PERCEIVED EFFECT OF AGENCY BANKING MODEL ON PERFORMANCE OF COMMERCIAL BANKS: A CASE OF EQUITY BANK LIMITED, KENYA

BY

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ABSTRACT

Agency banking is delivery of financial services outside convectional bank branches; through non-bank retail outlets, that rely on such technology as point of sale devices or mobile phones for real time transaction process. Having been implemented with varying degrees of success by a number of developing countries, particularly in Latin and Brazil, it has also been employed by financial institutions in Kenya to provide 'real-time' service to existing customers so as to enhance profitability through increased customer base and efficiency in service providence. However some of the banking institutions which have employed this concept continue to witness long queues in the banking halls, high level of dormancy of accounts while the bank's services have been brought right at the customers' door step. It is yet to be known the level the impact of agency banking on the bank's performance. The purpose of this study was therefore to determine the effect of agency banking model on performance of commercial banks in Western region. Specifically the study sought to: Establish the level of agency banking by Equity bank in Western Kenya branches; determine the relationship between agency banking cost and profitability of Equity Bank Limited; determine the relationship between agency banking risk and the customer base of Equity Bank Limited and determine the relationship between agency banking policy on the bank and its performance. The study was anchored on conceptualized framework. A descriptive survey design guided the study. A Census survey was employed. The study used both primary and secondary data. Validity and reliability of these instruments was checked using expert review and Cronbach's Alpha respectively (alpha =0.789). Data was analyzed using regression analysis. The study revealed that: the level of agency banking by equity bank agents was established at 74.07%; agency banking cost revealed a positive significant association on the profitability of Equity Bank Limited ($b=0.710$, $r=0.183$, $t=6.72$, $p<0.05$); the level of risk involved in agency banking had negative and significant effect on the customer base of the bank($b=-0.407$,$r=-0.267$,$t-0.950$, $p<0.05$) and the relationship between agency banking policy and bank performance indicated a moderate positive association($b=0.490$,$r=0.660$,$t=1.060$, $p<0.05$). It is imperative for the bank branches to participate in the agent recruitment process so that the banks can leverage existing relationships that branches have established. There is need for the banks to train their agents in making correct transactions and enforcement of anti-money laundering standards. The agents should secure operating systems capable of carrying out real time transactions, generating an audit trail, and protecting data confidentiality and integrity to mitigate on the agency banking risks. The study is expected to be of help to commercial bank policy makers in identifying the key challenges involved in agent banking operations and coming up with strategies that will improve performance.

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CHAPTER ONE

INTRODUCTION

This chapter introduces the background of the study, statement of the problem, objectives, hypothesis, research questions, scope and justification of the study.

1.1 Background for the Study

An agency refers to the relationship between two parties, where one is a principal and the other is an agent who represents the principal in transactions with a third party. Agency banking is a process whereby a second person; in most cases business people, works on behalf of the bank for an agreed benefit; thus there is a principle -agent relationship between the banks and the business people (Pandey, 2009). It is therefore the delivery of financial services outside convectional bank branches, often using non-bank retail outlets that rely on technology such as point of sale devices or mobile phone for real time transaction process. This is an abridged financial service mechanism that should enhance operational profitability of the financial institutions.

According to Layman, Mark and David. (2011), financial services can only be delivered to a majority of households if the service providers (banks) use retail distribution channels to get closer to where the poor live and at a fraction of the cost of traditional banking. Through agency banking, financial institutions are able to decongest the crowded branches by offering the services conveniently in the neighbourhood (Kitaka, 2001). Provision of these services by agents eliminates the need for commercial banks from having branches all over which are more cost effective as compared to banks establishing physical branches. Alliance for Financial Inclusion

(2008) states that currently, agency banking model is an integral part of modern banking in many African countries including Kenya. It is geared to help financial institutions like Equity Bank Limited divert existing customers from crowded branches by providing a more convenient channel of accessing bank services. Alliance for Financial Inclusion (2008)) further states that agency banking is quickly becoming recognised as a viable strategy in many countries. It has been adopted and implemented with varying degrees of success by a number of developing countries particular Latin and Brazil. Brazil is often recognised as a global pioneer in this area since it adopted the model earlier and over the years has developed a mature network of agent banks covering more than 99% of countries municipalities.

Kitaka (2001) further notes that equity bank had the largest customer base in Kenya, with over 5.7 million accounts in October 2010. This means there is still a big mass of Kenyans who are yet to be banked. To deal with the above challenges Safaricom come up with the first agency model called MPESA then followed with different banks coming up with their own agency model .This has brought about banking revolution in Kenya. In February 2011, the Central Bank of Kenya (CBK) released regulations to govern a new agency banking model. The regulations allow banks to offer services through third party agents approved by the Central Bank of Kenya (CBK). Agents can be Telco-outlets, SMEs, retail chains, savings and credit co-operatives (SACCOs), or even 'dukas' (corner shops) .It essentially incorporate any profit-making entity that has been in business for at least 18 months and can afford to fund a float account to facilitate payments.

Kitaka (2001), expresses further that the contribution of commercial banks to the development of Kenyan economy is of great importance for instance in the year 2011 the commercial banks advanced up to Ksh.220 billion to private businesses, Parastatals and other public entities receiving up to Kshs 28 billion. In Kenya today, commercial banks are not only worried about the safety of their funds and increase in returns on their investments but also customers demand on efficiency, fast and convenient services. Customers want a commercial bank that will offer them services that will meet their particular needs and support their business goals. They want to be able to check their balance online, find out if a cheque is cleared, and transfer funds within accounts and even access banking services via agents. The use of retail agents also potentially raises special concerns regarding consumer protection and compliance with rules for combating money laundering and financing of terrorism Duan, (1992). It is therefore important to establish how safe the customers are in the hands of the agents by analysing customers' attitude to the service they are given at the agent point. Equity Bank Limited, a leading bank in terms of customer base and use of agency banking model, has been on the fore front in rolling out its strategies to enhance customer efficiency .On the contrary, even with introduction of agency banking model, the bank has continued to witness long queues in its banking halls resulting in low service efficiency to its customers.

Agency banking has become the trend in African countries, for example, Uganda, Nigeria and Kenya. The number of bank branches in Kenya has tremendously increased in the recent years. Over the same period, the number of ATMs deployed has soared from an insignificant number to reach more than 1400 (Financial Sector Deepening Kenya, 2010). Kitaka (2001) further argues that as banks continue to invest in rolling out the branches that are complimented by various

delivery channels, the challenge of access to formal financial services remains a big impediment to financial inclusions. Kenyans are forced to travel long distances and spend huge amounts on transport in order to access a branch.

An important starting point for mobile banking in Kenya was the launch of MPESA in 2007. This service started off as money transferring system created by the worldwide cell phone provider Vodafone and its Kenyan affiliate Safaricom. In 2011 the service had roughly 15.2 million national users (almost 40% of the adult population) and about 30 000 agents throughout Kenya. One explanation for its huge success is the way the system is integrating with the formal financial sector as many commercial banks as well as other formal institutions provide their services using M-PESA as a channel. The possibilities with M-PESA have therefore widened and the system now includes all services covered in financial inclusion, namely remittances, credit, savings and even insurance. Another important contributor to the transforming financial landscape is agent banking, allowing institutions to hire agents to provide a wider customer base. Due to strong competition amongst commercial banks, actors within the formal sector is now realizing the benefits from adopting new ways of delivering their services so that even the low-income and rural individuals can access them (FSD, 2012).

According to the governor of the CBK (CBK, 2010) the traditional banking methods, limited reach of people to the bank branches located mainly in highly populous towns. Sections of population have been left out of the formal financial sector, for the mere reason that they are not located in densely populated areas. Such population has been left out and as a way to address this exclusion; the government through the CBK has come up with agency banking. Agent banking

increases the reach of banks to the people from the traditional branch network which is limited in growth by several factors such as the cost including the staffing costs and other costs which when compared to the benefits that is, the cost benefit analysis of setting up branches in such areas is negative. Agency banking is expected to be the solution to this problem since banks will expand rapidly riding on the infrastructure and manpower of third parties (CBK, 2010).

For the last one decade, the banking environment in Kenya has been very dynamic. There has been a shift from stable, non-volatile and predictable business environment to one which is quite volatile, unpredictable and competitive. Up to the very late 1990's, many banks in Kenya enjoyed unchallenged monopolies and government protection (Kaskende, 2008).

Manzano and mandrille (2010), states that Policymakers and regulators have been facing the challenge to reconcile a safe development of branchless banking operations with increased levels of financial access, Lyman *et al* (2006) indicate that protecting client funds is priority for many financial regulators, as loss of funds can have serious consequences for customers, as well as for public confidence in financial systems. Banks are usually required to comply with prudential rules created to ensure systematic stability and depositor protection. Therefore it is important to demonstrate the relevance of the agency banking policy on the performance of the banks; by analyzing the ability of the Bank's regulatory to control the performance of the bank.

CBK (2013) reports that there are 10,066 active agents in the east Africa nation .The agents contracted by eight banks made transaction worth 762 million dollars in the period. Leading in the number of agents was Equity Bank with over 3234 agents, then Kenya Commercial Bank

with over 2600 and Co-operative Bank with about 1800 agents. Property Kenya, 2012 further stated that an estimated 1.1 million Kenyans have opened new banking accounts in the past three months, pointing to early success of the new agency banking model and strengthening economic growth which has increased employment opportunities and people's disposable incomes. CBK, 2013) further shows the number of deposit accounts rose from 10 million in the second quarter to 11.1 million as at end of September. It is therefore important to establish how cost effective the agency model is to the banks; by analysing the operational cost of the agency and the reported banks profit.

Regulators want to achieve financial inclusion through a profitable, low cost delivery model that simultaneously protects consumer and the integrity of financial service. As agency banking becomes even more spread, it will reduce foot halls within branches and enable them to focus on delivery advice and premium service (Jayanty, 2012).This creates a need to demonstrate the extent to which the commercial banks have invested and continued to participate in agency banking in Kenya by analysing agency banking membership over the study time.

1.1.1 Profile of Equity Bank Limited

Equity Bank Ltd is a Kenya-based bank engaged in the provision of retail banking, microfinance, and related services to individuals, and small and medium sized enterprises in Kenya, Uganda, southern Sudan, and Rwanda. It offers various banking products, including current, equity ordinary, super junior investment, Jijenge, equity business and current accounts, and call and fixed deposit accounts; and business and development loans, agricultural loans, working capital loans, educational loans, medical loans, salary advances, equiloans, asset finance and insurance premium finance, shares finance loans, and Fanikisha loans. The Company also provides various

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services comprising banker's checks, standing order and remittance processing, among other. In addition, it offers trade finance services, such as letters of credit, documentary collections, guarantees and invoice discounting, among other. The bank's brand has also continued to strengthen resulting in the bank attracting more customers and transactions. The continued roll out of the agency banking in 2012 has seen the number of agents grow to 5,004 from 2,301 as at June 2011 which represents a growth of 117%. The bank agency network is processing 25% of all cash transactions and this has enhanced access by the customers to the bank's products and services and also enhanced convenience.

1.2 Statement of the Problem

Agency banking has been in place for the last three years with only few banks embracing the idea. For those banks that have officially launched agency banking initiative, the number and dispersion of agents has not been that wide and penetrative. It has been observed that commercial banks, microfinance institutions and other financial institutions establish branches in urban centers leaving out the rural areas which exclude a significant population from accessing financial services. This has been mitigated by agency banking which is being used by banks to take these services to the unbanked and under banked regions. Agency banking takes customers out of the banking halls to kiosks and villages in their neighborhood with an expected improvement on yield economic growth due to increased access to financial services by eliminating barriers of access, time and cost. However the banks are still crowded with long queues. The banks therefore still spends a lot of time serving these retail customers who could easily get the basic bank services from agents and allow banks to have more time to deal with their high net worth clients and SMEs. The inconsistency between the expected reduction in the

queues and the actual observation of the constant crowds in the bank halls seem to reveal insufficient realization from expectation which requires attention. Some of agent operators are highly unreliable: they are not fully operational or closed most of the time and those whose doors are open, some only concentrate on their businesses and turn away customers to seek the banking services elsewhere since their agency rarely operates. It is in light of the above factors that the researcher intends to establish the effects of agency banking model to the performance of commercial banks in Kenya.

1.3 Objective of the Study

The broad objective of this study was to determine the effect of agency banking model on performance of commercial banks in Kenya.

The specific objectives were to:

1. Establish the level of agency banking by Equity Bank in the Western Kenya branches.
2. Determine the relationship between agency banking cost and profitability of Equity Bank Limited, Western Kenya
3. Determine the relationship between agency banking risk and the customer base of Equity Bank Limited, Western Kenya
4. Determine the relationship between agency banking policy and Equity bank western Kenya,s performance.

1.4. Research Questions

The study sought to answer the following research questions:

1. What is the level of agency banking by Equity Bank in the Western Kenya branches?

2. What is the relationship between agency banking cost and the performance of Equity Bank Limited in Western Kenya?
3. What is the effect of agency banking risk on the customer base in Equity Bank limited in Western Kenya?
4. What is the relationship between agency banking policy regulation on the performance of Equity Bank Limited?

1.5 Significance of the Study

The study is likely to form a vital contribution to the existing knowledge in the area of agency banking .This in turn contributes to the well- being of the financial sector of the economy and the society as a whole. Therefore, the major beneficiaries from this study are commercial banks, regulatory bodies, the academia and the society as a whole in the country.

1.6 Scope of the Study

Banks are distributed all over the country but due finance and time constraints the study concentrated only on Equity Bank Limited branches in Western region. The research was conducted in all the eight branches in Western region. The study was restricted to agency banking model and performance of Equity Bank Limited .This is because Equity Bank Limited is one of the pioneer banks to start this Agency banking model.

1.7 CONCEPTUAL FRAMEWORK

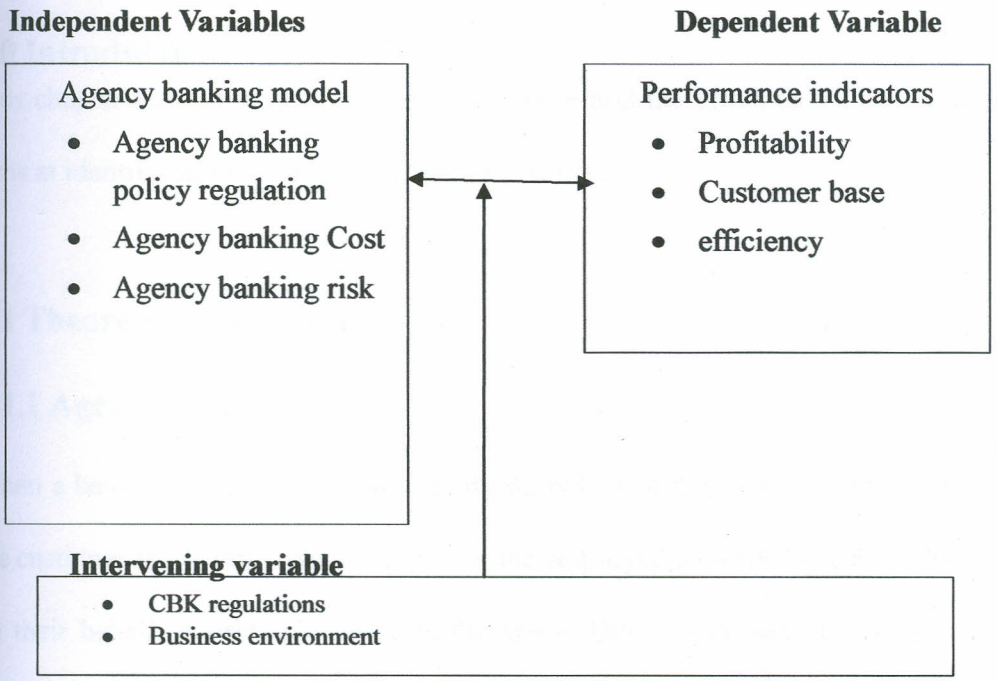

Figure 1.1: Conceptual Model Showing Interaction of Agency Banking Model and Bank's Performance

Source: Self conceptualisation, 2013

The study was anchored on a conceptual framework in Figure 1.1 that shows the interaction between agency banking model and performance. It further indicates external elements which may influence the performance of the bank such as CBK regulators and business environment. It further depicts agency banking model as independent variable with three elements namely: agency banking policy regulation, agency banking cost, agency banking risk and dependent variable with three dimensions namely profitability, customer base and efficiency.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter aims at reviewing related literature and the previous studies on agency banking. It aims at identifying knowledge gaps of these studies.

2.1 Theoretical Literature

2.1.1 Agency Theory

When a bank is dealing with a third party on behalf of the customer, the bank is an Agent while the customer is the Principal. An agent is one employed to work for a Principal to make contracts on their behalf. A principle instructs the agent. Other examples of principal agent relationship between bank and customer are when the banks arrange for insurance, sends money either abroad or within the country on behalf of the customer. Agency banking is another example of Principal agent relationship between bank and customer (Pandey, 2009). Jensen and Meckling (2009) concur by describing an agency relationship as a contract (implicit or explicit) in which one or more persons, the principal(s) engage another person, the agents, to take actions on their behalf. It thus involves delegation of some decision making authority to the agent. It is taken as unquestionable that an informed principal can benefit from this delegation to an informed agent and that it is in fact optimal for an uninformed principal to do so give their lack of skills, knowledge and experience.

2.1.2 Level of Agency Banking in Kenya

Layer, (2011) says that banks use approximately 160,000 agents-many with multiple outlets to provide financial services to all 5,564 Brazilian municipalities. In 2010, bank agents in Brazil handled 3.1 billion transaction (6% of all transaction), 2.85 billion in which involved the movement of funds .As recently as 2009, just 23% of Kenyan adults had access to formal financial services. Financial inclusion has risen in recent years, with aggressive expansion by Kenyan banks. Kenya now has 1,072 retail bank branches, up from 534 in 2005. Several factors have driven service expansion: the recovery of the Kenyan economy since 2003, advances in technology that support the administration of a large number of small bank accounts; and the wildfire spread of mobile money services through Safaricom's M-PESA that created a dual dynamic of both competition and co-operation with the banking sector (Keller, 2011).

In 2009, the Central Bank of Kenya (CBK) commenced measures to open up banking channels to non-bank agents. An amendment to the Banking Act (passed as part of the Finance Act 2009) allowed banks to start using agents to deliver financial services. Using small shops, petrol stations, pharmacies and other retail outputs as agents could have a dramatic impact on improving access to financial services, especially in rural areas. Bankele (2009), states that the sub-text of M-kesho and other variants is the emergence of agency banking in Kenya, a process endorsed by the Government of Kenya to bring more banking services to more of the (unbanked) population. Bankele further states Agency banking is supposed to take customers out of the bank halls and out to kiosks and villages. Waithanji (2012) asserts that agency banking has enabled bank customers to access the basic banking services, for example, cash deposit, cash withdrawal and bank balance inquiry conveniently or what would be termed as within the comfort of their neighbour-hood. The convenience of access to banking services and the extended hours that the

agencies work has been the most attractive features to the customer as most agencies work between 8am up to 8pm. The rural population has heartily welcomed this idea since they have had to sometimes go through Vexing experiences to access banking services due to the poor road infrastructure and high costs. It's imperative to take into consideration the fact that the size of the financial institution determines the approach that it takes. Small Banks may need to use agents and agency banking in Kenya to grow their customer base whereas Large Banks will focus on driving transaction volumes.

To achieve loyalty, a product or service must be beyond achieving visibility and differentiation. It should instead develop deep relationships with the entrepreneurs to a point where the brand becomes a meaningful part of the customer's life and or self-concept and when this occurs the customer was highly loyal (Atman, 1993). Thus, brand loyalty is at the core of relationship banking, which goes beyond traditional banking and focuses more on creating a pool of committed, profitable entrepreneurs. A successful brand aims to develop high quality relationship in which entrepreneurs feel a sense of commitment and belonging. Relationship banking aims at developing long-term entrepreneurs (Kitaka, 2001).According to Waithuka 2012, banking agents have become the backbone of banking, performing transactions over a bank device, which is most often a banking gadget. To enable clients to convert cash into electronic money and vice versa which send can be sent over their banking agent, clients will have to visit a branch, banking agent. Specifically, in remote and rural locations, where cash is still the most important way to pay and transact, a bank banking service is dependent on banking agents to enable clients to effectively use the service. Regulators want to achieve financial inclusion through a profitable, low cost delivery model that simultaneously protects consumer and the integrity of financial

service. As agency banking becomes even more spread, it will reduce foot halls within branches and enable them to focus on delivery advice and premium service (Sai jayanty, 2012) It is therefore important to demonstrate the extent to which the commercial banks have invested and continued to participate in agency banking in Kenya by analysing agency banking membership over the study time.

2.1.3 Agency Banking Cost and the Profitability of Banks

Profitability is the measure of the difference between revenue generates and the costs .That is the revenue a company derives from its operations, less all explicit costs (Gupta and Collins, 1997). Sangmi and Nazir (2010) state that capital adequacy is a reflection of the inner strength of a bank, which would stand it in good stead during times of crisis. Capital adequacy may have a bearing on the overall performance of a bank, like opening a branch, fresh lending in high risk but profitable areas. Kiragu *et al* (2012) argues that higher income generally reflects a lack of financial difficulties and so would be expected to reduce the likelihood of failure of a bank. They further state that liquid assets enable a bank to respond quickly to unexpected demands for cash and typically reflect relatively conservative financial strategies impose high interest expenses and are subject to quick withdrawal as a result we expect higher investment securities to reduce the chance of failure, whereas higher values of large certificate of deposit should increase the probability of failure. Sangria and Nazir (2010) further states the liquidity of the bank is what the blood is to human body. The bank should be in a position to meet its liability holders as a when demands arises. Thus the appropriate mixture of liquid and non-liquid asset is maintained.

Muriuki (2010) argues that through the introduction of agency banking has recorded different results on their profit and customers have continued to demand for the better services Banks have

therefore expanded on the range of products and services they offer to their customers at a low cost of expenditure through introduction of alternate channels such as ATM, POS, mobile banking and internet banking. However, developing a precise and realistic estimate of profitability necessarily requires understanding the drivers of profitability. Unfortunately, it is not easy to estimate agent profitability. While revenue calculation is straight forward, estimating the real costs associated with the business is more complex. Revenue can be fairly easily derived from the standard commission structure and transaction data, a record that most agents maintain. The transaction records are also easily retrievable from the servers of the bank. However, when it comes to the cost items, most agents do not record expenses incurred in conducting banking business. A good example of this is travel expense, incurred mostly in trips to banks to rebalance e-float/cash positions, which is a key cost driver for an agent with sizable banking transactions and making frequent trips to the bank. Most agents operate multiple business lines and this further complicates the calculation as many costs are shared among the business lines. These costs include rent, electricity. All these factors transform a simple task of calculating profitability into a challenging exercise of gathering precise data and identifying appropriate costing procedures to allocate the shared costs. Most agents operate multiple business lines and this further complicates the calculation as many costs are shared among the business lines. These costs include rent, electricity etc. All these factors transform a simple task of calculating profitability into a challenging exercise of gathering precise data and identifying appropriate costing procedures to allocate the shared costs.

Kitaka (2001) indicates that the cost and revenue estimation is done on a per account basis for transactional accounts, commitment savings accounts, reverse commitment accounts, and time

deposits. It focuses on the costs and revenues incurred by the financial agent bank associated with account opening, financial margin, and transactions for low-cost accounts. The revenue assumptions are based on a view that financial agent banks can and should charge for withdrawals and transfers through agent channels. Although some institutions in the sample do not, we contend that this may be counterproductive when reaching new low-income markets where entrepreneurs have a higher willingness to pay for nearby transaction services and where the financial margin earned on lower-balance accounts was insufficient to cover the cost of maintaining that account. We envision that clients will transact more with greater proximity to agents.

CBK (2010) notes that various banks have already invested in new core banking systems. This new systems are expected to facilitate centralization of operations, staff rationalization and support new technological products such as internet and mobile banking. Agency banking has helped to bring some banking services to rural areas. The prohibitive costs of setting up branches and ATMs vis-à-vis the expected returns have been a disincentive for banks to roll out their services in rural areas, but agency banking has provided an avenue to these markets at limited cost. Although some rural customers still have to travel some distance to branches for services that agents can't deliver, basic transactions are far more readily available

Mylenko (2008) further argues that agency banking represents a significant opportunity to reduce transaction costs such as travel for clients by bringing financial services to hard-to-reach and geographically dispersed areas. Banks and other financial institutions often do not have sufficient incentive or capacity to establish formal branches in these areas. The set-up of agency banks is

less costly and more flexible than for traditional bank branches: it reduces the need to invest in staff and physical infrastructure. The cost for establishing an agent is far cheaper than the one for establishing a branch. Additionally it brings banking to the door step of Kenyan citizen. By Central Bank of Kenya (CBK) encouraging establishment of agents will enable Kenyans to actually walk in the path of actualization of vision 2030.It is therefore important to establish how cost effective agency banking model is

As stated in the equity bank intranet of July 26, 2012, on regional banking group; Equity Bank continued to maintain its growth momentum with the profit before tax growing by 29% to close at Kshs. 7.62 billion in the six month period ending June 30th 2012 despite the challenging micro-economic environment characterized by high inflation, interest rates hikes and foreign exchange volatility. This is due to the rise in total income by 34% from Ksh 13.15 billion to Kshs. 17.56 billion mainly driven by the growth in the loans and advances, as well as prudent cost management measures. During the period under review, Equity Bank Group's loan book grew by 27% from Ksh 97.7 billion to Ksh 124.4 billion. Total assets grew by 29% from Ksh 171 billion to Ksh 220 billion compared to June 2011. Customer deposits also grew significantly by 22% from Ksh124 billion to Ksh151 billion. This is mainly attributed to the growth in customer numbers which increased from 6.3 million to 7.8 million. This growth is also as a result of innovative use of alternative delivery channels such as agents and the bank's mobile banking platform popularly known as Eazzy 247.

Karimi (2011) argues the growth in account holders' numbers increased total deposits by Sh600 million to Sh1.27 trillion in the three-month period. Bankers interviewed by Business Daily said

growth in the sector has picked up momentum, mainly driven by strengthening economic recovery and the new agency banking model that is riding on mobile banking platforms such as Equity Bank's M-Kesho, in partnership with Safaricom. The CBK report (2011) therefore reveals that the commercial banks opened 13 new branches in the third quarter alone; raising the total branch network to 1,030. This has helped tap deposits from previously un-banked areas. By end of September, CBK had approved 5,892 agents of which 4,392 are telecoms related while 1,500 comprise other types of enterprises. Although agency banking incurs higher variable costs from commissions to agents and communications, fixed costs per transaction for branches are significantly higher. Kitaka, (2001) further points out that setting up a banking agent costs two percent to four percent less of the cost of a branch cashier. At maximum capacity, a branch cashier incurs more than eighty three percent in fixed costs per transaction, compared to just eleven percent for a POS-enabled agent and percent or for a bank-enabled agent or bank wallet. It has been established acquisition costs are lower for bank-enabled agents and bank wallets.

2.1.4 Agency Banking Risk and Customer Base of Banks

Lyman and Stschem (2006) indicate that protecting client funds is priority for many financial regulators, as loss of funds can have serious consequences for customers, as well as for public confidence in financial systems. Banks are usually required to comply with prudential rules created to ensure systematic stability and depositor protection. Bank deposits also are covered by insurance in many jurisdictions. In addition, governments may provide an implicit guarantee to bank depositors, especially when banks are systematically important. However, in emerging branchless banking models, nonbanks may collect funds in exchange for electronically stored value, without being subject to the full range of prudential rules imposed on banks.

Mylenko (2008) states that risks Involved in branchless banking can be broadly classified into Agent-Related and E-Money Risks. Agents Related Risks are common to all transformational models and arise from substantial outsourcing of customer contact to retail agents, who may be operating in hard-to reach or dangerous areas, lack physical security systems and specially trained personnel. When retail agents are used to provide banking services, five of typical banking risk categories—credit, operational, legal, liquidity and reputational take on special importance beside elevated concerns regarding consumer protection and compliance with rules for AML/CFT. E-Money Risks are typical to Nonbank-Led model and relate to imprudent management of repayable deposits collected from retail customers by Non-bank entities that are not subjected to prudential regulation and supervision .Agents Related Risks arise from substantial outsourcing of customer contact to retail agents. From a typical banking regulator's perspective, entrusting retail customer contact to the types of retail agents used in both the bank-led and nonbank-led models would seem riskier than these same functions in the hands of bank tellers in a conventional bank branch. These retail agents may operate in hard-to reach or dangerous areas & they lack physical security systems and specially trained personnel. The lack of expert training may seem a particular problem if retail agents' functions range beyond the cash-in/cash-out transactions of typical bank tellers to include a role in credit decisions

Banking regulation typically recognizes multiple categories of risk that bank regulators and supervisors seek to mitigate. Five of these risk categories—credit risk, operational risk, legal risk, liquidity risk, and reputation risk—take on special importance when customers use retail agents rather than bank branches to access banking services. The use of retail agents also

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potentially raises special concerns regarding consumer protection and compliance with rules for combating money laundering and financing of terrorism. E-Money Risks relates to acceptance of repayable funds from retail customers by Non-Bank entities that are not subjected to prudential regulation and supervision. Risk is that an unlicensed, unsupervised Non-Bank will collect repayable funds from the public in exchange for e-money and will either steal these funds or will use them imprudently, resulting in insolvency and the inability to honour customers' claims (Duan,1992).

In countries where banking model has been successfully implemented, regulators and supervisors have addressed the potential risks of using a large number of agents to deliver financial services by adopting a risk-based approach to supervision where agents are supervised indirectly and banks must assume full responsibility for their agents (Kasekende, 2008). Banks have ensured that the clients' money is secure by sending an alert after every transaction done. These transaction alerts are generated by the Bank and hence confirm that the agent has processed the transaction successfully. Banks are secured by armed policemen and have stated measures of security .The agents are a bit compromised being that people believe they have a lot of money; for they are considered small banks .One of the measures bank has put in place is to have the agents insure their stock and their money (Waithuka, 2012).

Opm (2009) states that agency is still a new thing in the Kenyan banking sector thus there is still many loophole regarding the risk involved to the three parties. Central Bank of Kenya and the local branches are working day and night to protect their clients and the agents from fraudster of every manner. It is further stated that the principal institution is held accountable for all actions and commissions of agents when providing financial services on their behalf. The principal must also maintain an effective system of internal.In countries where models have been successfully

implemented, regulators and supervisors have addressed the potential risks of using a large number of agents to deliver financial services by adopting a risk-based approach to supervision where agents are supervised indirectly and banks must assume full responsibility for their agents (Kasekende, 2008)

Odhiambo (2012), states that there is still some scepticism regarding how well banks can manage risks remotely. Liability between the agent and bank must be well established and liquidity and credibility of the agent ensured, which means banks are keen to work with SACCOs and large well-known companies that have solid cash flows. The CBK regulations are also quite clear about the need for agent training and enforcement of anti-money laundering standards. The former in particular has been an enormous investment in building Safaricom extensive agent network, and monitoring and policing agents requires continuous efforts.

Wambugu (2011), states that the level and kind of risk to which a bank will be exposed as a result of its use of agents will depend on the extension of such use, the activities in which its agents are engaged, the banks management of the agent business. The FSD (2009) further reveals that the biggest risk faced by banks is agent fraud although on line systems limit the risk to clients from this source; the banking industry has a strong interest in ensuring that dishonest agents do not get fired by one bank only to appear, in another form, as agents of another bank. A further risk is agent churn, whereby for a variety of reasons, agents do not stay long of any one bank but either transfer to another bank, or else drop out from the system. It is therefore important to establish the impact of the agency banking risk to the reported profits.

2.1.4 Agency Policy Regulation and Performance of Banks

Government regulatory policies at the local, state and national level can also have an impact on the diversification decision. Government can limit or even foreclose entry into industries with such controls as licensing requirements and limits on access to raw materials (Porter, 1980). Regulatory controls on air and water pollution standards and product safety and efficacy should also be weighed. Pollution control requirements can increase the capital needed for entry and the required technological sophistication and even the optimal scale of facilities. Standards for product testing, common in industries like food and other health-related products can impose substantial lead times, which not only raise the capital cost of entry but also give established firms ample notice of impending entry and sometimes full knowledge of the new competitor's product with which to formulate retaliatory strategies. Many of these regulations, while enormously beneficial to society, can have a bearing on the ultimate wisdom of a diversification strategy (Porter, 1980).

Agent banking in Kenya should be branch driven and branch centric. In as much as many banks are viewing agency banking as an expansion channel, agent's need to be linked to the nearest bank branches for operational and administrative effectiveness. Processes and Procedures should be put in place to ensure seamless operations and minimal turnaround time. Branches should also participate in the agent recruitment process so that the Bank can leverage on market knowledge and existing relationships that branches have established with surrounding businesses (http://bankinginkenya.com). The Central Bank of Kenya (CBK) has set out to have Banks appoint qualified and professionally suitable entities as their agents in the wake of the growing networks of agency banking in the country. The Central Bank of Kenya (CBK) released revised

Prudential Guidelines and Risk Management Guidelines, 2011 for institutions licensed under the Banking Act for stakeholder and public comments which are still under review. In the guidelines, under Agency banking, the bank seeks that for Banks to appoint agents across the country they must establish their ability to be in business and sustain the agent station. Additionally the guidelines state they will check: Moral and professional suitability of sole proprietors, partners and officers licensed to run agency banking. In the case of a corporate entity, the institution shall assess the moral, business and professional suitability of the Chief Executive Officer and the officer in charge of or responsible for agent banking operations of the entity. Most banks in the country have rolled out agency banking services in a bid to exploit the potential of unbanked people especially in the rural areas .Having a third party transacting for the bank is a bit of risky, considering the fact that most of the agent have no formal education or rather training to handle the job. The issue pertaining knowing a fake note, handling of customers and maintaining of a brand can be a challenge to an agent. Opm (2009), further states that agent banking is rapidly evolving and its regulation plays a central role in enabling its spread regulators are required to strike a balance between promoting financial inclusion through profitable, lower cost delivery models and protecting consumers and the integrity of the financial systems. It is therefore important to analyse the importance of the agency banking policy to the performance.

Regulation enabling agent banking allows for sufficient business incentives for both agents and financial institutions to increase outreach by delivering financial services through a network of agents. Financial intermediaries have long been identified as unique institutions in free-market economies. The negative externalities deriving from bank failures have prompted a body of government regulation unparalleled among non-financial firms. In the U.S. a large segment of this regulation was enacted in the Depression era of the 1930's. For the next four decades all

seemed reasonably well but the 1980's brought a wave of bank failures that produced losses that exceeded in real terms the losses of the 1930's. Quite naturally this led to a questioning of the rationale and efficacy of then current bank and thrift regulation (Saunders, 2006).

It is stated by an anonymous writer that most agencies are in areas that are considered high risk .The bank needs to audit the security measures being taken by the agencies to ensure the customer can transact confidently without having to look behind their backs. The benefits from the agents banks with lower transaction cost ,service closer to client home; client would visit store anyway for groceries ,longer opening hours ,shorter lines than in branches, more accessible for illiterates and very poor who might feel intimidated in branches. Increased sales from additional foot traffic ,differentiation from other business ,reputation from affiliation with well-known financial institution ,additional revenue from commissions and incentives ,increases customer base ,and market share ,increased coverage with low cost solution in areas with potentially less number and volume of transactions ,increased revenue from additional investment ,interest and fee income ,improved indirect branch productivity by reducing congestion (Cohem, 2002). A businessman should always look at being in competitive advantage over his competitors: one way is to be an agent. And one way for this business to still maintain his position is to always protect the need of the customer. They should have good customer service. A customer should feel safe and that his needs are met by the businessman and are important to him.It's also important to note that different markets have different banking needs. A successful agent banking business plan needs to provide the right product offerings for the different market segments. Agency Banking in Kenya has provided a new platform for Kenyan banks to compete on which has been an advantage for customers. (http://bankinginkenya.com).

Appropriate consumer protection against risks of fraud, loss of privacy and even loss of service is needed for establishing trust among consumers which is the single most necessary ingredient for growth of m-banking. These risks increase when agents are involved and reach to a maximum in Nonbank-led model. As we will be dealing with a large number of first time customers with low financial literacy the risks become even higher. These risks can be mitigated by entering into mobile banking activities through known, already regulated players (banks) and by issuing adequate guidelines regarding privacy protection, network security and complaint redressed (Porteous, 2006). Lyman *et* al.(2006) states regulatory issues, from a financial regulator's perspective, concerning mobile banking are related to consumer protection, effect of m-banking on stability of banking & payment systems, legal definition of deposit, e-money regulations, provisions for agency agreements and AML/CFT laws.

Manzano and mandrille (2010), states that Policymakers and regulators have been facing the challenge to reconcile a safe development of branchless banking operations with increased levels of financial access. The Colombian authorities are committed to developing the use of mobile-phone and card-based branchless banking models to increase access to finance in the entire country. There is no regulatory obstacle preventing branchless/mobile banking from growing into an important tool for bancarization. On the contrary, there is still a lack of regulation, which may be the biggest barrier for the expansion of financial services through new technologies because it creates legal uncertainty, an issue for financial institutions that plan to offer mobile financial services.Kamau (2011), one of the researchers on the KBA survey, highlighted some of the pressing problems that have come up since the agency model inception. By its nature, the model was intended to take banking to the low income and rural populations. This places outlets in

areas where insecurity is a concern. They lack the sophisticated security measures of the bank branch (CCTV, armed guards) and as the researchers observed, large deposits (large here means over KES50,000) were in some cases turned away. The outlets also operate beyond standard bank opening hours, further exacerbating the security risk. Other problems include: lack of consumer information on agency banking, for example on charges, lack of sufficient float, image problems (shabby shops may turn off customers); system collapse; equipment breakdown and incompetent agents. Good customer service is one of the keys for successful business. Banks in Kenya does not neglect this fact at all; they go further by training their staff of this skill. A customer who is satisfied would surely come back for the service when needed. Podpiera, 2008 further states that there are no rules for the games in an emerging industry. The competition problem is that all the rules must be established such that the banks can cope with and prosper under them emerging industries share common characteristics relating to the absence of established basis for competition or other rules of the game or to the initial size and newness of the industry

2.2 Empirical Studies

A number of studies have been carried out on how agency banking affects performance of banks. These studies show that agency banking has been able to improve the lives of many people and also improved the structure of the banks. Agents have taken the role of being the intermediaries between the clients and the banks so as to bring efficiency to the banking sector and to make sure that more under banked and unbanked people have access to financial services.

2.2.1 Level of Agency Banking in Kenya

Berger (2003) in assessing agent management in Ghana found out that most banks employing agency banking were unwilling to infuse more resources in proper management and training of agents which in the long run negatively impacted on SME financial access. He further noted that when the managers and SMEs alike were asked about agent management, the significant response indicated that most traditional banks in a bid to save on cost preferred to manage agents from the headquarter banks often at the detriment of SMEs. However, the interplay of agent management and financial accessibility in the Kenyan context is still unknown. Kumar, Nair, Parsons and Urdapilleta (2006) emphasized that agency banking enhances banks turnover by making banking services available to the vast but higher risk populace through friendly format or medium

A survey on agency banking was carried out by Kenya Bankers Association (KBA) for its Centre for Research on Financial Markets and Policy, 40.9% of agents operations are cash deposits while 36% are withdrawals. The survey also revealed that customers are asking for additional services not on offer, including ATM cards, recommendations for a loan given the closer interaction, loan processing and advice on various bank products on offer. While these would offer a distinction from services offered by Telco's' mobile money services, they require more expertise than agents have, and closer supervision than they can be given. The survey also found that 91% of respondents will use an agency outlet because they trust the bank compared rather than the agent. Banks with positive images and long, stable operations are favoured. Agents use point-of-sale (POS) devices and/or mobile phones and must have access to the bank's core

banking system so that the clients' transactions are reflected in real time (www.pesatalk.com, 2012).

It is noted by Jayanty (2013), that the use of agents to increase the number of touch points providing financial access as well as reduce transaction costs is a key element of Mexico's financial inclusion strategy. It is the same with Kenya, which amended its banking act to permit small retail outlets to become agents. The role of agency banking in improving financial outreach around the world is well documented. Less known is its contribution to the redefinition of financial inclusion, from "banking the unbanked" to "the convergence of various bank and non-bank players to provide financial services to all end consumers of financial services, unbanked or otherwise. According to Donner (2005), there have been relatively few studies focusing directly on the way mobile phones are used in enhancing productivity among the users in the developing world. Some business also lacks the awareness regarding the potentials that exist in the use of mobile phones and ICT .It is therefore important to establish the level of agency banking model

2.2.2 Agency Banking Cost and the Profitability of Banks

Simpson (2002) suggests that agency banking is driven largely by the prospects of operating costs minimization and operating revenues maximization. Agency banking has a positive impact to the banking sector. This has reduced cost both for the bank and the bank customers and has promoted efficiency and effectiveness in our banking sector. In her paper, Clara Veniard of the Bill and Melinda gates foundation found that agency banking system are up to three times cheaper to operate than branches .Agency banking systems are up to three times cheaper to operate than branches for two reasons. First, agency banking minimizes fixed costs by leveraging

existing retail outlets and reducing the need for financial agent banks to invest in their own infrastructure .It is therefore important to establish how cost effective agency banking model is to the bank and to the customer. Gardner 2000 emphasizes by using banking agents instead of payment cards, bank wallets and bank accounts linked to a bank wallet are able to acquire entrepreneurs at less than seventy percent of the cost of a branch or Point Of Sale (POS)-enabled agent. In some countries, bank wallets may also benefit from lower-cost Know Your Customer requirements, such as the elimination of requirements to provide photographs and photocopies of documents. Ivatury and Mas (2008) established that agency banking leads to cost minimization by reducing maintenance cost of banks fixed assets such as buildings and cost of service delivery.

According to the oxford policy management (2010), agents make use of the mobile phone technology and internet banking technology to connect to the servers of the principal institutions to carry out customer transactions. (Adeya 2003) argues that the rise in customer deposits comes at a time when the deposit rate has been on a downward trend. This means that banks will be able to squeeze out more profits for every shilling lent from deposits. As of September, the average deposit rate stood at 3.53 per cent while the average lending rate stood at 13.98 per cent. The interest rate spread - the difference between the interest banks charge borrowers and what they pay depositors - dropped from 14.29 per cent in July to 13.98 per cent in September. According to research by Dyer & Blair Investment Bank (2012). Higher deposits are expected to help banks lend more at lesser costs, a move that should protect their profitability in an environment where the average lending rate is dropping and investing in short term government securities has been rendered unattractive as their yield has remained low, at below three per cent. Ambunya 2012

further argues an increase in deposit means we are able to push more loans, thus increasing profits from volumes.

Gupta and Collins (1997) argue that efficiency relates to the use of all inputs in producing any given output, including personal time and energy. The concept of efficiency can be regarded as the relationship between outputs of a system and the corresponding inputs used in their production. Efficiency is treated as being a relative measure that reflects the deviations from maximum attainable output for a given level of input. Gupta and Collins (1997) argue that the efficiency of a firm consists of technical and a locative efficiency. Technical efficiency is the ability of a firm to obtain maximum output from a given set of inputs, and allocative efficiency is the ability of a firm to use the inputs in optimal proportions given their respective prices. When these two measures are combined they provide a measure of total economic efficiency in the bank. The CBK regulations require that agents have secure operating systems capable of carrying out real time transactions, generating an audit trail, and protecting data confidentiality and integrity. This is all driven by technology: Transactions can be made via mobile phone, a point of sale (POS) system, or internet banking, and must be reflected immediately on the bank's side in the core banking system. Orange Money does this by operating on a shared real-time platform with its agents that allows customers to deposit cash into their Orange Money account and then access it immediately at an Equity branch or ATM. Shared infrastructure protects data integrity, reduces operation costs and keeps transaction fees low.

Podpiera (2008) argues that agent banking does improve the economics of institutions compared with branches, especially for high-transaction, low-balance accounts that are common among

poor users. The analysis focuses on four types of agent banking delivery channels: POS-enabled bank agent; this is an agent managed by a bank that uses a payment card to identify entrepreneurs. Banking agent-enabled agent – This is an agent managed by a bank that uses a cell phone to identify entrepreneurs. Beck, Cull, Fuchs and Getenga (2010) avers that due to low cost agency banking has increased the ease of banks' expansion hence outreach to remote areas consequently increasing revenue and profit.

Daniel et al. (2012) recommends that the government reduces the period of obtaining the legal documents in adopting agency banking. The government should support the program more often and reduce the high compliance costs, bureaucracy in registration and high cost of taxation. (Berger, 2003). Hasan, Schmiedel and Song (2009) in their study to provide a combined and integrated view of the importance and significance of retail payments for bank performance using country level retail payment service data across 27 EU markets found out that countries with more developed retail payment services, banks perform better, in terms of both their accounting ratios and their profit and cost efficiency. They further found that the relationship is stronger in countries with higher levels of retail payment transaction equipment, like ATMs correspondence (Agency) banking and POS terminals

2.2.3 Agency Banking Risk and Customer Base of Banks

Binswanger (1996) argued that compensation in the banking industry does not promote risk-taking. In their study they find no evidence that equity-based incentive increase the level of risk taking. On the contrary, they find a positive relationship between the use of equity-based compensation and the ratio of market-value to book-value. The use of more equity-based incentives by banks with high charter values is completely inconsistent with a propensity to increase risk. Gorton and Rosen (1995) produce similar results. Their conclusion is that

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managers with controlling interests tend to make safe loans while entrenched managers make more risky loans.

Kinyanjui (2011) noted that some of the things that have made people seek basic services like making deposits in banks as opposed to agents are security and confidentiality. Although agents are officially contracted by banks, it seems people do not trust them when it comes to confidentiality. This is because they are not bank employees. Some customers feel they may leak out information. Most agencies are also located in places where customers may perceive as high risky. Besides that, charges imposed on customers for using agency services have also made people avoid them. Customers are charged an average 0.94 dollars per transaction thus they prefer to go to banks because the same services are free. Pickens (2009) stated that agency banks have not contributed much to banks' revenue growth owing to customers' scepticism about its transactional security. Further, system failure and conservatism among customers who prefer brick-and-mortar model makes the model ineffective.

Ivatury and Lyman (2006) pointed out challenges facing agency banks such as loss of confidentiality of customer information; location of the agents in high risk areas poses security threat; poor customer service to the bank customer as the agents are not well trained; and, susceptibility of the agents to fraudulent transactions. Mwangi (2011) established that infrastructure cost and security influence the performance of commercial banks attributable to agency banking to a very great extent. The study recommends that agency banking should be given more attention on security measures including risk-based approach and that the banks should find better ways of screening their agents to ensure that the large cash transactions

handling is effectively carried out on their behalf; secure operating systems capable of carrying out real time transactions, generating an audit trail, and protecting data confidentiality and integrity.

2.2.4 Agency Policy Regulation and Performance of Banks

Danielle, 2008 in his study suggested that there is no one, perfect, regulatory model for agent banking in Nigeria: rather particular aspects of the regulation in each country can be adopted. In the M-pesa case in Kenya, an innovative business model emerged and scaled rapidly in a safe manner in the absence of an elaborate consumer protection framework. This challenges the perception of risk and promise that substantial consumer protection rules are a precondition for healthy development of branchless banking. The Kenyan case suggests that there can be providers that have their own (non- regulatory) incentives – such as reputation and the need to build trust in the market for a new service to act responsibly. M-pesa and other service providers have offered transparently and adopted safeguards to protect consumers, including those with little or no prior experience with formal providers.

Caprio et al. (2007) argues that banks have unique characteristics in such a way performance increases presence of strong shareholder protection laws aimed to avoid expropriation by controlling owners and reduce expropriation by insiders. Morgan, 2002, points out due to the higher opacity and complexity of banks investor protection laws alone may not provide effective protection to small shareholders. Allen and Gale, 2000;Levine, 2006 further points out banks' investment decisions are argued to influence economic growth and stability .Too little bank risk taking may hinder economic growth, whereas too much bank risk threatens economic stability. Hence, it makes sense for governments and institutions to regulate banks with the aim of shaping

and influencing bank risk taking and performance with the purpose to attain economic growth and stability. Karimi (2011) established that there is difficulty in enforcing appropriate oversight by the agent and customer interaction was inconsistent with overall banking regulatory framework. The findings revealed need for regular training of agents on changes in operational processes and policies in order to eradicate occurrence of error and mistakes that obstruct penetration of agency banking in Kenya thus enhance banks' financial performance. Ivatury, (2008) argues that the fact that Kenya is moving in the direction of a cashless society, although far away from being there, this puts pressure on the government to develop regulatory systems and other policies to meet the changing llandscapes of the financial market

2.3 Summary of Literature and Knowledge Gaps

From the literature review, the results show that the number and dispersion of agents has not been that wide and penetrative. It has been observed that commercial banks, microfinance institutions and other financial institutions establish branches in urban centers leaving out the rural areas which exclude a significant population from accessing financial services. An amendment was made to the Banking Act allowing banks to start using agents to deliver financial services. It is therefore important to establish the level of agency banking in western Kenya region.

It has further been noted that Kenyan banks are reporting high profits in their yearly performance. Muriuki (2010) argues that through the introduction of agency banking, banks have recorded different results on their profitability. Though it is not easy to estimate agent profitability this is because estimating the real costs associated with the business is more

complex. It is in light of the above issues that the study purposes to establish the relationship between agency banking cost and the bank's profitability.

It is reported further that there is high risk on allowing agents managing the banks activities in their business premises .On the other hand this agents are recruiting new customers for banks. It is therefore important to study the relationship between agency banking risk and customer base of the bank.

Atieno (2011) points out that there is still some scepticism regarding how well banks can manage risks remotely. To deal with the issue of management of risk, Central bank of Kenya roll out in the year 2009: the agency banking policy on the banks operating in Kenya. Opm (2009), states that agency banking plays a central role the evolution of banking. Thus the need for regulators to strike a balance between promoting financial inclusion and protecting consumers and the integrity of the financial systems. Danielle, 2008 in his study contradicts the above thoughts by stating that there is no one, perfect, regulatory model for agent banking .It is therefore important to be established how this policy has affected the performance of Banks

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CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter covers the research methodologies, which include research design, population, data collection methods and data analysis method.

3.2 Research Design

This study adopted descriptive survey research design which, according to Orodho (2002), is used in preliminary and exploratory studies to allow researchers to gather information, summarize, present and interpret for the purpose of clarification. Mugenda and Mugenda (1999) on the other hand give the purpose of descriptive research as determining and reporting the way things are. Borg and Gall (2009) note that descriptive survey research is intended to produce statistical information about managerial aspects that interest policy makers and educators. Additionally, the use of a descriptive study is useful in case study research as according to Baxter & Jack (2008) use of a case study in research 'takes into consideration how a phenomenon is influenced by the context within which it is situated' and therefore will be relevant for the case study as it was highly influenced by the context in which it was set.

3.3 Study Area

The target area for this study was Western region of Kenya; which comprises Kisumu, Mbale, Mumias, Kakamega, Awendo, Siaya, Luanda, Kisumu-angawa, Migori, Kisii, Kericho, Keroka, Homabay, Mbita, Bungoma, Mumias, Bondo, Kitale, Eldoret and Eldoret market. The region was selected because of its accessibility to the researcher.

3.4 Target Population

Target population was 40 staff comprising of 20 agency banking managers and 20 operation managers in the 20 equity bank branches in the Western region.

3.4.1 Sampling technique

A Census technique was employed on the entire population to who the questionnaire were administered and interview conducted based on its small size.

3.5 Data Collection Method

3.5.1 Data

Both Primary and secondary data was used in the study. Primary data was collected using a semi-structured questionnaire. The researcher administered the questionnaires and interview through the "drop and pick method". The questionnaires and interviews were administered to the operation and agency managers in 20 Western branches. Secondary data will be collected using document review and content analysis.

3.5.2 Data Collection

Questionnaires and interviews were administered. The questionnaires were used to collect data because a lot of information will be collected over a short period of time. The study on the other hand, is mainly concerned with views, options, perceptions, feelings and attitude and such information is best collected through the use of questionnaires and interviews. In addition to financial measures of performance, assessed by deposit mobilisation, the author attempts to include the subjective measures of quality and customer satisfaction as other indicators of performance.

3.5.2 Validity and Reliability

Validity and reliability are measures of relevance and correctness. Validity is the accuracy and meaningfulness of inferences, which are based on the research results while reliability is a measure of the degree to which a research instrument yields constant results or data after repeated trials (Mugenda and Mugenda, 2005). Validity of the research instrument was done using two experts from Maseno University from the Department of Accounting and Finance. Reliability analysis was carried out using Cronbach's Alpha method which yielded an alpha of 0.789 after comparing the two sets of data collected from the two pilot studies through test re-test method.

3.6 Data Analysis

Descriptive statistics such as percentage, standard deviation and the mean was used while regression and correlation analysis were used to determine the inter-relationship between the variables.

3.7.1 Model Specification

The study was guided by the following regression model (Kothari, 2004):

$$Y_i = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + e$$

Where the variables were defined as:

Y_i- Performance

X_1-Agency banking cost

X_2- Agency Risk Assessment

X_3- Agency banking policy regulation

e- Error term

Quantitative data was analyzed using descriptive statistics using the percentages, frequencies and

means. The data analyzed was then presented in the form of tables and graphs. Qualitative data on the other hand will be analyzed using thematic analysis. The Social Package for Statistical Science (SPSS) software aided in data analysis. Regression analysis was used to test for relationship between the independent variables and the dependent variable.

3.8 Data Presentation

Data was presented in form of tables

3.9 Research Ethics

The researcher had a standing principle that: The respondents had to be informed of the purpose of the research, duration, and benefits of the study. Privacy, confidentiality, and anonymity of the data collected were assured to the respondents

CHAPTER FOUR

RESULTS AND DISCUSSION

4.1 Introduction

This chapter describes the process of data analysis, presents results and draws discussion on information collected. The objectives of the study were to determine the level of agency banking of Equity Bank Limited in Western Kenya; determine the relationship between cost and profitability of equity Bank Limited; establish the effect of agency banking risk on customer base and to determine the relationship between agency banking policy on the bank and its performance. A total of 40 respondents who were branch managers from various branches within Western Kenya were used. The response rate was 100% since all the questionnaires were returned completely filled by the respondents.

4.2 Demographic Information of Respondents

Table 4.2.1: Respondents' Gender

Gender	Frequency	Percentage
Male	29	72.5
Female	11	27.5
Total	**40**	**100**

The study sought to find out the gender distribution among the key respondents in Equity Bank Limited in Western Kenya. The respondents were asked to indicate their gender and the results were recorded in Table 4.1. According to the results, majority of the respondents were male (72.5%) while the rest were female (27.5%). The results illustrated that there was a significant ($p<0.05$) variation in the gender distribution among the respondents since the expected 50% was

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not attained because the number of male was more than that of female who participated in the study. Therefore, gender equity among the respondents who participated in this study was not achieved. This could also point out that more male work in Equity Bank Limited in Western Kenya than women.

4.2.2 Education Level

The study sought to find out formal educational levels of the key respondents in Kakamega North District. The respondents were asked to state their formal educational levels.

Table 4.2: Respondents' Education Level

Level of education	Frequency	Percentage
Diploma	4	10.0
Degree	28	70.0
Masters	8	20.0
Total	**50**	**100**

Results show that most of the respondents (70%) were educated up to degree level, followed by 20% who were educated had master's degrees and only 10% of the operation and agency banking managers had diploma educational level. This shows that the Equity banks in Western Kenya had branch managers who had attained the basic education level and therefore understand agency banking and how this affects the overall performance of the bank.

4.2.3 Working Experience

The study sought to find out the working experience of the respondents. This was aimed at determining the number of working years and in turn knows how much experience the respondents had been exposed to regarding agency banking and the overall performance of the

bank. The results are shown in Table 4.3.

Table 4.3: Working Experience

Duration of employment	Frequency	Percentage
1 year and below	10	25.0
1 to 3 years	11	27.5
3 to 5 years	14	35.0
Above 5 years	5	12.5
Total	**40**	**100.0**

The results illustrate that 35% of the respondents have been working for 3 to 5 years, 27.5% working for 1-3 years, 25% for one year and below and those above 5 years were represented by 12.5%. This indicated that most respondents had acquired some experience, knowledge and skills to varying degrees to understand agency banking model affects performance of commercial banks. The results seem to indicate that experience, knowledge, competencies and skills increase with increase in years of performing the job.

4.3 Level of Agency Banking by Equity Bank in the Western Kenya Branches

This was the first objective of the study. The level of performance of Equity Bank Agents was based on the following variables: profitability of the bank, customer base of the bank and efficiency of the agents of the bank. Results are illustrated in Table 4.4

Table 4.4: Level of Performance of Equity Bank Agents

Variables	SA %	A %	U %	D %	SD %	Mean
Profitability of the bank	17(42.5)	18(45.0)	3(7.5)	2(5.0)	0(0.0)	3.54
Customer base of the bank	24(60.0)	13(33.0)	2(5.0)	1(2.5)	0(0.0)	3.88
Efficiency of the agents of the bank	23(57.5)	10(25.0)	0(0.0)	3(7.5)	4(10.0)	3.69

n = 40; Key: SA = strongly agree, A = agree, U = undecided, D = disagree and SD = strongly disagree

From the results, the respondents gave different views on the level of the bank as attributed to equity bank agents. For example, 42.5% of respondents strongly agreed, 45% agreed, 7.5% of respondents were undecided while 5% of respondents disagreed. This variable had a mean of 3.54. Therefore, banking agency contributed 70.8% profitability of the bank based on a five point Likert scale (strongly disagree=1, disagree =2, undecided =3, agree=4, strongly agree=5). Majority of respondents (92%) were of the opinion that customer base of the bank improved as a result of agency banking. This shows that most respondents agreed that the banking agency contributed a larger customer base in Equity Bank Limited. It can be deduced that banking agency contributed 77.6% customer base. The third question was to establish the efficiency of the agency banking. Majority (82.5%) of respondents were in agreement, 7.5% disagreed and 10% strongly agreed. Therefore, efficiency of the agency banking on remitting the banking service stood at 73.8%. On average, therefore, the level of performance of equity bank agents was 74.07%. Findings from the interviews also confirm the significant role of agency banking in Kenya. For example, quite a number of respondents said that agency banking has improved the lives of many Kenyans and also improved the structure of the banks. Agents have taken the role of being the intermediaries between the clients and the banks so as to bring efficiency to the banking sector and to make sure that more under banked and unbanked Kenyans have access to financial services. The finding is consistent with the study conducted by Muriuki (2011) that established that agency banking has been growing significantly both in terms of number of agents and value of transactions. The growth rate is expected to be maintained as more and more banks within the industry enrol agents especially in remote arrears .Waithanji (2012) findings revealed lack of connection between agent banking and financial deepening. Waithanji noted that

the relationship could not be conclusively determined due to the low number of banks that have implemented it and impact may become clearer once all banks adopt agency banking.

4.4 Agency Banking Cost and Profitability of Equity Bank Limited

To establish the association between agency banking cost and profitability of Equity Bank Limited, an analysis of descriptive statistics was conducted as illustrated in Table 4.5.

Table 4.5: Agency Banking Cost and Profitability of Equity Bank Limited

Variables	SA%	A%	U%	D%	SD%	Mean
It is cost effective to establish an agency bank	24(60.0%)	13(32.5%)	3(7.5%)	0(0.0%)	0(0.0%)	**4.53**
Agency banking has reduced the banks' operational cost	17(42.5%)	18(45.0%)	5(12.5%)	0(0.0%)	0(0.0%)	**4.30**
In my opinion it is cheaper to start an agency	21(52.5%)	16(40.0%)	2(5.0%)	1(2.5%)	0(0.0%)	**4.43**
The agency banking services are well structured & differentiated thus improving banks' profitability	8(20.0%)	8(20.0%)	9(22.5%)	9(22.5%)	6(15.0%)	**3.08**
The deposit mobilised due to agency banking is quite considerable	13(32.5%)	25(62.5%)	2(5.0%)	0(0.0%)	0(0.0%)	**4.28**
Customers have greatly increased due to agency banking	22(55.0%)	14(35.0%)	2(5.0%)	2(5.0%)	0(0.0%)	**4.18**
Agency banking has influenced the saving culture of the banks' clients	9(22.5%)	19(47.5%)	9(22.5%)	3(7.5%)	0(0.0%)	**3.85**

n = 40; Key: SA = strongly agree, A = agree, U = undecided, D = disagree and SD = strongly disagree

Results show that it is cost effective to establish an agency bank (strongly agree =60%, agree =32.5% and undecided =7.5%). This variable had a mean of 4.53. On the question asked whether agency banking has reduced the banks' operational cost, majority of respondents (87.5%) were of the views that agency banking has reduced the banks' operational cost while 12.5% of respondents were undecided. Respondents gave varied views on whether agency banking services were well structured and differentiated thus improving banks' profitability (strongly

agree =20%, agree =20%, undecided =22.5%, disagree =22.5% and strongly agree =15%). This question had a mean of 3.08. Majority of respondents (95%) were in agreement that the deposit mobilised due to agency banking was quite considerable while 5% of these respondents were undecided. This variable had a mean of 4.28. Eighty eight percent (88%) of respondents were in support that customers have greatly increased due to agency banking, 5% were undecided and 5% of these respondents disagreed. This question had a mean of 4.18.

Table 4.6: Agency Banking Cost and Profitability of Equity Bank Limited

Variables	Regression coefficient, b	Coefficient correlation, r	t-test	2-tailed sig.
Agency banking has reduced the Bank's operational cost	0.683	0.206	0.963	<0.05 (s)
Cost effectiveness of agency banking	0.534	0.142	0.723	<0.05 (s)
Agency banking has influenced the saving culture of the banks' clients	0.852	0.182	1.023	<0.05 (s)
The deposit mobilised due to agency banking is quite considerable	0.770	0.200	0.980	<0.05 (s)
Overall value	**0.710**	**0.183**	**6.720**	

n= 40; s-significant; ns-not significant; *Correlation is significant at the 0.01 level (2-tailed); correlation is significant at the 0.05 level (2-tailed).Levels of significance, p-value for correlation coefficients are indicated*

Regression analysis was carried out to establish the relationship between agency banking cost and profitability of Equity Bank Limited. Results illustrate that agency banking cost has a positive and significant association on the profitability of Equity Bank Limited (b =0.710, r =0.183, t=6.72, p<0.05). This signifies that 71% of profitability of Equity Bank Limited can be attributed to agency banking cost. The findings is consistent with the findings by Clara Veniard found that established agency banking system are up to three times cheaper to operate than branches .

4.5 Effect of Agency Risk on Customer Base

Regression analysis was used to determine whether there exists a relationship between agency banking risks and customer base. Customer base was the dependent variable while agency banking risks as independent variables. Results are shown in Table 4.7.

Table 4.7: Effect of Agency Risk on Customer Base

	Std. Error	Correlation coefficient, r	Regression coefficient, b	t-test	Sig. level
Customers are scared because of insecurity	0.213	-0.109	-0 .308	-2.035	<0.05 (s)
Bank consideration to operational risks	0.029	0.123	0.220	0.516	<0.05 (s)
Overall risk assessment hampering the banks performance	0.071	-0.661	-0.870	-3.621	<0.05 (s)
Equity bank agents are not well trained on how to handle business risks	0.024	-0.420	-0.671	-4.358	<0.05 (s)
Overall effect;		**-0.267**	**-0.407**	**-0.9495**	

n= 40; s-significant; ns-not significant; *Correlation is significant at the 0.01 level (2-tailed); correlation is significant at the 0.05 level (2-tailed).Levels of significance, p-value for correlation coefficients are indicated*

All the variables with an exception of bank consideration to operational risks (r =0.123, b =0.220, t =0.516, p<0.05) had negative associations on the customer base. Examples: Customers are scared because of insecurity (r =-0.109, b =-0.308, t =-2.1035, p<0.05); overall risk assessment hampering the banks performance (r =-0.661, b =-0.870, t =-3.621, p<0.05) and equity bank agents are not well trained on how to handle business risks (r =-0.420, b =-0.671, t =-4.358, p<0.05). The findings concur with the observation of Mylenko (2008) that lack of expert training in agency banking may seem a particular problem if retail agents' functions range beyond the cash-in/cash-out transactions of typical bank tellers to include a role in credit decisions.

This shows that the level of risk involved in agency banking is negatively correlated with the customer base of the bank. The results are statistically significant at $P<0.05$. This inhibits customers accessing the basic banking services, for example, cash deposit, cash withdrawal and bank balance inquiry conveniently. Therefore just as Rachel (2011) pointed out, there is still some scepticism regarding how well banks can manage risks remotely. Mwangi (2011) agrees by stating that infrastructure cost and security influence the performance of commercial banks attributable to agency banking to a very great extent. He recommends that agency banking should be given more attention on security measures including risk-based approach and that the banks should find better ways of screening their agents to ensure that the large cash transactions handling is effectively carried out on their behalf; secure operating systems capable of carrying out real time transactions, generating an audit trail, and protecting data confidentiality and integrity.

4.6 Relationship between Agency Banking Policy on the Bank Performance

To establish the relationship between agency banking policy and bank performance, regression analysis was carried out between the indicators of these two variables. Results are illustrated in Table 4.8. For example, agency regulation policy by CBK is compiled by the bank had a positive and significant relationship on the bank performance ($r = 0.481$, $b = 0.308$, $t = 1.035$, $p<0.05$). The variables on banks have the ability to control the agents under their jurisdictions had a strong positive association the bank performance ($r = 0.752$, $b = 0.512$, $t = 1.110$, $p<0.05$). The only variable that had a positive but insignificant association bank performance was that there is still a lack of regulation on introduction of new technology ($r = 0.745$, $b = 0.651$, $t = 1.021$, $p>0.05$).

Table 4.8: Relationship between Agency Banking Policy on the Bank Performance

Model	Unstandardized Coefficients		Standardized Coefficients		
	B	Std. Error	Beta	t	Sig.
Agency regulation policy by CBK is compiled by the bank	0.481	0.15	0.308	1.035	<0.05
Banks have the ability to control the agents under their jurisdictions	0.752	0.29	0.512	1.110	<0.05
There is still a lack of regulation on introduction of new technology	0.745	0.42	0.651	1.021	>0.05
Overall effect	**0.660**		**0.490**	**1.060**	

Source: Research Findings, 2013

The overall effect on the relationship between agency banking policy and bank performance indicated a moderate positive association between these two variables (r =0.660, b =0.490, t =1.060, p<0.05).The above findings signifies that effective and equitable agency banking policy will improve bank performance. Thus there is need for the Kenyan government to come up with good policy to enhance profitability. Manzano and Mandrille (2010) supported this view by stating that there is still a lack of regulation on introduction of new technology. According to them this may be the biggest barrier for the expansion of financial services through new technologies because it creates legal uncertainty, an issue for financial institutions that plan to offer mobile financial services. Allen and Gale, 2000;Levine, 2006 points out that too little bank risk taking may hinder economic growth, whereas too much bank risk threatens economic stability. Hence, it makes sense for governments and institutions to regulate banks with the aim of shaping and influencing bank risk taking and performance with the purpose to attain economic growth and stability. Caprio and Levine (2002) points out that even in the absence of regulatory or supervisory requirements, a bank would typically have policies and procedures in place to manage the risks of its agent business

The regression equation:

Table 4.9: Agency banking model on profitability

Model	Regression coefficient, b	Std. Error	Correlation coefficient ,r	t	Sig.
constant- (β_0)	0.654	0.1		0.880	<0.05
Agency banking cost	0.434	0.15	0.652	0.723	<0.05
Agency risk assessment	-0.208	0.071	-0.461	-1.621	<0.05
Agency banking policy regulation	0.145	0.29	0.342	1.021	<0.05
Overall effect	**0.123**		**0.178**	**0.041**	

Source: Research Findings, 2013

Agency banking model and profitability of commercial banks

$Y_i = 0.654 + (0.434X_1 - 0.208X_2 + 0.145X_3)$

Where Y_i –profitability;X_1-agency banking cost; X_2- agency risk assessment and X_3- agency banking policy regulation. These results therefore supported the research objectives which were stated in chapter one. The model illustrates that when all variables are held at zero the bank's profitability will remain at 0.654. The finding show that a 1% increase in agency banking cost would result in 43.4% increase in the bank's profitability. Furthermore a 1% increase in agency banking risk lead to 20.8% decrease in the bank's profitability. Lastly the bank's profitability will increase by 14.5% if the level of policy regulation increases by 1%. Results illustrate that agency banking has a positive and significant association on the profitability of Equity Bank Limited ($b=0.12$, $r=0.17$, $t=0.041$, $p<0.05$).This signifies that 12% of Equity Bank's profitability can be attributed to agency banking in general. Study findings show that both agency banking cost and agency banking policy regulation assessment had profound positive associations on the profitability of commercial banks while agency risk assessment had a negative association on the profitability of commercial banks.

Table 5:0 Agency banking model on bank's efficiency

Model	Regression coefficient, b	Std. Error	Correlation coefficient ,r	t	Sig.
Minimum turnaround time- (β_0)	0.339	0.449		0.933	<0.05
Agency banking cost	0.032	0.15	0.125	0.833	>0.05
Agency risk assessment	-0.265	0.16	-0.661	-1.621	<0.05
Agency banking policy regulation	0.245	0.42	0.359	0.843	<0.05
Overall effect	**0.042**		**0.046**	**0.438**	

Source: Research Findings, 2013

Agency banking model and efficiency of commercial banks

$Y_2 = 0.339 + (0.032X_1 - 0.265X_2 + 0.245X_3)$

Where Y_2 –efficiency; X_1-agency banking cost; X_2- agency risk assessment and X_3- agency banking policy regulation. These results therefore supported the research objectives which were stated in chapter one. The model illustrates that when all variables are held at zero the value of the banks efficiency will remain at 0.484. The finding show that a 1% increase in agency banking cost would result in 21.5% increase in the bank's customer base. Furthermore a 1% increase in agency banking risk lead to 30.8% decrease in the bank's customer base. Lastly the bank's customer base will increase by 22% if the level of policy regulation increases by 1%. Results illustrate that agency banking has a positive and significant association on the customer base of Equity Bank Limited (b=0.042, r=0.046, t=0.438, p<0.05).This signifies that 4.2% of Equity Bank's customer base can be attributed to agency banking in general. Study findings show that both agency banking cost and agency banking policy regulation assessment had profound positive associations on the profitability of commercial banks while agency risk assessment had a negative association on the profitability of commercial banks.

Table 5:0 Agency banking model on customer base

Model	Regression coefficient, b		Correlation coefficient ,r	t	Sig.
Minimum customers- (β_0)	0.484	0.071		1.035	<0.05
Agency banking cost	0.215	0.15	0.125	0.833	<0.05
Agency risk assessment	-0.308	0.071	-0.109	-1.035	<0.05
Agency banking policy regulation	0.220	0.029	0.123	1.516	<0.05
Overall effect	**0.042**		**0.046**	**0.438**	

Source: Research Findings, 2013 **Std. Error**

Agency banking model and customer base of commercial banks

$Y_3 = 0.484 + (0.215X_1 - 0.308X_2 + 0.220X_3)$

Where Y_3 –customer base; X_1-agency banking cost; X_2- agency risk assessment and X_3-agency banking policy regulation. These results therefore supported the research objectives which were stated in chapter one. The model illustrates that when all variables are held at zero the value of customer base will remain at 0.484. The finding show that a 1% increase in agency banking cost would result in 21.5% increase in the bank's customer base. Furthermore a 1% increase in agency banking risk lead to 30.8% decrease in the bank's customer base. Lastly the bank's customer base will increase by 22% if the level of policy regulation increases by 1%. Results illustrate that agency banking has a positive and significant association on the customer base of Equity Bank Limited (b=0.042, r=0.046, t=0.438, p<0.05).This signifies that 4.2% of Equity Bank's customer base can be attributed to agency banking in general. Study findings show that both agency banking cost and agency banking policy regulation assessment had profound positive associations on the profitability of commercial banks while agency risk assessment had a negative association

on the customer base of commercial banks.

Research findings on effect of agency banking on banks' financial performance have been mixed. Lozano and Mandrile (2010) states that agency banking has helped banks enhanced value chain and performance through economies scale and performance of the poor. Ivatury and Mas (2008) established that agency banking leads to cost minimization by reducing maintenance cost of banks fixed assets such as buildings and cost of service delivery. Kumar, Nair, Parsons and Urdapilleta (2006) state that agency banking enhances banks turnover by making banking services available to the vast but higher risk populace through friendly format or medium. On the other hand, Kamau (2012) established a low and negative impact of agency banking on financial performance. Pickens stated that agency banks have not contributed much to banks' revenue growth owing to customers' scepticism about its transactional security. Further, system failure and conservatism among customers who prefer brick-and-mortar model makes the model ineffective (Pickens, 2010).

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CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

This chapter presents summary of study findings, conclusions drawn, recommendations based on the conclusions and suggest recommendations.

5.2 Summary of Findings

The level of agency banking by equity bank in the Western Kenya branches was established at 74.07%. Findings from the interviews also confirm the significant role of agency banking in Kenya. For example, quite a number of respondents said that agency banking has improved the lives of many Kenyans and also improved the structure of the banks. Agents have taken the role of being the intermediaries between the clients and the banks so as to bring efficiency to the banking sector and to make sure that more under banked and unbanked Kenyans have access to financial services.

Results between agency banking cost and profitability of Equity Bank Limited illustrate a positive and significant association on the profitability of Equity Bank Limited ($b = 0.710$, $r = 0.183$, $t = 6.72$, $p < 0.05$). This signifies that 71% of profitability of Equity Bank Limited was attributed to agency banking cost.

Study findings between agency banking risk and customer base: customers are scared because of insecurity ($r = -0.109$, $b = -0.308$, $t = -2.1035$, $p < 0.05$); overall risk assessment hampering the banks performance ($r = -0.661$, $b = -0.870$, $t = -3.621$, $p < 0.05$) and equity bank agents are not well trained on how to handle business risks ($r = -0.420$, $b = -0.671$, $t = -4.1358$, $p < 0.05$). This shows

that the level of risk involved in agency banking has negative effect on the customer base of the bank and the results are statistically significant at $P<0.05$ ($b = -0.407$, $r = -0.267$, $t = -0.950$). This inhibits customers accessing the basic banking services, for example, cash deposit, cash withdrawal and bank balance inquiry conveniently.

The overall effect on the relationship between agency banking policy and bank performance indicated a strong positive association between these two variables ($r = 0.660$, $b = 0.490$, $t = 1.060$, $p<0.05$).

5.3 Conclusions

The study had the following conclusions:

The level of agency banking was established at 74.07%. This was also confirmed from the interviews that agency banking has improved the lives of many Kenyans and also improved the structure of the banks. Agency banking has helped to bring banking services to rural areas.

Agency banking cost and profitability of Equity Bank Limited illustrate a positive and significant association on the profitability of Equity Bank Limited .The 71% of profitability of Equity Bank Limited was attributed to agency banking cost. This implies agency banks improves banks performance as it reduces huge savings on cost of construction of bank premises and leasing costs than when banks are using the Agency premises. It also cuts on human resource expenses. The banks do not have to employ new staff to manage the agency and the cost of training if any is to the bare minimum. It further, saves on equipment like furniture and computers. Additionally, the convenience of access to banking services and the extended hours that the banking agencies work is attractive features to the customer. This also helps increase banks' revenue will minimizing costs.

The level of risk involved in agency banking has negative effect on the customer base of the bank and the results are statistically significant at $P<0.05$. This means that the higher levels of risks in agency banking the more pronounced and significant negative effect on the customer base of the bank. This implies the bank need to invest in more efficient information systems to make the agency model more effective, efficient and reliable.

The relationship between agency banking policy and bank performance indicated a strong positive association. This signifies that effective and equitable agency banking policy will let to improve bank performance. Banks are encouraged to come up with their own policy and procedures to enable effective operation on the agents. This will help to curb any loophole agency banking policy has.

5.4 Recommendations

The following recommendations were made based on the findings and the conclusions of the study: Given the relationship between agency banking and bank performance was strong and positive, then it is imperative for the bank branches to participate in the agent recruitment process so that the banks can leverage on market knowledge and existing relationships that branches have established with surrounding businesses.

Since the paper illustrate a positive and significant association of agency banking cost on the profitability of the bank then there need of intervention from the bank to enhance growth and acceptance of agency banking to the full in rural Kenya. To facilitate and improve agency banking acceptance in rural Kenya, there is need of the bank to do massive marketing through awareness creation, training, improving Agency capability, enhance and assure security, reliability and confidence.

Since the study revealed that agency banking risk affects the customer base negatively, there is need for the banks to train their agents in making correct transactions and enforcement of anti-money laundering standards. The agents should have secure operating systems capable of carrying out real time transactions, generating an audit trail, and protecting data confidentiality and integrity to mitigate on the agency banking risks.

The paper recommends policy makers especially Central Bank Kenya (CBK) to provide information on how the agency banking can enhance the banks operations and performance. This is because agent banking has an effect on financial growth of the country. As the higher the number of agents, the higher the number of customer

5.5 Suggestions for Further Research

From the research findings and conclusions, it was suggested that further research be done to:

Ascertain other factors affecting the agency banking in relation to performance of commercial banks. A similar study is carried out in other commercial banks to ascertain if consistent results can be obtained.

The study also recommends that further studies should be done on the effect of other factors in the banks such as number of branches on agency banking. A similar study should also be done whereby the data collection relies on primary data i.e. in-depth questionnaires and interview guide so as to complement this study.

This study studied was confined to commercial banks yet other financial institutions are engaging in it such as micro finance institutions, insurance companies and Sacco. There is need therefore to study effect of agency banking on the other financial institutions and how this agency banking model affects their operations and performance in general

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