, Inclusive Banking; Marius de la Rey, Channel Development Director, Standard Bank, 2013

Customer usage of AccessPoints has seen tremendous growth recently, as community buy-in increases. Standard Bank has recently launched an Above the Line marketing campaign to increase awareness of AccessPoints within the entry-level market.

**Illustration 4: Standard Bank AccessPoint:**



*Source: Business for Development, 2012*

Access agents are sales personnel who are directly recruited from the community in which they operate and are positioned at gazebos to sell the full Access account product suite. Access agents are enabled through the use of mobile phones that take photos of the customers personal documents and send them straight through to the processing back-office. Account activation and card-issuing are immediate. Standard Bank currently has 1200 Access agents in operation.

Access agents are also tasked with on-boarding new customers in using the alternative channel offerings, such as directing a new customer to an AccessPoint and stepping them through their first transaction. Access agents also register customers for online banking and enable customers to make use of Standard Bank's USSD string whereby customers can check their loan qualification.

Standard Bank's vision for entry-level customers is a system in which customers are originated by an Access agent within their community, where they can perform basic transactions at an AccessPoint or at an ATM, and they receive all other services they may require through an Access Banking centre.

Standard Bank notes that the traditional branches continue to serve a large proportion of the entry-level market. It adopts a monolithic brand strategy that depicts all branches with the same visual representation (irrespective of intended target market)<sup>40</sup>. Standard Bank has looked to adjust these traditional branches that predominately serve the entry-level segment, by offering extended trading hours, and

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<sup>40</sup> Interview with Carolina Reddy: Head of Distribution Planning, Inclusive Banking; Marius de la Rey, Channel Development Director, Standard Bank, 2013

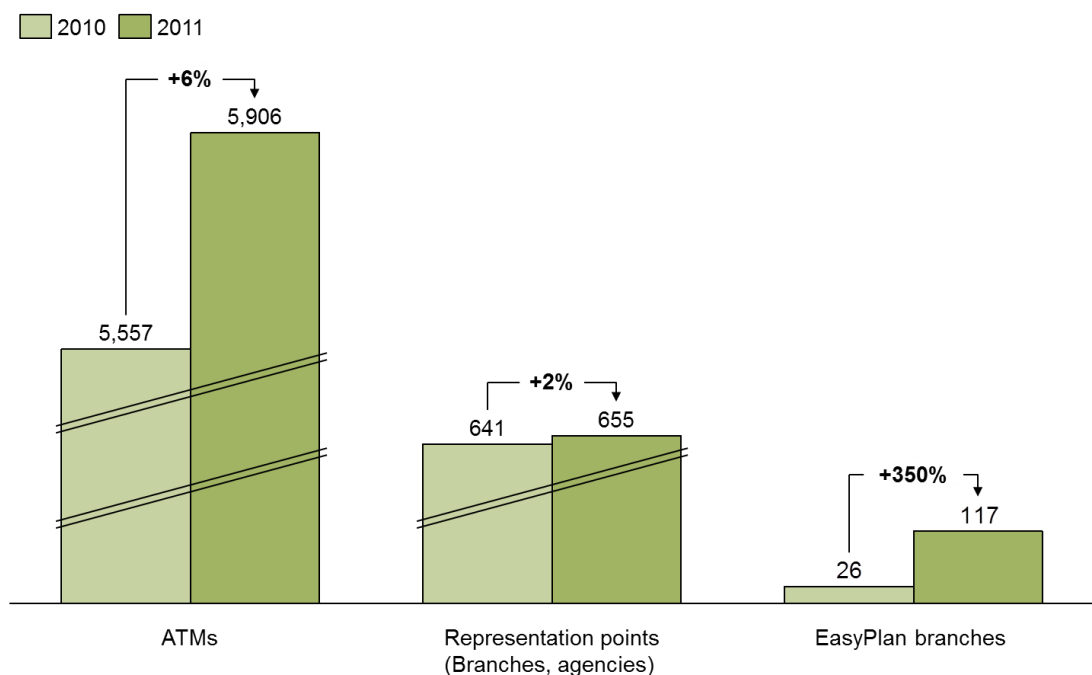
by ensuring that staff within these branches are fully-equipped to serve the entry-level customer segment<sup>41</sup>.

### First National Bank (FNB)

First National Bank's share of physical infrastructure in South Africa is around 19%<sup>42</sup>. It lags behind Absa and Standard Bank, despite being one of South Africa's most mature banks. While FNB has remained slow in increasing the size of its traditional branch footprint, Figure 12 shows there has been significant growth in EasyPlan branches:

**Figure 12: FNB's Physical Infrastructure**<sup>43</sup>

2010-2011



FNB rolled out its EasyPlan branches in 2009, to sell their Smart Solutions, which are aimed at customers earning between R0 to R100, 000 annually. FNB services around 130,000 customers per month within these EasyPlan branches<sup>44</sup>, where its total entry-level customer base is around 4 million<sup>45</sup>. FNB has one of the most clearly defined entry-level branch models, whereby the EasyPlan products are only sold in EasyPlan branches, and lower fees are charged to EasyPlan customers transacting in an EasyPlan branch.

As mentioned, the largest driver in cost reduction is making a branch cashless. FNB was the first to market with cash-accepting ATMs (or auto-deposit ATMs) in 2008<sup>46</sup>.

<sup>41</sup> Interview with Carolina Reddy: Head of Distribution Planning, Inclusive Banking; Marius de la Rey, Channel Development Director, Standard Bank, 2013

<sup>42</sup> Genesis Analytics team analysis, 2012

<sup>43</sup> FNB Annual Report, 2010-2011

<sup>44</sup> FNB Report to Society, 2011

<sup>45</sup> MoneyWeb, *Capitec made FNB rethink its model*, 2011

<sup>46</sup> ATM Marketplace, *SA banks embrace auto-deposit ATMs*, 2013

This enabled FNB to remove cash within EasyPlan branches, by locating a cash-accepting ATM outside of every branch. Critically, FNB has ensured customer acceptance by putting a staff member next to the cash-accepting ATM to assist customers in making deposits<sup>47</sup>. This is imperative where customers may otherwise have been reluctant to make use of the cash-accepting ATMs due to lack of understanding and trust in the technology. The drive to substitute over the counter branch cash deposits and withdrawals with the ATM equivalent benefits both customers, who are charged lower fees, and the banks, who have lower cost to serve.

FNB's EasyPlan branches are in general much smaller than traditional branches, with minimized fittings. The lack of cash in branches saves on staffing costs, insurance and related security expenses. FNB's delivery of convenience to the low-income segment is supplemented through extended trading hours during 'high-demand' periods from the 25th to the 1st of each month (when a large proportion of the customer segment are paid salaries).

FNB employs a mobile offering called the eWallet, where an FNB bank account holder can send money to anyone with a mobile phone. The recipient (who does not need a bank account) can withdraw the cash at any FNB ATM. The sender gets charged a transaction fee but the recipient does not have to pay to get the cash<sup>48</sup>. FNB had 580,000 eWallet customers in June 2011, with around R700 million in funds being transferred from 2010 to 2011<sup>49</sup>.

FNB's approach is to have all sales agents (excluding the branch manager) working at an EasyPlan branch to be fully mobile. Staff are paid on a commission basis, and are encouraged to go out and attract new customers into the branches, rather than rely on walk-ins. This empowers sales agents to take their own initiative in attracting customers, creates a competitive sales environment, and ensures that sales agents work at full capacity to push sales and customer growth<sup>50</sup>.

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<sup>47</sup> Interview with Gift Manyanga, FNB EasyPlan CEO, 2013

<sup>48</sup> MoneyWeb, *Capitec made FNB rethink its model*, 2011

<sup>49</sup> First National Bank, *FNB's Report to Society*, 2011

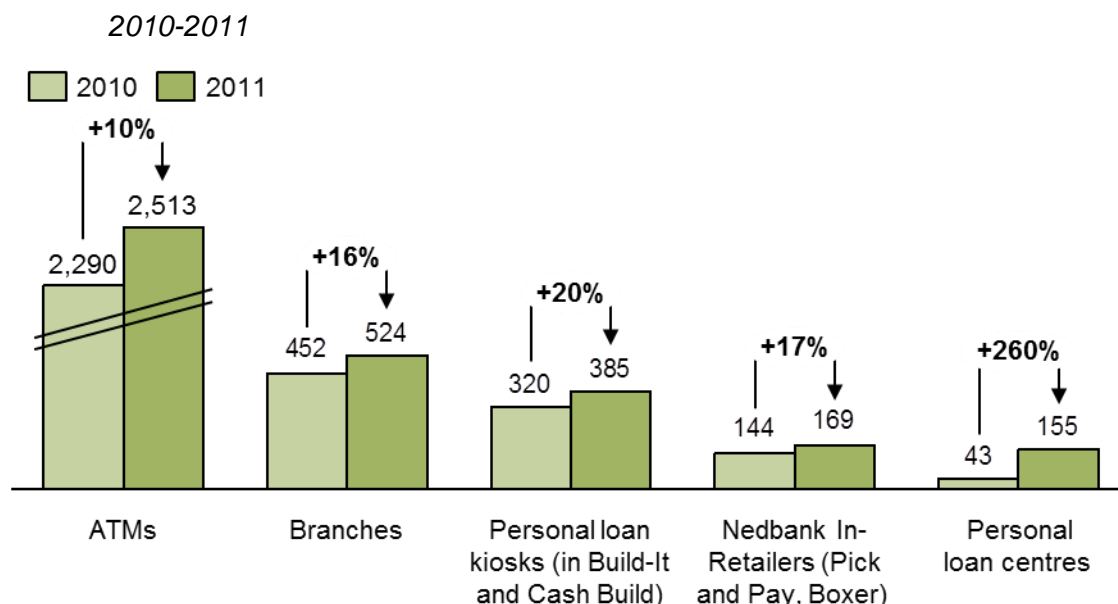
<sup>50</sup> Interview with Gift Manyanga, FNB EasyPlan CEO, 2013



## Nedbank

Overall, Nedbank's share of physical infrastructure in the banking sector is around 10%<sup>51</sup>, the lowest of the Incumbents. Nedbank has however been growing its physical infrastructure on all of its access points, as is reflected in Figure 13.

**Figure 13: Nedbank's Physical Infrastructure** <sup>52</sup>



While Nedbank is growing its entire infrastructure, the fastest growth is in alternative channel models, such as the in-retailers (Pick n Pay and Boxer stores), where Nedbank provides access to financial services (such as account openings and cash-in/cash-outs) within a carved out space in retailers. This is indicative that Nedbank is expanding its channels to meet the needs of entry-level customer segment.

Nedbank's channel approach is differentiated along customer segment lines, yet with parallel channel offerings. To serve the middle and upper-income markets, Nedbank has traditional branches, ATMs and in-retailer access points in Pick n Pay. To serve the lower-income segment, Nedbank has Personal loan centres, ATMs, personal loan kiosks and access points in Boxer stores. Through these channel offerings Nedbank serves around 3 million customers in the entry-level market<sup>53</sup>.

Nedbank has adopted a 'hub and spoke' approach to deliver the full service requirements of the customers. This translates into Nedbank viewing alternative channels, such as kiosks and in-retailers as complementary to, rather than substitutes for branches. Hence Nedbank will have a branch, a personal loan centre and an in-store outlet all located in close proximity to serve the local micro-market<sup>54</sup>. This 'hub and spoke' model is displayed as follows:

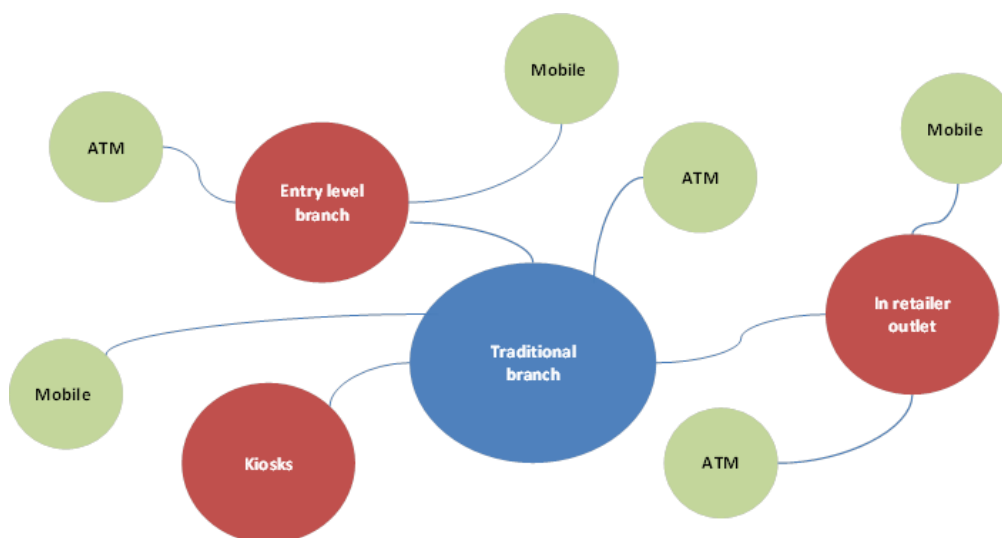
<sup>51</sup> Genesis Analytics team analysis, 2012

<sup>52</sup> UBS, *Charting a new path to sustainable, profitable growth for Nedbank Retail*, 2011

<sup>53</sup> *Ibid*

<sup>54</sup> Interview with Brian Duguid and Werner Terblanche; *Integrated Channels*, Nedbank, 2013

### Illustration 5: Nedbank's hub and spoke model



Source: Interview with Nedbank

Nedbank's Traditional and Lite branches are aimed at servicing Nedbank's full range of customers, including personal and corporate clients. As such, these branches perform cash-handling, have greater spatial requirements, and more sophisticated furnishings<sup>55</sup>.

Personal loan centres are what would be defined as Nedbank's entry-level branches. These branches are located in areas with high foot traffic, and are staffed mainly by loan consultants (with 1 banker to deal with transactions to every 3 loan consultants). These loan centres have much lower spatial requirements and are equipped with basic furnishings<sup>5</sup>. These are to be redesigned and relabeled as 'Entry-level branches', in-line with Nedbank's shift to offering a full-service transactional package to the entry-level segment<sup>56</sup>.

Nedbank's in-retailer outlets are generally between 12-30 square metres with operating hours from 08h00 to 18h00<sup>57</sup>, where customers can interact with 1 or 2 sales agents<sup>58</sup>. These outlets are focused on customer acquisition and sales. Personal loan kiosks, situated in Build-It and Cash-Build stores, are carve-outs within the hardware stores, where customers can access Nedbank Personal loans to spend on building materials within the store.

ATMs play an important complementary role to both the Personal Loan centres and to the in-retailer outlets, as they provide the means for a customer to access cash within the entry-level business model. Currently, around 50-60% of the personal loan centres have ATMs located externally, but these ATMs are not cash accepting. Nedbank is in the process of rolling out more of their cash accepting ATMs<sup>59</sup>.

<sup>55</sup> Mystery shopping exercise undertaken by the Genesis Analytics team, 2013

<sup>56</sup> Interview with Brian Duguid and Werner Terblanche; Integrated Channels, Nedbank, 2013

<sup>57</sup> Nedbank press release, 2009

<sup>58</sup> Interview with Brian Duguid and Werner Terblanche; Integrated Channels, Nedbank, 2013

<sup>59</sup> *Ibid*

Within the mobile money space, Nedbank offers M-Pesa, which allows for cash transfers using a cellphone. Nedbank partnered with Vodacom and launched M-Pesa in 2010. Customers can access and send funds without having a Nedbank bank account (although you need to be a Vodacom customer to transfer funds) at any M-Pesa outlets, which include stores, spaza shops, community service containers or a Nedbank ATM<sup>60</sup>.

Nedbank's original strategy in catering for the low-income market through their personal loan centres resulted in the bank securing around 13% market share in personal loans, after African Bank with 31% and Absa with 16%<sup>61</sup>. Nedbank has, however, begun to shift away from the focus on personal loans to a full product offering suite, and are looking to convert the existing infrastructure of the personal loan centres into transactional branches. Around 35% of existing personal loan centres in 2011 offered transactional banking, which will increase into the future. Nedbank is also shifting away from the labeling of personal loan centres, which are to be relabeled as entry-level branches<sup>62</sup>.

Nedbank differentiates Entry-level branches from traditional branches in terms of staffing requirements, product offerings, size and location and the handling of cash. Although these branches will continue to sell personal loans, the focus will be on offering Nedbank's entry-level transactional account, the Ke Yona account. This is a bundled transactional account, with an embedded funeral plan and access to the Vodacom M-Pesa mobile cash transfer service. Customers can also take a Pay as You Transact account called the Transactor Plus<sup>63</sup>.

### 4.3.2. Branch Placement

Part of the change of the banks infrastructure was a rethinking of the placement of branches. The Incumbent banks are now bringing their branches to the entry-level customer segment, by locating branches in high footfall areas. Careful thought and planning is given to each decision of where to place a branch based on a number of factors common amongst all the banks.

The factors which banks look at include the foot traffic in the area, the presence of competitors and retailers, patterns of urbanisation and government investment. Branch placement is carefully planned throughout, and banks may even place branches a block apart to capture different foot-flow patterns (such as the case of FNB EasyPlan branches located in Johannesburg CBD). These influences on branch placement are factors considered by all the banks and, as such, have often resulted in a high congestion of different banks' branches close together. The branches are also frequently competing with micro lenders in the area. This competition for space by the banks is intensified by the desire for banks to maintain a presence near their competitors, which may lead to a branch being opened for strategic reasons.

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<sup>60</sup> Fin24, *Vodacom and Nedbank launch M-Pesa*, 2010

<sup>61</sup> UBS, *Charting a new path to sustainable, profitable growth for Nedbank Retail*, 2011

<sup>62</sup> Interview with Brian Duguid and Werner Terblanche; *Integrated Channels*, Nedbank, 2013

<sup>63</sup> Mystery shopping exercise undertaken by the Genesis Analytics team, 2013

The strategy for banks with regards to where they place their entry-level branches in comparison to their traditional branches differs from bank to bank based on the branch models employed. Banks look at a combination of cost, geographic representation and economic viability of the market. FNB build their EasyPlan branches to provide a full service to the clients in this segment and as such may close down traditional branches within the same area. Alternatively Nedbank's hub and spoke strategy would be less likely to lead to branch closure as all service points are needed in close enough proximity to a traditional branch to ensure maximum client service and convenience<sup>64</sup>.

The issue of bringing banking to rural areas of South Africa is an important facet of financial access for low-income groups. Banks have been hesitant to bring services and branches to rural areas due to the small return on the large required investment. Small towns have relatively low population, with few middle and upper-income individuals. Traditional branch models would struggle to be sustainable with low volumes being unable to cover the costs of these branches. The emergence of entry-level branches brings with it the prospect of banks being more willing to have a significant presence in rural areas. Although the banks have started to establish more entry-level branches in rural areas, this is to a lesser degree than in urban areas, mainly as a function of the low volumes of customers (as high volumes are required to offset lower revenue streams). Rural branches impose greater challenges to the banks, such as the increased cash delivery costs and difficulties in sourcing adequate staff.

Instead of opening low-cost branches in all rural locations, banks are diversifying their channel offering into these areas to increase their access. Nedbank has a large presence in Boxer stores to increase its footprint in the rural areas, and most banks are increasingly making use of mobile offerings and small kiosks to bring banking to those in the rural areas.

#### 4.4. CHANGING PRODUCTS AND SERVICES

**Illustration 6: Absa's Product suite**



Source: Absa marketing pamphlets, 2013

Adjusting the strategy of where to place branches to reach customers was not all the incumbents did in providing an improved value proposition for the entry-level market. Understanding what products these customers need is vital in order to ensure that once they have entered the newly placed branches, they become and remain satisfied customers of the bank.

The Incumbents, in considering their product offerings, needed to avoid the situation that had arisen from the Mzansi accounts: a large

<sup>64</sup> Interview with Brian Duguid and Werner Terblanche; Integrated Channels, Nedbank, 2013

number of dormant accounts running at a loss for the banks. Along with this consideration, the customer value proposition had to be carefully considered, as while these were entry-level customers there should be no implication that they are low value customers.

The number of products accessible in entry-level bank branches is often smaller in number and simpler in comparison to the products offered in traditional branches. The four key products typically found in an entry-level branch (in one variation or another) include: a credit product, a transactional product, a savings product and an insurance product (almost exclusively a Funeral Plan). Absa's 1234 branches illustrate this perfectly, as the branches are named after the four products offered.

Nedbank's entry-level branches were first introduced into the market as pure loan centres, looking to capitalize on the potential revenue available in unsecured loans. However, the bank is currently going through a change in strategy, and these branches are increasingly offering transactional products. The range of products/services available is less than that of a traditional branch, with the Ke Yona products being sold to customers.

Nedbank offers Ke Yona in all of their branches, not only in the entry-level branches. This is in-line with the bank's push for convenience and full service for all of their customers from the main hub in their channel strategy<sup>65</sup>. The entry-level branches however, do not offer all the products and services offered in the full traditional branch and only offer simple products such as the Ke Yona transaction and savings accounts, personal loans and some insurance. The in-store kiosks operated by Nedbank also offer a limited service as they are primarily based around customer acquisition while increasing Nedbank's footprint.

FNB follows a different path in its product bouquet in branches. The EasyPlan products are only offered in the EasyPlan branches and not in the traditional branches. EasyPlan customers can, however, still use other services and take up products that they qualify for in the traditional branches.

While some products are limited to the traditional branches, they are not necessarily withheld from customers who bank in entry-level branches and may hold the transactional products from those branches. FNB, in particular, indicated a growing trend of Easy account customers going to traditional branches in order to get credit cards and other products they could possibly qualify for<sup>66</sup>.

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<sup>65</sup> Interview with Brian Duguid and Werner Terblanche; Integrated Channels, Nedbank, 2013

<sup>66</sup> Interview with Gift Manyanga, FNB EasyPlan CEO, 2013

**Table 1: Fees for transactional accounts\***

		<b>ABSA Transact</b>	<b>Capitec Global One Account</b>	<b>FNB Easy Account</b>	<b>Nedbank Ke Yona Account</b>	<b>Standard Bank Access Account</b>	<b>Ubank Transactional Account</b>
Monthly fee	Admin Fee	<b>Free</b>	R4,50	R4,20	R5,00	<b>Free</b>	<b>Free</b>
Balance Enquiries	Same Bank ATM	<b>Free</b>	<b>Free</b>	<b>Free</b>	<b>Free</b>	<b>Free</b>	R1,85
	Other Bank ATM	R3,35	R4,00	R3,25	<b>R1,50</b>	R4,00	R2,90
	SMS notifications	<b>Free</b>	R0,40	<b>Free</b>	<b>Free</b>	<b>Free</b>	R0,50
Debit Card Purchases		<b>Free</b>	<b>Free</b>	<b>Free</b>	<b>Free</b>	R2,00	R1,00
Cash Withdrawal	Same Bank ATM	R3,95	R4,30	<b>R3,25</b>	R5,50	R4,00	R4,50
	Other Bank ATM	R9,95	R7,00	R7,70	R7,50	R8,00	R9,50
	At a branch	R30,00	n/a	n/a	R10,50	R25,00	R12,50
	At a supermarket till	R1,00	R1,00	<b>Free</b>	R2,00	R4,00	R3,00
Cash deposit	Own Bank ATM	R5,75	<b>R2,50</b>	R3,25	R5,50	R4,00	n/a
	In Branch	R12,20	n/a	R3,25	R5,50	R25,00	<b>Free</b>

Source: Banks' Pricing Guides, 2013

\*Based on a transactional amount of R500

Bold indicates lowest fee charged

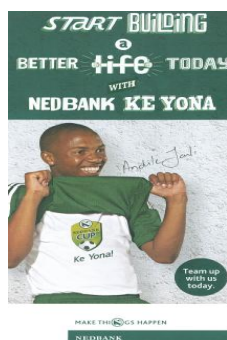
Note: African Bank is not comparable as only credit is offered

Table 1 compares the fees on transactional accounts across all of the selected banks. FNB's Easy Account transactional offering appears to provide significant value to the customer on a number of key aspects such as fees on debit orders, balance enquiries at the corresponding bank's ATM, debit card purchases, cash withdrawals at the till and at the corresponding bank's ATM as well as cash deposits at the corresponding bank's branch. These fees however only apply to customers being served in FNB EasyPlan branches (where Easy account customers pay standard fees in traditional branches). Although we compare in-branch cash transactions, these only apply for traditional branches, as customers cannot conduct cash transactions at the entry-level branches.

## 4.5. Changing Promotional Activity

Banks have the choice of either focusing on an Above the Line marketing strategy, which is deployed through mass media and non-segment focused, or alternatively a Below the Line strategy, which is tailored to a specific segment, and generally makes use of more direct communication channels. With regards to the marketing of the entry-level branches and the products available we see a much greater prevalence toward Below the Line marketing than Above the Line mass media campaigns. Banks have noted that Below the Line marketing campaigns have two main advantages over Above the Line marketing when directed at the low-income segment. Below the Line campaigns can be undertaken in a strategic location, such as outside the branch to draw customers in or alternatively within the low-income communities. More importantly, Below the Line campaigns can also embed a financial education element to better encourage customer understanding (and therefore usage) of the products being sold. As such, the Incumbents have adopted a stronger focus on Below the Line marketing for the entry-level customer segment, a shift away from the greater use of Above the Line marketing strategies for the general retail market.

**Illustration 7:**  
**Nedbank pamphlet**



*Source: Nedbank marketing brochure*

Nedbank's Below the Line marketing strategy involves direct promotion of offers to entry-level customers. Nedbank has tailored its Above the Line marketing campaign to target the entry-level market through the pamphlets it provides in entry-level branches, which are different to those found in traditional branches. These pamphlets are centered on sponsorships and promotional activities. Nedbank's main marketing driver is Nedbank Ke Yona Cup, which speaks directly to the target market in terms of attraction to the sport and in supporting domestic teams<sup>67</sup>. This is supplemented by strong positioning of their marketing pamphlets within entry-level branches, featuring identifiable local celebrities such as Andile Jali, who plays for Orlando Pirates.

FNB's marketing strategy within the EasyPlan branch space is predominately Below the Line campaigns, in which they strive to incorporate elements of financial education. Examples of these include a promotional campaign for the eWallet mobile service (held outside of the EasyPlan branches), whereby if a customer could explain how the eWallet service worked (thereby incorporating product explanation into the customer engagement), they received a pre-loaded eWallet amount. FNB seems to be running with a targeted marketing campaign within the EasyPlan branches, focusing on the maximum amount available from an Easy Loan, the features of the loan and detail around the Customer Protection Plan offered<sup>68</sup>.

<sup>67</sup> Interview with Brian Duguid and Werner Terblanche; Integrated Channels, Nedbank, 2013

<sup>68</sup> Interview with Gift Manyanga, FNB EasyPlan CEO, 2013

### Illustration 8: Absa pamphlet



Absa has not adopted a differentiated strategy to marketing to the entry-level segment, as its approach is that marketing campaigns are product-driven (rather than segment based). The direct agents play a significant role in Absa's Below the Line marketing strategy in terms of increasing product awareness<sup>69</sup>. Absa has made a concerted effort (and is the only bank of the Big Four to do so) to publish the marketing collateral available in Absa1234 branches in both English and Zulu, which relates to the entry-level customer segment better<sup>70</sup>.

Source: Absa marketing brochure

Standard Bank adopts a focused Below-the-Line marketing campaign (within their defined local market structures) where promotions, campaigns and sales incentives drives are run through-out their branch structures. Above the Line entry-level marketing campaigns are run on localised media channels (such as through SABC television channels) in the local language. These advertisements are targeted at the entry-level segment to ensure the target can relate, and differ significantly from conventional campaigns. An example of one such campaign, advertised on local media, was where customers could win an airtime rebate of R500 for buying R25 or more airtime<sup>71</sup>. Standard Bank's Above the Line strategy within the entry-level branches is currently focused on promoting the Access Banking product suite, and on shifting other entry-level accounts (such as the Mzansi and EPlan accounts) to the Access Account.

<sup>69</sup> Interview with Mike Bruwer (and team), Absa Sales and Service Distribution Type Specialist, 2013

<sup>70</sup> Mystery Shopping exercise undertaken by the Genesis Analytics team, 2013

<sup>71</sup> Interview with Carolina Reddy: Head of Distribution Planning, Inclusive Banking; Marius de la Rey, Channel Development Director, Standard Bank, 2013



## **4.6. WHAT HAS CAUSED ALL THE CHANGE?**

It is clear that the Incumbents have altered who they target, and how they target them. There are an ever increasing number of entry-level branches being rolled out across the country with simpler products aimed at lower-income individuals with innovative channels strategies to reach more of the previously unbanked population. Furthermore, banks are also looking to serve their existing entry-level customers with better focused value propositions, to reduce customer loss through unsuitable products and channels.

These movements clearly indicate that there has been a disruption to the market and the strategies of the Incumbents are changing to meet the new market conditions. Through our interviews with the big banks a few common underlying reasons emerged as to what may have shifted the market. These reasons include the changing macroeconomic environment, the increased unsecured lending margins, which contributed to the rise of banks such as Capitec and African Bank, and also the improvement in technology and how it is leveraged by the banks. All of these factors have worked in combination to contribute to the incentive for the Incumbents to move down-market, and were driving forces for the propulsion of Capitec and African Bank. Unlike with the Mzansi account, regulation has not played a significant role in this shifting change; whilst the banks still operating with the regulatory framework, this has not had an impact on the origination of entry-level branches.

## **5. DISRUPTION TO THE MARKET**

### **5.1. Changing demand factors In South Africa**

Due to the previous political system in South Africa many in the population had been financially, as well as physically, excluded from economic centres such as cities. Partly as a result of this the banking sector was perceived to be inaccessible to the majority of South Africans, and this stayed the case due to high banking costs charged by traditional banks, alongside the high poverty rates in the country and rural remoteness, which limited financial access.

With political and economic development, there have been changes in South Africa which have improved the profit opportunity that banks face in the entry-level market. Specifically, three trends have emerged that are contributing to the change demand factors: migration of population from rural areas to urban areas, increase in formal employment relative to informal employment and the rise of unsecured lending.

**Figure 14: Growth in Urban vs Rural Populations <sup>72</sup>**  
2002-2010

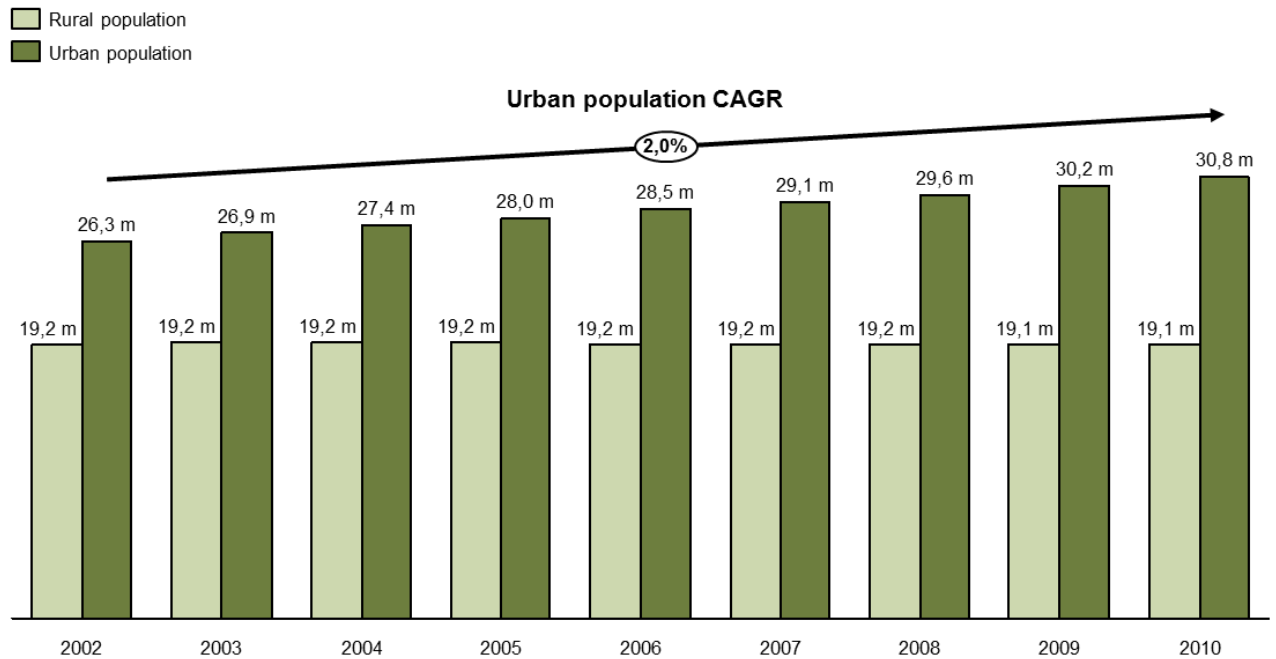
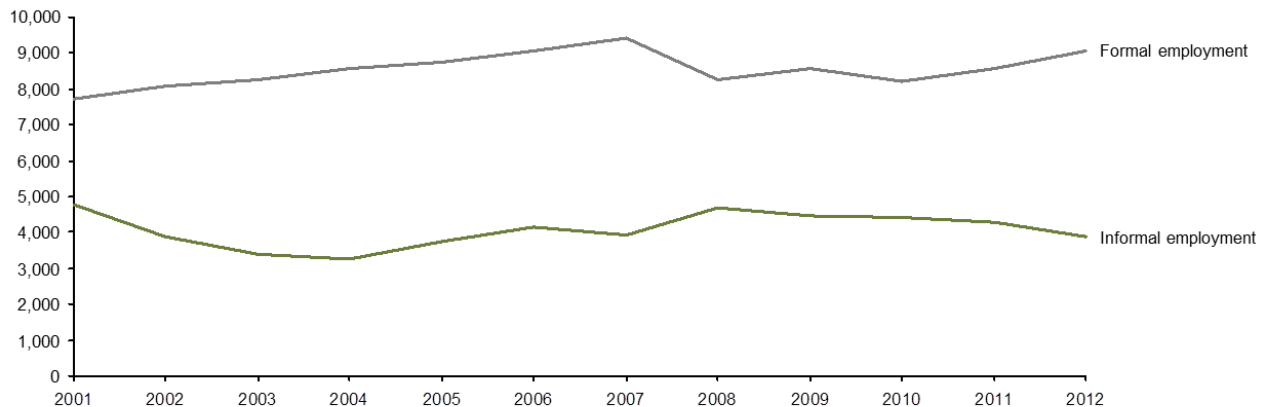


Figure 14 shows there has been a large trend of urbanisation in the country over time, with the urban population growing at nearly twice that of the rural population. With more of the entry-level segment residing in cities the market has become more concentrated and the entry-level consumers in cities could be targeted at a lower cost than if they had remained in more rural and remote areas.

The second trend experienced highlight in Figure 15 shows the increase in formal employment in the South African workforce in comparison to informal employment. With more and more workers entering the formal economy and gaining employment contracts, more customers in the entry-level market could qualify for unsecured personal loans.

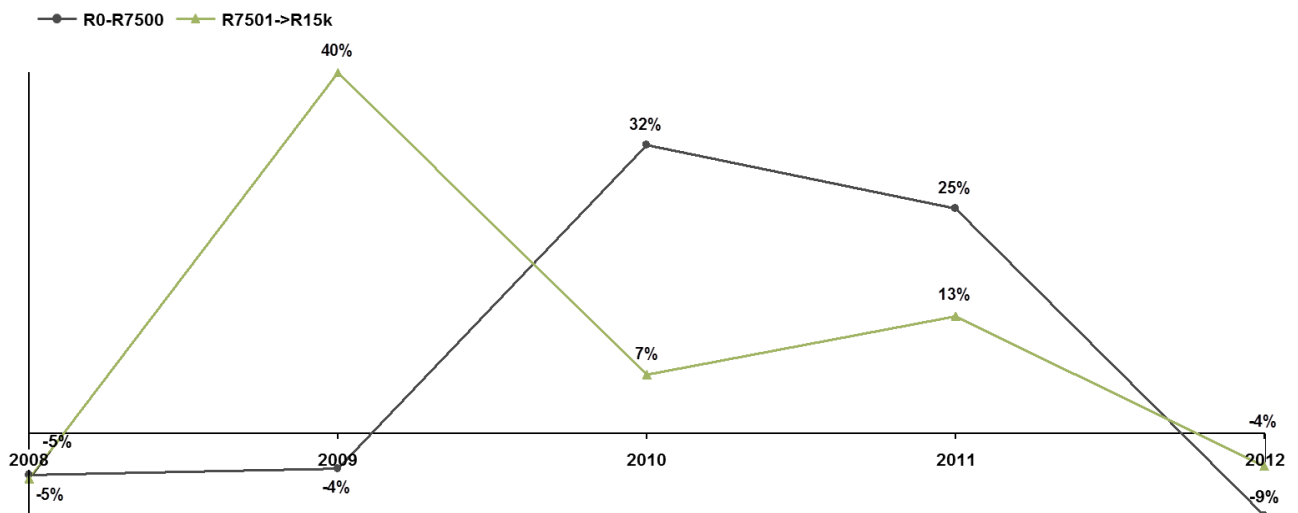
<sup>72</sup> StatsSA, 2002-2013

**Figure 15: Employment split between formal and informal <sup>73</sup>**  
2001-2012



These changes added to the rationale for banks to increase competition in the low-income segment market, particularly the credit market, targeting formally employed, low-income and previously financially excluded individuals. Figure 16 shows a large growth in the unsecured credit market in 2009 in the lower-income segment, where year-on-year growth in loans peaked at around 2009-2010. The banks were able to charge a higher margin to make up for the higher risk on these loans. These changes in the market were part of the growing opportunity for banks to provide a higher volume of small loans at an increased margin. This opportunity led to many of the banks entering the entry-level segment through personal loan centres.

**Figure 16: Growth in the number of unsecured loans per income segment <sup>74</sup>**  
2008-2012



The global financial crisis, which started at the end of 2008, also played a role in shifting the economic conditions faced by banks. These conditions had a large effect on the number of consumers accessing mortgage finance. The low growth in

<sup>73</sup> World Bank, 2001-2013

<sup>74</sup> NCR Credit data, 2008-2012

mortgages was due to a number of factors such as unfavorable property market conditions with depressed property market values, costs relating to bond origination, difficulties in realising security where credit providers experience challenges in evicting tenants, debt review process challenges, relatively low margins and an anticipated increase in capital requirements<sup>75</sup>. These factors have shifted some demand from secured lending to the personal loan space, which also saw an increase in the maximum amount offered.

Capitec and African Bank had already been making significant returns in the unsecured market, benefiting from the higher margins charged. If the larger banks were to play in this market they needed to adjust their segment focus and strategy, which they did in part through the entry-level branches.

## 5.2. Introducing The Disruptors

Capitec, African Bank and to a lesser degree Ubank are considered to be the Disruptors in the market, as upon their entry into the market, they achieved impressive growth and began to capture significant market share, which led to the disruption of the status quo in the banking arena. Capitec was the first new bank to enter into the South African banking space in 20 years<sup>76</sup>, and came in with a model which was different to what the other banks had in the market. These smaller banks disrupted the market as they identified the economic viability of the entry-level market.

### Capitec

Capitec was initially drawn to the lower-income segment through the identification that there was a profitable opportunity for micro-lending to the low-income segment in South Africa, given the associated high customer volumes. Being cognisant that loans to this segment were more risky, it was resolved that this should be launched in conjunction with a retail bank offering. The logic behind this was that establishing a transactional account provided the bank with the ability to better recoup loans, and to track a customer's financial activities as a means to determine creditworthiness.

From its inception in 2001, Capitec's approach to distribution channels was to set up standard branches that had a modern feel, an open atmosphere and that delivered convenience to its customer base. Capitec strived to ensure the simplicity and effectiveness of its in-branch processes. Capitec was the first to launch biometric verification and photo confirmation, meaning clients would not have to fill in forms, and identity could be confirmed without an ID document. While Capitec allows for in-branch cash deposits, cash withdrawals cannot be conducted over-the-counter. Instead, Capitec operates using ATMs for all cash withdrawals, as well as cash-back at retailers with partnerships with Shoprite Checkers and Pick 'n Pay. Additionally,

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<sup>75</sup> The DTI, *Research on the increase of unsecured personal loans in South Africa's Credit Market*, 2012

<sup>76</sup> Wits Business School, *Capitec: Entry-level Banking for Joe Average*, 2006

Capitec's push has been to shift customer behaviour in reducing cash preference, by promoting debit card purchases (which are free on the Global One account)<sup>77</sup>.

Capitec's branches are generally standardised, and can be considered entry-level given that they serve this market. These branches have simple yet modern furnishings, and have adopted innovative new queue management systems (where a customer can take a ticket as opposed to queuing). Spatial and staffing requirements are dependent on location. For instance, Capitec's flagship branch on Bree Street in central Johannesburg is relatively large and is staffed by around 10-12 people, whereas a smaller branch located off of Commissioner Street is smaller and is staffed by 4-5 people<sup>78</sup>. Capitec serves a total of more than 4.2 million customers within its branch network of around 500 branches, with customer growth figures estimated at around 90,000 a month<sup>79</sup>.

Capitec introduced a mobile banking offering in 2007<sup>80</sup>. Although this service, which is reliant on USSD technology, has stronger security features than some of the other banks (namely that it requires a security token), it also has lower functionality. The service allows you to make transfers to own accounts, pay Capitec clients, buy airtime and electricity and view balances (but has no facilities for debit orders, for example).

In response to customers' banking needs, Capitec offers the Global One account. This account combines a transactional product, savings products and credit options into a singular account, simplifying the overall offering. Further, unlike the big banks that differentiate product offerings to different customer segments, Capitec offers the Global One account to all of its customers. Capitec also simplified the pricing associated with this account, where it charges R4.50 monthly admin fee for all accounts<sup>81</sup>, and low fixed fees per transactions (as opposed to ad valorem fees). Capitec offers the largest unsecured personal loan amounts (at R230,000 over 84 months) in the market, which has been a strong factor in Capitec attracting entry-level customers that require access to credit.

Capitec appears to have adopted a broad Above the Line marketing campaign, encompassing television, radio, and print media advertising. However this is minimal in comparison to the Incumbents. Notably, Capitec is also a strong contender in the viral marketing space, where the bank has an active presence and a wide following and ranks 3rd in number of Facebook fans (second to FNB and Absa)<sup>82</sup>. Capitec mainly uses social media sites to run promotional activities and competitions. The bank also has a strong visual marketing push within branches, with TVs broadcasting a loop of promotional footage<sup>83</sup>.

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<sup>77</sup> Wits Business School, *Capitec: Entry-level Banking for Joe Average*, 2006

<sup>78</sup> Mystery Shopping exercise undertaken by the Genesis Analytics team, 2013

<sup>79</sup> Business Day, *African Bank aims to boost customer base*, 2012

<sup>80</sup> Wits Business School, *Capitec: Entry-level Banking for Joe Average*, 2006

<sup>81</sup> Capitec Global One marketing brochure, 2013

<sup>82</sup> Genesis Analytics team analysis, 2013

<sup>83</sup> Mystery Shopping exercise undertaken by the Genesis Analytics team, 2013

## African Bank

African Bank emerged at the end of 1999, with the rebranding of the Theta Group, and in 2002 it acquired Saambou's loan book valued at R2.8 million. The bank's objective was to provide affordable credit to the mass market, focusing on a target market of formally employed banked individuals within LSM groups 3-8. African Bank initially only offered unsecured personal loans (to the maximum amount of R180,000), but has begun to expand its product suite through its credit card options, where customers can take out a Blue Credit card (credit limit of R20,000), Silver Credit card (credit limit of R27,000) or a Gold credit card (credit limit of R46,000)<sup>84</sup>. This segmentation of different credit cards offered by African Bank is akin to the Incumbent banks customer segmentation across transactional products, where the big banks offer Blue, Silver and Gold accounts to transcending income groups.

African Bank's approach has been to offer competitive loans to the entry-level market, which is enabled through an efficient cost management approach. The group's strategy is to increase customer volumes through lower prices. This is maintained by a relatively flat operating cost structure, which is shown through their standardised and simple branch offerings. This targeted cost differentiation strategy enabled African Bank to achieve one of the lowest cost-to-income ratios in the industry, translating into performance figures that give it a market leader position in the microcredit industry in South Africa<sup>85</sup>.

African Bank makes use of a standard branch model in which all their branches are deemed low-cost. African Bank is able to carry out their branch operations within spaces that vary from anything between 50 square meters of space to 100 square meters of space<sup>86</sup>. Since African Bank only offers credit products and is not a transactional bank, it requires less space and less staff than a full retail bank<sup>87</sup>. As a result, African Bank is afforded the flexibility of very small branches which allows for significant cost reduction. Branches are constructed in the form of physical buildings, kiosks and 'carve-outs' located in the Ellerines Group.

The standard branches are aimed at lower-income individuals who typically earn an income of approximately R0 - R300 000 per annum (this income may be irregular in intervals and variable in amount). These branches generally have very basic furnishings with around 3-8 staff members in a typical branch. African Bank served 2.6 million customers in 2011, through a branch network of 643 branches<sup>88</sup>.

A large component of African Bank's distribution strategy is its in store carve-outs in the Ellerines Group<sup>89</sup>. The Ellerines Group includes Ellerines, Beares, Geen & Richards, Furniture City, Dial a Bed, Wetherlys and other furniture outlets, and African Bank has between 150-180 carve-outs within these retailers. A carve-out operates similar to a branch, where African Bank has 'carved-out' a proportion of the retailer's

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<sup>84</sup> African Bank marketing brochure, 2013

<sup>85</sup> Wits Business School, ABIL: Breaking Through Microfinance Frontiers, 2007

<sup>86</sup> Interview with Charles Chemel, Head of Sales, Distribution, Marketing and Product, African Bank, 2013

<sup>87</sup> *Ibid*

<sup>88</sup> African Bank Investment Limited Annual Report, 2011

<sup>89</sup> African Bank Investor Reports, August 2010

floor space to promote their banking business. Carve-outs operate as a branch, where the same credit products are available, and are generally staffed by around 3-4 people<sup>90</sup>.

African Bank also operates kiosks, which are distinctive from the branches and carve-outs in that kiosks are staffed by only 1 or 2 sales agents and operate within the Ellerines environment, providing credit for retail customers. African Bank has 40 kiosks in mining communities, and another 150 kiosks within the Ellerines Group<sup>42</sup>.

Notably, through the investment in both kiosks and carve outs, African Bank has established a presence in new geographical areas, and seen a 26% growth in new customers from 2010-2011, translating into R1.7 billion sales revenue<sup>91</sup>. African Bank currently serves 2.6 million customers, attracting 600,000 new customers a year and 250,000 repeat customers a year. These figures are not strictly comparably to the other banks, however, as African Bank is a credit provider and has a higher customer run-off with clients repaying or defaulting on loans<sup>92</sup>.

African Bank has recently launched an application called 'In Seconds' which is accessible through the internet or by dialing "49494" via mobile phone. This application is designed to allow customers to get a quote on a loan application in seconds<sup>93</sup>.

African Bank does not have an extensive marketing budget in comparison to the Incumbents and alternatively the bank relies on word-of-mouth to promote their brand and product offerings, especially within the local communities. African Bank does make use of local radio and print media to market their offerings however, it does not look to incorporate any extensive customer education. Its approach is that given that its product range is exclusively credit offerings, its customer interaction is limited<sup>94</sup>.

There appears to be clear cross-overs between the Capitec and African Bank branch models, where both are positioned in the market to serve the low income segment. Within what could be considered entry-level branches (based on the location of these branches), both of these financial institutions have similar lay-outs, spatial requirements and basic furnishings. Both institutions have a strong dependency on advanced technology as an enabler for branch efficiency and customer service delivery. For example, both Capitec and African Bank make use of biometric technology as a means of proving an individual's identity. Notably, this is highly appropriate for the low-income segment with a higher prevalence of lacking identification documents.

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<sup>90</sup> African Bank Investment Limited, Annual Results Presentation, September 2011

<sup>91</sup> *Ibid*

<sup>92</sup> Business Day, *African Bank aims to boost customer base*, 2012

<sup>93</sup> Interview with Charles Chemel, Head of Sales, Distribution, Marketing and Product, African Bank, 2013

<sup>94</sup> *Ibid*

**Illustration 9: Capitec's Rosebank branch**

Source: Genesis Analytics team, 2013

Johannesburg). This is likely the result of a number of factors. In Capitec's case, it has a growing middle to upper-income customer base as more individuals are attracted by the simplicity and affordability of its product offering.

What is interesting to note is that both African bank and Capitec appear to be moving upmarket in terms of their branch delivery, likely in conjunction with a vertical broadening of their target market. We see this as both institutions are setting up more advanced and sophisticated branches in what would generally be considered middle-income locations (for example, Capitec has a branch in Rosebank, Mall Johannesburg, and African Bank's branch in Eastgate Mall,

**Illustration 10: African Bank, Eastgate Mall**

Source: Genesis Analytics team, 2013

With African Bank, they may be expanding their branch locations and re-vamping their current branch lay-out as they see their customers migrate up the income scale. African Bank's new branch in Eastgate Mall Johannesburg speaks to African Bank enhancing its branch offering as it begins to push into the middle market customer segment. The branch location is indicative of being positioned to target the middle-income market that frequent that particular mall. More so, the physical appearance of the branch is much more modern and sophisticated than that of African Bank's standard branches, with more up-market finishes. The staff within the branch are highly receptive and knowledgeable on the bank's product offerings, and the branch in general is very welcoming and customer friendly<sup>95</sup>.

Capitec's branch in Rosebank Mall Johannesburg is also clearly positioned to attract the middle to upper-income market. This branch has slightly better aesthetics than Capitec's standard branches, with a welcoming 'open-door' feel. The branch is located directly opposite a Nedbank traditional branch, which may indicate that Capitec is directly competing with Nedbank for a piece of the middle market customer base<sup>96</sup>.

<sup>95</sup> Mystery Shopping exercise undertaken by the Genesis Analytics team, 2013

<sup>96</sup> *Ibid*



## Ubank

Ubank's origins lie in Teba Savings Trust, which was established in 1976 to deposit mineworker's savings. In 2010, it re-launched as Teba Bank, a full transactional bank to serve mineworkers and the surrounding mining communities<sup>97</sup>. Ubank has a unique ownership structure, where ownership is vested in a trust with the main trustees the National Union of Mineworkers and the Chamber of Mines, hence Ubank's customer base is also effectively its shareholders<sup>98</sup>. One of the motivating factors to rebrand from Teba to Ubank was to begin to diversify its customer base away from purely mineworkers, through expanding its footprint beyond mining communities<sup>99</sup>.

As Ubank is looking to push into the retail banking arena, this entails developing infrastructure in urban areas. As such, Ubank has a two-pronged distribution model that includes branches in mining communities and branches in the retail space. Currently, 90% of Ubank's customers are mineworkers (or within the mining communities), with the other 10% coming from the urban areas<sup>100</sup>. Ubank serves around 500,000 customers, having seen little growth in its customer base since 2010<sup>101</sup>.

Within the mining communities, Ubank generally operates as the sole financial services provider (as it remains unprofitable for other banks to move into this space). As such, Ubank is compelled to offer full-service branches within these areas, which includes cash-handling. This remains cost-effective for Ubank to operate as it has standing arrangements with the mines to lower the bank's operating costs (this may translate to lower rentals, lower security expenses, or other costs). These areas are usually isolated and low-income; however they represented a gap in the market as before Ubank, there was no provision for financial services. In this sense, Ubank has made a big step forward in increasing financial inclusion<sup>102</sup>.

Within the retail space, Ubank has developed an entry-level branch approach very similar to that of Capitec's. Its product offerings are standard, although Ubank is unique in that it offers a pension-backed home loan. The savings account product features heavily in Ubank's product suite, where Ubank offers a Savings account, a 32 notice deposit and a fixed deposit. The retail branches (located in urban areas, which are different from Ubank's rural branches) have tellers that accept cash deposits (but do not allow for cash withdrawals), and generally have an ATM located outside. These branches are generally between 170 and 180 square metres, staffed with sales agents and one branch manager. The branches have a clean and open feel to them, and are well sign posted from the exterior. These branches can serve up to 30 to 40 customers a day. Although they are located in retail areas, the majority of the

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<sup>97</sup> Sowetan Live, *Bank unveils its new strategy*, 2010

<sup>98</sup> The New Age, *Teba Bank renamed*, 2010

<sup>99</sup> Business Times, *Ubank spends 25m to boost image*, 2011

<sup>100</sup> Interview with John Bellis (and team), Ubank General Manager of Customer Solutions, 2013

<sup>101</sup> Financial Mail, *Ubank U-turn*, 2012

<sup>102</sup> Interview with John Bellis (and team), Ubank General Manager of Customer Solutions, 2013

customers served are very low-income, unemployed individuals<sup>103</sup>. Thus although Ubank is attempting to diversify its customer base, it does not appear to be pushing up-market (as with Capitec and African Bank), but rather to be horizontally shifting into the urban entry-level market.

**Illustration 11:  
Ubank pamphlet**



Source: Ubank marketing brochure

The products offered in the mining branches (located in rural areas, different from the retail branches) are standard, and include transactional accounts, savings accounts, and credit and insurance products. In terms of pricing, the transactional accounts are priced lower than in the retail branches. These lower fees are cross-subsidised against the higher interest income earned through high sales of credit products within these branches. Ubank also offers a specialised cross-border remittance service within the mining branches, where miners can transfer funds to their Teba outlets located in Swaziland, Lesotho and Mozambique. Ubank aims to have an ATM outside each of these mining branches. Interestingly, in some of the more commercial mining areas (such as Rustenburg and Klerksdorp), Ubank has begun to set-up more up-scale branches (in terms of size and furnishings) in a drive to offer a full-service banking experience to those in the mining area<sup>104</sup>.

Ubank teamed with Blue Label Telecoms to launch a mobile money-transfer service in late 2010. This operates much as the other mobile money-transfer services offered on the market, however this is differentiated in term of customer usage, where it is predominately used by mine workers to remit funds back to their families<sup>105</sup>.

With respect to Above the Line marketing, Ubank has adopted a localised strategy. They promote through billboards and local radio stations within the areas where they have branches located. For Below the Line marketing, Ubank runs with numerous 'on the ground' campaigns, as well as road shows throughout South Africa. Ubank also has direct sales agents located outside the branch as a means to pull customers in<sup>106</sup>. A large contingent of the pamphlets in Ubank branches are of an informative nature, and are focused around banking safety tips.

It would appear that Ubank is driving customer education around safe ATM usage (and safe banking in general) through marketing pamphlets available within branches<sup>107</sup>. Capitec also distributes pamphlets that highlight customer safety at ATMs, which is evidently an issue within this customer segment (potentially owing to the location of the ATMs), which these banks are attempting to address through increasing customer awareness of potential threats and offering safe habits for customers to adopt.

<sup>103</sup> Mystery Shopping exercise undertaken by the Genesis Analytics team, 2013

<sup>104</sup> Interview with John Bellis (and team), Ubank General Manager of Customer Solutions, 2013

<sup>105</sup> Ubank, *Ubank moves to take on Capitec*, 2010

<sup>106</sup> Interview with John Bellis (and team), Ubank General Manager of Customer Solutions, 2013

<sup>107</sup> Mystery Shopping exercise undertaken by the Genesis Analytics team, 2013

The Disruptors entered the market through offering personal loans to the entry-level segment. These banks were the first to identify the opportunity available within this space and act on it. Table 4 illustrates the current personal loan products available in the market from all the banks. The table shows that the Capitec and African Bank who are the leaders in the market still have the largest and most accessible loans.

Table 2 compares the personal loan products across the selected banks and shows that while the Incumbents compete with Capitec and African Bank in the credit space, they tend to be less flexible around certain aspects of the loan. For instance, Absa provides the same flexibility in the maximum payback period allowed in 84 months, yet the maximum loan amount offered is only R150,000, as opposed to Capitec's R230,000 and African Bank's R180,000. Standard Bank appears to be the least flexible of all the banks with the lowest maximum loan amount and the shortest payback period. While each of the banks appear to be following a different credit strategy, they are hesitant to discuss their strategies aimed to give them an edge in the market. These strategies are based on, amongst other factors, their customer value proposition, their own risk structure and other internal processes.

**Table 2: Personal loan products comparison**

	<b>ABSA Personal loan</b>	<b>African Bank Personal loan</b>	<b>Capitec Global One Account</b>	<b>FNB Loan</b>	<b>Nedbank Personal loan</b>	<b>Standard Bank Personal loan</b>	<b>Ubank Personal loan</b>
Minimum salary required	R2,000 p.m.	Not specified	Not specified	R2,500 p.m.	R1,200 p.m.	<b>R1,000 p.m.</b>	Not specified
Minimum repayment period	12 months	<b>1 month</b>	<b>1 month</b>	<b>1 month</b>	12 months	3 months	2 months
Maximum repayment period	<b>84 months</b>	<b>84 months</b>	<b>84 months</b>	60 months	60 months	42 months	36 months
Minimum loan amount	R3,000	R1,500	Not specified	R1,000	R1,000	<b>R500</b>	Not specified
Maximum loan amount	R150,000	R180,000	<b>R230,000</b>	R150,000	R120,000	R40,000	R50,000

Source: Bank websites and Marketing material

Note: Bold indicates most flexible terms

Capitec and African Bank's strategies of pushing large unsecured loans with long payback periods to the entry-level market sustainability has recently been brought to question. The National Credit Regulator (NCR) is currently reviewing both Capitec and African Bank's lending practices, where issues such as customers' ability to afford loan repayments and initiation fees charged are being looked at<sup>108</sup>. The outcomes of

<sup>108</sup> MoneyWeb, NCR accuses Capitec of contravening credit act, 2013

the NCR reviews and the potential impact on the credit market in South Africa remain to be seen. It would appear that there is an oversupply of credit in the market<sup>109</sup>, making it easier for low-income individuals to take out multiple loans, which has been cause for concern that there is a 'credit bubble' in South Africa. We note that the Incumbent banks have reacted to this by rebranding their loan centres (which exclusively pushed personal loans) into full service branches (which sell a full product suite) within the entry-level space.

### 5.3. The Increased Use Of Technology

Part of what the Disruptors did well was to make use of the improved technology that was available. Capitec was a leader in this area and maximised the use of technology to provide innovative solutions to customers while bringing the costs of banking down.

Capitec illustrated how a technology-driven business model can be a successful approach to serving the low-income population. Capitec's branches use excellent information technology including fingerprint biometrics, photo identification and card access which allow them to be paperless. This technology usage has aided in bringing the cost to serve down, allowing banking to be profitably extended to the entry-level market.

The Incumbent banks entry-level branches also make use of increased technology to bring costs down, where cash has effectively been removed from the branches and deposits and transfers are available on advanced ATMs at some of the banks. FNB was the first to introduce cash accepting ATMs in South Africa, with the other banks quickly following suit. While these machines require a higher investment amount than standard ATMs, they realise cost-savings through the ability to remove cash handling from the branch while moving customers into self-service channels and away from more costly branch service channels.

The increasing availability and use of cellphone technology such as smart phones has also helped banks rethink their channel offerings, with the mobile channel taking on an important role in supplementing branches and increasing the banks' reach into the entry-level market. The banks have begun to leverage off this improved technology to find innovative new ways to service customers. This is perhaps best displayed through Standard Bank's Access agents who are able to open an account for a customer and give them their card in under 10 minutes from any location through the use of smartphones. This means customers do not even need to travel to a branch.

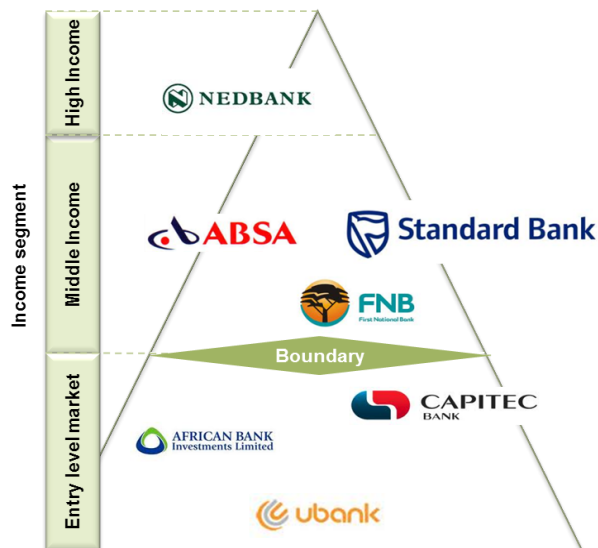
It is evident that the improvement in technology has been a contributing factor to the emergence of entry-level branches and the channel offering around these. Technology was central to the low-cost model Capitec brought to the market and with the help of technology other banks are catching up in the entry-level space, and also finding new and innovative ways to serve the market.

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<sup>109</sup> Fin24, *Customers don't say no to credit-Abil*, 2013

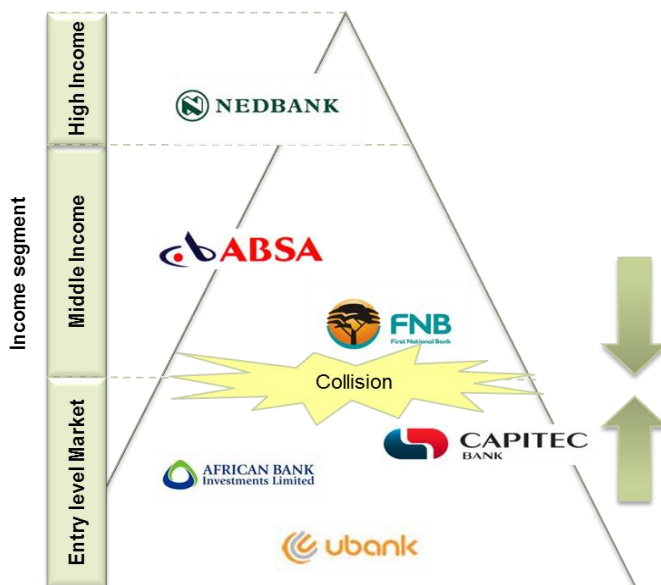
## 5.4. Colliding Paths

Illustration 12: Customer pyramid



Source: Genesis Analytics team analysis, 2013

Illustration 13: Bank Convergence



Source: Genesis Analytics team analysis, 2013

The Incumbents have long held a dominant position in the South African market, competing for the business from the middle and upper-income segments. The big banks had developed a cost model to service their clients, who formed the top of the customer pyramid. While the Incumbents had a boundary under which they could not affordably service customers, a group of Disruptors saw the potential in this segment and took advantage of it.

In order for this segment to be profitable, costs had to be low and volumes high, a strategy perfected by Capitec and African Bank. These banks demonstrated the viability of the approach and the Incumbent's responded by adjusting their business models to meet the needs of the lower segment of the customer pyramid.

However, while the Incumbents on the top of the pyramid are pushing their way down, the Disruptors, who have made their gains at the bottom, are also looking to make a move – up the pyramid<sup>110</sup>.

Capitec has emerged as a market leader in terms of its transactional product offering, product simplicity, convenience and affordability. African Bank established the market for unsecured lending as the economy shifted in the country creating a large market for credit. We see that these are some of the major aspects that the

Incumbents have adopted in their approach to capturing a share of the lower portion of the pyramid.

<sup>110</sup> Note that Ubank remains the outlier, as it continues to serve a very niche market

At the same time, it appears that the principles that make Capitec and African Bank successful in capturing the low-income customers, such as product affordability and simplicity, are transferable to the middle and upper-income segments. As such, we see some switching of customers within this segment to the Disruptors. With this migration of customers across targeted segments, both Capitec and African Bank have begun to modify their customer value propositions to better service the middle to upper-income segments. This is seen in the products and services offered (such as Capitec offering internet banking and African Bank offering a credit card product) and is visible in their physical infrastructure design and location.

It is our hypothesis that as we see the Incumbents shift their value proposition downwards, and as we see Capitec and African Bank attract more of the middle and upper segment customers, these shifts from both sides along the pyramid will eventually lead to some general convergence of the Incumbents and the Disruptors, in terms of product and service offerings, and also in terms of distribution channels. With regards to channel offerings, while all of the banks will continue to advance greater usage of electronic channels (across all customer segments), we still expect that branches will play an important role in the delivery of banking services as they provide a fundamental touch point for customers.

## **6. THE FUTURE OF THE BANKING LANDSCAPE**

### **6.1. The Realities Of Serving A Diverse Customer Base**

The Incumbent banks have and continue to serve a more diverse customer base than the Disruptor banks. Aside from the personal banking customers, the Incumbent banks serve high net worth individuals as well as business banking customers. The Disruptors; smaller, niche banks, are at an advantage in that they are in general serving a more homogenous customer base and do not have the legacy issues the Incumbent banks face. They can roll-out standardised branches across all market segments in comparison to the larger Incumbent banks that require differentiated branches to meet the different needs and attitudes of their customer base. Because of this, the Incumbent banks will always have a differentiated distribution model to that of the standardised model which the Disruptor banks can utilise. It is likely that the Incumbent banks will maintain this differentiated model as it remains very profitable to serve affluent and corporate clients.

At the same time, the Incumbent banks see the success of the entry-level branches within the low-income segment. The approach delivers greater convenience to the customers at a lower cost to the banks. The progression towards electronic channels in the future and the potential declining need for physical branches might lead to the Incumbents looking to adopt entry-level branches as a more affordable means to serve all retail banking customers. This could result in an overall convergence of the Incumbents and the Disruptors customer value proposition, including the product suite and channel offerings, to the entire personal banking customer base.

## 6.2. Consequences Of Convergence

The convergence of these branch types could result in pricing battles between banks competing for the middle market. We already see aggressive competition in the lower-income segment aimed at remaining profitable while offering the most affordable products to low-income customers. We expect to see a similar rise in competition in the middle-income market segment between banks that compete for these customers.

Given that the middle market banking population is already saturated, pricing will inevitably become one of the strongest competitive forces. This will likely drive banks to decrease the cost to serve the middle-income market and contribute to banks looking to extend the entry-level branch model to the middle-income market segment.

Increased competition to acquire entry-level customers is pushing innovation and progress in the market. Already, the strategy of serving the entry-level market through low cost branches has proven more of a success than the Mzansi initiative and banks are continuing to find new ways to profitably expand into the unbanked market.

The study indicates there has been a significant increase in entry-level customers within each of the banks interviewed. While some of this increase will be a result of more people opening multiple bank accounts, there has been an improvement in the access for those in the entry-level segment. Banks have designed products and processes to meet the needs of the customer segment and provide a complete banking solution rather than just a single product as was seen with Mzansi accounts. While it is still too early to tell, these customer-centric banking solutions are likely to see increased activity as they meet market needs.

The significant increase in entry-level customers has slowed after the initial rapid growth. While the banks have entered a consolidation phase many have reported further strategies in the pipeline to reach deeper into the lower-income market, and innovative ways to extend service profitable into the rural areas. As such, advances in technology and creative solutions will drive improved financial access.

## 7. INTERNATIONAL CASE STUDIES (3)

### 7.1. Equity Bank In Kenya

Kenya is an emerging economy with a financial sector that includes commercial banks, deposit-taking micro finance companies, a postal savings bank and active savings and credit cooperatives (among other financial institutions)<sup>111</sup>. Equity Bank emerged as a bank that targeted low-income customers in Kenya. In 1993, known then as Equity Building Society, Equity Bank was declared insolvent as a result of poor management and supervision. Equity Building Society received a capital injection from the Kenyan government such that it could continue its operations, which proved effective. By 2011, Equity Bank had 7.1 million customers and operated across Kenya, Rwanda, Uganda and South Sudan. The success of Equity Bank is largely owed to its change in strategy from financing mortgages to financing small, short term loans at a high interest rate, and an evolution in its delivery channels, products & services, systems and client relationships. We can compare Equity Bank's strategy to that of Capitec, as like Capitec, Equity Bank focused its efforts on growing its customer base through innovative products, services and channels.

Through the bank's market research, Equity Bank realised that many of its customers felt that the fees which Equity charged were unjust. With this information, Equity's management launched financial products that required no minimum balance, no monthly fees, no account opening fees and no fees for deposits, similar to the entry-level products we see in banks in South Africa currently. This had a significant impact on the sales of accounts. Equity also focused on building its reputation among its customers through transparency and credibility.

Equity realised that for it to be successful in the mass market it needed to extend its distribution channels, so that they reached out to a larger number of customers, however, this had to be done at a low cost. Equity achieved this by designing branches for volume operations, developing infrastructure (such as point of sale devices, ATMs and mobile branches) and increasing branch efficiency through improved branch operations.

Many of Equity's branches serviced more than 100,000 customer accounts. This was achieved through the use of technology to increase the efficiency of its operations in its volume-gearred branches. Equity upgraded its old banking system (Infosys) to Finacle, which was a volume based banking system solution. Equity also made use of branch based ATMs and later ATM banking halls (with ATMs that could accept cash deposits), equipped with a staff member- similar to FNB's approach to its cash-accepting ATMs.

Equity Bank also extended its operating hours, opening half an hour earlier in the morning and closing an hour later in the evening to provide more convenience

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<sup>111</sup> Center for Global Development, 2012



customers, much like the entry-level branches in South Africa located in high traffic zones.

Equity rolled out a mobile branch strategy in 2001, which operated out of a vehicle that made use of solar panels to provide electricity. These mobile branches travelled to far off villages and towns as geographical inaccessibility as a result of distance substantiated the high cost of financial services. The commercial viability of these mobile branches declined over time because of robberies of the vehicles.

Success for Equity Bank has come largely from its willingness to develop products and services designed for particular communities, which we see the Incumbent banks in South Africa looking to do.

## 7.2. Branch Transformation In South East Asia

Although the focus of the retail financial services industry in Asia has been towards shifting customers to e-banking (electronic banking), with banks deploying complete mobile phone banking propositions in 2009; most banks continue to enhance their branch propositions. This is seen as an important element of their overall network infrastructure; where branches play a key role in fostering sustainable customer relationships. Transformation of their branch networks is taking place as banks look to design branches to cater specifically for the surrounding communities, and that are customer-centric, service orientated and efficient<sup>112</sup>.

A survey was conducted by the Asian Banker Researcher and Diebold of 24 retail banks in Australia, Singapore, Hong Kong, Korea, Japan, Taiwan, China, India, the Philippines, Indonesia, Thailand and Malaysia, where the selected financial institutions were identified as banks that had a focused strategy towards branch development. The survey looked to determine both drivers and key challenges in branch transformation. Elements of branch transformation that were identified across these banks include:

- The downsizing of branch facilities' to optimise floor space- this then enabled better control over how staff interacted with clients
- A much more high-touch, personalised feel within branches, supported by advanced technology infrastructure
- Developing a 'one-stop-shop' branch, which can service a broad range of customer needs
- To optimise the value of a branch, branches are integrated with the external network points, which are further integrated back into the bank's back-end infrastructure

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<sup>112</sup> Asian Banker Research, 2011, *Successful Branch Transformations: Achieving needs-based sales and service-orientated delivery*

- Finally, banks are orientated towards multi-skilled front line staff that have a market-view. This involves considered hiring and extensive training of staff

The drivers of branch transformation that were identified by the banks include; the demographics of the market, customer transactional behaviour, risk preferences and the need to strengthen network integration.

What is interesting to note is that in South East Asia, which represents a completely different demographic market including vast degrees of financial literacy, and with different product preferences and transactional behaviours to South Africa, banks still recognise the need for physical branches. This is in line with our report's hypothesis that despite the growing prevalence of electronic channels, banks will continue to operate branches into the foreseeable future.

This is supported by the idea that customers, while they may shift more and more transactions to electronic channels, will always want a human-face to interact with for non-routine procedures. This is reflected in some of the aspects of branch transformation undertaken by the South East Asian banks, whereby staff are highly trained and customer-centric, in order to best deal with customer-specific issues (as opposed to routine transactions). We further predict that in South Africa, as is the case in South East Asia, technology will not just be seen as a substitute channel, but also as enabler for customer-staff interaction. For example, this could manifest where banking enquires are dealt with in real-time over an interactive website. Again, this highlights that human interaction remains a core component of a bank's service offering.

### 7.3. OPPORTUNITY INTERNATIONAL BANK OF MALAWI

Only 45% of the adult population in Malawi was financially included in 2008. Of the financially included population, a mere 19% were formally banked<sup>113</sup>. The Opportunity International Bank of Malawi (OIBM), a micro-finance bank, was established as a regulated commercial bank in Malawi in 2003<sup>114</sup>. In 2006, OIBM received a grant from the United States Agency of International development (USAID) to the value of USD 890,000 with the purpose of gaining 85,000 poor people residing in the rural areas of Malawi through basic banking, financial services and micro finance loans. At the end of 2009, OIBM had over 45,000 active loan clients and over 250, 000 depositors. This grant was intended mainly to develop and increase OIBM's mobile banking units, point of sale devices and ATMs.

Opportunity International is known to provide savings products, business and agricultural loans and crop insurance products<sup>115</sup>. Customers are able to access their savings accounts at OIBM through ATMs, major super markets, farm stores, BP gas stations and POS locations (within merchants). Today OIBM has 270,000 depositors and 47,500 loan clients. OIBM has also formed agreements with rural merchants to

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<sup>113</sup> Finscope, 2008

<sup>114</sup> The Seep Network, USAID, Opportunity International, 2009

<sup>115</sup> USAID, 2009

provide financial services from a POS device. Clients are able to use their debit cards in these merchant stores.

Technology and innovation has allowed OIBM to reach individuals who were previously excluded as a result of distance and poverty. One technological innovation introduced in OIBM was biometric fingerprint technology which is used to encrypt the finger print of a customer onto a computer chip and place that computer chip on a smart card when the customer opens an account. When a customer goes to the bank or ATM, they place their same finger on a scanner (after swiping the smart card) to verify that they are indeed the account holder. The customer's transaction is only processed once the print is identified as a match. This technology also meant that customers did not need to remember a pin.

Similar biometric identification and verification technology is utilised by both Capitec and African Bank, and has recently been rolled out by FNB. These system use real time verification linked to the Home Affairs National Identification System (HANIS)<sup>116</sup>. This technology reduces the incidence of fraud and identity theft in the branch. This also helps the bank build a trusting relationship with the customer.

OIBM has also made use of a hub and spoke model similar to that used by Nedbank. In OIBM's case the branch serves as the hub with the mobile unit (ATM van) and loan officers as the spokes. The mobile unit has call points along specified routes during the week. OIBM has achieved substantial success through this model.

The key output from this case study is that extending financial access goes beyond opening an account. Having the right combination of products as well as using the right technology can significantly reduce costs and produce a constant transaction volume. Also, rural populations are able to embrace technology, provided it is coupled with a strong financial education component.

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<sup>116</sup> FNB website, 2013

## 8. CONCLUSION

### 8.1. TRENDS IN ENTRY-LEVEL BANK BRANCHES

**Growth in entry-level clients:** The number banked within the entry-level segment (LSM 1-6) has risen from 30% in 2003 to 46% in 2011. This growth in entry-level customers is reflective of a variety of changing factors in South Africa, both external and internal to the banking landscape. External factors include the increased economic inclusion of the lower end of the income pyramid and government initiatives to drive increased financial inclusion in the lower-income segment. Internal factors to the banking landscape include the entry of new banks such as Capitec and African Bank servicing the entry-level customer segment, the Big Four banks' recognition of the economic viability of the segment and subsequently tailored product and channel offerings to the entry-level market. Further, technology has proven to be an enabler in bring down the cost to serve the entry-level market. Financial inclusion within this segment still remains relatively low compared to the middle and upper-income segments, meaning that banks will continue to look to grow their customer base within the entry-level segment.

In the period 2010-2011, Absa experienced a growth of 27%, Standard Bank experienced growth of 32% and FNB experienced growth of 30% in entry-level customers. This is in comparison to Capitec's customer growth of 26% and African Bank's growth of 13% over the same time period. Given that the Incumbent banks mostly launched their entry-level branches around 2010, a proportion of this customer growth may be attributable to the Incumbent banks becoming more accessible to the entry-level market through these branches.

**Growth in physical infrastructure:** All of the banks appear to be growing their entry-level branch offerings, although this is off a low base as most of the Incumbent banks only began to deploy entry-level branches in 2010. Given that the banks stated that these branches have proven to be economically sustainable, we expect banks to continue to grow the number of entry-level branches. We also expect to see strong growth of alternative channels into the future, such as cash accepting ATMs, retailer kiosks and bank shops. This will occur as (1) customer awareness and understanding of these channels, through banks' educational drives, increase usage and (2) banks push further into rural areas where these alternative channels are a more economically viable means to serve the market.

## 8.2. COMMON ELEMENTS OF ENTRY-LEVEL BANKING STRATEGIES

Entry-level banking has emerged as a critical component of all of the banks' strategies in South Africa. The result has been a significant uptake in entry-level banking products and a profitable extension of financial services to the underserved or unserved population. Operating in this market creates many challenges, the most critical of which is balancing a low-cost branch model with high volumes of clients.

Lack of uptake of the Mzansi account observed in this research highlights a need for banks to go beyond developing only low-cost products in the entry-level market, and to include considerations such as (i) the customer's ability to get to bank branches, (ii) their comfort in using these branches, and (iii) their other banking needs. This research observed success factors in all three considerations:

***Innovation in attracting entry-level clients:*** Branch placement plays a critical role in attracting large volumes of customers into the entry-level bank branches, but banks have also adopted a more aggressive approach to attracting new clients through a layered marketing approach. Banks utilise (i) promotional activities (ii) on-boarding (iii) customer education and (iv) a personal interaction to attract clients.

Promotional activities are not just limited to above-the line marketing strategies and banks have begun to use extensive below-the-line campaigns to attract entry-level customers. For example, FNB's EasyPlan staff are encouraged to go out and recruit new customers to the branch rather than just relying on walk-ins.

At the branch, banks identify potential clients that need further education for better understanding of the product, and ensure that staff are fully equipped to deliver this education. In other cases banks couple technology that increases access with educational components to encourage usage, such as Absa's educational zone. Standard Bank's Access agents are tasked with on-boarding new customers in using the alternative channel offerings, such as directing a new customer to an AccessPoint and stepping them through their first transaction.

Ubank is driving customer education around safe ATM usage (and safe banking in general) through marketing pamphlets available within branches. Capitec also distributes pamphlets that highlight customer safety at ATMs, which is evidently an issue within this customer segment. Banks are attempting to address this through increasing customer awareness of threats and safe habits to adopt. Absa has ensured customer acceptance of cash accepting ATMs by putting a staff member next to cash-accepting ATM to assist customers in making deposits. This is imperative where customers may otherwise have been reluctant to make use of cash-accepting ATMs due to lack of understanding and trust in the technology.

Finally, the branch includes face-to-face interaction to provide customers with a personal touch. For example, both FNB and Capitec have floor mangers to direct

customers upon entry into a branch. Absa ensures that even in its traditional branches, staff are able to assist entry-level customers (usually in their home language).

***Technology coupled with human interaction key to the value proposition:***

Technology has played a critical role in enabling low-cost access to financial services. Capitec illustrates how a technology-driven business model can allow for the profitable extension of financial services to the entry-level market. The Incumbent banks followed such a model by implementing innovations such as smart ATMs (cash-accepting), self-servicing kiosk and mobile banking. However, the drive to substitute over the counter services with technological equivalents needs to be complemented with a human interaction component to ensure adoption. The banks have done this by complementing the increase in access-enabling technology with a human education component to ensure customer acceptance and usage.

***Introduction of ‘one-stop-shop’ to deliver full-service banking to the entry-level segment:***

While entry-level branches have succeeded in driving down costs by being cashless branches, banks have endeavoured to ensure that customers can still access cash. Most banks have situated cash-accepting ATMs outside of entry-level branches to allow customers to make cash deposits and withdrawals. FNB and Absa both have cash accepting ATMs at entry-level branches, as well as sales agents to assist customers in using these machines.

Some of the other players have developed a more fragmented approach. For example, Nedbank’s ‘hub-and-spoke’ model views alternative channels, such as kiosks within retail stores as complementary to a branch, and will have a branch, a personal loan centre and an in-store kiosk all located in close proximity so as to serve the local micro-market.

Standard Bank clients can utilise Access agents within their community, can perform basic transactions an AccessPoint or at an ATM, and they receive all other services they may require through an Access Banking Centre. African Bank has carve-outs within consumer durables stores to attract customers at the point of credit need.

### **8.3. CONSIDERATIONS GOING FORWARD**

While the Incumbent banks are gaining more of the entry-level customer base, the Disruptor banks are shifting upwards and repositioning their focus towards the middle market customer segment. We foresee more commonality and intensified competition where they meet in the middle. We expect the Disruptors to increasingly capture more of the middle-income segment, and continue to position themselves accordingly with regards to location, service and product provision. We anticipate the Incumbents to further expand and develop their distribution channels directed at the lower end of the income pyramid (while maintaining their presence in the upper-income segments). Finally, we anticipate seeing an increase in competition within the middle-income segment with regards to pricing and product.

We further expect that there will be greater usage of electronic channels as customers across income segments become more accepting of new technologies. However, as international case studies have shown, despite strong migration to electronic channels, customers (especially within the lower-income segment), will continue to require branches for face-to-face interaction with bank representatives, and as such entry-level branches will continue to play a strong role in providing financial access into the future.

Finally, we foresee banks extending their services to rural areas. Rural communities have low customer volumes and are more costly to serve, limiting the extension of entry-level bank branches thus far. Ubank is the only bank currently with the majority of its operations in rural areas. To access this market, Incumbents and Disruptors alike are introducing mobile offerings and identifying opportunities to partner with entities (retail or other) that have rural a footprint. How the banks service this market segment will ensure a further shift in the banking landscape in South Africa.