

CGAP-*MicroSave* Virtual Savings Exchange Report
“Serving Small Depositors: Meeting Demand while Managing Costs”
Summarized by Madeline Hirschland¹

Conducted from December 5th through 9th, the Virtual Savings Exchange examined some of the chief challenges involved in mobilizing small deposits: cost management, products, delivery, promotion, and environmental factors. This paper summarizes the key points made during the conference.

I. Cost Management

To manage the costs of deposit mobilization, an institution must attract an adequate volume of deposits and control its operating costs.²

A. Achieving Adequate Volume

Attracting a large volume of deposits requires a multifaceted approach. Institutions must generate trust (see Section IV); supply appropriate products (see Section II); utilize or create adequate delivery channels (see Section III), and train and motivate their staff to mobilize deposits (see Section IV).

Managing liquidity well requires specialized skills. Viable savings mobilization requires that a significant portion of these deposits be invested at a high rate of return. At the same time, the financial institution must maintain enough liquidity to meet the demand for withdrawals. In addition to mobilizing a large volume of deposits, a financial institution must determine the percentage of deposits that are "core deposits," stable deposits that can be made available for loans or other high-yielding investments. (See CGAP Bald case.)

B. Controlling Operating Costs

Most managers do not know the level of administrative costs associated with mobilizing savings. The most accurate way to determine these costs is Activity Based Costing (ABC). However, conducting ABC while launching savings products for the first time may not be feasible. Yet even without ABC, managers who grasp how staff use their time will gain a good understanding

¹ The Exchange was valuable because of the insights and expertise shared by its participants. This report summarizes their contributions. To them much appreciation is due: Adnan, Angela Arevalo, Philip Odei Asare, Noni Ayo, Joachim Bald, Anil Bhattacharya, Bhavani, Mark Bienstman, David Cracknell, Nara Hari Dhakal, Emma Fernandez, Cheryl Frankiewicz, Gaamaa, Zvi Galor, Manju Mary George, Mouna El Ghormli, Getaneh Gobezie, Marie-Luise Haberberger, Alfred Hamadziripi, Kamewe Hugues, Jennifer Isern, Saiful Islam, Ahmad Jazayeri, Dean S. Karlan, Brian Kuwik, Gerry Lab-oyan, Dale Lampe, Kathryn Larcombe, Elsa Patricia Manrique, Mike McKay, David Meier, Hermann Messan, Gabriel Metz, Peter Moelders, Claudia Mueller, Tony Pell, Greg Pirie, Ramakrishna, Ana Babi Santamaría, Hans Dieter Seibel, Namrata Sharma, Navraj Simkhada, Girija Srinivasan, Mark Staehle, Davide Stefanini, Paul Thornton, Nick Walden, Graham A. N. Wright, Zahari Zakaria, and Carolina Zuniga. The Exchange was facilitated by Madeline Hirschland.

² This framework comes from Dave Richardson from “The Keys to Cost Recovery,” by Richardson and Hirschland in Savings Services for the Poor: An Operational Guide (Kumarian Press: Bloomfield, CT) 2005.

of their costs. Monitoring key drivers—such as the number of transactions processed, the volume of cash deposited and withdrawn, or the number of accounts opened—is essential to managing the administrative costs. Some specific guidelines follow.

1. Financial Costs (and Revenues)

Interest rates should be set based on product costs, competition, and the following rules of thumb. An MFI should pay a higher interest rate on fixed deposits than commercial banks pay, but they can pay a bit less than competitors if potential customers value its product more highly. To motivate larger and longer-term deposits without requiring them, MFIs should only pay interest on accounts with balances over a certain amount and pay a higher rate for longer-term deposits. Setting strategic interest rate tiers can persuade clients to save more. Depending on how interest rate sensitive the market is, however, paying a somewhat higher interest rate might not affect deposit levels much, and might significantly reduce profits. MFIs would do well to learn from the mobile phone industry which has reached lower income clients by designing a variety of well-priced products (phone plans). In-kind returns such as lotteries or sales promotions can replace part of the interest rate. Beware, though. These can become a standard feature in the market, not providing a competitive advantage but pushing up costs for all institutions.

On the revenues side, fees can be charged for ATM withdrawals, debit cards, penalties, maintaining an account (“ledger fees”) and the like. These fees can offset costs and may even generate profits. Fees should be set such that customers perceive them as fair, and they are motivated to move from higher-cost to cheaper delivery channels.

2. Direct Administrative Costs

Attracting large- and small-balance depositors is an important key to lowering average costs. But the institution must be able to handle the impact on liquidity management, and the staff must be able to interact with both types of clients. Larger accounts are lower cost, but they are less stable than smaller ones. Term deposits are the hot money that's here today, gone tomorrow. They should be intermediated into micro-loans much more cautiously than the stable, core portion of demand deposits. Attracting larger depositors can lead to mission drift as institutions attempt to meet the expectations of higher-income clients (such as fancier accommodations), which raises costs and moves them away from servicing the small depositor.

Staff salaries and benefits represent the largest administrative cost. In particular, guards and security to move cash from the branches at the end of the day are costly which makes it difficult to extend services to rural areas. These costs can be lowered by having clearly defined performance standards and by using staff or volunteers with minimal education.

Digital and online devices can be cost-saving mechanism as well as improve security. However, these options carry large up-front costs and their benefits may be significantly reduced in areas where electricity and client technical literacy are minimal. Institutions must carefully weigh the costs and benefits of digital technology with reference to their client base.

Account dormancy is costly and can hide growing client dissatisfaction. Institutions can charge a regular ledger fee to deplete dormant accounts and motivate savers to close them.

3. Indirect Administrative Costs

Branch infrastructure is very costly and credit programmes that seek to mobilize deposits often must upgrade and relocate offices closer to clients. Rather than building branches, MFIs can serve savers in groups in the field. Or, rather than serving clients directly, MFIs can partner with established institutions such as postal banks, commercial banks, or mobile phone service providers to extend services to the micro market. Affiliation with a national or regional network, a partnership or a joint venture, or membership in a deposit insurance firm can also cut costs while reducing risk or perceived risk. In an uncompetitive market, costs can be kept extremely low by using small simple offices, limited hours, and one or two employees.

Other indirect expenses include management and management information systems. These costs can be reduced by decentralizing supervision, having a lean administration, offering just one or two products, and relying on word-of-mouth advertising. Computerized systems can be relatively cheap and provide essential benefits: timely and easily retrievable information that can be important to attract clients and to appropriately price and design services.

II. Savings Products and Product Mix

Before developing their product offerings or *product mix*, managers must first understand basic product types and variants from the perspective of clients and the institution. There are three basic product types. **Demand deposits** are often the most popular product, especially for small depositors. A minimum balance requirement and 0% interest rate can help with this product's high administrative costs. **Contractual products** respond to clients' need for a disciplined mechanism to save for specific goals and are easier for financial institutions to manage. Irregular payments can be allowed for a lower interest rate. **Term deposits** meet the demand of clients who seek a high return. They pay interest monthly or at maturity. Administrative costs are low.

There are a handful of common variations on these three types. **Retirement accounts** attract savers seeking an attractive return on long-term deposits. Funds are stable, administrative costs are low, and withdrawals are heavily penalized. A regular income can be provided instead of a lump sum payout. **Child, school and youth products** aim to develop customer loyalty and the habit of saving in children, and to attract parents to become clients. Required minimum balances must be low and prizes may be offered. Administrative costs are high. A "**step-up deposit**" is a single deposit product that allows for withdrawal but earns more interest the longer the deposit remains in the account. Because of its flexibility, it pays a lower interest rate than a fixed deposit.

A. Product Design

In order to be attractive, savings products must genuinely meet the needs and preferences of the majority of actual and potential clients. The key to understanding these needs and preferences is well-designed market research.

Poor clients require products that allow for small balances, irregular transactions, and the ability to withdraw funds. Allowing clients to open cashless accounts and giving them a month to meet the minimum balance requirement may make it more possible for these savers to open accounts. Fixed deposit products often have a high minimum balance that, de facto, excludes the poor. The poor may also want a fixed deposit product. Providing one need not be costly.

In countries that have experienced bank failures, people may have the legal right to claim even their term deposits back within one to two days. This limits banks but makes a highly flexible product unnecessary. In Eastern Europe, people are afraid of losing money and prefer products from which they can withdraw without much loss.

As they design products, managers should keep in mind these guidelines:

- **Keep it simple:** People who are not used to banking need easily-understood products.
- **Design for volume:** A good product may have massive uptake that is challenging to manage.
- **Design to manage costs while attracting demand:**
 - A minimum balance requirement can help manage costs (and can be low, e.g. US\$ 2).
 - A liquid product does not necessarily make the MFI's liquidity planning less certain.
 - Emergency access can be a key selling point for clients but may rarely be used.
 - Linking savings with access to loans or to insurance encourages clients to save more.
 - Clients value being able to name the person who receives savings in the event of death.
- **Make it unique:** An MFI will be able to compete with larger, more secure commercial banks only if its product is truly special and different.

B. Product Mix

Opinions differ on the product mix an institution should offer. Some practitioners suggest offering a few easy-to-explain products that balance costs and risk and that meet the demand of the majority of clients. (This might include one liquid and one semi-liquid product or a demand deposit and a fixed deposit with a variety of terms. A standard product can have features that vary slightly depending on the market segment. Indeed, some research has found that savers prefer a single product option to choosing between many.) Other practitioners argue that an institution must provide a wider range of products in order to compete with commercial banks. Of course, more product offerings can increase costs and demand more of management.

A solution may be to combine several products into one. Bundling products (such as demand deposits and payment cards) can encourage clients to use new products so long as it does not increase their costs. It can also be simpler for the institution to manage, but more complicated for clients. Furthermore, if a contractual and a demand deposit product are combined into one, clients who use this product to accumulate savings will subsidize those who use it to transact.

In any case, each product should be designed with care. Its unique selling proposition should be identified and discussed by focus groups before being adopted. Pilot testing should ensure that it is free from operational challenges and is priced correctly. Financial institutions should be prepared to continuously evolve their products to meet clients' changing needs.

The following tools can help managers determine and refine their institution's product mix:

- **Competition analysis:** Compare the product mix with the competition's products, pricing and delivery mechanisms.
- **Market segmentation:** Examine the size, volume of transactions, and dormancy of the existing accounts for each product. This understanding can help managers determine

appropriate interest rates, whether and what types of additional products might be in order, and how different products are being used.

- **Product costing:** Examine the cost drivers and profitability of different products. Managers should understand the costs associated with promoting, processing, and delivering products (as well as supporting staff incentive schemes) in order to understand which products are truly profitable.
- **Randomized control tests:** Determine which product features work best, for which type of clients, and why. (Normally, these tests are sponsored by donors rather than MFIs.)

III. Delivery Options ³

When it comes to savings, poor people typically want convenience—easy access and short queues. Many find the ambiance of banks intimidating and their branches too far away. For their part, banks often find serving small clients to be very costly. For these reasons, alternative delivery channels like those described below can be a key to serving the poor.

Doorstep collection: Doorstep collection is common in West and Central Africa and parts of Asia. In Africa, customers typically pay informal collectors a monthly fee for the service which provides relative safety, convenience and an opportunity to accumulate capital. Doorstep collection also serves the needs of women who cannot travel freely. Research in the Philippines found that doorstep collection increased savings.

At the same time, collecting deposits outside of a branch increases the risks of theft and fraud, and it is costly in terms of staff, vehicles, and monitoring. The risks can be reduced by instituting appropriate monitoring and reporting; requiring collectors to post fidelity bonds; providing stamps to the depositor in exchange for the deposit; paying for in-transit insurance; and taking steps to assure the safety of collectors. The high costs of doorstep collection can be managed by serving markets that are clustered together. Collectors may cost-effectively serve municipal markets and town centers by walking or bicycling there daily; for rural areas, bicycle visits weekly or monthly can be feasible.

Self-Managed Groups: For savers, self-managed groups provide a savings service with low transaction costs while generating loan capital and returns for the group rather than for a financial institution. However, group members may save much less than they would if they trusted that their savings and returns were safe and accessible. If they save primarily to access a loan, then the service is, in effect, compulsory.

By aggregating small savings into larger deposits, self-managed groups also cut costs to the financial institution. Once groups develop more savings than they can loan to their members, they may deposit the excess with an MFI if it has an attractive savings product. (In Zimbabwe and South Africa, this takes about a year.) The cost of promoting groups is very low, but MFIs have avoided this strategy because they see the groups as competitors when in fact, groups can serve as a financial entry point, grooming individuals until they are ready to use the MFI's services.

³ The framework for this discussion comes from Savings Services for the Poor: An Operational Guide, ed. Hirschland (Kumarian Press: Bloomfield, CT) 2005.

Lockboxes: These small locked boxes have a slot through which cash can be deposited but not withdrawn. The MFI staff hold the key while the box is kept by the client who can deposit any amount at any time. A deposit collector collects the savings regularly or the client brings the box to the branch when she wants. Lockboxes can also be distributed to children or their teachers.

Simple low-cost offices: Locating lean branches near town centers provides easy access to small savers and can be a cost-effective way for MFIs and banks to serve rural areas. Personnel from the nearest branch staff the offices for a couple of hours or a day each week. However, security, limited hours to access funds, and monitoring can be challenging.

Mobile banking units: Many banks have tested mobile banking units to serve areas where they do not have branches. The results have been mixed. As with simple part-time offices, security, limited hours, and monitoring can be challenging.

Piggybacking services onto postal savings banks: Many savings banks work through the post office infrastructure. Postal saving banks provide rural outreach, low minimum deposits, and account balances that suit the poor, as well as low administrative costs.

Piggybacking onto existing credit operations: Piggybacking savings services onto a credit service can lower deposit transaction costs to savers and the MFI. At the same time, MFIs' borrowers tend not to be the large depositors needed to lower average costs. Payments only might be "piggybacked"--deposits might be accepted at the same time as loan payments--or credit agents might also cross-sell savings products. However, even when credit agents receive considerable training, motivating them to mobilize deposits often proves to be quite difficult.

Electronic banking: In the long, run e-banking solutions will significantly reduce costs and extend outreach. But in many regions, it must first overcome two challenges: inadequate infrastructure and potential customers' lack of trust in electronic banking.

Point of service terminals: Financial institutions can vastly increase their outreach by providing services using POS terminals at retail outlets such as state lottery offices.

Mobile phone-based systems: Phones may be able to vastly extend outreach as far as the mobile network. Agents (usually the vendors of pre-paid airtime) would provide the deposit and withdrawal facilities. Pending issues include how to use public call offices and shared phones and how to make the service valuable for customers and agents.

Using local merchants: Local merchants might overcome the depositors' distrust of technology and the limits of ATMs, which often cannot accept small denominations and tattered bills. The financial institution would sell cards to merchants, who would resell them to clients. The merchant would then deposit the money in the bank physically, by mobile phone, or via the internet.

IV. Promotion ⁴

Promotion is not about making tall claims. It is about communicating strengths that the institution actually has, for it is small savers who can ill-afford to lose their savings who are to be converted into our clients. Promoting savings is different from promoting credit. MFIs must first promote the *habit* of savings before promoting the institution or products. Secondly, MFIs must focus on building trust

A. Keys to Building Trust

Trust is built on two pillars: the institution and the people who work for it. Branches must be perceived by potential clients as stable, professional, and secure. Establishing faith in the MFI can be achieved through mass media, but advertising is a costly strategy that makes sense only if the institution already has good market penetration.

Building a reputation based on staff requires personal promotion and excellent service. Proper training is critical. MFIs should invest at least as much time preparing employees as they would on “traditional” promotional tools like brochures. Staff should demonstrate that they care for their customers in speech and actions. Talking to staff should immediately bring to mind words like “honesty,” “integrity,” and “reliability” for the client. More subtly, clients must feel that the staff’s ethnicity and social class are familiar.

The following guidelines can help establish trust in the institution and the staff.

Deliver what you say you will deliver, consistently and reliably. Put key commitments in writing; advertise how those commitments have been met. Don’t promise what the institution cannot deliver.

Craft promotional messages to answer the question, "Why should clients trust us?"

Messages might include leadership, history, values, staff, supervision, systems, deposit insurance, or partners. Management should ensure that potential clients know that the institution is legally licensed, is monitored by the government, lends out savings locally, and has a good repayment record. Using clients' own words to convey these reasons will be more convincing.

Demonstrate that the institution is part of the community and plans to contribute to its development over the long haul. Rather than putting up a billboard, invest in the town square, sponsor a local sports team, organize volunteer opportunities for staff, or offer a scholarship. Participation in community events makes customers perceive banks as part of their daily lives. *Public relations* is often the least costly and most credible form of promotion, particularly if managers provide press releases about the action and the media is hungry for pre-packaged materials to broadcast or print.

Focus on developing strong positive word of mouth. At least 60% of the new customers to MFIs are from hearing about accounts from a friend or relative. Word of mouth is developed

⁴ Marketing and promotion are not the same. Promotion refers to advertising, personal selling, public relations, sales promotions and word of mouth. Marketing is bigger: it includes promotion but also includes product, pricing, and how and by whom the product is delivered.

through branding, a positive stream of public relations, customer relationship building, dinners with opinion leaders, keeping promises, and excellent service. For example, opening accounts must be as easy as possible; many sales are lost because of lengthy account opening processes. Customers will talk about good (and bad) experiences. In rural areas, informal leaders are important; when they become savings customers, the community will follow.

B. Market Segmentation

Managers must understand the market segments they expect to serve: what they save for; what promotional tools, media and types of messages they respond to; and the financial value of their potential savings. This understanding will help in tailoring appropriate messages that sell the product's benefits according to the needs of specific groups of clients. By segmenting clients, IMFs can promote to them more appropriately.

Segmenting the market often will drive promotional strategies. If 5% of clients are found to hold 50% of value of deposits, using branch managers to sell to high-value clients might make sense. Small or rural savers may value personalized service, a positive relationship with the public, and word of mouth while large savers may respond more to advertisements, publicity and promotional gimmicks. Current loan clients may respond more to direct sales than to advertising, publicity, or branding.

C. The Promotional Message

Promotional communications should reflect the key value drivers of the customer in "clear, concise, client language." Promoting a savings culture and a corporate image closely related to local life is a key to success. Promotion should always sell the product's benefits for the clients, not the product's features. Prior to mass-printing, the unique selling proposition and message should be tested in focus groups to ensure they are valued and understood in the way that management wants them to be.

D. Staff and Promotion

Promotion is not just advertising. In the early days of a savings program, direct marketing should play a central role. In institutions that have primarily been engaged in credit, savings promotion may initially be carried out by credit agents, cashiers, and customer service staff. In any case, all staff must be trained in how to promote savings, should be involved in promotion, and should understand the local culture and community. They must grasp the importance of attracting people who will save more than they borrow; they must learn how to identify these people, particularly community leaders; and they must be able to find opportunities to mobilize a large number of deposits in one place (such as at a factory or place of worship). They must also be able to explain a savings product clearly, in terms that differentiate it from those of competitors.

Staff will mobilize more deposits if management charges branches a higher rate for capital than the interest rate paid for client savings; clearly defines performance standards; and has a well-designed incentive scheme. But incentive systems can have negative effects. If incentives are linked to deposit volume, staff may pressure clients unduly to deposit or not withdraw or clients may not trust that the staff are sincere about the solidity of the institution. Incentive schemes for savings should reward branches rather than individuals.

Even with considerable training and incentives, motivating credit staff to mobilize deposits can be quite difficult. Employing low-cost marketing officers (such as university leavers on a contract) may make more sense. In addition, branch managers might market services to high-value clients and in places where they can talk to many potential depositors at the same time.

Cross-selling can broaden the client relationship to the benefit of both the client and the financial institution. Clients can access more services while the institution generates more business. In addition, customers who use more services are more likely to be loyal and keeping a client costs much less than attracting a new one. Banks cross-sell savings products when they arrange to automatically deposit a part of a regular remittance payment into a savings account.

V. Environmental Factors ¹

The environmental factors that most strikingly affect the mobilization of small deposits are government regulation; policies that affect the financial sector; the state of the country's infrastructure; and the economic and political environment.

A. Government Regulation and Supervision

Lack of oversight can provide institutions with the flexibility to optimize their operations, but unregulated MFIs may fail to adopt prudent liquidity management practices, may not know how, or may be fraudulent. And when these institutions fail, it affects the entire industry by dissuading potential clients from saving with formal institutions.

Regulations may result in more limited outreach, especially to small and rural depositors, at the same time as they result in greater stability to depositors who are served. For example,

- High capital adequacy and liquidity reserve requirements increase costs and make it more difficult to serve small depositors and to branch out to rural areas. On the other hand, these requirements force MFIs to be serious, which is good for depositors.
- Requiring new institutions to have all key functions and management in place from day one can prevent new institutions from entering the market. However, requiring that suitably qualified personnel manage and oversee financial institutions is a plus for depositors.
- Regulatory requirements on infrastructure—particularly security-related infrastructure--can be extremely expensive. But being regulated also conveys trustworthiness, which can attract large institutional deposits that help compensate for the additional costs.
- In some countries, how an NGO-MFI can transform into an institution that is legally able to mobilize deposits is unclear. Often, it is the organizations that reach the poor or rural areas that cannot legally mobilize savings or can do so only from their members.

Some countermeasures to increase the security of unregulated or under-supervised institutions include affiliation with a regional, national or international network; supervision by a credible larger institution; and education of savers so that they can select institutions where their money will be safer.

B. Governmental Policies

Anti-money laundering legislation can exclude low-income clients from financial services. Complying with identification and confirmation of residence requirements can be challenging for customers without electricity or water bills, and it can increase the cost to clients and institutions of opening an account. Deposit insurance may not stimulate a great increase in deposits but may encourage institutions to pass their risk on to insurance companies rather than vigilantly controlling it. Government-mandated caps on interest rates may not provide MFIs with a viable operating spread (one large enough to cover the high costs of administering small deposits and loans). Finally, widely available subsidized credit undermines savings mobilization because institutions will mobilize deposits only if this source of funds costs less than others.

C. Infrastructure

Infrastructure affects outreach, particularly to rural areas. Poor rural telecommunications, lack of electricity and internet service, and poor rural roads raise costs and inhibit the growth of the industry, in particular e-banking. Clients must be able to reach the nearest service outlet within a reasonable amount of time. Operating the MIS in stand alone rather than networked branches limits services but allows branches to continue to provide basic services when the "coms go down." Without a centralized clearing system for MFIs, clients spend a lot more time accessing their checking accounts.

As e-banking develops, it will pose additional policy and regulatory challenges in a number of areas including communications policies, infrastructure, and the definition of roles such as that of a deposit taker (i.e., the person who can accept a deposit on behalf of a bank or MFI).

D. Economic and Political Factors

Political and economic instability undermine clients' trust and dampens savings mobilization. In a conflict environment, MFIs adopt coping strategies to survive rather than finding ways to expand their outreach and maintain their viability. Inflation, in particular, undermines savings mobilization because it undermines the value of financial savings. To some extent, this can be controlled by an inflation targeting system. High-yielding investment opportunities are crucial: savings operations can expand viably only if the MFI can invest the savings mobilized at a relatively high rate of return.

Where the economy is tied primarily to one seasonal cash crop, MFIs will struggle with liquidity management. On the other hand, a stable and growing economy coupled with equitable and sustainable rural development results in households and enterprises that can save.