

**An evaluation of the strategy of banking the unbanked for  
a leading South African bank.**

By

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## **CONFIDENTIALITY CLAUSE**

**Date: 2006-12-31**

**TO WHOM IT MAY CONCERN**

**RE: CONFIDENTIALITY CLAUSE**

Due to the strategic importance of this research it would be appreciated if the contents remain confidential and not be circulated for a period of 6 months.

Sincerely

K. PILLAY

096023

## DECLARATION

This research has not been previously accepted for any degree and is not being currently submitted in candidature for any degree.

Signed: Kevin Pillay

A handwritten signature in black ink, appearing to read 'Kevin Pillay', with a stylized flourish at the end.

Date: 2006-12-31

## **ACKNOWLEDGEMENTS**

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## ABSTRACT

With the establishment of the Financial Sector Charter, all the major banks are now 'committed' to provide banking facilities to anyone within a ten-kilometer radius of their home. Specific deadlines have been set, in which these banks will face huge penalties, if they have not achieved the agreed proposals.

The justification for this study is to have a look at the feasibility of this charter in meeting the goals proposed without having a detrimental effect on the long-term profitability of Standard Bank. Making banking affordable to the previously unbanked sector is paramount to the success of bringing more people back into the financial mainstream. Mention must be made that banks with poor business models, reckless management practices and poor corporate governance do go out of business in South Africa and elsewhere.

During this study, an in-depth literature review was done to analyze the causes of strategic failures in the South African financial services sector, as well as analyzing the strategies proposed by other leading financial institutions within the local and international financial services industry and comparing this to Standard Bank's strategy. The research technique is essentially qualitative, but will involve the collection of quantitative and qualitative data through the use of a questionnaire.

This dissertation investigates what the big four banks in South Africa (with emphasis on Standard Bank) have achieved regarding opening up access to their saving and lending facilities to the unbanked, taking cognizance of the trends locally and internationally, finally leading to a conclusion as to the most appropriate strategy for the future.

An investigation will be conducted into whether this financial institution should employ a prescriptive or emergent strategy approach in order to successfully compete in this sector. The different lending strategies, namely linkage banking, downscaling, and dedicated banks are analyzed with reference to the international experience.

## **ABSTRACT (cont)**

In contrast to their enthusiasm for the low-income market, all the major banks have shown a lack of interest to engage this market to participate in the banking community, until now. One of the biggest challenges for banks is how to sustain the growth momentum currently experienced in this sector. The answer could lie in the revenue that will accrue from the big four banks and Postbank's recently launched Mzansi account initiative and its associated spin offs. It is not foreseen that the big four banks can or will be involved in micro-entrepreneur lending in the future, rather that this be done by creating dedicated banks.

The findings do show that Standard Bank has missed an opportunity to grow revenues and their approach is one of "this has to be done because it is a government regulation". There is no proper business model in place, HR practices are not aligned to the strategy and marketing initiatives are non-existent. Recommendations have been made to address these inefficiencies.

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# **CHAPTER ONE**

## **THE CURRENT UNBANKED SITUATION**

### **1.1. Introduction**

Providing basic financial services to the poor is a challenge to all countries. In South Africa, the country must find a way to reduce the inequality of incomes, economic opportunities and access to services, which stems from the apartheid era. There is a political imperative that the major financial institutions help redress the historically weak system of services for lower income people as required under the Financial Services Charter.

South Africa, the chosen study field within the financial services industry, has four large old private banks (Standard, ABSA, First National and Nedbank), as well as about 50 smaller banks. These banks with well-developed conventional banking skills and impressive banking technology provide sophisticated banking services to the upper income minority population. But after years of international sanctions and isolation, and without much domestic or international competition, the dominant banks have a high cost structure. Now exposed to the forces of globalization, the banks are being forced to work towards economic efficiency, cut costs, automate, and attempt to rationalize pricing and cross subsidization.

The dissertation will analyze the strategy employed by Standard Bank in meeting the needs of this market with regards to its positioning, pricing, packaging and promoting of the newly launched Mzansi bank account. Information will be gathered from published books, newspaper articles, published government and banking journals, internet searches using words such as 'unbanked', 'low income' and 'mass banking'. The study will also look at research conducted by Standard Bank's own research teams as well as conducting interviews with the relevant target market participants.

### **1.2. Background to the Study**

With a population of about 42 million, over half of the South African population falls below the poverty level, according to a report on the structure of the South African economy by ABSA Bank (ABSA annual report (2004). The report also states that the median household income of the majority

black income was less than R4,000 per annum, while the median for white households was near R30,000 per annum in 1991. The previous disadvantaged population, i.e. non-whites, had limited educational opportunities under apartheid, and as a result, illiteracy rates are high. Wage levels are also extremely low and unemployment in the formal sector is roughly estimated at 40 percent.

According to the ABSA Group report (2002), "Is the South African Banking Sector still sound", the main point contributing to the current high unemployment statistics is the fact that approximately 32,000 jobs were created per year, during the 1985 -89 periods, while roughly 400,000 people per year were entering the labour market. As a result, many must earn income in the informal sector, which is entirely cash-based. So the majority fall well outside the segment of the population courted by banks and only a minority of the adult population has bank accounts.

Banks, insurers and the government signed the Financial Services Charter on the 17<sup>th</sup> of October, 2003, according to the Standard Bank Annual report in 2003. Banks must move fast to roll out services in poor areas or risk a clash with the government. Finance Minister, Trevor Manuel, stated in his 2005 opening parliament speech that the government would pass laws forcing companies to increase black participation in the economy if businesses did not do so on their own. Seven South African lenders have already banded together for the launch of a new bank account for those who cannot afford regular bank charges. The so called Mzansi savings and transaction facility will allow customers a limited number of free transactions a month. Mzansi, which means "south" in isiZulu, will let customers electronically transfer funds, check their balances, receive mini statements and buy connection time for cellular phones.

### **1.3. Literature Review**

There is a distinct lack of consensus amongst South Africa's leading investment analysts as to which of the big-four banks will edge out its competitors in the coming years (Standard Bank annual report 2004)

According to his report, "*Banking the forgotten market*", da Costa (2004) states that the bank that best tackles the challenge of banking the forgotten market will win the war. In his report, he points out that the most overlooked potential competitive advantage for the banks lies in South Africa's

unbanked population. According to the report, assuming there are around 45 million South Africans then, at most, only 15 million are currently banked: He argues that the challenge is there – it is just a question of who will tackle it first.

Costa (2004) points out that the current low interest-rate environment has put pressure on profit margins. The report goes on to state that European, American and Japanese banks have experienced similar pressures in the past, and have proven that the correct response is a combination of cost cutting and simultaneous increases in transaction volumes to combat the margin decrease. He suggests that the key for South African banks is therefore the ability to find extra transaction volume in what many would regard as a saturated market.

There is an assumption in his report that this product will have an appeal to the target market and will meet the price expectations of the consumer to encourage extra volume transactions. Another assumption made is that the overall potential of this market is huge and similar in size to the population of these countries of comparison. This will mean a significant increase in revenue for these banks if these customers are brought into the banking environment.

Costa (2004) further notes that banks need to modify their approach, their channels and the products they offer in order to attract more clients. By coming up with innovative business models, banks will effectively improve the living conditions of those they serve, while also helping themselves. According to Costa (2004), one of the priorities must be the opening of a new breed of branches, close to the new target segment. His report states that a recent study found that Spain, for example, has a branch: inhabitant ratio of one branch for every 1000 inhabitants (38 931 branches). Germany has one branch for every 2 000 inhabitants (41 139 branches). South Africa, on the other hand, has just one branch for every 12 000 inhabitants (approximately 3 400 branches). The comparison will only hold value if there is an assumption that the structural conditions of South Africa is similar to these European countries.

#### **1.4. Motivation for the study**

The author has pursued this particular topic as there has been limited research done around this topic in South

Africa. The fact that this initiative is a government regulation and could have significant impact on the banking industry has led the author to try to fill this gap.

According to the Standard Bank annual report of 2004, South African banks have seized the challenges and opportunities offered by developments in technology, and Standard Bank, with 4.7 million accounts electronically linked, has proven to be particularly innovative in using technology to expand banking services to previously unbanked communities.

Reducing the costs of transactions through its ATM reliant E-plan product, and changing distribution channels through the construction of kiosks called E-centres, the bank has managed to reach hundreds of thousands of new lower income clients.

Whether the business model underlying E-centres, will prove to be sustainable, will depend on the sophistication of low income and unbanked clients, their take up rates of the various products, as well as the cost structure and achievable scale economies. While many authors have stated that providing banking to the unbanked can be achieved, there has been no concrete practical business model for success, as well as a sustainable strategy explored. This study will attempt to provide a business model that is sustainable and innovative to the banking industry.

## **1.5. Problem Statement**

“Banking the Unbanked” is a viable business proposition and not a purely social responsibility initiative.

Or

The Financial Service Charter led to the banks discovering a new untapped market that could revive declining margins and banks will not have to build in a loss factor in providing banking facilities to the rural areas.

## **1.6. Research Objectives**

The first objective is to assess the overall potential of the unbanked market and determine if the charter will lead to social responsibility or profit maximization for banks.

Secondly, the author will then establish if the product will have an appeal, overall vs. key competitor on a blind and branded basis.

Thirdly, the study will then attempt to evaluate what are the price expectations of this product by the target market.

Fourthly, the study will assess the age appeal, user and usage occasion profiles.

Finally, the author will determine if there will be a concept / product fit.

## **1.7. Research Design and Methodology**

### **1.7.1. Introduction**

A quantitative research approach is required for this study.

Qualitative research was conducted by the Standard Bank New Generation Leadership delegates in their respective business areas. Focus groups were conducted at bank sites which consisted of Standard Bank staff and customers. The findings of these focus groups were used to arrive at the target market. Inference is made by the author in the dissertation with regards to some of these findings.

The quantitative research was conducted by the author using a questionnaire.

### **1.7.2. Objectives of the quantitative research**

The primary objective of this survey is to assess the anticipated usage of the Mzansi account amongst consumers as well as consumer's perception of the Mzansi account.

More detailed objectives include:

- Affordability amongst consumers
- Acceptable bank charge
- Frequency of using the account
- Method of using the account
- How will consumers benefit from this account
- Will this bank account meet the needs of consumers
- Consumers comments – top of mind

### **1.7.3. Questionnaire**

The structure of the questionnaire will be in line with the objectives outlined above. The estimated length of the survey will be approximately 5 minutes.

Questions to be posed will include:

- LSM and demographic questions
- How affordable is the Mzansi account to you?
- Do you feel that the current bank charges of the Mzansi account are affordable? If not then how much do you think is an acceptable price for you to pay?
- How often would you use your Mzansi account?
- What method of transacting on the Mzansi account do you think you would use generally? And most often?
- How do you think you will benefit from this?
- Do you think this account will meet your needs?
- Any comments or suggestions in general?

The wording of the questionnaire will be structured such that it is understood and interpreted in the correct manner. It is foreseen that the survey will require questionnaires to be translated into Zulu, Xhosa and Sotho as the level of English amongst the target market may jeopardize the interpretation of the questions and ultimately the data for analysis. A person with multilingual skills will be present to translate the vernacular into English, if the need arises.

### **1.7.4. Data collection method**

Due to cost implications, data will be collected on paper and pencil. Consumers will be approached at taxi ranks, bus stops and public hospitals. Further to this it would be necessary to visit informal settlements to conduct interviews at respondents' place of residence as there are a fair amount of consumers who are unemployed but do have an income in the form of grants and pensions. Since it is unsure of the literacy rate amongst the target sample, the person conducting the interview will fill in questionnaires.

It will be clearly explained to consumers that this is merely a survey and that no information will be divulged to any parties. It will further be explained that all information gathered will be strictly confidential. Consumers will also be assured that they are not obliged to participate in this survey. The areas of fieldwork have been restricted to that of Soweto, Alexandra, Mpumalanga, Limpopo and North West Province. This is largely due to logistical restrictions.



### **1.7.5. Sample and sample size**

Statistics from the AMPS®2001 database revealed that the penetration of the LSM 1-5 group in South Africa is 61%. Based on that fact it was calculated that a sample of 300 would be enough to analyze data from the survey with a minimal margin of error.

The sample will consist of consumers that are LSM 1-5 as this is the focus of the target market. If a consumer does not fit within the LSM 1-5 category, they will not be able to participate in this survey. Furthermore, respondents will have to be aware of the Mzansi account to be included in the sample. Thus, the sample will be randomly chosen with no specific quotas on any other demographics.

### **1.7.6. Analysis of the data**

The information gathered from questionnaires will be put in an excel spreadsheet. Average scores will be calculated using the functions of excel. The data will then be presented on a powerpoint chart for further analysis. Conclusions will be based on this outcome.

### **1.7.7. Resources**

The author has access to computer hardware and software. My employer has agreed to pay all incidental costs as part of my course expenses.

### **1.7.8. Limitations of the project**

The study will not include detailed financial analysis of Standard Bank and its competitors due to the sensitivity of the information. Anonymity will be granted to senior staff members of Standard Bank when quoting their remarks and input.

Data collected will be mostly from residents in Gauteng, Kwa-Zulu Natal, Mpumalanga, Limpopo, North West, Eastern and Western Cape areas and will be generalized across the country. There is a concern that due to financial and time constraints, the sample will not ensure a large base size for general analysis.

Any solutions presented will be specific to the Standard Bank group and not industry-wide.

## CHAPTER TWO

### Literature review

#### 2.1. Introduction

The charter requires banks to increase lending to the black owned companies and families in the townships. Banks must also ensure that 80% of South Africa's 47 million people can find a branch within 10km of their homes by 2008.

According to an ABSA spokesperson in an article published in the Business Report on the 2<sup>nd</sup> of November 2004, the bank currently has 41 outlet types referred to as Self-Service Centers that offer ATM services, as well as limited teller transactions in semi-metro (townships), rural and metropolitan areas. Planning is underway to roll out 30 additional physical outlets in the financial year 2004/2005 and 400 ATMS in these traditionally underserved areas.

FNB has developed several pilot projects including bold initiatives such as its Portable Branch, where a prefabricated building is constructed in an area, at a fraction of the cost and time that a traditional brick and cement building would take.

Costa (2004) states that communication will also be a fundamental issue and that all banks should seek to have systems with multi-lingual capabilities in the near future. He goes on to suggest that banks should be able to offer their customers the option of receiving all their written communications in their preferred language. In a country with 11 official languages, a financial institution that really wants to serve the majority of the South African population has to start thinking about communicating with its clients in their own languages.

Again, the assumption is made that customers will live and work in their origin of birth areas. Another assumption made is that these customers will be able to communicate in more than one official language. In terms of employee recruitment, this would place huge pressure on the banks as they can only hire staff from these indigenous areas to serve these customers. Staff will have to be trained in all official languages if customers from other areas come to transact at their branch that only caters for the one language of the area. Apart from India, few countries have more than two official languages and it is easier to implement this strategy in these countries. This view of Costa has to be analyzed in terms of the rand value of this market to the banks, and the

willingness of these banks to deploy even more resources to serve this segment.

## **2.2. The Banks' approach to addressing these issues**

According to a report by Rand Merchant Bank (2004), the use of bank deposit facilities by the urban poor in South Africa accelerated with the move to direct deposit of wages. Most workers don't earn high enough to qualify for cheque accounts and instead use saving accounts. These saving accounts can have high transaction costs and these customers queue in banking halls on payday to withdraw their funds. Within an hour or more of queuing in the banks, wage labourers are forced by the principles of cash management to withdraw their entire payroll just a few hours after it is deposited, always incurring a hefty service fee for using a teller.

The provision of banking services for low-income clients is difficult to do profitably because of the low balances kept on deposit. Even if moderate balances are maintained, the clients may undertake many small withdrawals, driving up the costs of operating bank branches. Even with very low deposit interest rates, these clients usually generate losses. The pattern of bunching transactions on Fridays and on paydays is costly to the bank because it requires extra branch staff at those times, computing facilities and sufficient cash to handle peak load. This also crowds the banking halls, imposing an externality on the other customers of the bank. Therefore banks must either charge sizable transaction fees or subsidize low balance, high volume accounts.

In recent years, the banks have tried to move passbook savings account holders onto card-based accounts that can be accessed from automated teller machines (ATMs), where costs are lower. Due to the high illiteracy rates, noted to be above 50 percent amongst blacks according to the Rand Merchant Bank report (2004), the card-based system is resisted by many.

Standard Bank's E-plan product initially successfully addressed these problems by developing a valuable package of banking products, including new services and greater convenience for the user, while keeping the costs to the bank of providing services, under control. The program exploits demand complementarities and bundles services, which are sufficiently valued by poorer clients, to justify a fee high enough to cover costs.

However, with the arrival of the Financial Sector Charter, this current offering does not satisfy the conditions laid out in the charter. The major banks have been forced to work together to provide banking accessibility to any formal settlement within a ten-kilometer radius. This must be achieved by providing a common product that can be used at any of the major banks, without incurring extra charges. All this must be achieved without the major players colluding on prices. For the big banks, the challenge is to meet the criteria of the charter without having a detrimental effect on the viability and stability of the business.

A review will be done on the Standard Bank of South Africa, as to how the company is positioned to meet the challenges of this untapped market. With 6 million accounts and total assets of R395 billion, Standard Bank is South Africa's second largest bank overall and is its largest retail bank by assets (Standard Bank Group Country Profiler, accessed 2003). The report further states that the bank has market share across all income groups, with 38% of the high income market, 30% of the medium income market, and 35% of the low income market.

The study will look at the bank's current product offerings and its ability to meet these customers' needs. The study will also undertake to trace the flow of money in the general sector, such as informal settlements (Soweto, Alexandria and Khayelitsha) as well as more formal sectors such as mining communities. This will enhance the understanding of the spending patterns and the remaining amount of disposal income to save in these communities.

These residential communities will comprise of self-employed, unemployed, as well as people on welfare, with a varying amount of income on a monthly basis. A comparison will then be made with the miners, who have permanent employment and hence, a steady monthly income. The study will also look at the "myths" or perceptions of the banking industry and how it compares to the realities of customers' banking needs. The study will then look at the corporate strategy employed by Standard Bank and compare it to the other industry players, as well as to other "unbanked" banking models that were successfully employed in other countries.

In an article published in the Business Times on the 4<sup>th</sup> of October, 2004, Neville Chester of Coronation Fund Managers stated that if banks were to lend in areas where there is no effective rule of law and very little property ownership, they would lose money. The article also stated that spending on

services to underdeveloped areas might harm banking growth if the lending rules forced institutions to abandon the ability to choose all their lending prudently.

The article referred above notes that local banks have been reluctant to provide home loans in poor areas, arguing that more than a fifth of the money they invest is never repaid. However, these risks have not kept Barclays, the UK's third biggest bank by assets, from trying to buy a majority stake in ABSA, South Africa's fourth largest lender. The article further notes that bank profits are rising after six interest rate cuts in the past 16 months as return on equity, a measure of profitability, was 22 percent or more in three of the big four banks in SA. That compares with a median of 13.3 percent among the 80 members of the Bloomberg Europe banks and financial services index in 2003.

Now branches are popping up all around the country. Standard Bank plans to add 21 more similar branches to the seven 'bank-in-a-box' it already has. ABSA plans to open 300 ATM's in townships over the next year.

Lenders have pledged not to profit from serving the townships, according to Cas Coovadia, in an article published in the Sunday Times, Business Report dated 4th October 2004. This does not look to be profitable in the short run for the banks, but hopefully, it will secure the customer base of the future should the country's effort to redistribute wealth be successful. One of the biggest challenges for banks will be to avoid attracting current customers to the cheap accounts. The product needs to be cheap enough to lure those without accounts, yet constrained enough to prevent existing customers from moving their accounts.

No matter how banks structure charges, the strategy is to get into the low-income market without making losses and then to profit as customers become wealthier. The banks will do this by pushing customers to the low cost electronic banking facilities such as ATM's, because the human interface at branches is where the cost is.

Tyobeka (ABSA annual report, 2004) mentions that to reduce costs, Absa plans to give bank representatives portable devices that let them carry out credit checks and issue cards while on the road. Like other banks, ABSA will also promote cellphone banking.

Banks are trying to set up storefronts as cheaply as possible. It costs Standard Bank less than R600 000 to build

and drop off a 'bank-in-a-box', notes Lincoln Mali, of Standard Bank's Convenience Banking unit in Johannesburg, in the Standard Bank Annual Report 2004. Mali also states that it is much quicker and takes only two weeks to set up, whereas a brick building could take months. He emphasizes that there has to be a first mover advantage to reap rewards as the bank that does open a branch first in a new community usually becomes the dominant bank in that community.

The approach, followed by the banks broadly corresponds with strategies that have already met with success internationally. These strategies include:

- *setting up from scratch*, a bank dedicated to provide basic banking services to the previously unbanked;
- *creating a separate division within an existing bank*, to serve this market (also referred to as downscaling);
- *linking banks with informal financial institutions*

The only strategy not tried in South Africa is that of credit granting non-governmental organizations (NGO's) transforming themselves into banks (also known as upgrading) due to, amongst others, NGO's not having reached the scale of activities necessary to make upgrading viable.

These points above indicate that not much has changed since the early 1990's with regards to the big four banks low income lending policies. One may argue that irrespective of the strategies followed by the banks, structural characteristics (high unemployment, low education levels and a skills shortage) unique to the South African economy may be responsible for this lack of progress.

In their annual report of 2003, ABSA states that its customers are served in the language of their choice at any of its outlets. The bank also plans to provide vernacular languages via the ATM network whereby customers can choose which language they would like to transact in. According to the bank, this project is currently in pilot phase and is being tested at numerous ATM's countrywide until the end of February 2006. Once the bank is satisfied with the results, it plans to have a national rollout in March 2007. This strategy is based on the assumption that most customers are literate and have technological savvy. One would have to doubt if this approach would have the proper appeal in terms of age appeal, user and usage occasion profiles in rural areas where access to banking is paramount. Based on these profiles, one has to doubt if there would be a

concept / product fit.

The report further comments that products and services also have to be revised, and must be understandable enough to prove to the most unsophisticated client the advantages of placing money in a bank account rather than under the mattress or inside a shoe box in the closet. This statement is based on the assumption that people are different and products must be adapted to the market. Currently there is a 'one product for all customers' approach being undertaken by all the banks.

Nedbank is working on a number of projects that will use new means of product delivery and service to make products more affordable. According to the banks Annual Report 2004, while it is recognized that the entry-level customers require the highest touch and levels of service, it is not possible to provide this due to affordability issues. The bank does admit however that there still needs to be a credible level of client support that fulfils client expectations irrespective of their social status regarding income earning potential. The report adds that most of the solutions being developed will be built on smart-technology platforms that will enable clients to access cash, make purchases and receive funds while product segment needs should not be individually assessed.

The reasoning is that while Nedbank does understand that all customers are not bankable at this stage, it does make the assumption that these unbanked customers will prefer to use technology over the in branch service platform. The report also advocates the objective that this initiative is more a social responsibility and that these customers will have to adjust to the bank's current offerings as opposed to the bank creating an offering that will appeal to these customers to become a part of the financial mainstream.

First National Bank's (FNB's) approach to this challenge, according to their annual financial report in 2004, is the introduction of smart accounts which attract some 40 000 new customers each month by providing transactional services at low cost. The bank's no-cost value add-ons include medical advice, legal assistance, emergency evacuation, R2 000 guarantee of medical payments, repatriation of mortal remains and teacher on-line. All these value add-ons are available on a toll-free number. FNB's approach can be commended as it is only through value added initiatives that more people will bring their cash into the banking environment. However, there is an assumption by FNB that the price expectations of this target market are being met in terms of what the banks call 'low costs'.

The latest competitor to attract the unbanked is Postbank, which is the savings institution that is a division of the South African Post Office. In an article published in the Star newspaper dated October 18, 2004, the bank issued a statement stating that its pricing structure would be particularly competitive. The article noted that Postbank already has more than 1.8 million savers, and with access to more rural areas than the banks have traditionally serviced, the Post Office's infrastructure will complement the Big 4 banks' delivery footprint.

Once again, there is a statement around pricing this product competitively. As a government institution, there is a hint of profit maximization by Postbank over the social responsibility of getting people to save. Surely the costs associated with a government organization should be lower than other business entities especially in terms of their savings on taxes. Postbank should be in a position to offer this product at a much lower price than the other competitors. Without price collusion, the market is open to gain as much profit out of this segment as would otherwise be allowed by all the banks.

The article published in The Star newspaper dated October 18, 2004, further notes that the most difficult aspect of dealing with the forgotten market will be on how to manage credit risk while affording credit to a very heterogeneous market. This article suggests that in order to lower the credit risk associated with lending money, the banks should lend money to communal interest groups rather than individuals. This might be a group of 50 people building a new home together, or a civic-responsibility group wanting to finance appliances conjointly.

By approaching their potential clients through community groups, banks will minimize their risk by leveraging the whole group's commitment not to default. An assumption is that this segment is heterogeneous and that the banks will provide a product and customers of this segment should be grateful and accept it. Until they become more responsible in terms of the banks' criteria and pose a lower risk to the banks, this is all that will be given to them. For now, the banks will decide what the concept / product fit is.

ABSA agrees that managing credit risk amongst the lower end of the market is a major challenge. In their annual report 2004, the bank notes that several organizations have been involved in community and cooperative banking in South Africa, but there have not been major successes to date. The reports states further that expected introduction of



legislation enabling 2nd- and 3rd-tier banking will provide the regulatory framework for prospective participants in community banking and should reduce the costs of providing products and services in these structures. Again, there is the affirmative that banks will still lend prudently and will not be pushed into making decisions that will affect their stability. One has to question if the Financial Services Charter will force banks to venture out of their conservative approach and commit to social upliftment in the hope that the potential of this market will be profitable in the long term.

FNB and Rand Merchant Bank (RMB) have already undertaken several housing projects by providing finance to housing associations rather than financing individual properties. According to FNB, some 2 447 houses were financed via the King Williamstown Housing Association. As yet, no results have been posted by FNB to state that this has been a successful business model in terms of limited payment defaults.

Upon analysis of these different reports it can be argued that those banks that start implementing the appropriate functional models to address these 30-million unbanked South Africans will experience two major benefits.

The first is the fact that these new clients may become increasingly sophisticated - and sooner than many would predict. They will soon be buying other products, enabling the banks to reach the transaction and sales volumes they really need to survive in an evolving market. The assumption that this product will have the correct user and usage profile will have to hold true for this to happen.

The second, and certainly not the least, is the satisfaction of knowing that their financial institution has done the right thing and has been a significant contributor to the success of South Africa. This assumption is based on the fact that all stakeholders are willing to share the responsibility of uplifting society in partnership with government, and investors in banks will not look at other investment vehicles to maximize their returns.

According to a survey conducted by Finmark Trust on their website in 2003 (<http://www.finmarktrust.org.za>), a survey of the current levels of access to financial services among the different income groups shows an estimated 17.6 million individuals who do not have bank accounts – or are unbanked. Thirty two percent are economically active and they predominantly reside in either rural areas (35%) or urban informal settlements (24%). About one in five (21%)

work in the formal sector, either on a part time or full time basis.

The survey reveals participation in the formal financial system as follows:

- 1) 13.7 million adults currently banked
- 2) 3.7 million adults previously banked
- 3) 9.5 million adults never banked

The survey notes that ambitious targets have been set for these population segments (LSM 1-5), which make up about 65% of the population (Annexure 16). The findings suggest that reaching the target market (LSM 1-5) will require a concerted effort between private sector and government, and new forms of public-private partnership

According to Warren Porteous from Finmark, the survey reveals that only 7% believed that banking costs are too expensive and 3% found banks inaccessible. The survey found that the time it takes to cover the physical distance is more of a barrier than the cost of travel. This contradicts the belief that people are currently unbanked because of the high fees charged by banks.

The Finmark findings also contradict the belief that this segment finds that banks makes them feel as if they don't belong there and the belief that there is not enough representation in some areas. The survey however does not show how many branches were closed because of a drop in customer base (no job, no money, no need for bank accounts) and for security reasons.

Other Finmark findings include:

- One in eight adults has no source of income.
- Family members play a crucial role in the support structure – most South Africans receive support from family members. Reliance on family is the least prevalent amongst White South Africans.
- Most grocery purchases are paid for in cash.
- Of money in circulation, the majority does not make its way into the banking system.
- Most South Africans do not have savings and investment products.
- Overall, there is a very low usage of mainstream investment vehicles – instead bank savings accounts and burial societies still account for higher usage.
- One in five South Africans has a store card.
- The majority of South Africans live in formal housing, most in brick houses.

- One in five black South Africans live in informal housing.

Using this information available to the different role players, the study will (at a later stage) have a look at the competitor activity to analyze what progress has been made to maximize this statistical information. The study will go on to show how the previous published research has informed the author's research questions and objectives.

According to the economic journal published by the Absa Group Limited (2002), *Is the South African banking sector still sound*, the South African banking industry has long been regarded as fundamentally stable. Its capital adequacy levels are good, amounting to 11.1% as at January 2002. Its 10% return on equity (ROE) in 2001 was also sound and at 62.2% as a percentage of total income in 2001, its operating expenses were also acceptable. In 2005, capital adequacy levels of all banks could be as high as 14% if need be, and ROE was in excess of inflation plus 65 % for three of the four major banks. Operating expenses were well under 55% for the major banks.

With banking conditions this great over the last few years and no previous initiatives from banks to help the unbanked market, one has to doubt the willingness of the major banks to sincerely contribute to society unselfishly. Rather, there is a case of 'it is the law and we have to do something about it'. While the big banks have been financially sound, one has to analyze the impact of the smaller banks on the industry as whole.

The series of small bank failures in South Africa in recent years has held negative connotations for the banking sector. Small banks are often more prepared to take risks and venture into new markets than bigger banks. One of the problems facing a developing economy such as South Africa is the severe lack of risk capital available to entrepreneurs. That is why small banks have started to address the needs of the low income South Africans by providing access to credit. South African small banks also provide some competition in certain areas of banking business. Major banks in South Africa today, such as Investec and Rand Merchant Bank, were once small banks.

Unfortunately, market conditions in South Africa have made life difficult for small banks. Low growth has implied limited fixed capital formation activity. These banks often fall prey to the temptation to try to expand too rapidly, taking on unjustified risks and acquiring poor quality assets. Other

fundamental macroeconomic factors have also hindered small banks. In particular, the poor domestic savings ration in South Africa and especially the 0.3% of personal disposable income saved by households. If the big banks had been more willing to make credit available to this market, one has to assume that there would not have been such a low level of entrepreneurial activity and a propensity to save by this market.

The latest pressures show that, although small banks have a role to play in South Africa, the role should not ideally involve acting as the custodian of the nation's savings to any significant extent. According to ABSA's Third Quarter report, (2002), small banks are not good outlets for small savers. The fortunes of the micro lending industry cannot be separated from those of the South Africa's banking system as a whole. The big banks have extended loans to these micro lenders and should the micro lending industry collapse; the rest of the banking system could be badly shaken.

Banks with poor business models, reckless management practices and poor corporate governance do go out of business in South Africa and elsewhere. Propping up weak banks by using central bank or government funds can be a recipe for ongoing instability in the banking sector of any country. Japan's banking sector crisis during the 1990's serves as evidence of this. The decision by the South African Reserve Bank (SARB) not to bail out Saambou (a small bank) is a case in point. Many would argue that the SARB supports the current monopoly of the big 4 banks and this results in an injustice to the people of South Africa as they are held ransom to high bank charges due to lack of competition. Supporters of the Reserve Bank's stance would argue that this is the reason why the banking industry is so respected worldwide and has therefore avoided any huge financial crisis.

According to the IMD's *World Competitiveness Yearbook for 2002* published on their website ([www.imd.com](http://www.imd.com)), South Africa was ranked in 39<sup>th</sup> position out of 49 countries evaluated. However, South Africa was ranked 19<sup>th</sup> in terms of the level of banking services available in the country. This indicates that the banking sector plays a significant role in enhancing the country's international competitiveness. According to the IMF and World Bank, South Africa strives to meet international best practice in financial regulation and supervision.

The banking sector is also a window on the economy for international investors and traders. It gives them an indication of the state of the economy. Banks, like many other industries, have been subjected to various structural changes in the domestic and international environment. Not only have changes to the monetary policy framework effected a different environment for interest rates and inflation, but also the credit and savings preferences and behaviour of economic agents have shown significant shifts in recent times.

Inflation peaked in the mid 80's but remained in double digits until around 1992. High interest rates were the major weapon used by the monetary authorities to bring inflation down. The relatively high inflation environment afforded banks the opportunity to attain higher return on assets (ROA) and return on equity (ROE) figures than would otherwise have been the case. The banks' net margins (the difference between the average weighted lending and borrowing rates) were also previously higher than they are now, in the current lower inflation rate environment. This lessened the need to aggressively pursue avenues of non-interest (fee) income. With conditions still at similar levels, one cannot see banks willing to risk decreases in profit margins to serve a market they still refer as too costly to serve.

Since the early 1990's, lower inflation has forced banks to allocate even more resources to other financial services, such as securities trading, insurance, life assurance and asset management activities. The need for more fee base income also increased while aggressive cost cutting exercises have been continuing across the banking sector. The result is that South African banks are now generally more diversified (in terms of product offerings) while their costs structures are more in line with those of banks in developed countries.

It has been suggested in the ABSA annual report 2004, that a bank deposit insurance scheme should be introduced in South Africa, since such a scheme may prevent runs on banks (where depositors become scared for whatever reason and withdraw all their funds). A deposit insurance scheme, involves the collection of a small premium from depositors to protect them from losses arising from the closure of bank. However, such schemes can also encourage depositors to disregard risk aspects, and place their funds with high-risk banks paying higher interest rates. For this reason, bank deposit insurance schemes normally offer protection only to small depositors up to a certain amount. Bank deposit insurance schemes will therefore not necessarily avert runs

on banks or prevent the onset of curatorships, although they do make the process of paying back small depositors more orderly, equitable and transparent. Regulatory controls will have a major impact on the way banks do business into the future.

The New Capital Accord, known as *Basel II*, is a radical reform of the previous accord and will apply to all major banks in the G10 countries as from 2005. Basel II will impact on banks on various fronts, including regulatory capital, credit and operational risk management, data requirements and investor perceptions. Changes to banks' capital requirements will imply that capital adequacy ratio will increase from 8% to 10% whereas the primary capital needs to increase from 50% to 75% of total capital. Among other implications, these changes could have significant tax implications for banks.

With regards to risk management, banks will increasingly have to monitor and manage their exposures to market risk, credit risk, liquidity risk, operational risk, bankruptcy risk and reputation risk. According to the journal article published by Lobenhofer, JS, Bredenkamp, C, and Stegman, MA (2003), in terms of technology and delivery mechanism, South African banks now have 1.1 million registered Internet users. Technology will probably afford banks the opportunity to locate their physical branches more strategically. Branches could also be smaller in size and the costs per branch lower. The assumption on technology is gain based on the fact that the target market has equal access to education, is literate and trusts technology.

The report states that ongoing innovation in Web based financial applications and banking technologies, as well as the accompanying reduction in the costs of account maintenance and transactions, suggest that the lower income market segment is no longer as unbankable as in the past. In particular, the emergence of banking products based predominantly in ATM transactions, with minimum in-branch services, has helped lower the costs of providing banking services while reducing the risks of overdrafts for the low income customer.

Some players in the banking industry are realizing the income generating potential of this technology. Transforming their ATM's into more sophisticated portals for financial services and moving from traditional branches to e-branches, so that accompanying cost-savings will enable them to expand their market to client segments that they were previously not able to serve profitably. For this strategy to

work, extensive education programs will have to be implemented regarding ATM and other technological usability.

Recent years have seen a number of efforts by financial institutions to harness technology to reduce the costs of serving their clients, particularly low-income, low-balance customers. ATM 's are one of the most frequently used technological devices, though other electronic payment systems such as point of sale (POS) with debit cards and stored value cards are gaining popularity. Stegman in his journal article in 2002 titled, *"Banking the unbanked: untapped market opportunities for North Carolinas financial institutions*, notes that the prevalence of this approach to banking the unbanked can be seen in the United States, where a third of all banking transactions are conducted via ATMs.

ATMs are an incarnation of developments in kiosk technology and the banking sector has made use of the convenience, accessibility, and income generating and cost saving advantages of this form of technology for decades. Banking companies here and elsewhere have begun using card technology and ATMs to expand their client base and reduce operating costs in innovative ways. This includes the electronic distribution of wages to employees with bank accounts as well as the transferring of money abroad by immigrants.

Stegman's (2002) report further states that in the USA, there is a possibility that Mexican migrant workers with card only accounts will be able to obtain duplicate cards for family back home, enabling them to withdraw from Mexican ATMs. This will facilitate the transfer of remittances and eliminate the costs of international money orders. This could be a possible strategy for Standard Bank as South Africa has a number of migrant workers from neighboring countries and the bank has branch representation in each of these countries. This will be based on the assumption that there are no major structural and legal differences in the banking environment between these countries.

With respect to the card only accounts, First National Bank (FNB) has developed a payroll card to reduce crowding in the branch lobbies on paydays, as workers without bank accounts attempt to cash their pay cheques. Card only accounts have been opened for employees and employers deposit wages directly into the accounts.

According to the Rand Merchant Bank (RMB) journal published in 2004 on the FNB website, ([www.fnb.co.za/economics](http://www.fnb.co.za/economics)), these employees have proven to be very good customers, making use of other bank products and services.

Stegman (2002) further comments that in the United Arab Emirates, the 'meBank' approach of the Emirates Banking Group is certainly one of the most progressive in the world. This is very different from traditional labour intensive branches as each branch contains a number of ATMs and PCs on which clients can themselves conduct all routine transactional services. Rather than dealing with mundane everyday transactions, the staff's job is to welcome customers and offer advice on loans and other financial services. These branches are also conveniently located in accessible places such as corporate buildings, airports, universities and coffee shops throughout Dubai. One has to question the relevance of this strategy to the South African market in terms of the differences in educational and understanding abilities.

Standard Bank had previously launched an even more ambitious electronic delivery system called E plan to target low-income customers. Among other e-banking efforts for the unbanked, the E plan concept is innovative in its use of a separate brand or product suite as opposed to a single account, as well as for the challenging context in which it occurs. Considering the success of this product over the years shows that Standard Bank has the capability to address this market successfully but at their own pace and risk comfort. Standard Bank's E plan will be assessed in detail, including the banking and social contexts in which it exists, specifics of the product, and the challenges it faces moving forward. The study will also have a look at the Mzansi savings account and assess it on similar criteria as the E plan savings account.

In general, the South African government has issued guidelines rather than prescriptive regulations governing the development of e-commerce. This approach has offered the country's banking institutions regulatory flexibility, enabling them to test different approaches in an effort to meet both market demand and their business requirements. One has to bear in mind that majority of the black population only had access to a computer when they entered the working environment. This is in stark contrast to other countries where children are exposed to computers at a primary school level.



The dearth of banking opportunities for lower income people arises from the difficulties on the supply side, where banks traditionally have not been able to profitably serve the poor. International experience suggests that small account balances and low volume of transactions result in high administrative costs for these accounts, especially in over the counter banking environments, with the consequence that people with incomes below a certain threshold may be denied bank accounts. The introduction of the Mzansi account initiative does contradict business belief that any initiative should have a level of profitability attached for the strategy to be deemed successful.

In South Africa, the banking products and distribution channels of most established financial institutions have been found to be appropriate for the minority few. Even the most basic accounts have features that lack transparency, are costly and feature complicated permutations of charges, minimum account balances, or sliding scales for withdrawals and transactions.

With respect to distribution channels, the operating costs associated with labour intensive regional offices and branch networks are too expensive for banks to profitably serve clients who maintain low account balances. The question of who determines what is a low balance and whether banks believe that many cents can add up to lots of rands (South African currency) has to be asked in order to test this assumption that banks cannot serve clients profitable if they maintain low balances.

Yet drawing low-income people into the financial mainstream is recognized as critical to economic growth and social stability in South Africa. This has been the motivation for the research.

Electronic funds transfer - or delivery of government support through direct deposits present new opportunities for financial institutions to better serve unbanked and marginally banked populations. Doing a better job of bringing the unbanked into the financial mainstream is important because one's banking status has profound implications for long-term family self sufficiency. According to the ABSA Group journal published in 2002, the median value of all assets held by unbanked families was R2300 compared to the median value of R136 000 of banked families in the year 1998.

Lack of savings is particular important to low and moderate-income families; as well as unbanked families in general as

these people are unlikely to be covered by a retirement plan at work.

The benefits to this sector will result in social upliftment in these societies and reduce dependence on the government to provide help with social grants.

The launch of the Mzansi account will give affordable access to the formal banking system to all South Africans for the first time. Ten years in the planning, the national banking account hopes to bring more than 13 million citizens into the banking mainstream.

But the birth of South Africa's latest strategy to include more people in the banking sector has not been easy. The past few months have been painful with labour union and political party unhappiness threatening to thwart the initiative. The Congress of South Trade Unions (Cosatu) and the SA Communist Party threatened to boycott the financial services sector, withholding support for the Mzansi initiative. They have since expressed their support after each was given three seats on the charter council.

Participating banks have promised to provide their potential new clients with access to core banking services for about half the costs of existing products.

Mzansi will be offered by ABSA, First National Bank, Old Mutual Bank, Nedbank, Standard Bank, Peoples Bank, Postbank and the Eastern Cape's Meegbank.

With about 13 million customers in the offering, banks will have to chase after these new clients. Banks will co-brand their Mzansi offerings – with the risks that the accounts may cannibalize their existing low-end offerings, but with the benefit that they should be able to migrate Mzansi customers onto their mainstream platform over time.

Banking is a volume game that relies on passing high fee-based transaction volumes over bank's information technology infrastructures to drive down unit costs. The greater the take of Mzansi, the more attractive it will be for banks and the more likely the charges will remain low.

Proposed banking legislation in the form of the Dedicated Banks Bill and the Co-operative Banks Bill could stimulate the creation of more banks willing to participate in the Mzansi scheme.

In the United Kingdom (UK), the government tried four years ago to establish a universal bank using the six major banks

and 18 000 Post Office outlets. But the idea died over government indecision on who would qualify for these accounts and the high cost of providing them. The UK has reopened talks on the idea. South Africa's Mzansi product provides an inspiring model.

The study will now analyse the manner in which the five banks built a brand through "co-opertition".

### **2.2.1 The introduction of the Mzansi account**

When the banking industry committed to the Financial Sector Charter to making banking accessible to all South Africans, they realized that it would not be business as usual. Two years before the launch of the Mzansi Account, a dedicated group of bank employees across First National Bank, ABSA, Standard Bank, Nedbank and the Post Office, through Postbank, started working behind the scenes on this project. The banks adopted an approach referred to as "co-opertition" – competitors working together to access a new market and to compete in that market for objectives beyond commercial interests.

From a marketing perspective, it seemed an almost impossible task to get five competitors, each with a different marketing philosophy, to agree on a joint brand and marketing strategy. The marketing committee, one of a number of inter-bank committees, was given nine months to launch the product. In that period a brand strategy had to be developed, the marketing plan had to be finalized, agencies had to be selected and appointed, as well as the campaigns had to be produced. None of the marketers were involved on a full time basis and their collaborative Mzansi responsibilities were in addition to their usual work load.

Given the complexity of the project, it became clear that no single person or agency could manage this project alone. The marketing committee soon realized that they needed the expertise of different specialized agencies to complement their marketing knowledge. The Mzansi launch succeeded (500 000 accounts were opened in 3 months) because of the professionalism and drive of all the people and agencies involved.

Developing the Mzansi brand was the key to encouraging a strategy that might reap awards in the long term for each bank. The first step was to develop a brand strategy. The challenge for the banks was to convince the target market that they were welcome and that the banks had suitable and

affordable offerings for them. The banks all have strong brands to which the target market aspires, however the banks needed a “mechanism” to help them to relate and interact with the target market. Under the guidance of the Enterprise IG, the banks developed a brand strategy in order to:

- Support and align to the brand architectures of the participating banks.
- Ensure best use of the cooperative space to build awareness and educate the target market.
- Ensure differentiation within the competitive space in order to leverage the existing equity of the banking brands.
- Enable migration and limit cannibalization of existing products where possible.

The robustness of the brand strategy was proven when the Minister of Finance objected to what appeared to be “collusion” amongst the banks and belated adjustments had to be made to the standardized offering. Despite these changes, the existing brand strategy needed no changes to comply with the requirement that the marketing of the product had to be competitive. After the brand strategy was agreed on, Enterprise IG developed the style and visual language for the new brand. The next step was around developing an effective communication strategy.

The challenge for the banks in developing a communication strategy was to bridge the gap between the existing perceptions and the aspiration of the target market and what the banks have to offer. Although the target market feels intimidated by the banks, they certainly don't want a “poor man's bank”. The banks had to convince the market that that they offered an account which was affordable and accessible but which offers all the benefits of being a customer of one of the big banks and Postbank.

The banks realized that only a broad communication approach that included advocacy, PR, experiential marketing and advertising, would enable the gap to be bridged. In conjunction with advertising agency, Inroads, and experiential marketing agency Exp Momentum, an elaborate and pro-active communication plan was developed. It was decided that a phased approach to the campaign would be most effective.

In the first phase before the launch, key stakeholders and interested parties were informed of the initiative. The aim was to ensure a soft landing for the initiative by explaining

the initiative to organizations and individuals who influence public opinion. Prior to the launch, Fleishman-Hillard was commissioned to run the PR campaign. During this period a coordinated media strategy was used to ensure that the media had access to the right information.

The success of these initiatives was evidenced at the nationwide launch events of the Mzansi Account on 25<sup>th</sup> October 2004. The events received substantial media attention and were well attended by representatives of civil society.

In the third phase, awareness of the Mzansi Account was created through a broad advertising campaign using radio, television, outdoor and print. Radio, including community radio, was used to reach the broad target market informing them of the benefits. The radio advertising was accompanied by editorial inputs through interviews. Television was used to create credibility in the target market and create awareness in the critical phase of the launch. Print was used to accompany the information provision through editorial. Outdoor advertising, provided by Clear Channel, was used to reach the target segment where they live and work. More than 350 billboards were used.

Simultaneous to the advertising campaign, the Mzansi account was taken to the target market by means of an outreach campaign. For six weeks, five teams in Mzansi-branded trucks toured the country. The teams visited 625 locations promoting the generic product through industrial theatre and by talking to local "opinion makers". The campaign aimed to educate and encourage trial and usage of the Mzansi Account.

Commentators have referred to the marketing efforts as a "low-key marketing campaign". Given the results, it could be said that the marketing campaign struck the right chord. The banks had to learn fast how to communicate with a market of which they had little understanding. They realized that only a broad and thorough approach would guarantee success. Instead of having an aggressive advertising campaign on mainstream radio and television, the banks chose to take the campaign to the target market. In this way they reached the target market in a myriad of ways in their daily lives, out of sight of many readers and writers of the financial and marketing press.

The real success of the launch campaign came about when the marketing team realized they had to overcome the dilemmas of "marketing by committee". Good marketing

requires courage. When a committee develops marketing, it is easy to hide in the group as there is always safety in numbers. Initially, the members of the team adopted the stance: "As long as it does not harm my bank, I am okay". However, when the advertising agency hit hurdles with the creative, the team realized that they had to collectively take responsibility if the campaign was to work.

Another reason for the success is the way in which a relatively large number of advertising, PR and marketing professionals were able to work together. Everybody involved were enthused by what the banks were trying to achieve and the fact that the banks wanted to try innovative ways of reaching the market.

Opening half a million bank accounts in just over three months is no small achievement and no coincidence. The banks have managed to develop the right product to address the needs of the unbanked and built on what appears to be a powerful brand. Without proper marketing, 500 000 people would still believe that they are not welcome in the banking system.

However, the banks realize that they will only be able to claim victory when a substantial number of the millions of unbanked have been brought in the formal financial system. The Mzansi brand has a role to play in reaching the unbanked and there is still a lot to learn on how to manage this kind of brand. Nowhere in the world have commercial competitors established a brand to better service a particular market with the aim of aggressively competing with each other in client acquisition and servicing.

### **2.3. Summary**

In the new economy, it is as important to have access to a basic banking account as it is to have access to electricity, running water and telephone. The release of the Financial Services Charter, in which the major leaders of the big 4 banks were involved in drawing up, has become a firm commitment by these institutions with the persuasion of government, to ensure that every South African has access to a banking facility at a maximum of 10 kilometers from an established community. Specific deadlines have been set, in which these banks will face huge penalties, if they have not achieved the agreed proposals.

# **CHAPTER THREE**

## **Analysing the concept of strategy**

### **3.1. Introduction**

As South Africa celebrates 10 years of democracy, one needs to pause and reflect on far as a country they have come, whilst also casting gaze on what is still needed to strengthen their democracy. Clearly, one of the major areas of focus for the future has to be the extension of financial services to a larger section of the population. This is both a business and socio-political imperative.

In terms of the business imperative, the pressure on margins is forcing SA banks to extra transaction volume to counter this effect. Unlike more mature financial markets that faced this challenge previously, South African banks have an opportunity of a huge market that is still unbanked and underbanked. The key to service this market is through innovative products, delivery channels and business models. The question that needs to be asked is which of these banks have a winning strategy that is good enough to reap the rewards that this market presents.

Using the definition by Richard Lynch (2000), corporate strategy is concerned with an organization's basic direction for the future: its purpose, its ambitions, its resources, and how it interacts with the world in which it operates. Every aspect of an organization plays a role in this strategy- its people, its finances, its production methods, and its environment. An examination will be undertaken on how these broad areas need to be structured and developed if the organization is to continue to operate effectively.

Corporate strategy is complicated by the fact that there is considerable disagreement between researchers on the subject and how its elements are linked together. There are two main routes that we will examine: the prescriptive process and the emergent process. Use will be made of these two models to explain the above-mentioned subject. Use will also be made of Porter's diamond model in the analysis.

### **3.2. Analyzing the meaning of the word 'strategy'**

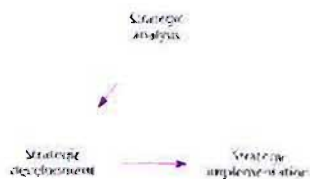
According to Hitt et al. (2002), in exploring corporate strategy, it is useful to begin by examining why it is

important and what it contains. A useful distinction can be drawn between its process, content and context. The two main routes are then explored and the key question explored – what makes ‘good’ strategy.

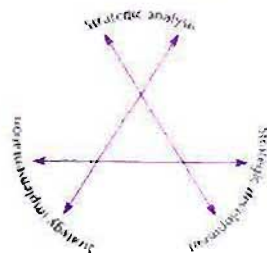
An analysis will be undertaken of the environment, the market and competitors and of the customers with regard to customer profiling and customer value added. A further analysis of the resources in terms of human, financial and operations will then be completed as well as an analysis of the purpose of the organization, which is shaped by the vision, leadership and ethics. Finally, the dissertation will look at developing a winning strategy and the implementation of this strategy.

### 3. 2.1. What constitutes a good strategy.

(a) Sequential approach – one area follows another for reasons of clarity and development



(b) Simultaneous approach – all three areas may be implemented at the same time for different parts of the organization



**Fig 3.1: The three core areas of corporate strategy**

Source: Lynch, R (2002). *Corporate strategy*, page 19 (Second edition), Prentice Hall Publications, Essex.

According to Richard Lynch (*Corporate strategy*, second edition, p28), in order to determine what makes “good” corporate strategy, several important questions need to be asked around the three areas of corporate strategy (Fig 2.1) such as the ones below:

- Was the purpose itself reasonable. For example, perhaps the purpose itself was so easy, that any old strategy would be successful.



- What do we do when it is difficult to define the purpose clearly, beyond some general objective of survival or growth. Such vagueness may make it difficult to test whether a “good” strategy has been developed.
- Since the whole purpose of strategy is to explore what we do in the future, can we afford to wait until it has been achieved before we test whether it is good.

Essentially we need some more robust tests of good strategy. These lie in two areas. First, those related to the real world of the organization and its activities, application related. Second, those that rely on the disciplines associated with the basic principles of academic rigour which are originality, logical thought and scientific method.

The next step is to analyze what are the tests of good strategy: application related.

Lynch advocates on (p29) that there are at least three tests available that provide some means of assessing whether a strategy is good:

- 1) *The value added test* – a good strategy will deliver increased value added in the market place. This might show itself in increased profitability, but might also be visible in gains in longer-term measures of business performance such as market share, innovative ability and satisfaction for employees.
- 2) *The consistency test* - a good strategy will be consistent with the circumstances that surround a business at any point in time. It will take into account its ability to use its resources efficiently, its environment that may be changing fast or slow and its organizational ability to cope with the circumstances of that time.
- 3) *The competitive advantage test*- For most organizations, a good strategy will increase the sustainable competitive advantage of the organization.

The next stage is to now analyze what are the tests of good strategy: academic rigour related.

Another five tests mentioned by Lynch (p32) might also be employed that relate to the above but are more fundamental to the basic principles of originality, logical thought and scientific method.

- 1) *The originality test* – the best strategy often derives from doing something totally different. However, this will need to be used with considerable caution or it becomes just another excuse for wild and illogical ideas that have no grounding in the topic.
- 2) *The purpose test* – Even if there are difficulties in defining purpose, it is appropriate and logical to examine whether the strategies that are being proposed make some attempt to address whatever purpose has been identified for the organization. Such a definition of purpose might be taken to include the aspirations and ambitions of the leaders of the organization, along with its stakeholders.
- 3) *The logical consistency tests* – Do the recommendations flow in a clear and logical way from the evidence used? And what confidence do we have in the evidence used? Do we trust such evidence?
- 4) *The risk and resources test*- Are the risks and resources associated with strategies sensible in relation to the organization? They might be consistent with the overall purpose, but involve such large levels of risk that they are unacceptable. They may require resources that are substantially beyond those available to the organization- not just finance, but perhaps people and skills.
- 5) *The flexibility test* – Do the proposed strategies lock the organization into the future regardless of the way the environment and resources might change? Or do they allow some flexibility depending on the way that competition, the economy, the management and the employees and other material factors develop?

By the late 1950's, writers such as Ansoff (Lynch 32) were beginning to develop corporate strategy concepts that would continue into the 1970's. During the 1960's, the early concepts of what would later become one of the main approaches to corporate strategy – prescriptive corporate strategy (Fig 1.2) – began to take shape. According to Lynch (p32), Ansoff argued that there were environmental factors which accelerated the development of corporate strategy. Two trends can be identified:

- 1) *The accelerated rate of change*. Corporate strategy provided a way of taking advantage of new opportunities.

- 2) *The greater spread of wealth* – Corporate strategy needed to find ways of identifying the opportunities provided by the spread of increasing wealth.

It was during this same period that the early research was conducted which subsequently led to the development of the second main approach to corporate strategy, emergent corporate strategy, although this only came into prominence in the 1970's and 1980's.

(a) The prescriptive approach



(b) The emergent approach



**Fig 3.2: Prescriptive and emergent approaches to the three core elements**

Source: Lynch, R (2002). *Corporate strategy*, page 25 (Second edition), Prentice Hall Publications, Essex.

The author will now look at prescriptive corporate strategy (Fig 1.3) in practice starting with the *basic concept* which states that a prescriptive corporate strategy is one where the *objective* has been defined in advance and the *main elements* been developed before the strategy commences.

- Prescriptive strategy starts with the search for an agreed objective, such as maximization of the return on the capital involved in a business.
- The environment in which the organization operates is then analyzed and projections made for the future.
- Based on this work, forecasts then form the background for the organization's strategic plan. At this point, the objectives may be reviewed: if the forecasts are particularly positive or negative, then the objectives may be changed.
- After making a forecasted projection of the expected environment, various options are identified to enable

the business to achieve the agreed objectives – there is usually more than one way of achieving an objective.

- One option is then selected which is best able to meet the objective.
- The chosen option is implemented by the organization's managers.

The advantages of the prescriptive process are as follows:

- A complete *overview* of the organization is established early on.
- The possibility of making a *comparison* with the defined objectives is available.
- A summary of the *demands* on the *resources* of the organization, including people, physical assets, finance and cash flow is readily available.
- A picture of the *choices* the organization may have to make if resources are limited are known to the organization up-front.
- The possibility for the organization to *monitor* the agreed plan as it is implemented, so that it can evaluate the progress that is being made is available to management from the start.



**Fig 3.3: How the prescriptive corporate strategy process works**

Source: Lynch, R (2002). *Corporate strategy*, page 53 (Second edition), Prentice Hall Publications, Essex.

Prescriptive strategic analysis has borrowed from *economic theory*. According to Lynch (p56), Adam Smith, writing in the eighteenth century, took the view that human beings were basically capable of rational decisions that would be *motivated most strongly by maximizing their profits in any situation*. Subsequently, modern strategy theorists, such as

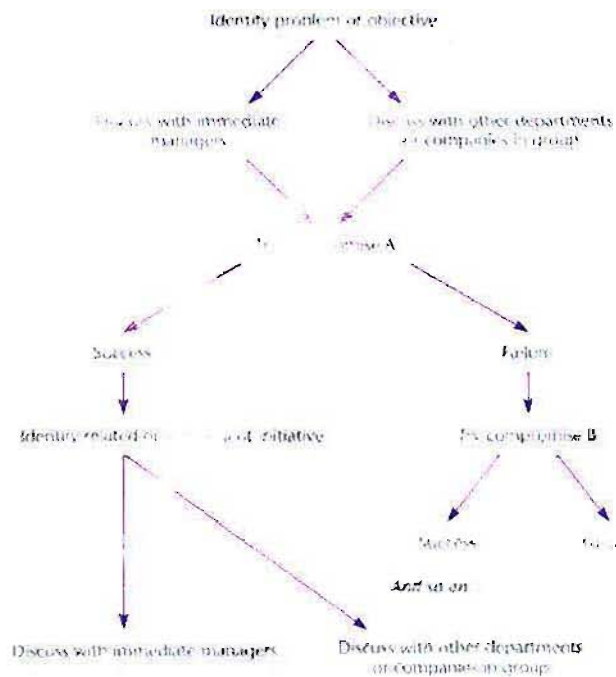
Professor Michael Porter of Harvard Business School, have translated profit maximization and competitive warfare concepts into strategy techniques and structure that have contributed to prescriptive strategic practice.

Lynch (p58) argues that Porter suggested that what really matters was *sustainable competitive advantage* versus competitors in the market place: only by this means, can a company have a successful strategy. Lynch (p59) notes that others have taken this further, for example, the Boston Consulting Group used market data to develop a simple, strategic matrix that presented strategic options for analysis.

The prescriptive strategic process is claimed to be logical, rational and capable of real insight into the problems of an organization. It focuses on the major issues that each company needs to address. Despite the advantages claimed for prescriptive strategy system operating at the centre of organizations, there have been numerous critics, none more than Professor Henry Mintzberg of McGill University, Canada.

According to Lynch (p61), Mintzberg had researched the decision making at corporate strategy level and suggested that a prescriptive strategy approach is based on a number of dangerous assumptions as to how organizations operate in practice. There is significant research to show that these assumptions are not always correct. For example, markets can change or employees may not like an agreed solution and find ways to delay it or not implement it at all. Given this evidence, emergent strategy has developed, as an alternate view of the strategy process.

The study will now look at the emergent corporate strategy in practice starting with the *basic concept* that states that the emergent corporate strategy is a strategy whose final objective is unclear and whose *elements* are developed during the course of its life, as the strategy proceeds (Lynch (2000), page 59).



**Fig 3.4: One view of how the emergent strategy process works**

Source: Lynch, R (2002). *Corporate strategy*, page 61 (Second edition), Prentice Hall Publications, Essex.

Deriving from the observation that human beings are not always the rational and logical creatures assumed by prescriptive strategy, various commentators have rejected the dispassionate, long-term prescriptive approach (Lynch p63). They argue that strategy *emerges*, adapting to human needs and continuing to develop over time. Given this, they argue that there can only be limited meaningful prescriptive strategies and limited planning from long term planning.

According to Lynch in his book *Corporate Strategy* published in 2002 (p60), research into how companies and managers develop corporate strategy practice has shown that the assumption that strategies are always logical and rational does not take into account the reality of managerial decision-making. He states that:

- Managers can handle only a selected number of options at any one time.
- Managers are biased in their interpretation of data.
- They are likely to seek a satisfactory solution rather than maximize the objectives of the organization.
- Organizations consist of coalitions of people who form power blocs. Decisions and debate rely on negotiations and compromise between these groups, termed political bargaining.

- To take decisions, managers rely on a company's culture, politics and routine rather than on a rational process of analysis and choice.

More recently, the research of Pettigrew, Mintzberg and others (Lynch p65) further developed the *people* areas of strategy. Their empirical research has shown that that the development of corporate strategy is more complex than the prescriptive strategists would imply: the people, politics and culture of the organization should all be taken into account.

Strategists, such as Senge (Lynch p66), have emphasized the *learning* approach to strategy: encouraging managers to undertake a process of trial and error to devise the optimal strategy. As a result, according to these researchers, corporate strategy can best be considered as a process whereby the organizations strategy is derived as a result of repeated experimentation and small steps forward: in this sense, corporate strategy is emergent rather than planned.

If the emergent view of the strategy process is correct, then the implications for the corporate strategy are profound:

- 1) Strategies emerge from a confused background and often in a muddled and a disorganized way: the resulting strategies themselves may therefore be unclear and not fully resolved
- 2) The process is unlikely to reflect reality: options identified will not be comprehensive and the selection process will be flawed.
- 3) Considering 'implementation' after the rest of the strategy process does not reflect what usually happens.
- 4) Managers are unlikely to seek the optimal solution: it may not be capable of identification and, in addition, may not be in their personal interests.
- 5) Working within an organization's routines and culture will allow the optimal culture to emerge rather than be forced by an artificial planning process.

According to the emergent view of the strategy process, implementation does not follow strategy development but is an integral part of the development. It can best be considered therefore a compromise. Emergent strategists believe that the national and logical analysis of the prescriptive process towards achieving the highest return on shareholder's capital is flawed. Strategies are better seen as emerging during the process of negotiation and discussion. Objectives may not maximize the good of the organization or even add value. Options and selection do not always lead to rational decision making and are not wide ranging.

Those who favour emerging strategy, argue that market place comparison with competition rarely produce the real strategy insights and development. Sustainable competitive advantage has some value but what really matters is the organization's own skills, resources and knowledge: these must form the basis of the development of the unique advantage that will allow the organization to survive in the long term. Looking at a banking organization's own skills, resources and knowledge leaves us with a question in need.

The next question that is of concern is what strategies have been implemented in the past with regards to providing banking assistance to the unbanked sector and how successful were they.

Research done at the time, that took into account the international experience, set an order of preference for the strategies to increase substantially local banks' lending to micro-entrepreneurs, namely linkage banking, downscaling and the least preferred, a dedicated bank (Schoombee, 1998 & 1999). The question that needs answering relates to this order of preference still applying.

The study will first have a look at the linkage banking strategy.

Linkage banking, the then most preferred strategy, is mostly found where banks link with informal financial sector self-help groups (SHGs), grassroots social organizations formed to address the financial needs of their members in a collective manner. NGOs play an important role in this strategy, either as an intermediary between banks and SHGs or in establishing and training new SHGs. The high default risk banks have to face when lending to micro-entrepreneurs is solved by the social collateral (peer pressure) in the SHGs, and the high transaction costs by dealing with groups and not individuals.

Locally stokvels, group-based rotating savings and credit associations, function as SHGs. The prevalence of stokvels was one of the reasons for preferring the linkage strategy for South Africa. However, the lack of suitable NGOs impeded the implementation of this strategy.

The concept of "village banking", as applied locally, is also a type of linkage banking and was at the time of research referred to, thought to hold much promise to open up bank lending to rural micro-entrepreneurs. Village banks, known as Financial Service Co-operatives (FSC's) in South Africa,



are semi-formal financial institutions owned, via shareholding, and managed by the members of a specific community / village to create access for its shareholders to basic financial services.

FSCs are exempted from the Bank Act's ban on providing deposit facilities, but in terms of the same exemption are required to have a business arrangement with a bank of its choice, the link bank. Deposits received by FSCs are deposited at the link bank and lending is only possible once a certain percentage of the loan has been saved. The bank must undertake to provide support, training and advice to the FSC.

Linkage banking, as a strategy to increase substantially the big four banks' lending to micro-entrepreneurs has not been a success locally. The question that needs answering is if it is still a successful strategy internationally. The linkage project in India, under the auspices of the National Bank for Agriculture and Rural Development (NABARD), is in terms of outreach, undoubtedly a winner. It has half a million SHGs (with 8 million members) linked to 20,000 rural outlets of more than 440 banks, with a loan book of R1.8 billion (Stegman 2002).

One needs to assess if it has been profitable lending for the banks involved. Stegman's report indicates that it has, and that for a number of banks the returns of the linkage project have significantly exceeded the profitability of other bank departments. Not all banks though, find it profitable. Banks that do not make profits from their linkage activities are often those who, because no NGOs are involved, have to establish and train new SHGs, and finance the very costly activities themselves (Stegman, 2002).

Linkage banking is still an option for the big four banks to supply micro-loans to micro-entrepreneurs, but no longer the preferred strategy. Linkage lending via FSCs is still also a prospect, but only if villagers demand for lending increases substantially (why are villagers not taking up loans?) Is the reason because there is little entrepreneurial activity or is the downscaling strategy the preferred one.

This strategy, where existing banks create either a separate division or a subsidiary to enter the micro lending market, has been the major vehicle of the big four banks to achieve this purpose.

Looking at the experience of other developing economies should provide clarity as to whether this strategy is also a

viable option. Valenzuela (2002) researched the experience of 53 downscalers that have since the mid-1990s opened up their banking services to the previously unbanked. Not all have been successful. Most though have succeeded in undertaking micro-lending profitably, and similarly to the linkage strategy discussed above, some even generated higher profits than the other departments in their respective banks.

It is important to assess the reasons at why some downscalers do well and others not. Stegman's research (2002) found that:

- smaller banks performed better than larger banks (problems encountered when integrating micro-lending into a big bank structure);
- subsidiaries dedicated to the micro-lending market were a better option than establishing a separate division for this purpose (subsidiaries are more successful in detaching the micro-lending activities from the organizational culture of the existing bank);
- the presence of an 'operational champion' (an individual who believes in the micro-lending product, knows what is required to develop it and is able to manage the provision of this service) guaranteed success; and
- those downscalers that received technical assistance from international donors (e.g. in regard to credit methodology, service delivery and training) do better than those that did not.

Relating the above research to the South African position provides some evidence why downscaling by the big four banks have not resulted in loans being supplied to micro-entrepreneurs. One option to consider is if there should be a move toward opening dedicated banks.

The order of preference previously established for strategies to increase local banks' lending to micro-entrepreneurs awarded the last place to a bank dedicated to exclusively serve this market. It was felt that modest profit expectations in the short to medium term would deter large-scale private sector participation, especially if the bank had to start from scratch. Upgrading NGO's if the necessary regulatory changes were put in place and suitable prospects were to appear, would have been preferred.

Globally, this approach has gone from strength to strength. The upgrading strategy has been particularly successful in Latin America as per a banking journal published in Peru (Rhyne, 2001). However, upgrading has not been attempted locally, and is still not an option. Setting up dedicated banks by means of specialized public-private partnerships is now the preferred strategy to roll out micro-entrepreneur lending on a substantial scale in South Africa. The reason for this choice is twofold.

First, both the linkage and downscaling strategies undertaken by have not been successful and exhibit certain inherent deficiencies linked to the characteristics of these banks (e.g. their size) and the local environment (e.g. no suitable NGOs).

Second, some of the most serious problems experienced by all of the big four banks, namely not having access to the technical know-how of those knowledgeable in serving micro-entrepreneurs and the lack of grant funding and or government subsidies to finance this access, are addressed by these specialized partnerships.

What is needed to initiate this strategy is for such a specialized private investor, of necessity from outside South Africa's borders, since these expertise are not available locally, to take a plunge and establish a new bank in partnership with a donor organization. The demonstration effect, if the venture is successful, should lead to others following suit.

### **3.3. Summary**

The chapter covered the theoretical section of the dissertation. The author compared the merits of the prescriptive strategy versus the emergent strategy when it concerns the decision around the choice of corporate strategy. Different renowned authors and strategists' viewpoints are presented with regards to what they consider to constitute good strategy.

There was also a discussion around previous strategies employed in the banking sector with regards to providing finance to the unbanked sector, namely the strategies of linkages, downscaling and dedicated banks. The study looked at the previously preferred strategy choices of banks and whether this order of preference still applies today. The study will now move forward to provide a detailed review of the strategy employed by Standard Bank.

## **CHAPTER FOUR**

### **Current Standard Bank strategy**

#### **4.1. Introduction**

Banks, insurers and the government signed the Financial Services Charter on the 17<sup>th</sup> of October, 2003, according to the Standard Bank Annual report in 2003. Now branches are popping up all around the country. Standard Bank plans to add 21 more similar branches to the seven 'bank-in-a-box' it already has. ABSA plans to open 300 ATM's in townships over the next year.

The charter requires banks to increase lending to the black owned companies and families in the townships. Banks must also ensure that 80% of South Africa's 47 million people can find a branch within 10km of their homes by 2008.

Lenders have pledged not to profit from serving the townships, according to Cas Coovadia, in an article published in the Sunday Times, Business Report dated 4th October 2004.

Standard Bank, ABSA and Nedcor say they don't expect to lose money from expanding into the poorest parts of the country. In the ABSA annual report 2004, Jenny Tyobeka of ABSA's Flexi Banking Services unit suggests that all the banks need to be smart about how they handle this issue. She argues that banks cannot invest in townships simply for social reasons when these companies have a corporate social investment division for that.

At the same time, banks must move fast to roll out services in poor areas or risk a clash with the government. Finance Minister, Trevor Manuel, stated in his 2005 opening parliament speech that the government would pass laws forcing companies to increase black participation in the economy if businesses did not do so on their own. Seven South African lenders have already banded together for the launch of a new bank account for those who cannot afford regular bank charges. The so called Mzansi savings and transaction facility will allow customers a limited number of free transactions a month. Mzansi, which means "south" in isiZulu, will let customers electronically transfer funds, check their balances, receive mini statements and buy connection time for cellular phones.

This does not look to be profitable in the short run for the banks, but hopefully, it will secure the customer base of the future should the country's effort to redistribute wealth be successful. One of the biggest challenges for banks will be to avoid attracting current customers to the cheap accounts. The product needs to be cheap enough to lure those without accounts, yet constrained enough to prevent existing customers from moving their accounts.

No matter how banks structure charges, the strategy is to get into the low-income market without making losses and then to profit as customers become wealthier. The banks will do this by pushing customers to the low cost electronic banking facilities such as ATM's, because the human interface at branches is where the cost is.

Banks are trying to set up storefronts as cheaply as possible. It costs Standard Bank less than R600 000 to build and drop off a 'bank-in-a-box', notes Lincoln Mali, of Standard Bank's Convenience Banking unit in Johannesburg, in the Standard Bank Annual Report 2004. Mali also states that it is much quicker and takes only two weeks to set up, whereas a brick building could take months. He emphasizes that there has to be a first mover advantage to reap rewards as the bank that does open a branch first in a new community usually becomes the dominant bank in that community.

The study will now look at the structure of the Standard Bank organization and their current strategy in terms of their current product offerings to the low-income sector.

#### 4.1.2. Standard Bank of South Africa (history of the organization – convenience sector)

		CONVENIENCE BANKING			
PRODUCT	Transactional	<ul style="list-style-type: none"> <li>E Plan</li> </ul>	SALES AND SERVICE	POSITIONING/MARKETING	
	Lending	<ul style="list-style-type: none"> <li>E Loan</li> <li>DreamStart</li> <li>Credit Card</li> </ul>			<ul style="list-style-type: none"> <li>Primarily serviced in a standalone AutoBank E centre</li> <li>Limited physical demonstrations</li> <li>Pamphlets and brochures (educational facilities are restricted to reading material)</li> <li>Consulting areas are designed to accommodate individuals rather than groups</li> <li>No consistent or standardised service is offered</li> </ul>
	Savings	<ul style="list-style-type: none"> <li>BonusPlus</li> <li>PlusPlan</li> <li>Notice Deposit</li> <li>Fixed Deposit</li> <li>Society Scheme</li> <li>E Plan (savings purse)</li> </ul>	DISTRIBUTION		<ul style="list-style-type: none"> <li>Efforts are being made to ensure that the brand is perceived as being warm and open, but some view the brand as too formal, elitist and uncaring</li> <li>Despite having been phased out, the E brand is strongly prevalent and associated with by both Bank staff and Customers in this segment</li> <li>Soccer is currently sponsored</li> <li>Radio Waya Waya</li> <li>Corporate Social Investment (CSI) initiatives</li> </ul>
	Wealth	<ul style="list-style-type: none"> <li>Funeral Plan</li> <li>Dependent CarePlan</li> </ul>			<ul style="list-style-type: none"> <li>Network of AutoBank E centres and ATM facilities</li> <li>PORs (points of representation) do not fully meet the needs of the Customers</li> </ul>

**Table 4.1: Research findings by Kwa-Zulu Natal research team**

The diagram above breaks down the current strategy of Standard Bank in terms of their current product offerings to the low-income sector. The bank has four product offerings to this market that are categorized under the following headings: transactional (everyday depositing and withdrawing) products, lending (credit / borrowing) products, savings (long term saving or investment) products and wealth (assurance) products.

The diagram also critically reviews the manner in which this sector is served and how the products are presented to this market (Sales and Service). The research group highlights the fact that this sector is treated differently as the bank tries to isolate these customers from the main branches by building standalone centers called Autobank E's. Although this segment is treated as homogenous, the buildings are designed to serve customers on an individual basis rather than in groups. This should mean that products should be tailored for individual needs but this is not the case. Education of customers is presented through brochures and pamphlets yet more than 75% of this segment is illiterate.

In terms of Standard Bank's physical distribution strategy, the group points out that there are two distribution channels. One is the AutoBank E channel and the other is the main branches. The group highlights that although the main

branch network can serve this market, the staff are not fully skilled to understand and assess these customers' needs. This deficiency is based on the cultural and language barriers of the staff with respect to seeing these customers as adding value to the bank's profits.

In terms of the way this product is marketed or positioned to the public, the group's findings reveal that not all customers see this product as welcoming and adding value to their lives but rather as a downgrade or lower level offering. The product is positioned as an entry level offering where a customer is made to believe that only if he conducts his account in a manner that is acceptable to the bank, he will be upgraded into the main banking stream.

The bank still uses soccer as the main channel to reach this segment and advertisements are limited to low key radio stations. This shows that the bank has no clear definition of what the income level should be for this market or if the media outlets used are aligned to the correct market segment.

Standard Bank was the first financial institution to provide financial services to the lower end of the market, through its E Banks in 1994. It has since maintained a lead as a provider of financial services, and has over the years extended its service offering for this market. However this offering has certain limitations. It does not address the financial services needs of the very poor who need a basic savings account to deposit surplus funds, and who cannot service the account on a monthly basis with a dependable salary.

According to their Annual report of 2004, Standard Bank states that the bank has around three million lower income customers, excluding those taking up the Mzansi initiative, which seeks to provide banking for the poorest. The report notes that the bulk of their convenience banking customers earn between R2000 and R3500 a month and previously they offered only transactional accounts (deposits and withdrawals), but now they provide lending products as well. The bank provides stokvel saving schemes whereby people that want to save together can open a joint account. It also offers funeral plans and a basic home loan package.

The study will now look at the actual product: Mzansi Blue Account as marketed by Standard Bank on their website ([http://intranet.sbic.co.za/Our B...Sales Support/Easy Aid/Mzansi.ht](http://intranet.sbic.co.za/Our%20Business%20Sales%20Support/Easy%20Aid/Mzansi.ht)). The study will highlight the target market as per Standard Bank's definition.

### **4.1.3. The introduction of the Mzansi Account**

Mzansi Blue Account is targeted at a significant segment of the population to whom banking services still remain inaccessible. It aims to bring on board people who have never been able to access basic banking services for various reasons and caters for seasonal and migrant workers, social grant recipients and the unemployed. It will for the very first time, introduce people to the world of banking. Standard Bank still needed to decide on how they would position this product to the target market.

One of the major challenges that is faced in targeting the lower end of the market is to enlist pride and trust in the product. Serving lower income customers is about working with people who need convenient, secure, and affordable banking services provided in a caring, respectful way. This is an affordable value-adding product for hard working South Africans to help them as they go about their day-to-day activities. The next stage of the study involves an in-depth critical look at the product offering followed by an analysis of the product offering in meeting the needs of the target market.

The Mzansi Blue Account is an account that will help customers to manage their finances on a day-to-day basis and to help them save for the future. It includes:

- An ATM card with the account
- The card enables the purchase of goods at merchants via the maestro facility
- It enables basic banking at an affordable price
- Store of value: no maintenance fee and pays interest on the daily balance

Some of the Key Benefits of this product involve

- No monthly maintenance fees
- Pay as you go
- Free transactions: deposits and information
- Transactors will only pay for transactions actually incurred
- No additional costs for using other banks ATM's
- Streamlined account opening procedures
- Interest rates will preserve capital for customers who want to save



Asking the question of what can be done with this account will go a long way to assess if this product offering is what the target market is looking for. The following features of the product are described below:

- Deposits
- Withdrawals
- Cellphone airtime top-up
- Receiving a salary, pension or government grant via EFT
- Bank cheques (over the counter)
- Enquiries
- Point of Sale (POS) purchase
- POS purchase and cash back

Looking at the limitations of this product offering will give insight into whether the look and feel of the product is a process or profit driven decision. The following are the transactions that cannot be done when using this product.

- Statements via mail
- Stop orders
- Debit orders
- Electronic account payments
- Inter account transfers
- Cheque issue via the self-service channels

The key objective for the bank is to assist the customer in making the right product choice. Whether the customer asks for an Mzansi Blue Account or another product, the following key principles should be kept in mind:

- Ask about the key functionality required by the customer
- If basic functionality is required, such as withdrawals, deposits, and enquiries, then the customer is a clear cut Mzansi candidate.
- If debit orders, stop orders, EAP's (electronic account payments) or EFT's (electronic fund transfers) are required, then the customer may be a clear cut E –Plan candidate
- Explain the key differences of the two accounts i.e. monthly maintenance fees, charges and benefits of each

Another issue to consider for Standard Bank is the existing customer migration from one low income product offering to the other. Issues to consider comprise of the following decision making criteria when it comes to Standard Bank's products.

If a customer moves from an E-Plan to Mzansi account

- Customer may be an active E Plan customer and still choose to have an Mzansi Blue Account as a secondary account. In this case, his E Plan will remain open, and we will proceed to open an Mzansi Blue Account
- Customer may not be actively transacting on E Plan and wants Mzansi Blue Account because it is a more affordable account. Ideally, the E Plan should be closed and the Mzansi Blue Account opened. It is not in the customer's interest to have both accounts, especially when the question is one of affordability.

If a customer moves from a Mzansi to E Plan account

- Account balance reaches R15,000.
- Customer who has an Mzansi Blue Account enquires about debit order, stop order or any other functionality not currently offered on the account.
- Customer needs analysis must be completed.
- Customer enquires about micro-loans or loans.

The next issue to consider for Standard Bank is around which service delivery channels are to be used by this new segment and their transactability. The bank proposes the following.

- Standard Bank outlets (opening of accounts, withdrawals, deposits, mini-statements, balance enquiries, queries)
- Other bank outlets (withdrawals, balance enquiries)
- Standard Bank ATMs (withdrawals, deposits, mini-statements, balance enquiries, cellphone top-up)
- Other banks' ATMS (withdrawals, balance enquiries, cell top-up)
- South African Post Offices (withdrawals, balance enquiries)
- POS (purchases and cash back)
- Telephone (balance enquiries and other account enquiries)

In order to reduce revenue cannibilation by customers moving from the E-plan to the Mzansi account, the following restriction was put in place for balances greater than R15,000.

Deposits to the account are still accepted but all withdrawals will be blocked (including of POS and cash back). Two options can be considered when a Mzansi Blue account reaches a maximum balance of R15,000.

The first option is to transfer the account. The customer will be required to open a FICA (Financial Intelligence Centre Act as per government regulation) compliant account and transfer excess funds into this new account.

- The customer can still use the Mzansi Blue Account, but is still subject to R15,000 limit.
- Should this limit be exceeded again, the account will be frozen and the customer will be required to
  - Visit the branch
  - Withdraw the excess amount
  - Deposit it into his KYC'd (Know Your Customer – as per South African regulation) account

Option 2 would be to close the account. If the customer fails to accept the first option, he will have no choice but to close his Mzansi Blue Account and withdraw his funds.

To ensure that the account is being used by the correct target market, the bank has specified the Opening documentation requirements as follows:

- Verification of positive RSA identification
- Name
- Phone number (optional)
- Address (verify as far as possible)

To combat the issue of illiteracy, the Bank has created an Important Help Number (0860 121 191) in this regard for the customer. It is called the Customer Contact Centre (CCC).

According to Mali in their annual report of 2004, Standard Bank's current position regarding their strategy comprise of the following:

- the strategy is largely focused on the establishment of AutoBank-E's as a primary delivery channel.
- there are minimum staff facilities at AutoBank E's.
- there is restricted access to other delivery channels and acquisitions are largely through AutoBank-E's.

- there is a limited, off the shelf product set available via Auto Bank E's
- there is multiple points of representations (POR's), yet there is no optimal leverage of mix
- no consistent service delivery against agreed standards is in place.
- there are limited ATM hours of operation in rural and metro areas.
- there is limited cover of major settlement areas in terms of banking facilities.

After launching the product, the Bank drew 40000 Mzansi clients in its first month. Jacko Maree, Standard Bank's Chief Executive, said previously in a television interview on their internal bank channel that the unbanked market is one of Standard Bank's most exciting business areas and plays an integral role in their future strategy.

He noted the pricing of the account was based on what an unbanked customer would find affordable while at the same time ensuring the long term profitability of the bank and the financial sustainability of the banking sector.

According to an article published in The Star newspaper dated 18<sup>th</sup> October 2004, Mzansi, the low cost bank account, has surpassed expectations, growing its customer base to about 560,000 since its launch in October. The article quoted that figures released by the Banking Council shows that more than 6000 new accounts are opened daily, which means Mzansi should have 1 million customers by the end of April 2005. The article further states that these customers have amassed R160m in Mzansi accounts, with an average balance of R290.

The article mentions Colin Donian, of the Mzansi Banking Council as stating that he believes that the response was probably two or three times bigger and better than anticipated.

The article further noted that Postbank had overtaken Standard Bank with the most customers. However, it has been promoting Mzansi as its main offering to the market, rather than its Flexi card account. It now has 152 000 customers or 27.3% of the market, followed by Standard with 25.9%, ABSA with 23.9%, First National Bank with 16.2% and Nedbank with 6.7%.

Donian further commented in the article that 90% of Mzansi customers who opened the accounts were new customers and had not held an account at that bank previously, while

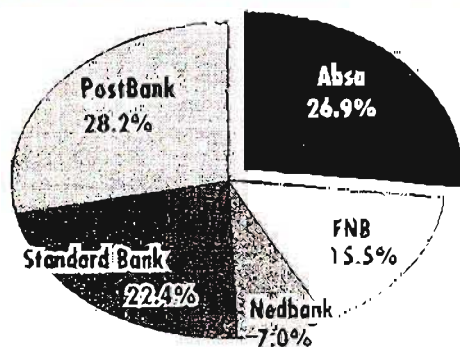
the other 10% were from the banks' existing customer base. However, some customers might have moved over from other banking groups. Donian expressed that more than half of Mzansi customers were female and about two thirds of customers were in the 25-54 age group.

In a newspaper article published in the Business Report on the 20<sup>th</sup> of October 2004, an additional 4 percent of the population had been brought into the formal banking system in the past seven months. This means that South Africa ranks alongside Argentina and is a step away from Malaysia in terms of banking its population.

A follow up article in the Business Report on the 20th May 2005 stated that by the middle of May 2005, over a million Mzansi accounts had been opened and almost the same number of unbanked South Africans had gained access to the formal banking sector. The article further commented that over 6000 accounts were opened every day and with an average of R325 held in each account, about R325 million was being held in by the participating banks.

The article confirmed that Postbank continued to outperform the 4 major banks with 28.2 percent of the total Mzansi accounts as per figure 4.1. The article stated that that Postbank's deposit base increased 46 percent to R1.8 billion in the year to March. The article also confirmed that of the major banks, ABSA has taken the lead with 26.9 percent market share, followed by Standard Bank with 22.4 percent, FNB with 15.5 percent and Nedbank with 7 percent.

The data showed the largest take-up of the account came from the black community and the majority of account holders were between 25 and 54 years. Donian also stated that 91.3 percent of the Mzansi account holders were new to the institution at which they had opened their accounts. This data does not indicate if these customers previously held accounts at other institutions. Therefore the data cannot unconditionally confirm that these are brand new customers to the banking sector. One cannot also say that migration is not occurring on an inter-bank basis, where customers are closing accounts (which is more expensive) in one bank and opening in another bank.



**Fig 4.1: Mzansi market share amongst the key players**  
 Source: Bridge, S (2005), "Mzansi accounts brings 4% of population to formal banking", *Star Newspaper*, Johannesburg, p4, May, 20.

The article went on to state that of the major banks, Standard Bank and ABSA could be best placed to take on new Mzansi accounts holders. The article quoted Wayne van der Vent of Futuregrowth Asset Management who stated that these two organizations have opted to take up space in Futuregrowth's malls which are built in rural areas. If the secret to Mzansi success for any of the country's big four banks lie in economies of scale, Standard Bank and ABSA's direct access to 16 percent of South Africa's poorest citizens will give them a head start.

The author is of the opinion that the idea of creating new service centre in rural areas will only work if banks promote a savings culture and the products are more accessible, particularly to smaller savers. South Africa's savings rate is ranked amongst the lowest in the world, but a number of private and public sector initiatives may help increase the amount of capital that South Africans invest.

The article highlighted that the budget tabled by Finance Minister Trevor Manuel in 2005 shows total national savings were 14.7% of gross domestic product (GDP) in the third quarter of 2004, down from 16.2% of GDP a year earlier. Although corporate savings increased to 12% of GDP from 11.7%, household savings were stagnant at about 2.5%. Government savings were also flat at about 0.2%.

According to the article, Adenaan Hardien of the South African Savings Institute noted that increased savings will help South Africa's development. He stated that one of the challenges for a developing country is to access sufficient savings given the fact that they have a higher propensity to consume than in a developed country. He further commented that access to an international pool of savings is quite

important for a developing country wanting to embark on a higher growth trajectory.

Hardien suggests that recent moves by the public and private sector, including government's retail bond and the low cost Mzansi account, are encouraging. He argues that a primary driver of savings is income and this includes current income as well as expectations of future income. He states that the national treasury has provided an added incentive to save by increasing the proportion of discretionary savings that is exempt from taxation.

According to the same newspaper article, Bridget Lamont, also of the South African Savings Institute, believes that while local banks are already doing a lot to promote savings, more can be done. She notes that the financial services institutions can do a lot more in terms of information and education of consumers. She admits that although this is being done, it's quite disparate and a more holistic approach is needed within and between banks. Lamont suggests that products and services need to be made more accessible, particularly at the lower end of the market. She notes that lower transaction fees and easier accessibility will help attract more savings and points out that banking in SA is made more expensive for people living in areas where there are no banks, so transport costs have to be taken into account. She further comments that the wide array of products available may also be confusing for consumers.

She goes on to add that banks need to help consumers understand whom they are; how they differ and help customers make decisions. Lamont admits that the Mzansi account is a step in the right direction as it encourages deposits and does not levy monthly administration fees, however it may be difficult to persuade low-income earners of the importance of a "savings reservoir" to the country's economy. Her final comments in the article centers around the fact that for people earning very little, the macroeconomic issues probably do not matter very much and that instead, banks have to show customers the practical aspects of how savings can change their lives for the better.

In an article published in the Business Report newspaper on the 21<sup>st</sup> of May 2005, Standard Bank director, Keith Fuller stated that the Mzansi account is not an effective store of wealth as it is primarily a transaction account. He noted that the bank is trying to address the lower convenience market in terms of their needs and he believes that at Standard Bank, there is a distinction between a transaction vehicle such as the Mzansi and a store of wealth.

The article states that research by the Banking Council indicates that a Mzansi account holder who performs few transactions (a low transactor) can expect to pay R8.58 a month. If a customer performs a "moderate" number of transactions, the customer will pay an average of R19.06 a month. If the customer performs a "high" number of transactions, the customer will pay R27.28 on average a month.

Examples quoted in the article mention "low" transactors as account holders who, in a month, make one cash deposit at a branch, make one ATM withdrawal using their banks ATM network, one ATM withdrawal using another banks' ATM network, and have an average balance of R100 in their account.

In a month, a "moderate" transactor, make one cash deposit at a branch, make two ATM withdrawals using their banks ATM network, one ATM withdrawal using another banks' ATM network, pays for two purchases using their card and have an average balance of R250 in their account.

In a month, a "high" transactor receives five electronic funds transfers into his or her account, make one cash deposit at a branch, make three ATM withdrawals using their banks ATM network, two ATM withdrawals using another banks' ATM network, pays for two purchases using their card and have an average balance of R50 in their account.

Using these statistics, it came as no surprise when an article published in the Business Report newspaper on the 31<sup>st</sup> of January 2005, ran with the heading that the low cost account may fail. According to the article, FinMark has warned that Mzansi may fail despite the banking industry's effort to make it work.

The article mentions that according to Mark Napier, Mzansi may have few takers. He notes that although Mzansi is a positive step, it is not the whole answer. Napier further stated that cost is a significant but relatively small determinant in what causes a person to want to have a bank account or not.

The article argues that although participating banks have committed to providing affordable banking to the poor, but on closer inspection, the fees, established independently by each bank, appears expensive.

Tami Sokutu of African Bank in the same article stated that there is concern that the Mzansi account may alienate the



target market. She noted that there is concern about the creation of a secondary economy. She argues that the labelling of the account as a special product for lower income earners reminds people of where they are and not where they aspire to be. Sokutu questions the sustainability of Mzansi, given that it was driven by political pressure. Both she and Napier were eager to see if banks would deliver on their promises to look to adding to the basic deposit and withdrawal functions of the account. According to Napier, if competition causes the features of Mzansi to be more reflective of what the poor consumer wants or needs, then it will have proved to be a very positive initiative.

The study will now look at the comparison between the Standard Banks' perceptions of this market and the realities of this market. These findings are listed below (Table 8.2). One can see why the assumptions made by Standard Bank in the past have resulted in this market not being afforded the opportunity to progress into the financial mainstream. Although the bank was correct in assuming this market was illiterate, they still pursued a strategy of technology to serve this market. No attempt was made to investigate this segment firsthand and therefore there was an opportunity lost. The bank did not understand the credit needs of this segment and were wrong in their assumptions that this segment did not have faith and trust in the banks.

The bank also did not understand the status importance that this market places in their sense of belonging to the financial mainstream. The bank just assumed that all these areas were homogenous and all customers had the same needs. The assumption that these communities were generally poor was true but no note was made that there were exceptions to this assumption. The bank therefore lost an opportunity to capitalize on.

Perceptions VS Reality of the Unbanked Market

Perception	Reality
<ul style="list-style-type: none"> <li>▪ High degree of illiteracy</li> </ul>	<ul style="list-style-type: none"> <li>▪ Illiterate, not innumerate, street-smart, multi skilled, high capacity for learning</li> </ul>
<ul style="list-style-type: none"> <li>▪ Household income supplemented by social grants.</li> </ul>	<ul style="list-style-type: none"> <li>▪ True</li> </ul>
<ul style="list-style-type: none"> <li>▪ Low-income levels. Poor communities</li> </ul>	<ul style="list-style-type: none"> <li>▪ General consensus. however exceptions noted.</li> </ul>
<ul style="list-style-type: none"> <li>▪ Poor public infrastructure in the informal areas</li> </ul>	<ul style="list-style-type: none"> <li>▪ True, lack of tarred roads, electricity, water and sanitation.</li> </ul>
<ul style="list-style-type: none"> <li>▪ Market aware of funeral plans</li> </ul>	<ul style="list-style-type: none"> <li>▪ True</li> </ul>
<ul style="list-style-type: none"> <li>▪ Borrow money from loan sharks</li> </ul>	<ul style="list-style-type: none"> <li>▪ Not preferred but convenient. Lack of education re alternatives.</li> </ul>
<ul style="list-style-type: none"> <li>▪ Large households</li> </ul>	<ul style="list-style-type: none"> <li>▪ True</li> </ul>
<ul style="list-style-type: none"> <li>▪ Informal settlements are prone to crime.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Not always true.</li> </ul>
<ul style="list-style-type: none"> <li>▪ General distrust of financial institutions.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Not the general consensus</li> </ul>
<ul style="list-style-type: none"> <li>▪ People work away from home (informal settlements)</li> </ul>	<ul style="list-style-type: none"> <li>▪ True for the majority.</li> </ul>
<ul style="list-style-type: none"> <li>▪ Not homeowners</li> </ul>	<ul style="list-style-type: none"> <li>▪ Majority own homes in rural areas</li> </ul>
<ul style="list-style-type: none"> <li>▪ No need or want for banking accounts</li> </ul>	<ul style="list-style-type: none"> <li>▪ Definite desire, considered status symbol. General need exists.</li> </ul>

**Table 4.2: Research findings of the Standard Bank research team in Gauteng (Standard Bank – Twister research report)**

Although the bank was aware of the majority of this segment working away from home, no thought was given to the fact that these customers still had to make these funds available to their families in their homelands. The bank did not realize the value of the market (in rand) and also that these societies were strictly cash driven and all this cash could have been brought into the mainstream at quite a tidy profit. The assumption that this segment was a secondary economy has cost Standard Bank hundreds of millions in lost revenue.

In Table 4.3 below, the research group of the Great North Region found that Standard Bank was quick to offer a product that suited the bank's structure while customers had to adapt and accept this product. Standard Bank assumptions that they were adding adequate value to these customers were also wrong. These customers want to have

the personal touch as their value of time is different to your upper affinity segment. The bank's assumption that this market could only handle a certain amount of information at a time was also off the mark. The bank assumed that these customers were on a need to know basis.

In the mining industry, these customers are hungry for information but need more convenient access to the bank and its staff. An assumption was also made that these customers are equally not adept to handle new technology similar to the rural customers of other areas. The findings of this group definitely contradict this assumption with the high cellphone and ATM usage.

ASSUMPTION	REALITY
1. High cell phone usage	1. High cell phone and ATM usage
2. Lack of need for good service	2. Need for good service
3. No personal contact	3. Limited relationship needs with banks
4. Don't trust banks	4. High regard and trust of banks in general
5. Lack of understanding of banking products	5. Hungry for education and information
6. Already adding adequate value to market	6. Need to create more value for miner
7. Most of the miners do not stay with their families	7. Most of the miners interviewed stay with their family.

**Table 4.3: Research findings of the Standard Bank research team 'Twisters' in the mining sector of Mpumalanga, Limpopo and North West provinces (Great North Region).**

This part of the chapter above looks at how the different banks co-operated to develop the Mzansi account. The chapter also has a look at Standard Bank's history in this segment, the products and services it provides, as well as a description of the target market and the actual product offering. A study was developed using different newspaper and journal articles that will provide more insight to the reader in their understanding of the target market and the different Banks' strategies. The next chapter will look at evaluating Standard Bank's strategy, comparing what the company has "done well" and what they are not currently doing well in order to be a dominant company in this market segment.

## **4.2. Critical Analysis of the Standard Bank strategy**

### **4.2.1. Introduction**

In order to analyze Standard Bank's business environment, certain analytical procedures has to be undertaken. One also needs to draw a distinction between two types of results from the analysis:

- 1) *Proactive outcomes*. The working environmental analysis will identify positive opportunities or negative threats. The organization will then develop proactive strategies to exploit or cope with the situation.
- 2) *Reactive outcomes*. The working environmental analysis will highlight important strategic changes over which the organization has no control, but will need to be able to react if they do happen.

Before exploring specific aspects of Standard Bank's business environmental analysis, one needs to consider the basic conditions surrounding the organization. Special attention needs to be directed to the nature and strength of the forces driving strategic change – the dynamics of the environment.

### **4.2.2. The Critical Analysis**

Standard Bank is faced with a market that is difficult to predict the degree to which the business environment is likely to change. The organization, like many large corporations in South Africa, is affected by social and political complications.

Due to this environment, Standard Bank is a "Be Careful Organization". The organization is responsive and flexible and can adapt quickly, while at the same time, developing new initiatives. This is essentially an *emergent* approach to the development of corporate strategy.

### **4.2.3. The use of different strategic tools to analyse Standard Bank's strategy**

**PEST Analysis** (Political, Economic, Social and Technological)

One can see that the Banking Charter committee did a business environmental analysis. This was done more on a general financial environment as opposed to the specific banking industry. In terms of political future, legislation in terms of taxation and employment law was definitely considered important to the committee. The level of the relationship between government and the four banks would have influenced proceedings in a major way, having a huge impact on corporate strategy for each bank. Some of the socio-cultural factors that influenced the banks' strategy would have been distribution of income and shifts in values and cultures.

Economic factors that would affect corporate strategy would be consumer expenditure and disposal income, interest rates, currency fluctuations and exchange rates as well as unemployment. Technological factors that would have contributed to corporate strategy would be government policy. To the prescriptive strategists, the analysis can be used as a forecast of the future although it is based on what happened in the past. Since there was no past market, one could argue that it is a useless prediction tool. Judging by the take up figures so far of the Mzansi product, one can conclude that this is a fast-moving market and emergent strategists may be correct in stating that these predictions may have little value.

### **Scenario based analysis**

Standard Bank did not concern themselves by looking into the future and not predicting the future. They should have commissioned their own internal teams to conduct some scenario based analysis. They could have started by creating scenarios from an unusual viewpoint by looking at situations such as the stance of a major competitor or a radical change of government. They could have developed a qualitative description of a group of possible events and how it will unfold. They would then look at the outcomes as the "most optimistic outcome" and a "worst possible outcome". They would use these scenarios to lead to new strategic thinking rather than merely the continuance of the existing strategy.

### **Industry Life cycle analysis**

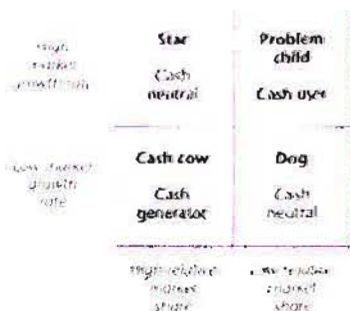
In terms of analyzing the rate of market growth, Professor Michael Porter from Harvard University School (Lynch (2002) p85), has described the *industry life cycle* as the "grandfather of concepts for predicting industry evolution". The basic hypothesis is that an industry (or market segment within an industry) goes through four basic phases of

development each of which has implications for corporate strategy.

Looking at this market segment within the industry life cycle, Standard Bank was quick to see the attractiveness of the market and the organization already had the business strength to take advantage of the situation as it had previously marketed a similar successful product called the E-Plan. Unfortunately, because of the implications of the Financial Sector Charter, there could not have been a collusion of pricing which could have made the project increasingly financially viable judging by the 500,000 new accounts opened in the first three months by all the banks.

### Growth Share Matrix Model

To Standard Bank, this project was just an extension of their retail arm, and if one had to use the BCG Matrix Model (Fig 4.2), one could see that it is a highly attractive market and Standard Bank does have the required business strength.



**Fig 4.2: The growth share matrix**

Source: Lynch, R (2002). *Corporate strategy*, page 176 (Second edition). Prentice Hall Publications, Essex.

In terms of this model, the bank should invest and grow their market share and use their positioning and brand strength to capitalize on new earnings. This, the company has done extremely well and have saved in the running, as the costs was shared with the other banks mentioned in the Charter. The bank's strategy is to invest to penetrate and the current market share justifies their actions.

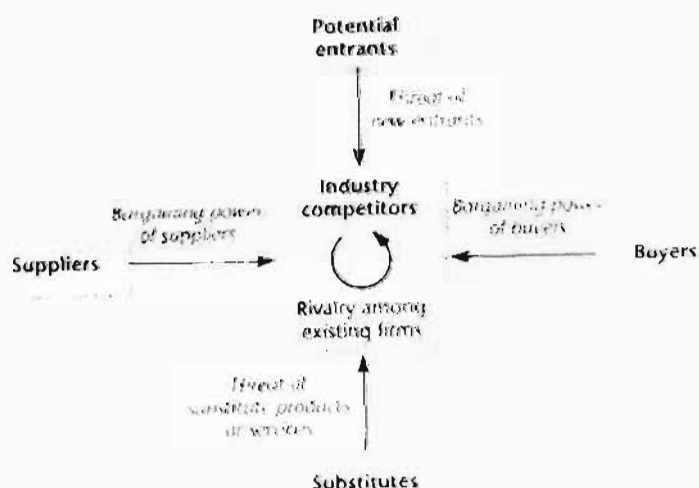
### Key Success Factor analysis

Although Standard Bank is one of the big 4 banks in this market, they have failed to a certain degree, as they should seek to dominate this market in the introduction phase. The most innovative strategy might well come by doing something different and breaking the mould. The bank should have looked at their Key Success Factors (KSF) for their industry and capitalized on it. More attention should have been paid to

their branding, network distribution, market leader status in convenience banking (through their E Plan initiative) and their array of specialized products. The bank has not examined their type of resources and the way they are employed in the industry and used this information to dominate this market. They could have used this as an opportunity to develop a competitive advantage over their rival competitors.

### Porters Five Forces Model Analysis

The objective of analyzing the competitive industry environment was structured and presented by Professor Michael Porter of Harvard Business School. His contribution to our understanding of the competitive environment of the firm has wide implications for many organizations in both the private and public sectors. His Five Forces Model will be used in the analysis below.



**Fig 4.3: Porter's Five Forces Model**

Source: Lynch, R (2002). *Corporate strategy*, page 125 (Second edition), Prentice Hall Publications, Essex.

The objective of such an analysis is to investigate how the organization needs to create its strategy in order to develop opportunities in its environment and to protect itself against competition and other threats.

The basic assumption of the model is that all organizations will wish to benefit and protect their own interests first. Whether this can hold true will be examined. The implications of corporate social responsibility as written in the Financial Sector Charter, contradicts this. Banks, however, do have an advantage as there are only a few suppliers and there are no substitutes for the product.

However, this product is not seen as important, value adding and life enhancing to the banks' itself.

Banks are also at a disadvantage in terms of any increase in price of this product would be seen as a decrease on the value added to the consumer. There are also only a few suppliers and to switch would not be difficult for a customer as there is not much difference in pricing and service offering as well as convenience to the customer. This will place a lot of bargaining power in the buyer's hand and loyalty to the brand will count for little.

The threat of potential new entrants is limited by capital requirements and economies of scale. Cell phone companies are the only players capable of entering this market. Government policy will also hinder the entrance of new players as the Charter is very specific in its requirements. There is no/very low threat of substitutes with the cell phone industry only being a potential major player.

The extent of competitive rivalry is very low as all the banks have a "wait and see" approach. Standard Bank could really use this low rivalry in this segment to dominate this base. The bank should however be prepared in that any attempt by them to increase their customer base in this segment will result in greater rivalry. One must stress, however, that the other banks are not keen on over investing at this stage. Standard Bank should be using their extensive network of E-Plan outlets to gain market share. In this way, the bank can utilize their current resources more effectively and gain market share without appearing to be more optimistic than their competitors about the opportunities that this new target market presents in terms of increased profits.

The bank has a responsibility to its shareholders and other stakeholders to maximize profits and as the bank has outlaid a huge amount of cash to comply with legislation, every attempt should be made to realize a profit. The attitude of "we have to comply as it is legislation" only results in a '*hit and hope*' strategy. The market is huge and untapped and Standard Bank should be more aggressive in their approach based on their past successful experiences in this market. The one criticism of Porter's Model is that it is more prescriptive than emergent and up till now, Standard Bank has utilized an emergent approach. As well as competing with rivals, most organizations also co-operate with each other.



## **Analysis of the strategy of joint ventures, cooperative linkages and mergers**

Although the Mzansi Account is a joint venture between the four big banks and Postbank, it will prove really beneficial to Standard Bank to gain the upper hand in this market if it exercises its brand power and other resources. With the threat of cell phone companies reducing market share, the bank should look at forming a joint venture with one of the big cell phone players. The bank has been slow to optimize this opportunity. There are rumours at this stage that there could be a joint venture with MTN called Yellow Bank. Cooperative linkages, such as the one listed above, is likely to involve an emergent approach to strategy development. This venture is similar to the successful "Go Banking" initiative launched between Nedbank and grocery retailer Pick & Pay.

Standard Bank should have gained a sustainable competitive advantage by cooperating with other banks (fixed costs are reduced) such as Capitec Bank but they have not capitalized on this. Standard Bank is one of the bigger players but not the market leader in this segment. Revenue is extremely important in keeping shareholders happy and since customers generate revenue that keep organizations in business and deliver its profits, customers are crucial in corporate strategy.

Back in the 1960's, Theodore Levitt, former Marketing Professor at the Harvard Business School, wrote a famous article that argued that the main reason some organizations were in decline was because they has become too heavily product oriented and were not sufficiently customer oriented. Standard Bank has missed the boat in defining this market accurately. If one looks at what the customer wants and what the bank has delivered, one can see an "off the shelf" product that has been produced. It seems that the bank wants to give the customers what it (the bank) sees as the right product. According to the research carried out in Kwa-Zulu Natal, Mpumalanga, Western and Eastern Cape, customers don't want a 'one size fits all' approach (Annexure 1).

The bank should use their research findings in this market to adapt their product and their strategy to meet their customer's needs. A look at the research findings in the mining communities (Table 4.3), show that there is a huge discrepancy between the myths of customers needs and their abilities with the reality of their understanding of banking and their minimum service acceptance levels. A look at the

money flow in these communities will enhance understanding in this market (Annexure 2). Furthermore, the bank needs to analyze their future customers as well as their current customer profiles. This will involve some prescriptive strategies to forecast future trends. The trick is for this company to remain flexible to adapt to new trends in the market.

Standard Bank has not moved beyond *mass marketing* (one product is sold to all types of customers) to *targeted marketing*. Customers are asking to be seen as different as their needs are different but the bank still has the 'one product should fit all size' approach. This does not allow for extenuating circumstances and the convenience sector (formerly mass market) are not able to get the financial assistance they require because the bank's rules and regulations are so rigid. This is evident in the research conducted by all the Standard Bank research teams (Annexure 3).

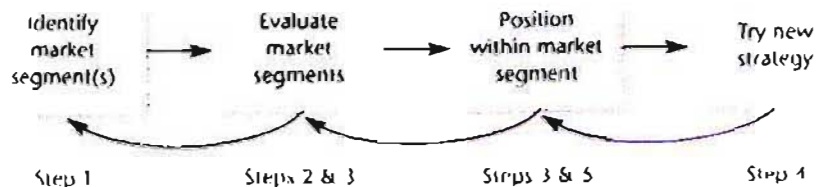
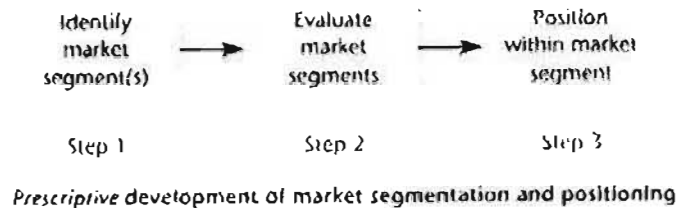
The bank needs to develop different market offerings that will be attractive to this segment. The mining community exemplifies this point as direct deposit into a bank account is a condition of employment. This shows that the needs of miners who have a steady income are different to the needs of an informal trader in Soweto who has no steady income on a monthly basis (Annexure 6). The bank does this very well in its more affluent market but although it recognizes that the convenience sector is the next revenue generator for the bank, it has been slow to differentiate its offering and approach. The bank has introduced a new innovative savings product for this segment called the 'Blue Save' but one will still have to monitor take up figures to see if this product will be successful in meeting the needs of their customers.

Standard Bank needs to note that certain segments may have low profit margins but their size may make them attractive even at these levels of profitability. The bank also needs to acknowledge that this segment has a limited number of competitors and there is hesitancy amongst the others to attack this market. By the same token, the bank needs to assess if this segment is growing faster and offer more developmental opportunities or is the black middle-income earners the market to concentrate on. The bank that understands the importance of segmenting their customer base and positioning their strategy correctly will have an advantage in capturing this market potential.

## Positioning and Segmentation

Porter uses market segmentation to draw a basic distinction between two major basic generic strategies:

- 1) Broad target segments – involve large number of customers
- 2) Narrow target segments – small niches in the market segment.



**Fig 4.4: Market segmentation and positioning**

Source: Lynch, R (2002). *Corporate strategy*, page 211 (Second edition), Prentice Hall Publications, Essex.

Standard Bank can really dominate this segment if a change of strategy is implemented. They can create niche markets in this broader segment to really meet the needs of their customers. The joint venture between Nedbank and Pick & Pay bears testament to a bank creating a successful niche in this segment. It will take lots of courage and a vision to embrace that people are different and proud of it. Customers want the banks to offer solutions and not products. A deeper understanding of this segment's gaps and opportunities (Annexure 4) will alleviate this problem. Standard Bank have been successful in doing this time after time in the upper affinity segments and should have no problem tailor making solutions for their customers as they welcome them into the banking mainstream. This only confirms that customers should be seen as a vital part of corporate strategy.

## Customer Driven Strategy

The bank has failed to analyze customers as part of the strategy development. More exploration should have been

done to regarding the nature of customer driven strategy – what is it, why is it important and how it can be developed? If the old adage, the purpose of an enterprise is to create and keep a customer, is believed to be correct, then the prime focus of strategy becomes the development and retention of customers: the *customer driven* strategy. The findings of the research group from Gauteng and the Western Cape also stress to place the customer at the centre of the bank's strategy.

At this stage, there is no indication that Standard Bank has a retention strategy in place for this new market segment. Customers are asking the question of why they should stay with Standard Bank, but no answer has been provided yet (Annexure 7). The bank needs to realize that as long as customers have a choice, the development of corporate strategy will also need to consider the customer options available from competitors.

Customer strategy therefore needs to be linked to competitor strategy. This is crystallized through the sustainable competitive advantages possessed by an organization. Such advantages will attract customers and keep them, rather than allow them to move to competitors. A look at the SA index for 2004 places Standard Bank at the top of their industry (Annexure 8 & Annexure 9) and yet their customer retention figures are way below their competitors in this segment. Customer driven strategy is designed to build such loyalty and customer satisfaction, something that is lacking in Standard Bank's approach to this segment.

One needs to assess if Standard Bank have correctly identified the customers in this segment. There is acknowledgement that everyone has the right to a banking account, but perhaps not everyone is bankable. According to the Standard Bank research team in Kwa-Zulu Natal, who conducted research in rural agricultural areas, not all people are bankable in that particular area due to inconsistencies in income, availability of basic amenities and distance to urban areas. The low literacy levels amongst these customers also support this stance. Standard Bank needs to realize this and ensure that action plans are in place to address this issue. If customers are not correctly identified, then it is quite possible that these companies, who are competing for the same customers will be left out of competitive analysis.

The importance of defining customers accurately lies in developing strategies that target them correctly and in ensuring that competitors have been properly identified. Standard Bank's 'one product fits all' approach does not

allow the correct target markets to be identified so that sustainable revenue can be generated and value added products can be provided that recognizes and satisfies individual needs. However, Levitt's approach has been deemed as unrealistic in its broad definition of customers. As an alternative, Professor Peter Doyle of Warwick University has proposed a "better way" on analyzing customers based on three guidelines:

- 1) *Customer segmentation*: the number of segments to be served by the strategy.
- 2) *Customer needs*: the range of needs to be met.
- 3) *Technology*: which technologies to master in pursuit of customers.

This will help narrow down the customer definition in a way that is relevant for strategy development. Standard Bank could look at segmenting this market further. Using LSM 1-5 as a benchmark is still too broad a definition and assuming that once people are in the banking system, they will not leave could prove detrimental. At this stage, there is no definite measurement to establish what constitutes a low income person in South Africa. Studies around the world show that people have entered and left the banking environment very quickly. They have remained outside of the banking system for years and don't see the banks as a value added business in their lives.

Standard Bank needs to understand what the main elements of their customer driven strategy are. The bank must show that they understand these customers. They need be responsive to these customers needs. They also need to show that their products do add value in these customers' lives. The bank needs to understand the flow of money in both a rural and metro environment (Annexure 2 & Annexure 5) and then devise strategies to serve these markets.

Credit must be given to Standard Bank for reaching out to these communities in this segment. The bank has gone out in research teams and had direct contact with customers on many levels. However, there has not been widely disseminated research on key customer findings. The bank has identified the key players in the money flows and yet no attempt has been made to utilize this information by creating innovative products that attract these key players into the banking mainstream. There is little understanding around what makes these players' key in that value chain. No strategy is in place as to how the banks can enter this value chain (Annexure 6).

There is also limited knowledge around why existing customers will choose Standard Bank to open the Mzansi Blue Account (Annexure 7). This could be vital for the bank in their understanding to attract and retain these customers. The bank has been excellent on their responsiveness to customer complaints and suggestions though, with a call centre set up to deal with these issues.

However, there has been limited tracking on key customer data on the company's image versus their competitors. Why people trust the Post Office (Postbank) more than the major banks is yet to be answered. More could be done by Standard Bank to reward the staff of the organization based on their performance with this market segment customers. This will provide real value for money for these customers, and encourage staff to see the importance of this market towards revenue generation in the bank. It will also encourage staff to display the commitment to uplift the community as signed in the Financial Sector Charter agreement.

The customer driven strategy argues that only by attracting and retaining customers, will long-term profits be obtained. This view of the organization is important because it suggests that simple financial measures of profitability will not be enough to ensure the growth and survival of the business. They need to be linked to customer satisfaction and customer loyalty. There is substantial evidence to support this view:

- Loyal customers are more profitable: they tend to account for the majority of the sales of the organizations and their loyalty means that they are less sensitive to price increases and may even encourage new customers.
- Attracting new customers cost more than retaining loyal customers: the extra costs may be three to five times as much.
- Retaining existing customers can dramatically increase profits: some 10 per cent of customers will leave an organization every year. However, increasing customer retention by 5 per cent can produce an 85 per cent increase in profits (ABSA annual report 2004).

Customer driven strategy can therefore be expected to enhance company profitability and increase customer satisfaction. The bank needs to understand that an *emergent strategy* approach may be needed in the context of unmet customer needs or more general marketing research

in difficult areas. It may also be required to ensure that customer service and quality are continually improved.

A prescriptive approach will be required in other contexts, especially where the customer is concerned. If the customer is to be assured of value for money, then it will be necessary to have a clear understanding of the product or service being sold at the price quoted.

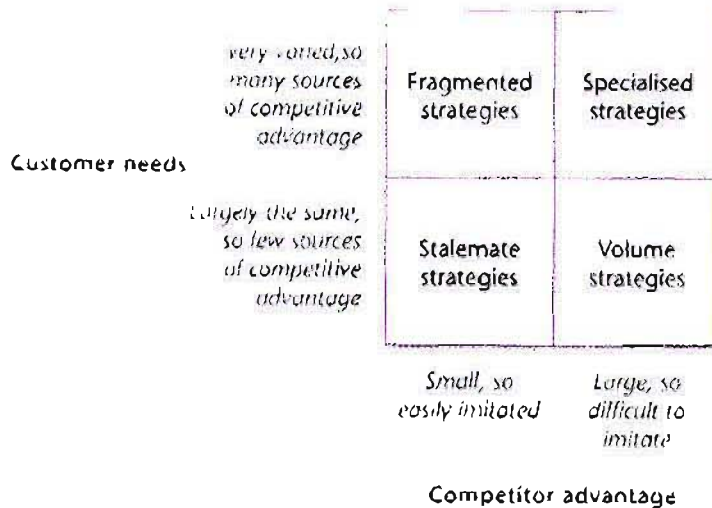
Standard Bank needs to assess if they are adding value to their customers lives in this segment. The bank does not have differentiating capabilities such as specialist technology or unique location of service outlets that will tie the customers to the organization. The "Bank in a Box" concept could change this perception and provide real value. The Bank has not been able to use its service delivery channels in terms of its vast ATM network as well as its Auto E outlets to dominate this market. ABSA has mobile consultants that issue bank cards on site and FNB has their mini-BOB ATM's that work in even the most rural areas. The Standard Bank brand is one of the respected and most trusted brands but it has not been fully utilized to attract this market on a dominant basis.

The bank's "one product for all" approach has not differentiated its approach from the other banks mentioned in the Charter. Its brand has not been magnified to attract customers in droves to the organization. The relationship with these customers, in terms of formal and informal encounters, does not endear this target market to the organization. There is no loyalty attached and the perception amongst staff is one of they have to do serve this market as the bank has committed itself. This will definitely hamper retention strategies.

Customer profiling is extremely important if Standard Bank is to dominate this market. The bank needs to understand that some customers have the same needs as others and the sources of competitive advantage will be limited to variations in price or quality. An analysis of the customer / competitor matrix will define this approach more clearly.

### **Customer / Competitor matrix**

It is important to recognize that some customers have infinitely varied needs. Here the bank will have to look at type of service, adaptability / flexibility of the product to sustain a competitive advantage. The bank should use a combination of fragmented, specialized, volume and stalemate strategies based on these needs (Figure 4.5).



**Fig 4.5: Customer / competitor matrix**

Source: Lynch, R (2002). *Corporate strategy*, page 125 (Second edition). Prentice Hall Publications, Essex.

Fragmented strategies should be used to satisfy highly varied needs in a particular segment such as mining. Specialized strategies could be used to target many different customers who all have varied needs often on a large scale such as the motor industry workers such as the 'Go Banking' initiative between Nedbank and Pick and Pay. Volume strategies could be used to sell to customers that basically want standard products with little variation. The stalemate strategy could be used to sell to customers that don't have any steady income, are not loyal and are bound to close the account in a few months such as the Kwa-Zulu Natal rural customers. In this way, it would be easy to identify customer needs and provide the right solution to them.

The bank can concentrate their efforts on smaller areas so that the company's resources can be employed more effectively. The bank would be able to see that there is strength in a group, even though the overall market is large. It would be even more profitable to have a large share in a group than a small share of the main market. The bank must see this market as the next revenue generator to help against the endowment effect if this strategy is to be successful. All this is possible through the analysis of the resources of the organization along the lines of value added and sustainable competitive advantage.

The value added route shows how the organization adds value to the input it receives from its suppliers. The competitive advantage route examines the special resources the organization has in order to compete. Both emergent and prescriptive approaches to strategy development regard



resources as important. However, their perspectives are very different.

#### **4.2.4. An analysis of the Prescriptive vs Emergent strategy**

Prescriptive strategists take the view that it is important to use resources efficiently and build on resource strengths. Standard Bank takes the view that it is important to use resources efficiently but is not building on their strengths when it comes to the unbanked market. Resources are seen as inanimate objects without feeling to the bank but they are not manipulating and moulding these resources to provide a more efficient organization. Judging by the profits the bank derives from the convenience sector (in excess of R400m – Standard Bank Annual report 2004), one would assume that the company would build on this platform.

Emergent strategists would tend to disagree on the assumption made by prescriptive strategists that change is achievable. Emergent strategists probably lay more stress on the impact of human resources than their prescriptive counterparts. Standard Bank could also follow suit and concentrate on their human resources to meet this new market's needs. The bank should realize that people resources are human beings that can help or hinder strategic change. In this way, because of the changing and unpredictable market, the bank must foster a culture of resources that are flexible and aimed at survival.

These differences of views are reflected in the two models used in this dissertation. In the prescriptive model, resources deliver a definite result to the organization and its future strategies. In the emergent model, the resources and subsequent strategies are much more fluid and interrelated. As with any strategy proposed, one has to mention funds that will be invested.

Prescriptive strategists have a very clear view of financial appraisal for strategy decisions. They take the investments to be made and predict the financial returns in the future. Standard Banks have used the same criteria in their approach where they use forecasts of demands, resources, inflation and tax regimes. The whole process was built using a computer spreadsheet and has a precision and consistency that is a model of rational decision-making. They have also added some more judgmental evaluation of:

- the *risks* involved,
- the *financial exposure*, if the project were to fail.

- the *opportunity costs* of the strategy; that is, the benefits that would arise if the funds were used for an alternative investment.

One needs to take into account that the bank had to be involved in this market development as a commitment to social upliftment, but there has been no indication that they are confident of their returns. Speaking to leaders higher up in the organization, the consensus is that this is a "hope and see situation". The bank wants to be seen as a contributor to the economy on a corporate social level and if they break even in this development, it would be a bonus. There is no emphasis on profit maximization and strategies to dominate which will ensure that an optimal return is achieved in conjunction with providing a service to the greater community.

Understanding how Standard Bank competes at this present stage in this unbanked market, one would be tempted to say that none of the three generic strategies proposed by Porter in his books *Competitive Strategies* (1980) and *Competitive Advantage* (1985), are evident here. There is no indication of cost leadership, differentiation or focus. One could assume that Standard Bank (and the other banks in the Charter) has defied Porters claims or that these banks don't see this market as an important market that could derive great rewards. One could assume that this is the reason for the lack of competitiveness amongst the banks and the reason that each bank refuses to make their mark in terms of differentiating their offerings. The final assumption is that this is purely a social responsibility and hence there is no focus on sub-segments in this market.



**Fig 4.6: Generic strategy options**

Source: Lynch, R (2002). *Corporate strategy*, page 565 (Second edition), Prentice Hall Publications, Essex.

According to Porter, every business needs to choose one of these in order to compete in the market place and gain sustainable competitive advantage. These South African banks have proved that there are no rewards to be gained in competing, and are more than willing to build a loss factor into their calculations regarding the unbanked market.

Expanding on this point, the current strategy of Standard Bank has no content as the organization has no actual strategy. The organization has no clear objectives when it comes to this market. They do have a process in place that involves a team of managers who will contribute to the task and outline the way they will communicate and discuss with each other, in order to make selection decisions. Unfortunately, with no clear objectives, this is extremely hard to achieve. This project has no definite ties with the overall organization's mission and objectives to add value to their customer's lives.

As the bank cannot reject this option, their aim should be to realign the new projects mission or change the overall mission and objectives of the organization. More effort should be put in to testing assumptions about the future to ensure that they are reasonable and valid. To encourage the feasibility of this option, more should be done to increase the commitment of managers and employees. Stakeholders should see this venture as more than a social responsibility. It should be seen as an opportunity to grow the business and their customer base.

Most worthwhile strategies are likely to carry some degree of risk. Standard Bank needs to explore the contingencies that will lessen the difficulties if things go wrong. Unfortunately, deciding if the risks are acceptable to the organization is not a luxury afforded to this bank. They are in for the long haul with huge investments deployed already and sensitivity analysis would be the most useful form of analysis for them. Essentially, it explores the "What if?" questions for their impact on the strategy under investigation. The basic assumptions behind each option (economic growth, currency fluctuation, etc) are varied and the impact is measured on return on capital employed, cash and other company objectives.

One has to mention that the current strategy is not consistent with the mission of the organization. It does not deliver on its objectives since its objectives are not defined clearly. The unbanked strategy does not build on the strengths of the organization. It does not exploit the opportunities that have been identified. There is no plan to

overcome the threats identified. The strategy just avoids the weaknesses of the organization.

Customer segment analysis offers the analyst a rational method in which to frame the scope of corporate strategy. Scope must be limited for two reasons.

The first and most obvious reason is that it is impossible for the firm to serve all customers. The second reason is subtler and strategically relevant as it speaks directly to the essence of dynamic competition: even it were possible to serve all customers, this would not be the most profitable strategy for the firm to pursue. This does place Standard Bank in a dilemma.

They are compelled by law to serve all customers even though it will result in not the most profitable thing to do. However, Standard must remain alert to the existence of loss leaders. That is, some unprofitable activities will be part of the larger system of activities that provide value to the firm's target segments.

#### **4.2.5. Segmentation strategy**

Segmentation strategy is viable in markets where customer value is premised more on tastes and preferences than on price, where different groups of customers exist in a market, and where the economies of scope and focus pre dominate the economies of scale within the market. When employing this strategy, an organization tries to create a niche market within a segment. An organization will attempt to diversify the product offering in the hope of penetrating and dominating a particular segment. The organization wants to attract the customers who want to feel that they are special and rightly recognized as so.

In these types of markets, growth and diversification strategies offer feasible opportunities to deliver profitable growth through a strong and differentiated approach. Standard Bank should adopt a market penetration approach with a little product development and diversification strategy, in their search for a profitable approach. While these customers are price sensitive, they also want to be seen as different and not as a "one size fits all" approach as used by this bank.

Businesses in South Africa are increasingly tailoring their products to attract spending by low-income groups. This group represents a massive R171-billion market. Banks, cell phone operators and retailers are among those that see

great potential in this market. Clothing retailer, Edcon, is winning customers through its Jet Club, which offers valuable services at low cost. Membership benefits include funeral benefits and roadside assistance, as well as antiretroviral therapy for the accidental contracting of HIV / Aids. For this, members pay R13 a month. This strategy is working as Jet was the star performer for Edcon in the 13 weeks leading up to 1 January 2005, as sales were up 28% compared to the same period in 2003/2004 (Business Report, Jan 20, 2005).

In an article published in The Star dated October 18, 2004, Dot Field of Vodacom stated that pre-paid customers were generally lower income earners. She also commented that the market is by no means saturated.

In the same article, rival MTN stated that its subscriber split was 80% prepaid and 20% on contract. Bernice Samuels, of MTN, stated that if one looks at LSM (Living Standards Measure) trends of the past two years, one will have found that cellular access among South Africans in LSM 5 (with earnings of up to R3500 a month) has almost doubled from 17% to 31%.

The article went on further to mention that furniture and appliance retailers, such as Relyant and Ellerines, which cater specifically for the lower income market, are expected to return between 15% & 16% sales growth for the fourth quarter ended December 31, 2004.

The media are also profiting. The Daily Sun, aimed at the working class reader, now boasts a daily readership of 400 000.

The lower income group is more vulnerable than most to inflation. An upward change in interest rates and inflation will dent their spending power although higher interest rates would not affect their spending power by too much. They do however; feel the effects being the first to get fired when companies and households start to feel the higher interest rates. Lower income people accounts for almost 62% of the country's household. In a stark demonstration of the disparity of wealth in South Africa, their total consumer expenditure is slightly less than that of the top 5.7% of the country's household, who accounted for consumer expenditure of R172.4-billion last year.

Segmentation will be an excellent analytical tool to determine which of these strategies will lead to profitable growth. Differentiation, volume, quality and low cost can now

be achieved simultaneously. Mass customization could be the answer to Standard's attempt to dominate this market. While banks accumulate financial services charter points through high profile black empowerment deals and the launch of the Mzansi account, the bigger question of competition in the banking sector is still to be addressed.

The national treasury and the Reserve Bank regarding competition in the banking sector have commissioned a report. The report apparently speaks of a complex monopoly in the banking sector and raises concerns about the grip the big four banks have on the South African economy, through their control of the payments system. Not only do they own the system, but according to some estimates, the big four banks account for more than 99 percent of all transactions.

They can set whatever charges they like for withdrawals, deposits, ATM fees or other services. They can also allow others into the system or not and they can set the conditions for entry. Bank executives would be wise to spend less time on designing complex BEE deals and more time working out ways to show the minister that competition is alive and well in the banking sector.

#### **4.2.6. The effect of legislation on defining strategy in the banking sector**

In terms of legislation affecting strategy, historically, the regulation and provision of financial services to the poor in this country has mainly been based on exemption notices to the Banks Act.

However, in 2002, an alternative model for providing financial services to the poor was put forward by the National Economic and Development Labour Council (Nedlac). The South African Reserve Bank announced in its 2002 annual report that it envisaged amending the regulatory framework to allow for the establishment of different classes of banking institutions, such as second and third - tier banks.

To this end, draft legislation has been published by the National Treasury in the form of the Dedicated Banks Bill and the Co - operative Banks Bill. The goal is for this legislation to act as a means of providing access to the banking sector to interested participants, ensuring a flow - down of banking services to the wider community and providing financial services to a broader market.

This discussion focuses on the Dedicated Banks Bill only. The bill lowers the entry requirements to act as a bank as prescribed by the Banks Act. It will result in "dedicated banks" providing certain financial services to consumers while being subject to less onerous formalities than those imposed on traditional banks. These dedicated banks will not provide the full range of financial services that are available at a multifunctional bank; rather, it is envisaged that such banks will concentrate on core services such as taking deposits from the public.

The bill creates two classes of dedicated banks: savings banks and savings & loan banks. Savings and loan banks are permitted to conduct a wider ambit of business activities than savings bank. Savings banks may take deposits from the public and provide payment services on behalf of depositors. Savings and loan banks, in addition to taking deposits and providing payment services, may also open money market deposit account in a depositor's name. Dedicated banks are subject to capital adequacy requirements, as are traditional banks. Therefore the protection of deposit holders is unequivocally pre-eminent in the mind of the legislature, even though dedicated banks have fewer formalities to which to adhere, depositor protection has not been compromised.

The newly proposed Credit Bill is set to revamp every type of credit. Some of the more controversial aspects of the Bill aspects of the Bill are likely to include the principle of set off used by the banks- in which a bank can take money from one of your accounts to pay off money that you owe in another and the charging of interests for early loan settlements. This will affect the banks' profitability, as the government may be able to cap interest rates that can be charged depending on the rand value involved.

The Bill also introduces a number of provisions aimed at regulating how credit is marketed. Banks will not be able to increase your credit limit on your credit cards automatically using negative option marketing – this is the practice of offering you something where it is assumed that you accept the offer, unless you actively decline it. This will result in a drop of earnings for the major banks. In order to maximize returns, banks will need to think innovatively. New innovative business models will need to be designed and implemented. The Pick and Pay / Nedbank initiative is a prime example of innovation. Aggressively advertising its middle market offering, Go Banking, Nedbank believes there is a case to be made for a premium brand in the lower end of the market.

#### **4.2.7. Competitor analysis**

As everyone prepares for the Mzansi launch, attention inevitably turns to consumer friendly alternatives such as retail group Pick and Pay's 'Go Banking' platform. Operated as a division of Nedbank, Go Banking's target market is the middle- income market, which it defines as those earning between R5000 and R20 000 a month. Go Banking's target market embraces the 3 million of the 5 million customers who shop in Pick and Pay store every year. As a result of the retailer –banker relationship, Go Banking is probably the closest South Africans will come to real consumer banking. Rivals admit to admiring its low cost business model.

In the UK, consumers have long been accustomed to banking with supermarket groups Tesco and Sainsbury. The concept of providing as many services as possible under one roof is not lost on Pick and Pay or Nedbank, from both a customer convenience and income stream perspective.

Customers win because they can shop and bank in one location. The ability to offer banking facilities is a drawcard for the retailer while the appeal for the bank lies in low cost access to additional transaction fee based income streams. Go Banking is able to provide competitively priced banking services because it operates on Pick and Pay's national network and technology infrastructure.

Nedbank has not had to incur the expense of opening new outlets or ATM's to expand its customer footprint while Pick and Pay can manage the amount of cash held in its tills. It is a win-win situation for all parties concerned. Another example of innovation and a winning business model is the one employed by Capitec.

Standard Bank's strategy to "hope to break even" in the near future is way off the mark and their limited offering on the Mzansi account will really not help to leverage their resources effectively. A number of other banks such as Capitec have long had products, which offer everything that Mzansi does, and more.

According to an article published in the Business Report dated 20<sup>th</sup> January 2005, the Mzansi initiative is not expected to break even for 5 years, but the success of Capitec is that it is already profitable. In an article published in The Star newspaper dated February 13 2005, Capitec was issued a banking licence in 2001, and in four years has acquired more than 350 000 customers. The challenge to banks has been to rapidly extend their footprint, and Capitec



Banks' solution has been to acquire and convert cash loan shops into fully fledged retail banks.

Capitec Bank's success stems from a total focus on the mass market that is looking for accessible and affordable banking. Their initial objective was to establish a national distribution network, a client base and an income stream. According to Capitec's Riaan Stassen who states in this article that the difference between the big four banks and Capitec, is that Capitec was geared for this market from the outset while the big four cater for the full spectrum of customers.

Stassen also argues in this article that the banks cannot address this market with a product alone. He suggests that success in this market depends on achieving a balance between a distribution network, service delivery, communication to the target market, product specification and pricing.

He further argues that the market has four core needs: accessibility, affordability, simplicity, and personal service in terms of advice. His example that Capitec levies a standard rate of R2 on most transactions while in comparison, Mzansi account holders will be paying between R8 and R10.75 for cash withdrawals and between R5 and R10.75 for cash deposits made after the first free transaction afforded to account holders. The article also mentions that Capitec offers all aspects of the Mzansi account – as well as debit and stop orders.

One of the success factors is that when Capitec opens a new branch in rural areas, it employs local people who reflect and understand the market as well as paperwork has been completely removed from all branches. The bank also uses a client pin number for all transactions – the customer does not have to remember bank account details and complete a myriad of bank forms.

Another example of Capitec Bank's innovation and focus on rural unbanked areas is the introduction of South Africa's – and the world's first – preauthorized Master-Card microchip debit card. The banking fees of the microchip card are designed to be the most affordable in South Africa - funds are loaded onto the chip free of charge, as are account queries. Any purchase made at participating retail stores has a fixed fee of 50 cents per transaction. Capitec is not the only company that is using technological advances of finding a way to bring banking to people in remote areas. Net1 has risen to the challenge, both in SA and in exports markets.

Their innovation strategy is based on two drivers (Fig 4.7), namely, technology and the market needs of customers.



**Fig 4.7: The two major drivers of innovation**

Source: Lynch, R (2002). *Corporate strategy*, page 500 (Second edition), Prentice Hall Publications, Essex.

Their product is an alternative banking system based on smart card technology. It's the software in the card that makes the difference. It works in a totally different way to traditional banking systems that operate through an online account.

The cards work very simply. People each have a card and the cards connect with each other. You can put money in the card and take it out, using fingerprint recognition for security. Each card has 255 different pockets, each for a specific need. One can be a savings account that would earn interest, you can have another for prepaid utilities, or for transport, or for cellular phones. There can be automatic debits from the card. All this can take place offline. People can use the card in the same way as they might traditionally have used different boxes under their beds to keep money for different purposes, but with far more security.

Net1 has 3.5 million clients in South Africa and 6 million customers worldwide. The company does business in Rwanda, Burundi, Mozambique, Zimbabwe, Malawi, Ghana, Latvia and the CIS republics. The system can be used for wage payments, pensions and welfare distribution as well providing a myriad of financial services, including loans and debit orders – all things the bank offer.

Net1 have about R700m of business in SA and R200m outside. The idea is to build this across Africa, South America and in the Asia Pacific region. The card would then be usable around the world, serving those who are currently labeled as unbankable. It will be a transaction card that can serve as a credit, debit or change card. The question that needs to be asked is will the costs of these micro-chip cards

result in increased fees on an annual basis. One has to question what initiatives are there in place to minimize the pricing increases that are bound to appear as declining margins put pressure on the big four banks bottom lines.

#### **4.2.8. Pricing and the effect on strategy**

Less than a year after the launch of the Mzansi, banks are talking about reviewing the pricing of accounts and increases have not been ruled out. In an article published in the Star newspaper dated March 29, 2005, ABSA has stated it would review its Mzansi pricing structure in October 2005.

Up to March, it has attracted almost 700 000 account holders. This attraction is based on its lower charges. ABSA has not made a decision on whether there would be an increase, a limited increase or no change at all.

In the article Colin Donian notes that the original discussion between the banks led to an undertaking that pricing adjustments would be tied to the annual inflation rate for fees and charges, and interest rates would be adjusted in line with moves in the prime rate. This was before the banks' plans to collaborate on the roll-out of the Mzansi were stifled by Finance Minister Trevor Manuel, who stated that each bank should compete individually. Donian added that now individual banks were free to adjust their pricing as they saw fit.

In the article, First National Bank did not comment on whether it would leave its charges unchanged for Mzansi, while Nedcor indicated that there would be no adjustment on the account.

While the Mzansi account fees may be increased or not, South African banks, realizing that they would have difficulty justifying price increases above inflation, are expected to increase banking charges by 4 percent or 5 percent on average this year across the board in a bid to subsidize this new account.

ABSA, the country's largest retail bank, stated in the same article above that it would increase its banking fees by 4 percent on average. Louis von Zeuner, group executive director at ABSA, noted that last year's release of the Falkena report entitled 'Competition in South African Banking', the financial services charter and pending new legislation that aimed to introduce increased competition into the industry through the establishment of second-tier and third-tier banks, had forced banks to think about the way they did business. First National Bank, which reviews its

pricing structures in October every year, said in November that it had an average overall increase of 3.71 percent that would be enforced for most of 2005.

Martin Pienaar, the head of wholesale product management at Nedbank, said that Nedbank's annual pricing review would come into effect from July 2005. South African Banks which have prepared a collective response to Falkena's 16 recommendations (Annexure 11) are fighting growing criticism over what Von Zeuner believes is the "emotive issue" of banking charges.

Falkena's report found that local banks charged far more than for basic transactions than those in Australia, Britain, Canada, Germany, Ireland, New Zealand and the US. It has also found that South Africans paid for services, like deposits, that were free in developed countries. It found charges had been increasing at a rate well above inflation.

On the issue of excessive profits, Von Zeuner stated that ABSA had commissioned a study by KPMG to analyze the return on equity (ROE) of the South African Banks compared with that of banks in other countries.

Reserve Bank Governor Tito Mboweni stated in the same article that while rocketing oil prices posed the biggest threat to the economy, he was also concerned about spiraling household debt and was considering how to deal with high bank charges.

Rob Davies, the chairman of the portfolio committee on finance, said that the result of the study had been shocking. It showed that compared with the top 100 banks worldwide, South African banks were more profitable because of higher bank charges. He was particularly concerned that the charges were particularly loaded for the poor, which discouraged saving.

#### **4. 3. Summary**

The chapter looks at the best practices of Standard Bank as well as what they are not doing in order to be a successful company. Different business models such as the ones employed by Nedbank's 'Go Banking' and Capitec are analyzed and discussed. Segmentation of this market, pricing and legislation (Dedicated Banks Bill and the Credit Bill) are discussed with regards to the implication on the organization's proposed strategy. One needs to realize that

the unbanked society will remain cash driven for a while into the future.

Although banks have been actively targeting the low-income market for some time, the value of the opportunities remaining is surprisingly large. This is due mainly to the fact that the aspiration levels of banks in terms of servicing low-income customers are often set by local peer comparison and self-imposed limits on feasible achievement, rather than by true stretch targets. The other reason, and not entirely independent from the first, is the difficulty of changing entrenched mindset across large organizations.

In the next chapter, discussion will take place over what the company has done well and should continue to do so over the years. Mention will also be made of the issues that company is not attending to and recommendations will be provided to establish remedies to place the company in a positive frame and improve overall organizational performance.

## **CHAPTER FIVE**

### **Recommendations**

#### **5.1. Introduction**

Two out of three South Africans are currently unbanked. At the same time, South African banks have experienced a significant decrease in income due to dropping interest rates and the resulting pressure on profit margins. Banks therefore need to modify their approach, their channels and the products they offer to convert the unbanked. What is the market challenge facing these banks?

Estimates vary but assuming there are around 45 million South Africans, then at most only 15 million is currently banked. This assumption has tremendous significance and quite a number of serious consequences. It means that two out of three South Africans are unaware of the benefits and advantages of banking their money. The important question is can everyone be banked? The next question concerns minimum acceptable entry-level income that should initially be targeted. There is currently no agreed instrument to measure or define a low-income earner in South Africa.

As a result, there is a divide between those that believe that a low-income earner takes home R1000 a month and those who say that the figure could be about R2000.

According to its website, the University of South Africa's Bureau of Market Research ([www.archives.saarf.co.za](http://www.archives.saarf.co.za)) has developed an instrument called the Minimum Living Levels (MML), which basically considers anyone who earns less than a MML to be a low income earner. Defined as the lowest sum on which a family of any size could live in South Africa, MML indicates the minimum financial requirements of members of a family if they are to maintain their health and have acceptable standards of hygiene and sufficient clothing for their needs.

It is calculated annually, in March, using a sample of people in fifteen urban areas including Durban, Bloemfontein, Nelspruit, Johannesburg and Polokwane. Last year the median for all areas measure was R1946 for an average family of three to six members.

According to the website, Percy Moleke, at the Human Research Science Council, believes that designing a national

instrument to measure a low-income earner would be an unwise move. She argues that provinces have different standards and costs of living. Therefore, a person living in Polokwane would have a different monthly income and buying power than one in Johannesburg, Gauteng. She suggests that it would work better if it were designed for a province rather than a country.

Statistics SA, the official statistics body, states on its website ([www.statssa.gov.za](http://www.statssa.gov.za)) that it has not yet devised such an instrument. Knowing and being able to define the target market correctly goes a long way to segmenting and offering the correct solutions to these customers as well as recommending the corrective actions to be implemented by Standard Bank to readdress the imbalances of the past.

## **5.2. Recommendations**

According to an article published in The Star newspaper dated March 29, 2005, chequebook charity is not the answer to uplift society.

People must be empowered to help to grow. Businesses have invested significantly in corporate social investment (CSI) projects that are company specific. Business leadership is an important part of the CSI equation. It is vital that the top executives be informed about the key challenges facing society and the economy. It is equally important to engage with government, because what executives perceive as solutions may not be sustainable if they based purely on personal opinion. South Africa leads the way in understanding that from a business perspective, global and local sustainability challenges can only be engaged effectively in a collective manner. Collective business leadership is critical to transcend individual company interest and effect social change. As such, business leadership can help to shape and improve the competitive environment of business, while contributing to the overall wellbeing of the country.

Business can no longer maximize profit margins at the expense of the communities and environments in which they operate, notes Nicky Newton-King of the JSE Securities Exchange SA (JSE) in an article published in the Business Day dated February 15, 2005. She adds that as stakeholders raise their voices, business has been forced to acknowledge that focusing on the triple bottom line – environment, society and economy, is the only way forward. A structure that will drive this strategy is highlighted below.

The segment has to be integrated into all relevant structures of the bank. Through matrix management, the bank needs to develop dual reporting lines to ensure consistency and integration in areas such as:

- lending
- transactions and savings
- network distribution

The calibre and quality of people working in this segment should reflect the seriousness and ambitions that the bank has about the future of the segment. The segment will have to have appropriate skills and resources or the ability to tap into such resources in any part of the group in order to be able to compete.

The present structure will be changed through recruitment, assignment of new responsibilities to existing staff, promotion of performing individuals and restructuring in order to align to the new challenges. Values-based strategies can unlock the potential of employees and address Standard Bank's challenges.

Strategic planning is the exciting topic in corporate corridors but too often it lacks accountability. When planning strategy, one often become overly enamored with our imaginings of the future and get so completely engrossed in analyzing and fine tuning the detail that the plan takes on a life of its own and becomes, in and of itself, the end goal.

When this happens, one forgets that success has little to do with planning and a whole lot more to do with "doing". Defining strategy, as difficult as it may seem, is the easy part. By far the hardest part is making strategy happen. The brutal truth is that the difference between companies that are successful and those that are not is their ability to execute and that depends on people.

An imperative for Standard Bank is to gain sustainable competitive advantage by unleashing extraordinary performance from people. This challenge goes broader and deeper than just training. They need to question their philosophies, how they craft strategies, structure their organizations and design management processes, their cultural beliefs, prejudices and preconceptions, their values and style of leadership and management. The result of their questioning should be an alternative approach to developing organizational strategy. The question moving forward is what must Standard Bank do in order to gain sustainable competitive advantage. Every organization, public or private,



small, medium or large, must seek answers to this question if it is to survive and grow.

The typical approach to finding answers is to conduct research, analyze the research and apply a variety of synthesizing methods and processes of logic that distil thinking into a strategic plan. The plan is prioritized, tactically arranged and allocated to chunks of time. The organization then attempts to align around the plan and hopefully flowing from this, appropriate action is taken that finally bears fruit and produces the expected performance.

Graphically, this approach would look like illustration A (Fig 5.1).



**Fig 5.1: Illustration A**

Source: Kerrigan, M (2005), "Time to unleash the extraordinary", *Business day*, Johannesburg, p1, March 07.

Within this approach, senior management's role is to monitor alignment and ensure compliance – in other words command and control is the underlying belief. But this approach holds within it a fatal flaw. The great power – and fatal flaw of the strategy – structure – systems framework lies in its objective: to create a management system that could minimize the idiosyncrasies of human behaviour.

Indeed if the three elements above were properly designed and effectively implemented, large, complex organizations could run with people as replaceable parts.

According to Hawkins (2003), the complexity of human behaviour that our traditional approach inherently seeks to control is unfortunately very familiar to all of us and based on the following negative assumptions we tend to make about people:

- People are effort averse;
- Management and employee interests are not aligned;
- People are opportunistic, self interest seeking and dishonest;
- Managers need to design incentives to overcome these difficulties;
- High powered incentives (i.e. money) are better than low powered incentives: and
- People work for money and will comply with management to obtain it.

Such assumptions drive companies to implement strategies and control systems designed to catch the 5-7% of employees who do not fit into their organization (or have ill intentions). If the bank is to compete globally by unleashing the performance potential of their people, doing more of the same is not going to help.

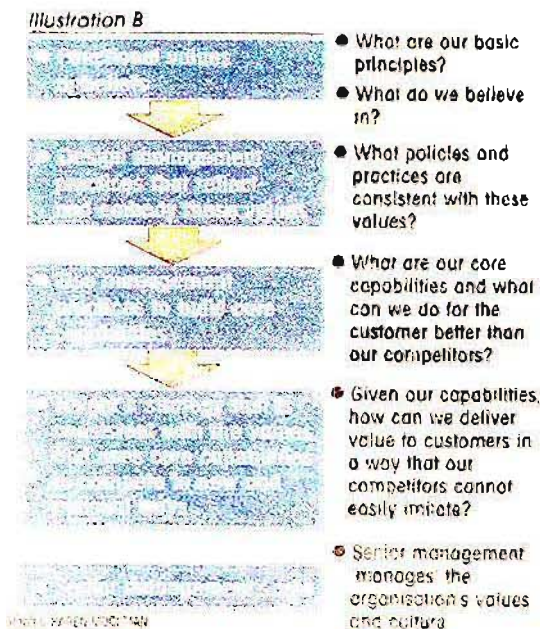
Perhaps if the bank took human resources more seriously and adopted a values-based view of strategy, they would consider people practices as integral to their strategy rather than as an afterthought or subservient to strategy. With this approach, it would seem logical and feasible to design systems and management processes that suit the 93-95% of people who are attracted by their values and culture, and then let them manage the 5-7% misfits.

For such an approach to work at Standard Bank, they need to enforce the assumptions that people:

- are responsible and willing to be held accountable for their actions;
- are capable of making decisions;
- like challenges and learning new things;
- are motivated by good intentions;
- desire to make a positive contribution; and
- are unique and don't like to be treated like machines.

A values-based approach to strategy is exactly what is proposed.

Consider the strategy process in illustration B (Fig5.2). Senior management's role in this approach is to:



**Fig 5.2. Illustration B**

Source: Kerrigan, M (2005), "Time to unleash the extraordinary", *Business day*, Johannesburg, p1, March 07.

- define the core values ;
- develop and build the culture (norms) based on these values;
- craft business strategies that leverage these capabilities; and
- ensure organizational alignment and consistency of strategy and human resources practices.

Essentially this means values and culture come first. People are employed primarily on whether they fit in with regards to the organization culture. Power is devolved to the lowest levels through widespread information sharing of operational and financial data. There is a greater reliance on teams where the emphasis is on equity and non-monetary rewards and leadership is preferred to management.

Values-based organizations place less emphasis on following a clear strategy than on building a rich corporate purpose, they focus less on formal structural design and more on effective management processes: are less concerned with controlling employees' behaviour than with developing capabilities. Such a transformation must and can only start with top management at Standard Bank.

Such a transformational approach to developing strategy is not only possible but essential if the bank is to address the

challenges they face in South Africa. If senior management adopted values-based strategies and the resulting people-centered practices, the bank would be able to kick-start processes that would win the hearts and minds of their employees, overcome the bitterness of the past and invent a brighter future. Together with those bold enough to lead the way, they can then summon the Herculean effort required to unleash the performance potential of ordinary people in Standard Bank. The literacy levels of South African people and customers will be of paramount importance in implementing this strategy.

According to the Standard Bank research group, the 'Shakas' from Kwa-Zulu Natal, the KZN rural communities live from hand to mouth. There is very few instances where there is surplus to save. There is a belief that not all the rural community should be banked at this stage. The bank's involvement should concentrate on social upliftment in partnership with other stakeholders. This should mainly be around education and financial literacy. An awareness and availability of the financial services, and of their own changing circumstances, will in time create the need for rural agricultural community to be banked.

In an article published in the ABSA Banking Journal in 2002, it is claimed that in the US, there are many people unable to read a street map, understand directions on the back of a product, or make informed consumer decisions. This may prompt a person to ask what does this have to do with banking. According to the article, if people could read, they'd have better jobs, and if they had better jobs, they would have more money. Banks would certainly benefit. The article further mentions that in the US, people who are illiterate, use the old fashioned bank, a pawn shop. The article claims that focusing on the poor is expensive. A bank with one thousand accounts containing \$100 each has a higher overhead than another bank with fatter account averages. Drew Allbritten, of the American Association of Adult and Continuing Education, notes that commitment is needed. She asks the question of who is going to commit to urban areas and the poor.

Paula Schlusberg, editor of New Readers Press states in the same article that there are several ways banks can benefit poor readers and themselves. She suggests that not only can banks participate in local literacy efforts; they can also sponsor their own workplace literacy programs. Schlusberg argues that bank employees usually come from the surrounding community and by upgrading the skills of bank employees; one can produce a circle of benefits. She further

comments that employees become spokespeople for the bank, and bring in their friends and families, mentioning that the bank is a good place to work and bank.

Schlusberg also suggests that banks simplify and standardize their most common terms and conditions. She advocates that the variety of choices is intimidating and confusing, even for literate customers. Standard Bank could take a leaf out this book by simplifying their terms and conditions.

A third option is to launch publicity campaigns to explain and bring bank services to poor communities. The article mentions that Nations Bank, for example, hold 'banking days' in depressed areas by bringing in loan officers and tellers to work at portable booths, explaining procedures in several languages and offering services. Schlusberg notes that as banks improve communities, there will be more need for banking services.

Standard Bank has started to host banking days by holding indabas (informal meetings) in major townships around Gauteng. They also have portable teller machines that are deployed in rural areas and sporting events. They have yet to have implemented mobile officers that go out into the poorer communities to offer services.

Solutions, proposed by the Standard Bank research group 'Kaofela', involves taking banking to the people. They proposed to introduce a *starter pack* (Annexure 12) to open bank accounts. This is similar to the prepaid cell phone package. The starter pack consists of card, pin number, picture based – own language activation and user guide. Sales agents can be kiosks, door-to-door, retailers and taxi owners. To activate the account, SMS or call a branch with ID and card and the branch responds with an account number. This will ensure a more convenient product for the customer.

The pricing philosophy entails basic banking for free. The first ATM – cell transaction is free. The cost of the starter pack is R10. There are no monthly fees. An insurance element can be added such as a funeral plan. This helps to build credit ratings with the bank. Costs are minimized – no systems opportunity cost, no statement costs, no closure costs, no re-opening costs. In terms of development of this product, the bank can look at lifting transactional limitations. Other opportunities involve the ability to grow loans with support (based on track record), cross sell other products as customer matures. The research conducted by the author

confirms that high costs are a barrier to people opening banking accounts with over 80% of people interviewed claiming that the costs are too high (Annexure 17).

According to Standard Bank's 'Twisters' research group from Mpumalanga, Pretoria, Limpopo and North West Province, one of the most important observations made was that the miners did not have adequate knowledge of how the banks could serve them. The recommendation made is that banks need to invest more resources towards educating and informing their clients about the opportunities available to the mining community at the bank.

It is predicted that through this strategy the bank will address many, if not most, of the immediate concerns or needs of this segment of the population, with reciprocal benefit to the bank. Having 'on site' banking days will help to solve this issue.

Other solutions from the Twister research group involve the 'Bank the Family concept'. The bank proposes to link different products together to form an offering to a family. A practical example entails the Dad (miner) having an E plan account, kids 16 years and older having a sum1 account, the wife having a Mzansi account and so on. Linked to this will be a funeral plan as well as a savings pocket. This is similar to a 'basket approach' of product offerings at a discounted price. The bank should try to provide incentives to attract new business, as this has proved successful in America (Rhyne, (2001).

The article also mentions that Americans have a variety of reasons for avoiding traditional banking. Many, however, could be enticed to become customers if presented with the right incentives, according to the article. Michael Barr, a professor at the University of Michigan Law School, stated in the article that many people avoid banks because they considered them institutions for rich people and felt that those without a lot of money would be unwelcome.

In the article, Michael Zamorski, of the Federal Deposit Insurance Corp's (FDIC) division of supervision and consumer protection noted that a lack of consumer education is one key reason so many people in this nation may be unbanked.

A number of organizations are working to educate unbanked people about the benefits of traditional banking.

Many banks go on site in the community to enhance financial education and encourage the opening of bank accounts,

using incentives such as account matching. There are a number of incentives that many banks use to bring the unbanked into traditional banking.

Among them were:

- free cheques
- low cost money orders
- matching funds on initial deposits
- direct deposit bonuses
- waiving credit history check
- convenient locations and hours
- culturally competent staff
- a casual atmosphere
- free tax counseling

The article also quotes Alabama congressman, Spencer Bachus, who stated that many of the people without a relationship with a traditional banking institution, are people who have had bank accounts in the past but subsequently had a negative experience and left their bank.

Another example of the successful strategy of using incentives to attract new business is based on the banking industry in Puerto Rico as per the article published in the ABSA Banking Journal in September 1996.

According to the article, Puerto Rico's unbanked segment is estimated at 36% of the island's population. The article notes that 41% of the unbanked households in Puerto Rico are employed. There are many reasons why people are unbanked in Puerto Rico.

They may not make enough money, may not perceive a need or benefit, or may believe that the account-balance requirements are too high. Additional reasons are the complexity of managing cheque accounts, the desire to keep financial information private; and the lack of savings habits.

It is acknowledged in their banking sector that the key to connecting the unbanked segment to financial services is direct deposit. Standard Bank could offer companies incentives to deposit directly into their staffs' accounts.

The Centre for the New Economy (an organization dedicated to developing economic strategies) has identified two principal methods for attracting the unbanked situation. The first option is to expand banking services. Banco Popular, a traditional bank in Puerto Rico has introduced a product Acceso Popular, which allows the separation of daily transactions from savings.

Since 2001, it has opened more than 200,000 accounts with average deposits of \$311. Of the account holders, 50% have activated the savings component. Standard Bank has this facility on their E plan product although the interest rates earned are not very attractive.

The second way is encourage the building of assets. Some maintain that poverty is the absence of income, while others says poverty is the lack of capability – the capability needed to grow economically through the development of personal assets. Economic advancement for the unbanked, whether in the form of a home, a business, or something else, is linked to asset accumulation, which will validate credit, collateral, or guarantee requirements. Trends show banking institutions are working with unbanked families by developing custom-tailored products and services that will promote asset accumulation.

Standard Bank is piloting community based lending in the Eastern Cape using donor money / government money as collateral. This is similar to what FNB has done with the King Williams Town municipality. There is also an initiative with the Metro Rail Company to produce bank cards that can be used as a store of value to swipe as customers are about to board a train. This will reduce the risk of carrying cash for both the customer and the railway companies as well as encourages people to participate in the banking environment. The research conducted by the author confirms that 68% of the sample interviewed would consider opening a Mzansi bank account and 70% feel that they would benefit by having this account (Annexure 18).

A further solution proposed by the Twister research group is the 'cell phone to cell phone' value transfer. This involves smart card technology. This is a safer, more convenient way of transferring money. The bank would have to form a cellphone-industry alliance. This could prove to be an opportunity or a threat. There is a great chance that cell phone companies could go it alone because of the technology and huge customer base and thereby reduce fee income for the bank.

Taking technology to the unbanked is of paramount importance if the strategy is to be implemented successfully. According to Neil Katkov, a Celent analyst, ATM technology and a thorough understanding of consumer needs will be central to banks efforts to serve the difficult to reach unbanked market (McAndrews,(2003). He states that by 2005, banks will leverage advances in ATM functionality



enough to capture five percent of the unbanked market, or more than \$1 billion. By 2010, he says the figure will grow to 22 percent, or \$3.3 billion.

A number of players have started taking steps to serve this market. Convenience and retail stores are introducing highly functional ATM's, in conjunction with transaction based software companies, to provide the market with check imaging software that allows ATMs to cash a payroll cheque on the spot. The research conducted by the author confirms that around 57% of the sample interviewed would consider using ATMs with over 80% claiming that they would use the ATM technology at a minimum of twice a month. This shows that the target market is willing to learn about new technology but they have to be trained and educated (Annexure 18).

For example, through 7-Eleven's new financial kiosk, Vcom, unbanked customers can cash their pay cheques using Certegy's check imaging platform. After a social security number is verified, customer inserts a cheque into the Vcom machine, which is scanned by a magnetic reader to determine the account it was written from. The cheque is finally scored through a number of Certegy databases and is cashed in what 7-Eleven officials say is a five minute long transaction.

Infonox has purportedly made self-service cheque cashing systems safer for banks by using biometrics to verify a customer's identity. The Infonox ATM takes a picture of the user as they stand at the machine. The ATM then scans the customer's picture ID with an 'active verifier'. Then, using biometric imaging, the two pictures are electronically compared. If the pictures are deemed to match, the cheque can be cashed as soon as it is cored and approved. Judging by this, in terms of innovation, Standard Bank is lagging way behind other developed economies.

Offering customers the opportunity to cash cheques at ATMs are not without drawbacks. Advanced machines with cheque imaging and user ID software are expensive, with costs starting at \$40,000. Then there is also the issue of time. If it takes 5 minutes to process, it will hold up the queues at the ATM, and can result in revenue loss if the customer decides to go somewhere else. In rural areas where time is not of the utmost importance, this could be an idea worth implementing by Standard Bank.

According to the research compiled by the 'Russians' group from the Gauteng area, failure to acknowledge that the

customer is central to the solution will result in no solution at all. Their solution entails a customer driven strategy (Fig 5.3) as follows:

- *Product* – existing product available, value adds to be considered
- *Customer acquisition* – member get member, possible partnerships with Retailers, market through existing customer base, create an awareness amongst younger generation, deploy mobile consultants at targeted areas
- *Service* - Fulfilling customer experience, customer education, servicing channel outside of branch network, emphasis on self service
- *Expansion* – customer usage, retention and loyalty. Grow with the customer



**Fig 5.3: Analyzing Customer strategy: the main elements**  
 Source: Lynch, R (2002). *Corporate strategy*, page 125 (Second edition), Prentice Hall Publications, Essex.

The *Infinity X* group's (from the Johannesburg provincial team) research solution entails using Standard Bank's branding in strategic places to create awareness. Their solutions involve the bank co-branding everyday highly consumed products such as maize meal, to market the Mzansi product. The group proposed that the bank use the other side of the actual product to advertise their product. Therefore, a customer buying their maize product for the month will see the Iwisa signage on one side of the package and the Standard Bank product on the other side (Annexure

14). The language used will be synonymous with the area and province involved.

The group also proposed branding taxi ranks and other public places with the Standard Bank logos (Annexure13). This involves painting / covering the existing steel and concrete structures with the Standard Bank logo to fully promote the brand so as to create brand awareness. After all this is the market the bank is trying to attract. This is the market that the bank should be trying to find ways of lending money to them, so that they can be part of the financial mainstream.

In their approach to micro-lending, the big four banks have focused up to now on low income salaried individuals. This was a rational decision as the fast growth of the formal micro-lending industry in the nineties assured the banks of the profit potential of such lending.

The big four banks lack of enthusiasm to engage micro-entrepreneur lending is to a certain extent vindicated by the international experience. The experience indicates that big banks have serious problems in integrating micro-lending operations into existing bank structures, making downscaling problematic. The international experience has also shown that for linkage banking to be successful, NGOs are needed to establish and train SHGs. Suitable candidates to undertake the latter functions are in short supply locally. But the banks apathy toward micro-entrepreneur lending can also be explained by the absence of entrepreneurial skills among the poor in South Africa.

Given the above circumstances, establishing banks dedicated to micro-finance by means of specialized public / private sector partnerships emerge as the most appropriate strategy to get the banking sector involved in micro-entrepreneur lending. Proceeding along these lines will ensure the availability of the technical assistance and funding vital to successful lending in this market. However, such partners will have to be convinced to invest in South Africa.

The Reserve Bank's reluctance to lower the banking sector's capital adequacy requirements (CAR) despite the fact that this would make it easier for banks to lend to the poor has also contributed to the banks' cautious approach to micro-lending. According to the Basel 2 accord, which advises central banks on how to maintain financial stability, South Africa might have the space to reduce the CAR from 10 percent to 8 percent, which is the international norm.

Standard Bank's hesitance to forge ahead in the micro-lending industry seems to be their downfall if they intend to dominate this sector. The big banks are again looking for opportunity in South Africa's R17.2 billion micro-lending industry.

Michael Jordaan, of FNB, states that in the annual report of 2004, his bank is looking to aggressively compete in the lower end of the market, where it has 1.6 million customers by offering personal loans and affordable home loans. Jordaan recognizes that there were clients in that market who were good risks but struggled to get finance. He notes that commercial banks had all but ignored the needs of the 15.6 million low income earners but were waking up to the opportunities that had until recently been left to the over 1600 registered micro-lenders.

The Banking Council has hinted that the Mzansi account could eventually be used to award loans to the low-income market. According to the council, the big four banks plus African Bank account for 55 percent of the micro-lending loan book. Typically awarding loans of about R1500, the microfinance industry has an estimated 123 600 customers (Standard Bank annual report, (2004). With a growing customer base, Standard Bank seems to be missing first mover advantage and this could have huge implications for revenue growth.

It is not foreseen that the big four banks can or will be significantly involved in micro-entrepreneur lending in future. Their focus in micro-lending will remain on consumption related loans for low-income salaried individuals.

If South African continues on their current path, according to the FNB annual report of 2004, the bank believes that by 2014:

- growing confidence will drive economic growth
- economic growth will rise to between four and six percent.
- the rising middle class will spur investment.
- crime will continue to decrease year on year.
- everyone will all have access to housing, water and electricity.
- economic growth will cut poverty by half.
- the land issue will be resolved equitably.
- Aids will make us pull through as a nation.
- tourism will become one of our biggest job creators.



- the 2010 World Cup will spark a sporting Renaissance.

The challenge is there – it is just a question of who will tackle it first. The bank that acts first will definitely have first mover advantage and dominate this segment.

### **5.3. Summary**

A major new foreign competitor in South African retail banking space, a string of new black shareholders in big banks, new initiatives to bank the unbanked and gearing up to comply with complex new regulations are some of the challenges faced by the local banking sector over the past year.

One of the biggest challenges for bankers may be yet to come. That is, how to sustain the growth momentum. The answer could lie in the revenue that will accrue from the Mzansi account initiative and its associated benefits.

The Mzansi account isn't perfect but it is a welcome move towards extending basic financial services to the poor. In the absence of a bank account, the poor pay twice: first they get low incomes; then they have higher transaction costs – as well as the threat of theft. Workers paid in cash must get home safely, find some place to keep it and then make payments in person. That means additional travel costs as well as insecurity.

The lack of access to the banks is particularly harmful to pensioners, one of the most vulnerable groups in society. As they can't get electronic transfers, most wait in line for payouts. That imposes the burdens of travel, queuing, vulnerability to crime and even in some cases corruption by payment agencies. Moreover, the cost to government of physical payment is higher than electronic transfers.

The Mzansi account does not meet all the needs of the poor and unbanked. For pensioners the costs are still relatively high. The limits on transactions mean many informal traders will still have to use cash and the account currently does not permit any debit orders, making it hard for account holders to get insurance, deal with housing bonds – or pay their union fees.

But the Mzansi account can only reasonably go so far. South African government still needs to find ways to address the

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financial sector's concentration and narrow control. They must encourage more diversified financial institutions with broader ownership, especially village banks and savings and loan co-ops. Unfortunately, until appropriate legislation is tabled, as the treasury promised in 2004, one can expect little improvement in this area.

The true test will be to see how the account is actually used by consumers. The banks also need to ensure that it is the right target market that is opening Mzansi accounts.

The following needs to be changed by Standard Bank in terms of their organizational mindset with regards to high yield lending. Standard Bank needs to devise a low-income lending proposition as soon as possible. The organization needs to expand its distribution centres, create and understand this segments' risk assessment methodology as well as grow its asset based lending book.

There are several options, but what really matters is that Standard Bank must find a *South African* way of addressing this forgotten market's needs. They must avoid imposing on their customers a western banking model. It is no use trying to impose ATM transactions, internet banking, credit card operations, foreign exchange products or hedge funds on those who simply need a place to deposit wages and basic credit facilities to enable them to cover the basic needs like housing and education.

Only when this is achieved, will the bank be able to dominate this segment and derive the necessary rewards as well as add value in the lives of their customers. The biggest issue for Standard Bank is thinking about how to keep growing the business irrespective of changing market conditions. The answer is to attack the opportunity that the unbanked sector presents as the next great source of revenue will come from this stream.

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## LIST OF ANNEXURES

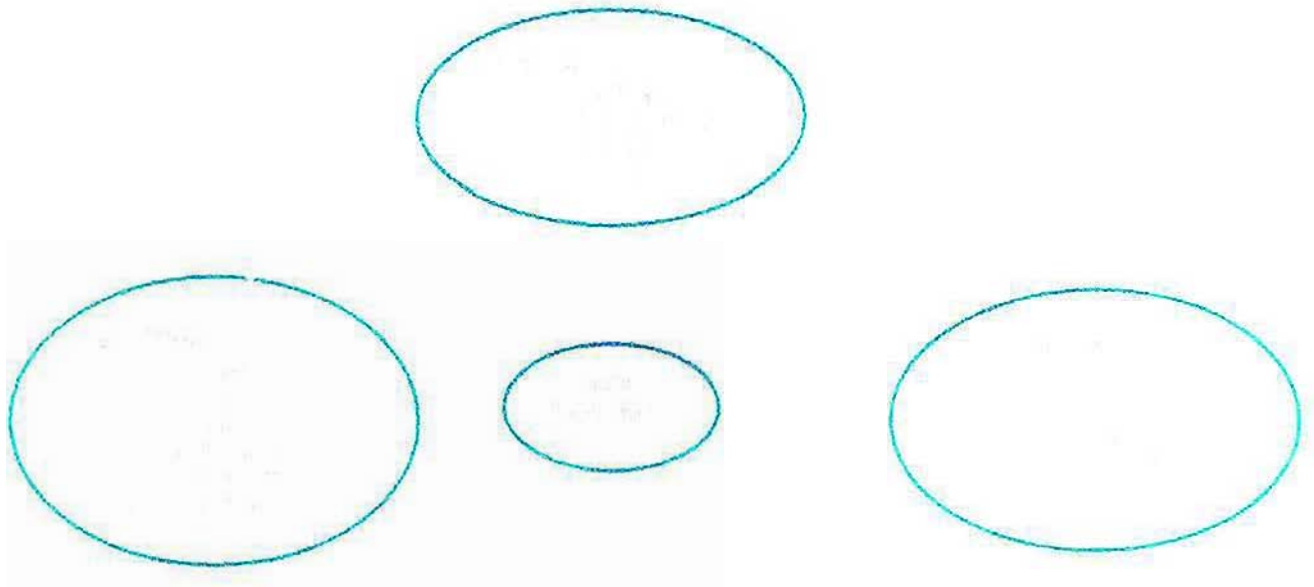
### Annexure 1: Customer needs versus current offerings of Standard Bank

Source: Research findings of the Standard Bank research group "Twisters" of Mpumalanga, Limpopo and North West.

NEED IDENTIFIED	CURRENT OFFERING
Strong Family Values	Independent products to independent users
Need for human touch	Off the shelf banking
Accessible Point of Contact	Limited access in mining communities. Reactive personal touch in branches
Hungry for Education / Information	Limited radio broadcasts "Radio Weye Weye".
Need for flexible (credit) borrowing	Off the shelf credit offerings "one size fits all"
Desire to Save	Variety of savings vehicles
Need to transfer funds to family	Limited access in local rural communities

**Annexure 2: Money flow in the Unbanked sector**

Source: Research findings of the Standard Bank research group 'Shakas' of Kwa-Zulu Natal



## **Annexure 3: Insights of field trips in the Unbanked sector**

Source: Research findings of the Standard Bank research group called the 'Russians' from Gauteng Metro.

### INSIGHTS OF FIELD TRIPS

#### Tembulihle Informal Settlement

- Informal settlement is a stone's throw away from the formal settlement
- Clean well kept homes
- Not many people were visible or available
- Very few spaza shops
- Residents work as vendors, domestic workers, sales people or hawkers at the Lenasia shopping centres.
- Large expenditure of income on food, education, transport and rent, very little spent on clothing or luxury items.
- Bank accounts held with FNB, ABSA and Postbank
- SBSA perceived as elitist, bank accounts cannot be opened without a monthly income and fittings on credit bureau.
- Differing views on funeral plan, Interest from those who don't have a bank account, those who do bank are sceptical of product.
- Active informal sector
- Lack of knowledge

#### Soweto

- Evidence of formal and informal living
- Informal settlements relatively empty, other than young children and older people
- Strong appearance of FNB and MTN
- FNB perceived as bank for the people.
- Security is a concern - banks should consult with local council to identify secure locations.

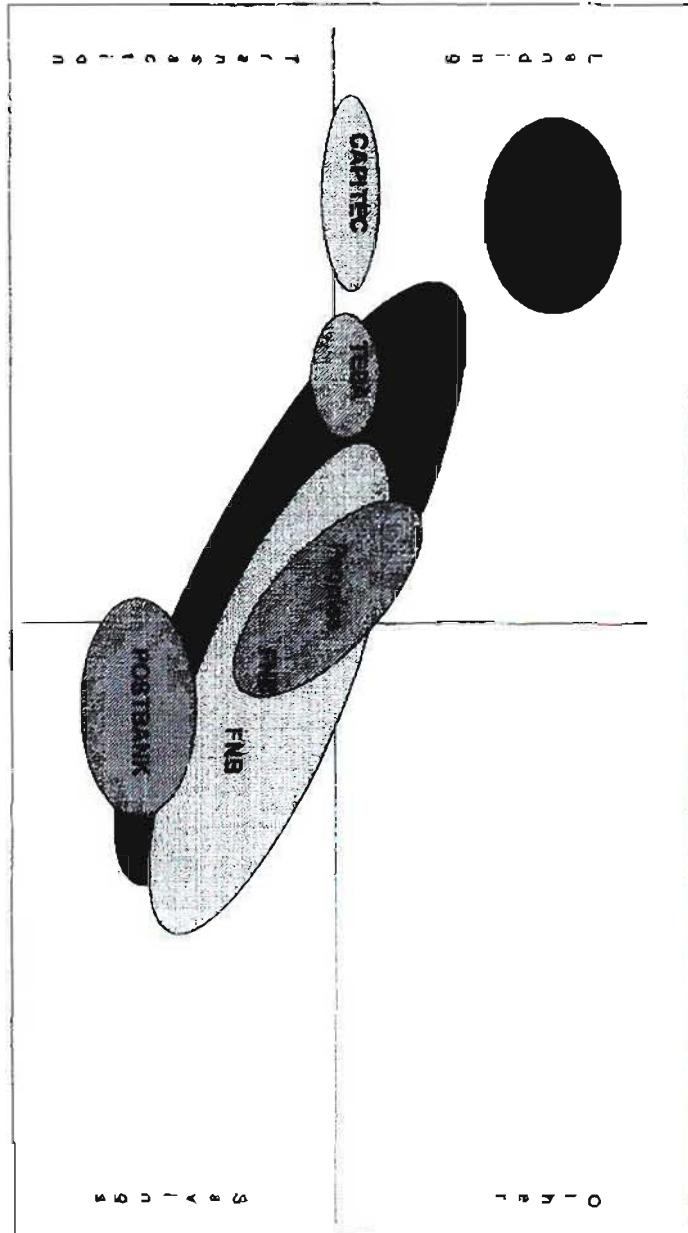
#### Diepsloot

- Councilor has an integrated development plan on infrastructure which is an opportunity for financing development and marketing exposure.
- Substantial money flows amongst stokvels and church groups and burial groups.
- Closest SBSA representation is Fourways and Randburg branch.
- Few shops, 3 private schools, clinics and many churches.
- Residents interact at community centre, main form of communication is word of mouth and visible advertising
- Majority of residents owned property in homelands, and money was regularly remitted to the rural areas, by sharing of bank accounts, or sending money home with family or friends.
- Discussion with municipal leader indicated that ABSA has plans to establish a container with two tellers, an ATM and consultants.
- Investment from the private sector is appreciated as this creates job opportunities for the residents, and provides a social status to the community.
- SBSA does not have a presence compared to MTN, Vodacom, Cell C, and FNB. SBSA seen as elitist.
- Strong presence of churches, stokvels and burial societies with substantial cash flows
- Assumptions cannot be made on the income levels and status of people residing in informal settlements.
- Micro-Lenders/Loan Sharks are more approachable, despite the higher cost.
- Strong need for personal service.



# Annexure 4: Opportunities and Gaps in the Low Income market

Source: Research findings of the Standard Bank Convenience team.



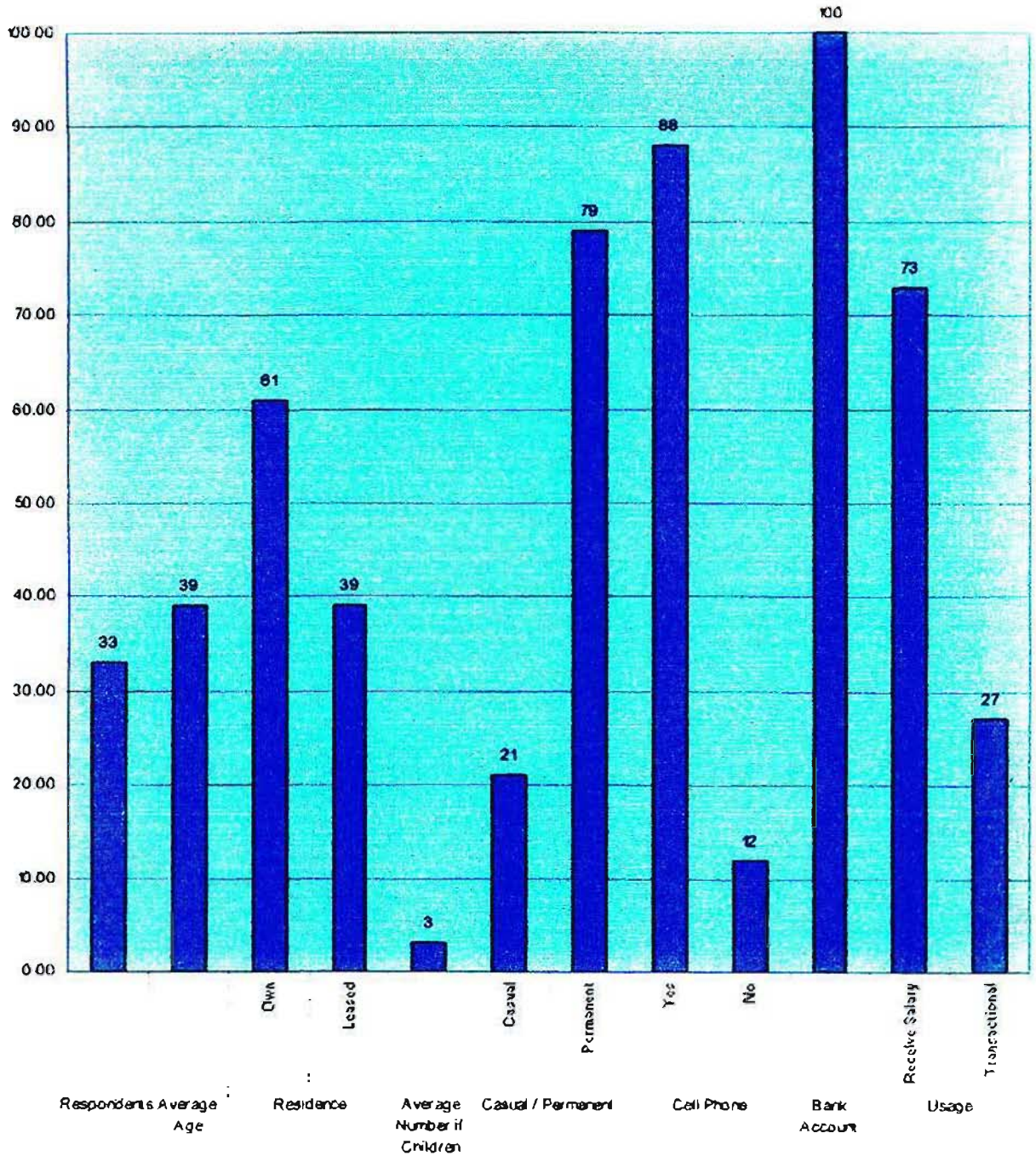
Gaps and opportunities for Standard Bank



**Annexure 5: Graph of the mining survey questionnaire in Mpumalanga, Limpopo and North West**

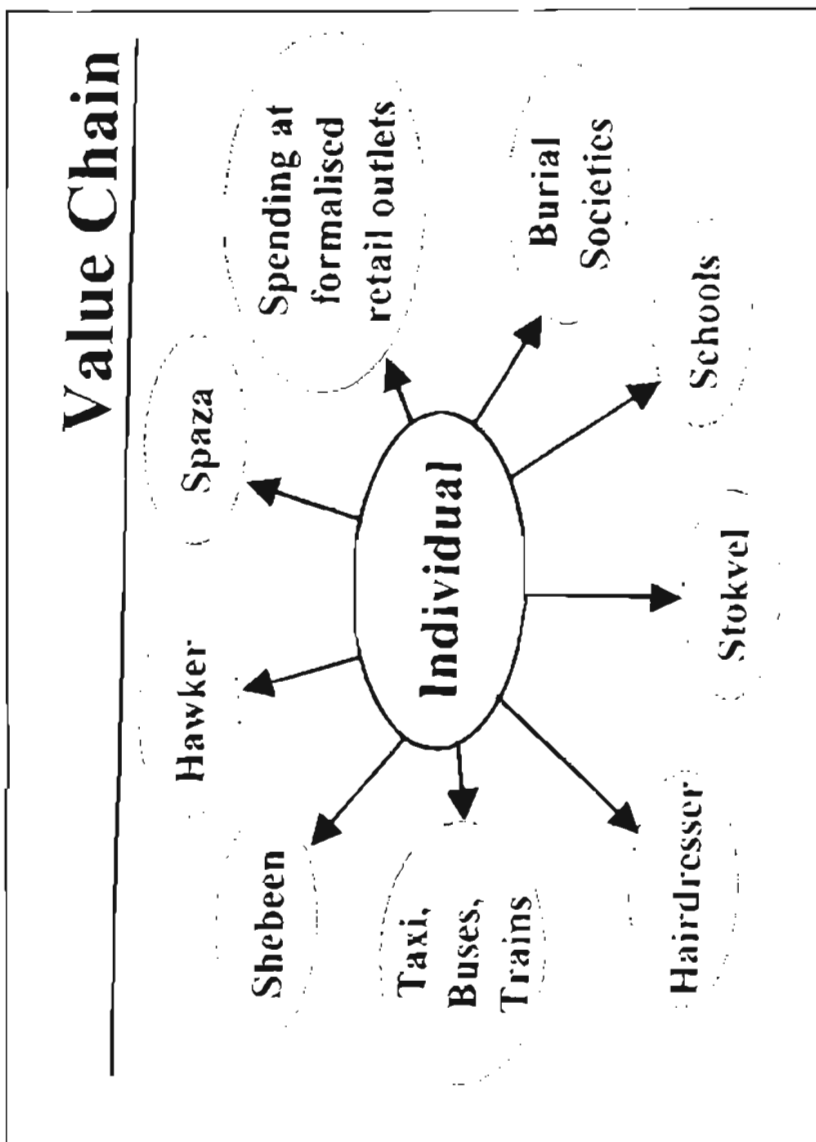
Source: Research findings of the Standard Bank Twister research team.

**Mining Survey**



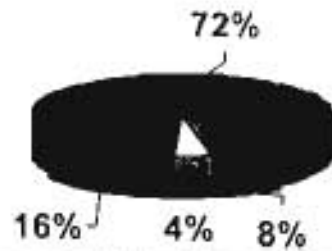
**Annexure 6: Value chain of the Low income Sector**

Source: Research findings of the Standard Bank Convenience team.



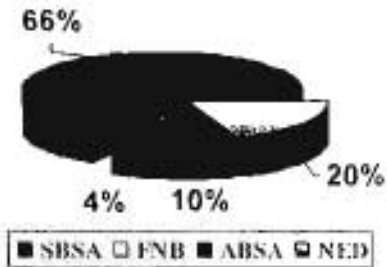
# Market Research

## Reasons for not Banking



- Safety
- Access
- Affordability
- Don't's know How

## Where do you Bank



## Reasons for Choice of Bank

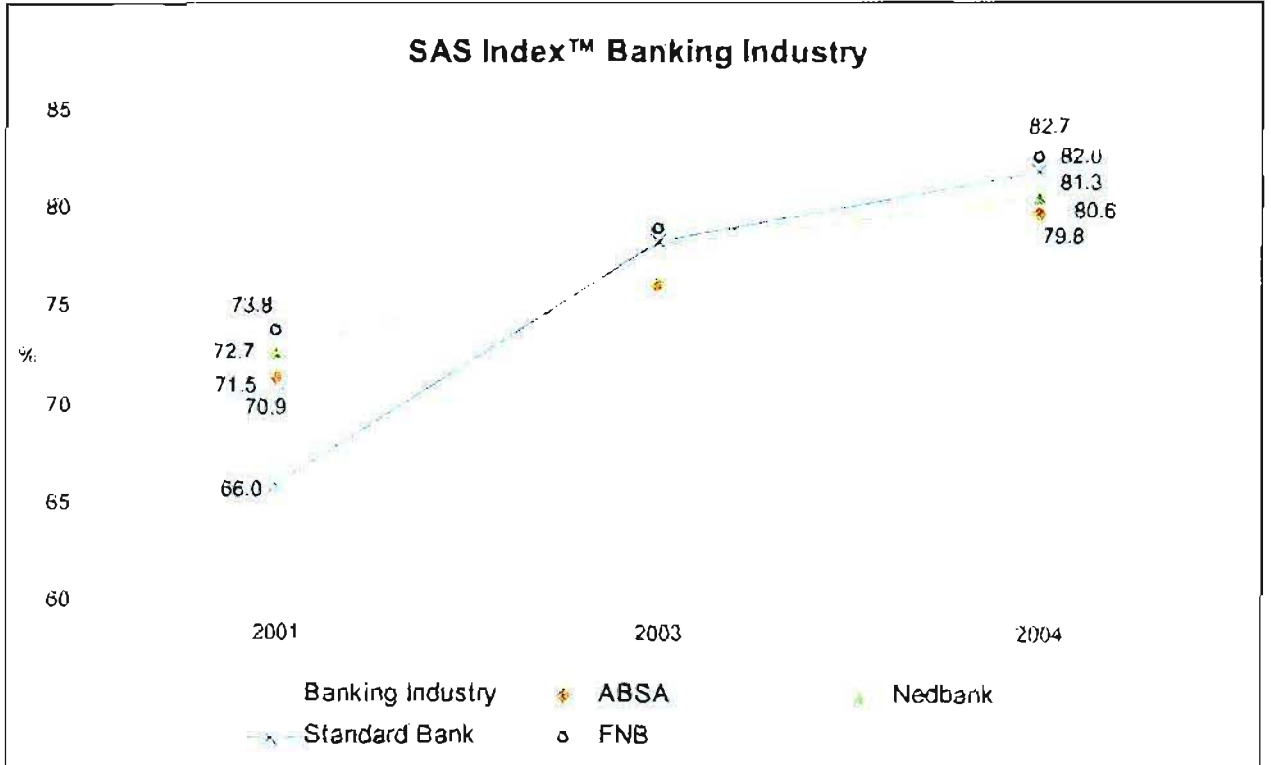


- Service
- Access
- Affordability
- Employers Choice

**Annexure 7: Market research of the Low income Sector**  
 Source: Research findings of the Standard Bank Convenience team.

### Annexure 8: SAS Index of the Banking Industry

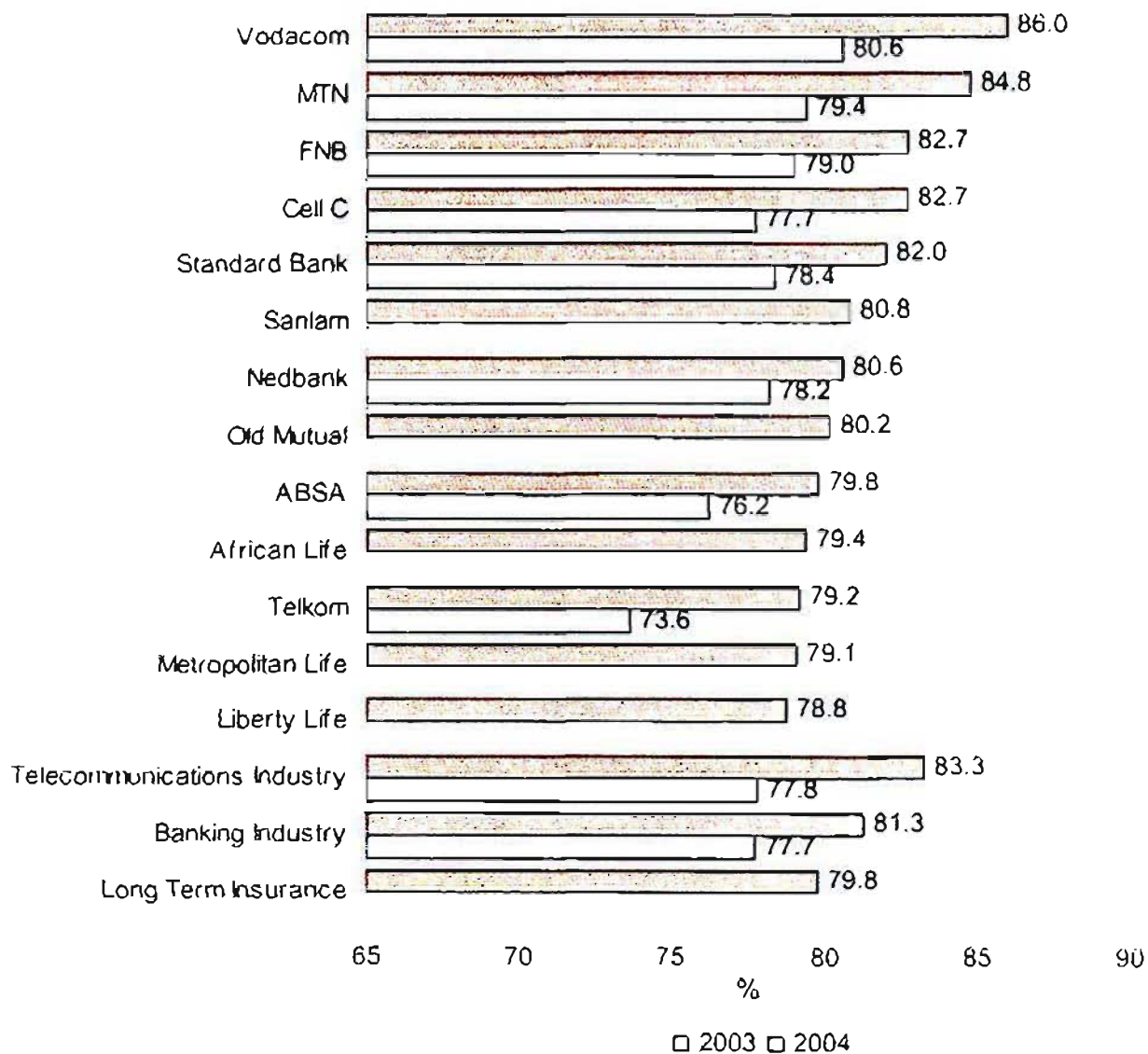
Source: Research findings of the SAS Index Media Brief 2004.



## Annexure 9: SAS Index – Ranking of Industries

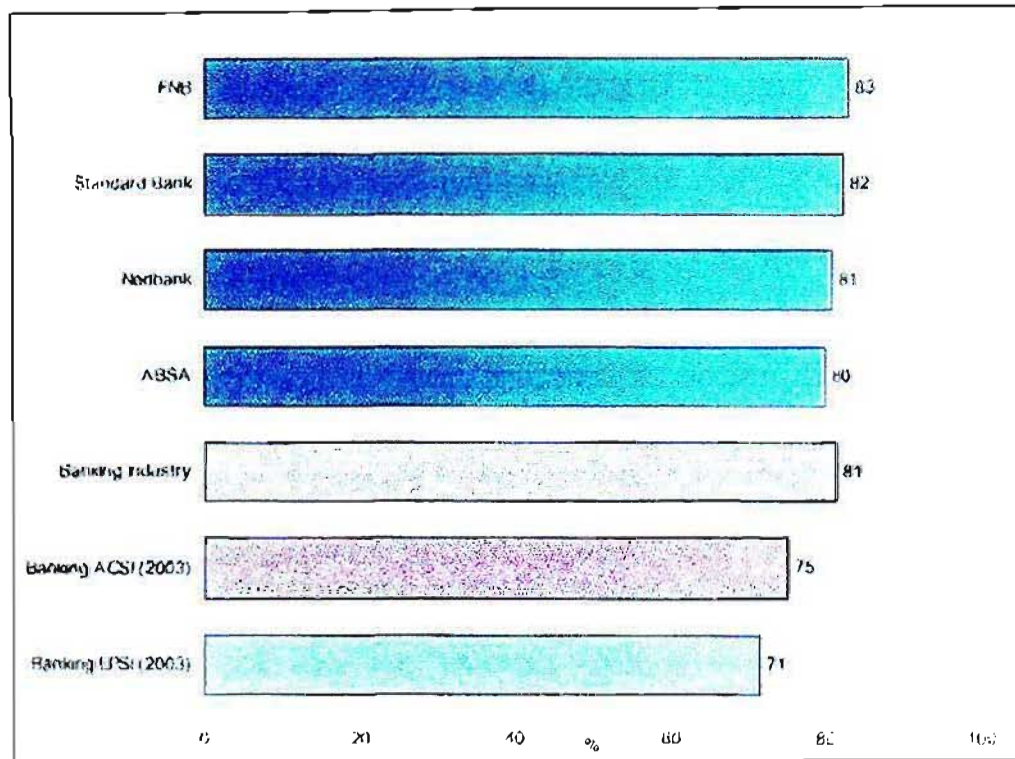
Source: Research findings of the SAS Index Media Brief 2004.

### SAS Index - Ranking of Industries



### Annexure 10: SAS Index: Banking 2004

Source: Research findings of the SAS Index Media Brief 2004.



## **Annexure 11: Falkena Report Recommendations**

Source: Bridge, S (2005). *Business Day newspaper*, Johannesburg, p2, February 5.

# Falkena report recommendations

1. Improved disclosure.
2. Banks to offer unbundled service and pricing options.
3. Penalty fees, charges for essential services or charges for services not open to competition on a cost-plus basis and open to regulation.
4. Monitor banks' compliance of pricing disclosure requirements.
5. Sharing of client information to lower information barriers to entry.
6. Pass enabling legislation for second- and third-tier banks.
7. Greater access to financial services – no collusion or subsidisation.
8. Investigate feasibility of transforming Postbank into a state-owned bank.
9. Promote the entry of and competition by foreign banks by addressing capitalisation requirements.
10. Extend inter-operability and access requirements to the payments system.  
Access by second-tier banks to the payment system on competitive terms should be facilitated.
11. Investigate the feasibility of implementing an e-money directive enabling electronic transmission facilities by suitably regulated non-banks.
12. The concept of a complex monopoly should become part of the remit of the competition commission.
13. Competition commission should investigate the possibility of a complex monopoly in payment system.
14. Prohibit any preferential processing mechanism for payments.
15. Banks deposit-insurance scheme.
16. Banks to consider the competitive impact of their regulation.



## Annexure 12: Proposed starter pack solution

Source: Research findings of the Standard Bank research group called the 'Kaofela' from Gauteng Urban.

**Services Proposal**

**Full Entrepreneurial Model**

- Kiosks
- Door to Door
- Retailers
- Taxi's

**Optional Funeral Plan**

**4. Funeral Plan**

**Account Opening**

Activation  
SMS / call / branch  
With ID # and Card #  
Reply with account #

**Product Limitations**

- 1 account per ID
- Max Total monthly withdrawals – R10000
- Max Total Monthly deposits – R10000
- (Max deposit within a 24 hour period – R10000)
- Max balance – R200000
- No fund transfers outside of SA

**Fees**

- Basic banking is free
- First ATM / call transactions are free (MAX allowable transactions)
- Attractive interest rates (dr and cr)

**Savings**

**Standard Bank**

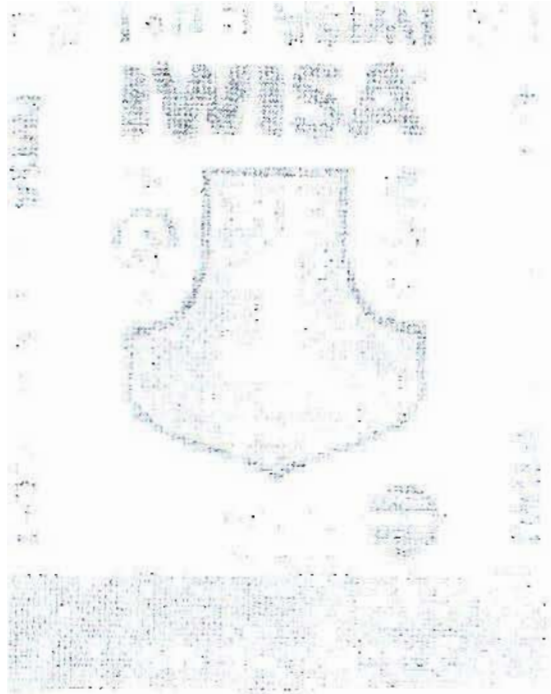
**Annexure 13: Proposed branding solution**

Source: Research findings of the Standard Bank research group called the 'Infinity X' from Gauteng.



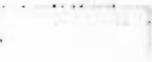


**Annexure 14: Proposed co-branding solution**

Source: Research findings of the Standard Bank research group called the 'Infinity X' from Gauteng.





**Standard Bank**

 +  + 

**Affordable Banking**

Made . . . .  
Simpler  
Better  
Faster

**TOLL FREE 0860 000 000**

## Annexure 15 – Questionnaire

Project Mzansi	
Unique Id no:	
Name of respondent:	
Area of fieldwork	

Hello, my name is \_\_\_\_ and I would like to know if you have 5 minutes to spare to answer a few questions. I am conducting a survey about banking and would like to assure you that this is strictly confidential. None of your details will be given to any of the banks or any other organization.

SQ1. Would you still be interested in continuing?

Yes	
No	

If 'yes' then continue.

SQ2. LSM classification

Do you have a washing machine?	
Do you live in a metropolitan area?	
Do you own a car?	

If 'yes' to any of the above questions then thank respondent and end the survey

If 'no' to all of the above questions then classify respondent into LSM 1-5 and continue with the rest of the survey.

SQ3. Do you currently have a bank account?

Yes	
No	

If 'no' answered above then ask

SQ4. Why don't you have a bank account?

It is too expensive	
I cannot afford it	
Do not know how to open an account	
No availability of ATM's nearby	

If 'yes' mentioned in SQ3 then ask

SQ5. Do you have an Mzansi account?

Yes	
No	

If 'No' mentioned above then ask  
 SQ5. Are you aware of the Mzansi account?

Yes	
No	

Regardless of the response above, read the following to the respondent.

An Mzansi account is a bank account offered by the 4 major banks as well as Post Bank. You do not have to earn a set income to open this account. The fee to open this account is R20 at all the 4 major banks and R10 at Post Bank.

Question 1

How affordable do you think the Mzansi account is?

Very affordable	
Affordable	
Unsure	
Slightly not affordable	
Not at all affordable	

If answered 'Slightly not affordable / not all affordable' above then ask

Question 2

How much do you think is an acceptable price for you to pay?

---

Imagine that you currently have an Mzansi account, if you don't already have one, I am now going to ask you some questions on what you think that you would do on that account.

Question 3

How often would you/do you use your Mzansi account?

3-4 times a month	
Twice a month	
Once a month	
Once in 3 months	
Once in 6 months	
Less often	
Don't think I would ever use it	

Question 4a

What method of withdrawing money do you think you would use generally?

Withdrawing from an ATM	
Withdrawing from a branch	

Question 4b

And which one would you use most often?

Withdrawing from an ATM	
Withdrawing from a branch	

Question 5

In your opinion, do you think that you would benefit from this new offer?

Yes	
No	

**Ask if 'no' mentioned in SQ3 or SQ5**

Question 6

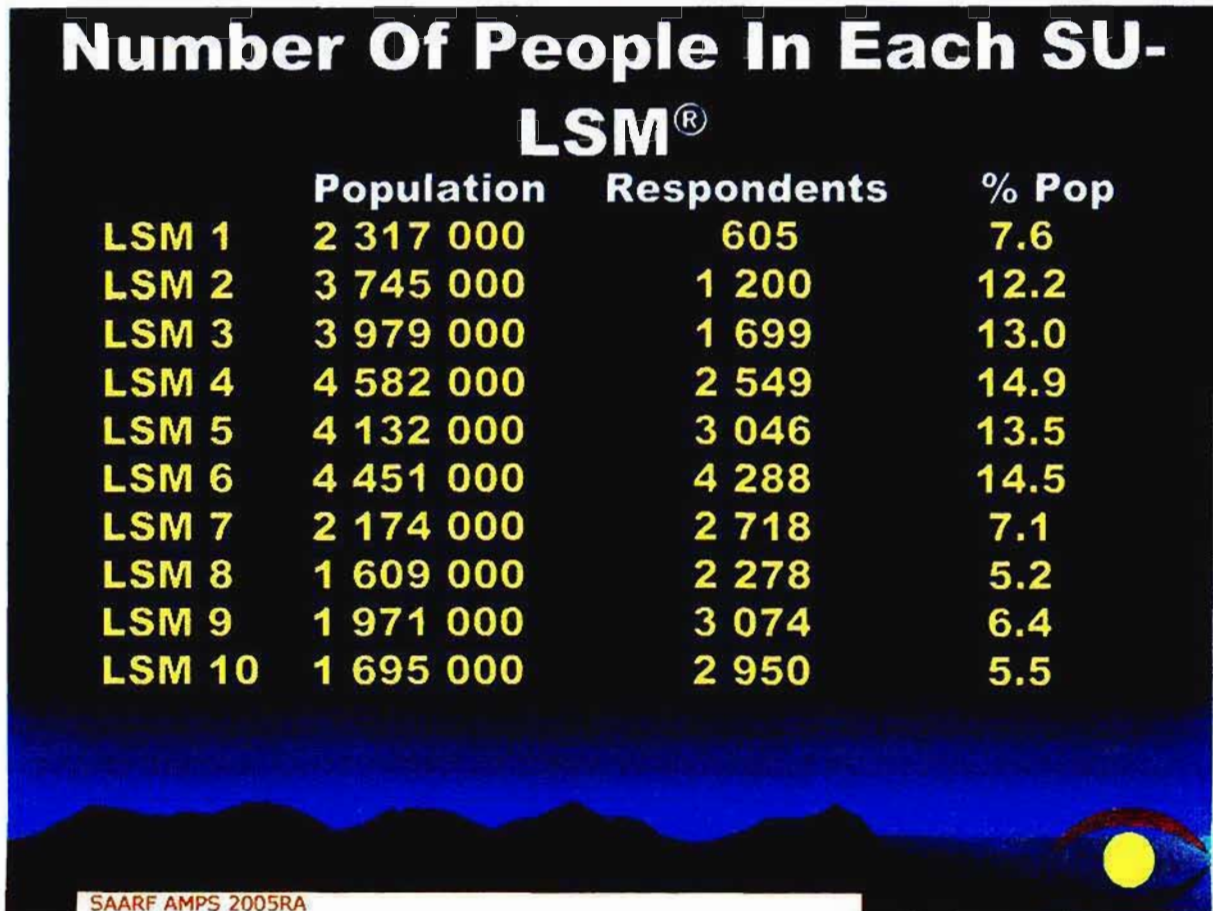
Would you consider opening an Mzansi account?

Yes	
No	

**THANK RESPONDENT! THIS IS THE END OF THE INTERVIEW.**

**Annexure 16 – LSM Chart**

Source : [www.saarf.co.za](http://www.saarf.co.za)



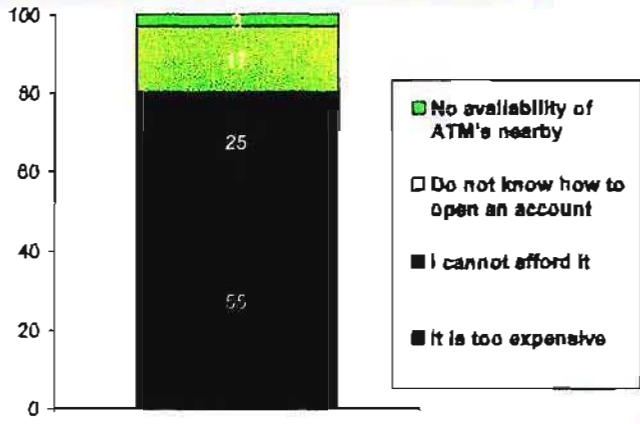
## Number Of People In Each SU-LSM<sup>®</sup>

	<b>Population</b>	<b>Respondents</b>	<b>% Pop</b>
<b>LSM 1</b>	<b>2 317 000</b>	<b>605</b>	<b>7.6</b>
<b>LSM 2</b>	<b>3 745 000</b>	<b>1 200</b>	<b>12.2</b>
<b>LSM 3</b>	<b>3 979 000</b>	<b>1 699</b>	<b>13.0</b>
<b>LSM 4</b>	<b>4 582 000</b>	<b>2 549</b>	<b>14.9</b>
<b>LSM 5</b>	<b>4 132 000</b>	<b>3 046</b>	<b>13.5</b>
<b>LSM 6</b>	<b>4 451 000</b>	<b>4 288</b>	<b>14.5</b>
<b>LSM 7</b>	<b>2 174 000</b>	<b>2 718</b>	<b>7.1</b>
<b>LSM 8</b>	<b>1 609 000</b>	<b>2 278</b>	<b>5.2</b>
<b>LSM 9</b>	<b>1 971 000</b>	<b>3 074</b>	<b>6.4</b>
<b>LSM 10</b>	<b>1 695 000</b>	<b>2 950</b>	<b>5.5</b>

SAARF AMPS 2005RA

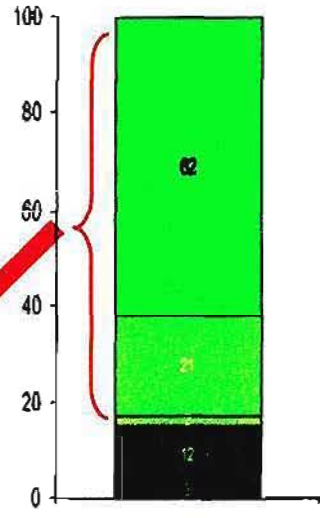
**Annexure 17 – Findings from the research undertaken by the author**

**SQ4. Reasons for not having a bank account**



**40% (n=116) would pay on average R5.00 and 60% (n=175) would want the account with no charges**

**Q1. Affordability of the Mzansi account**



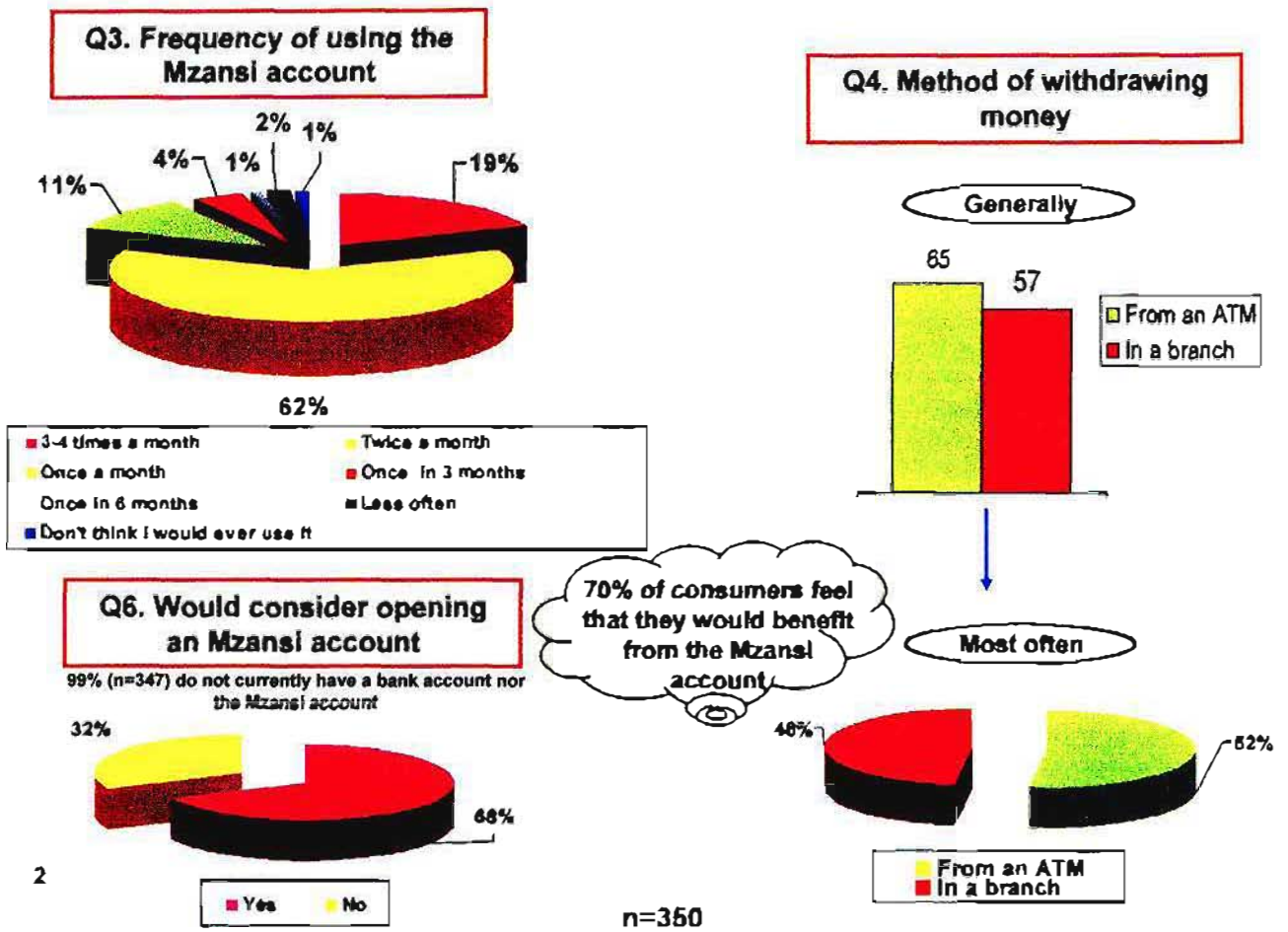
■ Very affordable      ■ Affordable  
 ■ Unsure                      ■ Slightly not affordable  
 ■ Not at all affordable

1

n=350



Annexure 18 – Findings from the research undertaken by the author





UNIVERSITY OF  
KWAZULU-NATAL

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WESTVILLE CAMPUS  
TELEPHONE NO.: 031 - 2603587  
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20 MARCH 2007

MR. K PILLAY (202524347)  
GRADUATE SCHOOL OF BUSINESS

Dear Mr. Pillay

**ETHICAL CLEARANCE APPROVAL NUMBER: HSS/0091/07M**

I wish to confirm that ethical clearance has been granted for the following project:

**"An evaluation of the strategy of banking the unbanked for a leading South African Bank"**

Yours faithfully

A handwritten signature in black ink, appearing to read 'P. Ximba'.

MS. PHUMELELE XIMBA  
RESEARCH OFFICE

cc. Faculty Office (Christel Haddon)  
cc. Supervisor (Bruce Rhodes)