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NON-BANKING FINANCIAL INTERMEDIARIES IN THE STRATEGY OF A BANK IN THE RETAIL MARKET

The presence of non-banking intermediaries in the retail market of financial services creates a new situation for banks. In the article, the types of parabanks existing in Poland, the basic determinants of their competitive force, their scope of activity and role in national economy are presented. Due to the activity of parabanks rendering numerous services to retail clients, banks are facing increasing competition. This should not be however perceived solely as a threat. Banks may exploit the chances which appear as a result of closer co-operation with "bank agents"; like better access to the client, better services, easier utilization of banking products, limited credit risk, etc. The role of "bank agents" is illustrated in the case study of PKO BP bank. An original concept of "banking franchising" is presented, and basic conditions and rules for its effective application are discussed in detail.

1. INTRODUCTION

The aim of this paper is to present the "banking franchising" as an efficient method to create a competitive advantage of a Polish bank in the retail market. This method makes use of trends observed in the evolution of parabanks, and in particular non-banking financial intermediaries in the Polish market of financial services.

The incorporation of an idea of franchising into banking practice is a novel approach to the known problem: how to assure, at the same time, both the economic safety and competitiveness of the bank in the retail market of financial services. The proposed method is the result of:

1. Author's observations concerning the re-orientation of some Polish banks strategy in the retail market due to:

- generally increased market orientation of these banks in search of new income sources;

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- threat of strongly increasing competition of Western European banks which is the result of progressive liberalization, referring to the starting conditions for foreign bank branches and agencies, and guarantees of national treatment;

- clearly progressing development of parabanks, competing to attract retail clients, i.e. households or small and medium enterprises.

2. Author's active participation in some activities aimed at strategy creation at a Polish bank to improve and strengthen its competitive position in the retail market.

It has been assumed that parabanks are, on the one hand, a threat for a bank operating in the same market, on the other hand, however, this threat can turn into a chance, under the condition that possible co-operation with some of them would be considered and analysed. The advantages resulting from this chance can be properly exploited only when the tendencies of integrated public supervision over the financial market, observed both in Europe and in Poland, would be taken into account when establishing the co-operation.

To attain the assumed goal it is advisable to make a survey of parabanks existing in Poland, to analyse their basic determinants of competitiveness, to learn the possibilities and main limitations in utilizing the so-called financial intermediaries being active in the retail market, and finally, to present both the general idea of franchising applied to the co-operation of a bank with a financial intermediary, and the case study for PKO BP.

2. TYPES OF PARABANKS IN POLAND AND THEIR BASIC DETERMINANTS OF COMPETITIVENESS

The notions of a parabank are imprecise, though parabanks are the subject of regulations in many countries. In practice, only some part of parabanks, i.e. the institutions giving services similar to those of banks, are subject to banking supervision and licensing procedure, like true banks. This concerns the institutions which fulfil several conditions, i.e. those which render banking services as a part of their permanent activity, have a defined legal status and appropriately qualified management, and some minimum capital endowment. Other institutions, being in fact also parabanks, are not submitted to the above requirements. To the first group of parabanks belong: savings and benefit associations, municipal credit institutions, building societies, investment companies, financial companies, specialized financial institutions (e.g. hire-purchase companies, banking-insurance companies). Banks are able to create some of these parabanks and to use them as a tool in their expansion in the retail market. However, due to the relatively high requirements concerning their minimum capital endowment, some barriers appear in the extension of their territorial network and increasing availability of their services. Much more mobile in

this context are the parabanks of the second group, to which belong co-operative savings and credit associations, savings and loan associations, housing co-operatives, leasing, factoring and consulting companies, exchange offices, and non-banking financial intermediaries, i.e. credit brokers, or trade and service companies serving the banks (Szpringer 1998, p. 24). This group of parabanks would compete with a true bank in the retail market, if the bank did not co-operate with them (due to the lack of legal possibilities or just by not taking into account the existing possibility).

If a bank operating in the retail market is lacking a proper attitude towards this new competitive force presented by parabanks, it faces a threat to its current position, since parabanks enjoy a good competitive position due to the created legal possibilities. Compared to banks they have a number of financial and economic privileges, depending however on the kind of parabank. These privileges include:

- lack of obligation to charge and pay in the obligatory reserve (which for banks is an element of obligatory costs of their activity);
- general lack of obligation to pay in the fees for the Banking Guarantee Fund and to participate in the deposit guarantee costs (which for banks are obligatory costs of their activity);
- in the case of existing obligation to pay in the fees for the Banking Guarantee Fund, their rate is preferential for parabanks;
- system of state guarantees accorded to some parabanks, leading to increased confidence among the public;
- lack of obligation to disclose details of undertaken credit activity to tax offices, which also leads to increased confidence among the public.

Most of these privileges are valid also for non-banking financial intermediaries, who lack however state guarantees. A dynamic development of these intermediaries, not submitted to the banking supervision, can be observed. For banks, they can either form a strong competition or give a chance to strengthen their competitive position, by making use both of these intermediaries, and their financial and economic privileges.

3. NON-BANKING FINANCIAL INTERMEDIARIES – THEIR SCOPE OF ACTIVITY AND ROLE IN THE ECONOMY

Non-banking financial intermediaries are commonly known in the bankers' slang as "bank agents". The main role of an "agent" (parabank) is the mediation between different banks or a bank and its retail credit beneficiaries. Some agents perform also banking desk operations. The role of a bank may be limited

solely to disbursing money for credits and loans. Other activities, like gaining clients, obtaining legal securities for credit or loan repayment, monitoring, and vindication of liabilities, may belong to the bank broker. The scope of services offered by an intermediary to the bank depends on the type of intermediary. Three types can be distinguished:

1. Large intermediary companies organizing their own systems of hire-purchase sale;
2. Small intermediaries servicing the hire-purchase sale organized by banks;
3. Small intermediaries performing desk operations and the sale of selected banking products (credit, deposit, insurance), up to some defined size.

To the first group of bank agents belong: Lucas SA from Wrocław, CLA SA from Wrocław, PHU "Żagiel" from Lublin, BEST PH SA from Sopot. These companies form their product quite individually and are to a great extent autonomous when choosing procedures, defining the criteria of credit capacity and the way of management. Their activity is however always based on the capital of banks. Some of these companies, like CLA SA, take over from the co-operating banks (BIG BANK and BPH) some additional tasks, like records of repayments, full accountancy and settlement of credit contracts, recalculation of the credit value in the cases when a client applies for an early retirement of received credit, calculation of possible overpayments, full reporting for statistical purposes. They also take over responsibility for unrepaid credits and follow the vindication procedure individually. In return for these responsibilities taken over from the bank, the company receives an increased commission.

The second group of intermediaries is formed by companies appointed by a bank. They gain new clients, provide these clients with all the necessary information before making a credit agreement, gather the documents and formulate, together with clients, credit agreements. These intermediary companies do not take responsibility for unrepaid credits. Usually, private partnerships belong to this group, like Lumar from Łódź, OPCJA from Gdańsk, DGF from Wrocław. They receive commission for the offered services, being a defined percentage of the value of allowed credit, lower however than for companies from the first group.

Finally, in the third group of intermediaries we find companies working mainly for a bank, but in their own name. They are interested in selling various products of the bank, including credit products, in the framework of competence granted by the bank. In conducting their activity they can also depend on the capital of the bank. In principle they do not have any autonomy in introducing their own credit procedures. For their services they are usually offered commission. At present, an example of such intermediaries in Poland

are the agencies of PKO BP bank. These agencies are engaged mainly in desk operations, but in view of the rapidly increasing competition in the market they are strongly interested in assuming other responsibilities, typical for the intermediaries from the first and second group, and also including insurance services.

It can therefore be expected that parabanks will be able and will start to undertake other functions. The catalogue of new functions remains open and will increase along with the expansion of these institutions in the financial market.

The importance of “bank agents” is the basis for changes which occur in banks operating in the retail market. These changes occur simultaneously on three planes: access to the client, availability of the product, and the changing range of product offer. Access to the client should be understood as a measure of quantity of retail clients served by a given bank. Many factors influence this element, e.g. advertising, quality of customer service, location of the bank premises, creation of confidence and image. This in turn is connected with the availability of banking products, the possibility for a client to take advantage of the offered services. The availability is defined by e.g. the credit capacity of the client, his appropriate age, presented and acceptable security, proper income level. Availability is reflected in the range of products offered by a bank.

The three above mentioned planes are the basis for the creation of intermediary companies, which perform a number of functions:

- towards the client: easier utilization of banking products by reduced formalities and better access to clients thanks to the more dense network of service points, more favourable conditions of acquiring the product, (e.g. credit) by lower cost of legal securities for the client (e.g. a lack of civil pledge for the repayment of a credit);
- towards the bank: easier creation of bank money, limited credit risk, as the intermediary takes out the obligation to cover losses due to bad credits.

To sum up, as a result of such co-operation it is possible for a bank to lower the costs of operation in the retail market, to limit the banking risk, in particular the credit risk, and at the same time to reach the marketing goal – better access to the client. However, both these groups of effects, the marketing and the economic ones, may be threatened by some commercial practices used by some parabanks co-operating with banks, which are not only unacceptable by society, but often also illegal. This is in particular true for those intermediaries who took over vindication operations with the guarantee of credit repayment. The bankruptcy of clients of such parabanks, being a result of their financial losses, may spoil the image of the co-operating bank. In the long term, the deteriorated image of a bank is a threat to its economic stability. Therefore, if the co-

operation of a bank with parabanks is intended to turn into success instead of failure, it is necessary to choose the proper stable non-banking partner and to define forms and rules of mutual co-operation. Most generally, the proper choice is the choice which does not lead to an impaired image of a bank, both in the short and the long term. It seems that most appropriate in this sense would be intermediaries belonging to the third group. The common activity of a bank with such partners could be based on the idea of franchising, which protects at the same time the marketing and economic interests of the bank and the intermediary.

4. THE CONCEPT OF “BANKING FRANCHISING” AS A POSSIBLE ELEMENT OF BANK ACTIVITY IN THE RETAIL MARKET

The general idea of franchising consists in granting to some company by another company the sole right of selling economic goods or rendering services on the defined territory. This includes the totality of economic property, intellectual property and trade mark rights, the use of the company's name, marks on premises (logo), designs, know-how in the broad sense, all this applied to selling and services. This is a form of a licence agreement. The beneficiary of this agreement is obliged to buy permanently and continuously defined quantities of a given product and to sell them according to the strict requirements of the supplier, including the price fixed by the supplier. The basic advantage for the franchiser who signs agreements with other companies is the extension of his own marketing system and the broader dissemination of his own brand name and trade mark, without extra capital costs. He also obtains an additional source of revenue, namely the fees paid by the franchisee for the received licence.

The franchise agreement is profitable for the franchisee, as it permits:

- to take advantage of the organizational and commercial experience of the franchiser, and of reputation connected with the name of the company and its trade mark;
- to get some help from the franchiser concerning the organization and current affairs of the company (financial management, training, advertising etc.);
- to limit the risk connected with the undertaken business activity, to increase their own credit rating and the possibilities to obtain the preferential credit;
- to enlarge the market for products and technologies, to learn the marketing strategy of the franchiser;
- to keep the position in the market, as franchisers do not let weaker companies to fail, they rather take over their operations, even if it could lead to losses – they take care of their marketing image (Penc 1997, p. 127).

If the franchiser is a bank and the franchisees are “banking agents” being the franchising agencies, we will conventionally call this organization the banking franchising system. With regard to the mutual advantages for the parties of banking franchising such an idea can be realised in practice, the more so that the forms and methods of Polish banks functioning are still in development, and so widespread and stable patterns of their activity are not yet elaborated.

The ways of creating “banking franchising” may be different. We can list the following:

- Formation from the very beginning, finding the companies not co-operating with the bank until now and being ready to enter “banking franchising” structures;
- Transformation, as a part of the rationalization of the bank’s territorial network management, of organizational units of a bank (branches, agencies, sub-offices) into “banking agents” acting in the scheme of “banking franchising”;
- Modification of the former co-operation of the bank with its “banking agents”, concerning the scope of services offered by agents and the rules of mutual relations between the bank and its agents, and between the agents themselves.

Due to the limited size of this paper the concept of “banking franchising” will be presented in a synthetic manner only. This concept has been prepared for one of Polish banks and is based on a modification of its previous co-operation scheme with agents in the retail market.

The important elements of each concept of “banking franchising” should include the position of a bank with respect to the basic problems. What should be the role of “banking agents” under the conditions of increasing inter-bank competition? What is the importance of “agents” for the bank? What should be their function? What consequences may result for the bank if they abandon the idea of “banking franchising” in the retail market?

In the case study made for the PKO BP bank a number of answers has been obtained.

The role of PKO BP agents has been defined as follows:

1. Agencies clearly fulfil the requirement of proximity to the client. If, for some economic reasons, PKO BP cannot physically create its own branch, the agency, necessarily advertised as a part of the bank organization, can help. Thereby, PKO BP would be closer to the client.

2. Agencies may – if PKO BP takes care of the transparency of mutual co-operation and keeps the agents motivated – fulfil the demand of true and immediate help in solving the bank’s clients financial problems.

The importance of agencies for PKO BP has been defined as follows: the existence of agencies must be motivated, first of all, by marketing not commercial considerations,. The agencies should confirm in practice the client orientation,

should be as close to the client as possible, even in the suburbs, so the client can have an easy access to the bank and its professional services. The way to attract and keep clients durably attached to PKO BP is to make them strongly convinced that the bank is primarily anxious to fulfil the expectations and financial needs of the clients. The bank is remunerated for the satisfaction given to the client, not for making any kind of operations, which may be perceived by the client as having little importance and leading only to extra profits for PKO BP, without giving certain satisfaction. If solely commercial approach persists, a negative phenomenon can develop: PKO BP would not be eager to pay adequately for these activities of an agent, which facilitate or help the client to take the decision concerning the purchase of some product, but do not necessarily oblige him to buy it. This means that the agent should be paid by PKO BP mainly for his efforts in attracting clients and strengthening their links with the bank. These efforts should not be necessarily accompanied by selling the product offered by the agent. A financially motivated agent will be permanently interested in the enlargement of the group of his clients, who potentially would bring him some profits in the future. Agencies – legally being the outside entities – make the means to attract and satisfy the clients of PKO BP. The client would not have the impression that the operations of the bank have a usurious character.

Therefore the price policy of PKO BP when co-operating with agents should be based on the following two assumptions:

1. The client using the services of an agency should not have an impression that the prices for the services are higher than at the agencies of other financial institutions. Such an impression might be due to the fact that he has to pay not only the bank, but also its intermediary.

2. The moment when the obligation to pay the due amount is presented to the client should be defined in such a way that the client has not to pay before the whole transaction is finalized; fees and commissions for the operations necessary to finalize the transaction have to be included into the total price. It is easier for the client to accept the payment when he is fully satisfied.

The agencies should create and strengthen such feeling among persons who:

1. Usually live far away from PKO BP own branches and for whom access to distant bank branches is onerous; who have no possibility (or do not want to use it) to make orders from their domicile;

2. In the given moment are in a place where there is no own branch of the bank, and have no possibility to use home banking, but who nevertheless want to realize their needs (e.g. to buy things);

3. Prefer contact with reliable persons who could help them immediately in solving problems, e.g. to explain the rules, usefulness, shortcomings and advantages of the banking products, to assist in filling-in the necessary forms, to

inform them about the changing services of the bank which might be of importance for the client – all this at a place convenient for the client (at the agency premises or at the client's home);

4. Are small entrepreneurs doing business in the vicinity of the agency, and are known to the agent. In practical terms, the agent can better evaluate the enterprise's ability to make profits and its attitude in the business activity.

The role and importance of PKO BP agents implies their following functions:

1. To gain new clients for PKO BP by promotion of banking products, interest in the client's financial problems and immediate help in solving them, to deliver forms, to explain, to inform;

2. To strengthen links with PKO BP by contacting the client upon his appointment and informing him about currently occurring changes in banking products, under mutually agreed conditions;

3. To sell individually some products which are characterized by low risk level for PKO BP, including credits, based on the knowledge of the client. The resulting benefits should be: the client buys the product immediately without travelling to a distant PKO branch, the agent gets some revenue, PKO BP is released from the transactions which are minimal and low-risk and can concentrate on other, bigger clients, other transactions with a higher risk level and rationalization of the functioning of their own branches.

If the hitherto observed attitude of PKO BP towards agencies would not change, some negative phenomena could appear and intensify.

- Agents can give up their activity having no prospects of improving their income position;

- Agents can undertake additional activities, also in other fields like trading of consumption or durable goods, and so on. The result for PKO BP would be: lower interest of agents in improvement and extension of agency operations, increased tendency to give up their job if more certain sources of revenue appear, increased probability of losing the most efficient agents who most often look for extra sources of income;

- Professional agents of PKO BP can be taken over by other financial institutions offering better conditions of co-operation.

The means to materialize the idea of banking franchising is the agency with the scope of banking services extended in comparison to the current one. Such an agency should perform desk service of retail clients, provide them with help and banking consulting, lead the canvassing of PKO BP products, sell retail credits up to the competence accorded to the agents, make internet service of clients and day-to-day service of small enterprises in the limits of accorded competence.

An appropriate licence from PKO BP is necessary to lead such an agency. The licence gives permission to render services in one of the two types of agencies:

- purely stationary one, i.e. acting at service points,
- giving of the so-called banking home care services, somewhat close to the work of an insurance agent, so not only in agencies, but also – by appointment of the client – at his domicile or premises.

A properly working franchising agency should be characterized by a number of basic attributes:

1. Comprehensive range of services and products. The range of an agency should be regularly adjusted to the needs communicated by clients, and this requires the efficient system of continuous monitoring of these needs (best of all with the participation of the bank).

2. Sufficient quality of services offered by an agency. To this aim, the bank should establish the licensing system and the procedures to withdraw the licence, for the full scope of services.

3. Conditions of service convenient for the client. The appropriate standard of work organization as well as technical and computational outfit are necessary.

4. Prompt service for clients. A comprehensive system should be established for financing the agents' investments, leading to quick and efficient services for clients. The financial sources could be: own resources of the agent, preferential credit from the bank, leasing of the equipment belonging to the bank, etc.

5. Reasonable financial conditions for the client and agent. The currently binding price tariff for agents should be modified.

6. Functioning procedures for a franchising agency. Their catalogue should be drawn up.

A full set of principles, compatible with the theory of franchising, should include those described below for the studied bank, though particular solutions for a given bank could be different.

The rules of financial assistance in investments aimed at the development of the agency network could include: criteria which an agent should fulfil to take advantage of bank's financial help, criteria defining the order of investments in particular agencies, rules of repayment of financial aid accorded by the bank.

Equally important are the principles of introducing new agents and training them in all aspects of activity, in view to obtain and maintain the licence – an authorization to run the franchising agency. Each agent should be trained in methods which are necessary in managing the agency according to the pattern. This training should include the utilization of equipment, sale and canvassing methods, utilization, selection and training of the staff, accounting and reporting methods, marketing.

An idea of the design of agency premises, allowing it to identify it with the bank, should be formed.

The rules of permanent guidance and help given by the bank (or other appointed institution) are of great importance. These rules should include regular visits of the bank staff (or institution) to the premises of the agencies with the following aims: to assist in corrections and prevent deviations from the pattern; to assure contacts between the bank, the given agent and all other agents permitting to exchange ideas and experiences; to create innovative banking products sold through agencies (including investigations of the ability to create the demand and compatibility with the present scope of activity of an agency); to facilitate training and improvement of skills of the agent and his staff; to investigate the agency market; to organize promotion and advertising at a local and national scale made by the bank on behalf of agents; to consult and offer services in management and accountancy; to conduct investigations concerning sales techniques and materials or canvassing of bank's products.

The rules which guarantee the proper activity of an agency may in turn include: creation by the agent of an obligatory guarantee fund (limiting the consequences of possible abuses of the agency cashier, bad credits, losses due to disasters like robbery or fire); insurance from the risk connected with managing the agency (which could substitute those presently required by the bank insurance of cash transport against theft or robbery, paid by the agent); payment of a single franchising fee for including the agency into the franchising agencies network and taking advantage of the corresponding prerogatives.

Indispensable are the rules of withdrawing the licence for franchising agency and cancelling the contract with an agent, both as a result of the agent's fault and due to circumstances independent of him.

5. CONCLUSION

Based on analyses carried out in PKO BP, and in view of the great elasticity observed among non-banking financial intermediaries in creating various forms of mutual interaction with banks, one can draw a conclusion that the utilization of the banking franchising concept can be a real and possible way of bank activity in the retail market. This concept should protect the marketing and economic interests of a bank, and simultaneously assure its stable or even improved competitive position, despite increased competition in the financial retail market.

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