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## Barriers to Basic Banking:
## Results from an Audit Study in South India

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# Barriers to Basic Banking: Results from an Audit Study in South India

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***Abstract***

We conducted an experiment in urban South India to examine the barriers faced by customers in purchasing a low-cost savings product. We found that banks have a high ability to influence financial access outcomes, even when product availability and eligibility rules are non-discretionary. Nearly all banks refused to market the regulator-mandated basic accounts, despite the customers being atypically persistent in asking for "basic accounts." Additionally, in more than half (55%) of the bank branches visited, customers were turned away when they attempted to negotiate for an alternative, affordable savings product—in half of the cases, the bank refused to accept the customer's valid identity or address proof, while in the other half of the cases, the bank refused to market an alternative low-cost product. For the accounts that were opened, the banks demanded excessive identity and address documents, withheld key information about the product's terms and fees, and imposed significant time, effort, and incidental costs on the customers. Given the benefits of low-cost accounts and their linkage to the Indian government's broader financial inclusion goals, our findings suggest a need for careful monitoring and targeted enforcement of India's financial inclusion policy implementation.

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## 1. Introduction

India has a low rate of formal savings. A 2011 national survey found that only 35% of adults hold an account at a formal financial institution and only 12% had saved at a formal institution in the 12 months preceding the survey (Demirguc-Kunt and Klapper, 2012). Despite these low levels of formal savings, households are India's biggest contributor to national savings, contributing nearly three-fourths of all savings in 2012–2013 (Kant, 2014). However, financial assets account for only one-third of total household savings; financial assets have fallen sharply over the past five years, as the share of savings in physical assets such as gold, property, and business assets has grown (Yamini and Deokar, 2012).

### 1.1 Welfare gains from savings

At an economy-wide level, a greater level of financial savings would allow companies and the public sector to access capital more cheaply through financial markets, and the vast majority of households could benefit from the inflation- and risk-adjusted returns that savings in the formal sector could provide. Low-income households and the currently unbanked could enjoy particularly strong potential welfare gains. Since low-income households often lack credit and insurance, one of the core benefits of access to formal savings is to "enable the building of safety nets to smooth shocks" (Karlan and Morduch, 2009). Importantly, formal savings permits the transformation of small amounts of savings into larger, useful lump sums (Rutherford, 1999). The recent empirical literature measuring the impacts that access to savings has on welfare starts with Burgess and Pande (2005), who used a natural experiment on bank expansion in India. They identified a 2.22 percentage point reduction in rural poverty per 1 percentage point increase in the share of savings held by rural banks. More recently, experimental field research has produced a body of evidence on the precise channels of savings impact (Ashraf et al., 2010; Dupas and Robinson, 2013a, 2013b; Karlan et al., 2014; Prina, 2013).

## 1.2 Savings products for low-income households

Although research has demonstrated that even very poor households are willing and are able to save (Collins et al., 2009), savings is typically undertaken to smooth consumption and protect against shocks. For households where meeting consumption is difficult and incomes are volatile, saving for long-term horizons such as retirement is challenging (Rosenzweig, 2001). While retirement savings and long-term savings are the focus in developed countries and for wealthier households in developing countries, "for many low and moderate income households there is much greater need to focus on basic banking services and short term savings options" (Barr et al., 2008: 15). Basic accounts (with low fees and minimum requirements) can serve as a gateway or "entry" products. Several European countries and the U.S. have successfully used entry products for the financial inclusion of previously unbanked consumer segments (World Bank, 2014).

## 1.3 India's recent policies to encourage small savings

India's bank-led approach to financial inclusion began in the 1960s and was dominated by a supply-side, credit-driven approach. However, its recent strategy towards savings for low-income households has followed the global trend, which aims to remove access barriers and promotes low-cost accounts as a gateway to financial access. In an early move to use basic savings accounts to advance financial inclusion, the "No Frills Account" (NFA) was introduced in 2005 as a basic account for low-income households. Banks were asked to relax their proof of identity and address requirements for low-income customers who maintained low balances. Although the accounts were free, there were restrictions on the number of transactions, which varied from bank to bank. These accounts were targeted at low-income households, and the targeting guidelines also varied from bank to bank. Some banks offered to make these accounts available only to those households with income that was below a certain monthly income; other banks offered to make them available only to people who maintained an account balance that was below a certain maximum balance. The country embarked on a national drive where certain districts were targeted for 100% financial inclusion. This first effort to increase demand for accounts—by eliminating cost barriers and creating universal supply—was expected to be a success.

However, surveys of households in one district with "100% inclusion" in Karnataka found that nearly one-third of the households remained without bank accounts, and a large share of the accounts remained dormant after being opened (Ramji, 2009). Another study of a "100% financially included" district in Tamil Nadu found that 25% of the households remained without accounts; further, of those households with accounts, nearly 75% of the accounts had zero or near-zero balance after one year (Thyagarajan and Venkatesan, 2008). India has continued to push an ambitious financial inclusion agenda. However, success has been mixed, and attempts to innovate based on technologies that were successfully introduced in other countries—M-Pesa mobile banking in Kenya, the Business Correspondent (BC) model in Brazil, for instance—have met with resistance from banking regulators.

# 2. Framework

The question of why individuals and households fail to save enough or fail to save in the "right" types of instruments is the subject of a broad, global research. A full discussion of the extant literature is beyond the scope of this review. However, important areas of research and intervention relevant to savings by low-income households—especially in the Indian savings context—include the barriers of identity proof, information and cognitive bias, stigma, and transaction costs. For each of these barriers, the design of institutions and regulatory incentives play an important role in shaping individual savings decisions.

## 2.1 Proof of identity

### 2.1.1 Know Your Customer requirements

The identity and address verification procedures required of banks under the Know Your Customer (KYC) and Anti-Money Laundering (AML) policies[1] are frequently cited as reasons

[1] Banks are required to confirm both ID (legal name and identity) and current address of accountholders. For identity, banks may accept any one of the following as proof (whichever satisfies the bank): passport, PAN card, voter ID card, driving license, identity card (subject to the bank's satisfaction), or letter from recognised authority verifying identify and residence of the customer. For correct permanent address, banks may accept any one of the

for low savings participation rates (Karlan et al., 2014). In India, a recent national household survey found that a large proportion of non-users of financial services reported lack of sufficient identity and address proof as the reason for not having a bank account (Demirguc-Kunt and Klapper, 2012). Documentation requirements are more likely to lead to the exclusion of women and migrants (who have residence documents in their place of birth) as well as low-income or informally employed individuals (who are less likely to possess multiple identity documents) (Allen et al., 2012). In addition, low-income households or the unbanked may lack the social connections necessary to obtain a "letter of introduction," which is one of the few ways that the KYC norms can be relaxed.[2] Even for individuals who are able to meet the documentation requirements, the time and incidental costs associated with collating the documentation may create another barrier: in a survey of rural and urban account holders in Tamil Nadu, collating the required paperwork to open an account was found to take an average of five hours (Mowl, 2013).

### 2.1.2 Rare problem with unambiguous support and clear solutions?

In response to the banks' claim that the due diligence requirements of KYC/AML policies—and the associated penalties for violation—form one of the challenges in opening accounts for low-income households, the governor of the Reserve Bank of India (RBI) proposed that the penalty for accepting incomplete or invalid documents should be reduced or waived in the case of low-value accounts (Rajan, 2014). Further, in late 2013, the RBI's Committee on Comprehensive Financial Services for Small Businesses and Low Income Households recommended waiving the requirement for proof of current address in order to open accounts. In addition, the government is actively promoting a free national biometric ID card, called Aadhaar, which would function as proof of ID as well as address.

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following as proof: telephone bill, bank statement, letter from recognised public authority, electricity bill, ration card, or letter from employer.

[2] For individuals unable to meet full KYC compliance, particularly individuals unable to prove current address, banks can demand a letter of introduction from an existing bank client. The existing client must have met full KYC norms and should have had an account at the bank for more than six months. In practice, this "letter" is a signature from an existing client on the client's application stating that the "introducer" verifies the applicant's current address and identity.

### 2.1.3 Or partial solutions, at best?

However, three pieces of evidence suggest that financial providers already exercise discretion in enforcing the existing KYC/AML policies. First, in an audit study testing the willingness of banks to open low-value, low-risk accounts based on streamlined yet legally acceptable documentation,[3] Das (2013) found that banks misrepresented identity and address requirements to screen out low-income customers. Second, in a recent investigation of several of India's largest banks, bank staff were found to be quick to waive the KYC/AML requirements for journalists posing as customers offering to undertake high-value, profitable transactions (*The Hindu*, 2013). Finally, in order to register a new customer, Indian cell phone companies are required to meet the same KYC/AML requirements that banks need to satisfy. India has an extremely high rate of mobile penetration. However, documentation requirements are rarely mentioned as a barrier to access in the context of new mobile phone connections, and the compliance of mobile providers with KYC/AML norms is not widely questioned. Taken together, this evidence suggests that selective policy enforcement on the part of providers rather than lack of documentary proof provided by clients plays a greater role in exclusion than was previously assumed.

## 2.2 Financial literacy, information, and cognitive bias

### 2.2.1 Financial literacy and information

The low level of financial literacy of Indian households is often cited as the reason for low demand for formal financial services, and this has provided the rationale for the government's large-scale financial literacy initiatives. However, the search for a causal link between financial literacy and improved decision-making have had mixed results (Carpena et al., 2011). There are many ways in which financial education can be delivered, with various levels of success, and

[3] All banks in India are mandated to offer a "small account," which requires essentially no proof of address or identity—only a photograph and self-certification, approved by the bank staff. The accounts can initially be opened for period of 12 months, after which the account-holder needs to provide full identity and address proof. Since the account has almost zero documentation requirements, it is accompanied by high restrictions on the size and nature of transactions: the accounts have strict limits on annual turnover (INR 1,00,000), maximum balance (INR 50,000), and frequency of transactions. Migrant workers constitute one of the target groups for this account.

little clarity exists on the "best practice" for taking advantage of any potential change (Karlan et al., 2014).

Even for those individuals who are financially literate, the awareness of banking products and services is a prerequisite for take-up. Low-income households may not have social networks that are engaged in financial services or may not be exposed to advertising. Some researchers have argued that awareness can be framed as a cost that the individual faces when learning about a programme. Currie (2004) finds strong empirical evidence that "awareness" is sensitive to the relative size of the benefit of a programme or policy.

### 2.2.2 Cognitive bias

Behavioural economics has made multiple contributions via theory and strategies to approach the problem of under-saving. Although there are various biases that occur in the financial decision-making process (see Barberis and Thaler, 2003; DellaVigna, 2009; Karlan and Morduch, 2009; Mullainathan and Shafir, 2009), the dominant insight for savings behaviour comes from people's tendency to have a stronger preference for more immediate payoffs relative to later payoffs. This is termed "present-bias preferences" (O'Donoghue and Rabin, 1999) or "hyperbolic discounting" (Laibson, 1997), and it manifests in short- and long-term savings decisions.

To compensate for bias in short-term financial decision making, many formal financial products typically involve some form of "default" settings, such as opt-out features. However, low-income households typically lack access to various products, especially to products with these progressive features. For example, individuals employed in the formal sector typically have employer-linked bank accounts to which their salary is automatically deposited, making it virtually impossible to remain unbanked. In India, these accounts are known as "salary accounts." These accounts offer benefits such as the waiver of the minimum balance requirement, i.e., no penalty is imposed on the account-holder for not maintaining a specific minimum balance in the account. Simple "default" options can lead to not only higher participation rates but also higher levels of savings. Comparing a banked and an unbanked person with equivalent incomes, "the greater tendency to spend cash in the wallet compared to funds deposited in the bank suggests that the first, banked person will spend less on impulse and save more easily than the person who is unbanked" (Mullainathan and Shafir, 2009: 127).

## 2.3 Stigma

Studies on micro-inequities have demonstrated the power of small signals and cues to demean and diminish (Rowe, 2008), with individuals from historically stigmatised groups being more sensitive to these cues.[4] For low-income individuals faced with a cascade of signals "that banking is not intended and should not appeal to people with lesser means…a poor client may feel reluctance, shame, and a general sense that he or she could never be an important or valued customer at a bank" (Bertrand et al., 2006:12). A low-income individual's sense of exclusion could be reinforced by simple distinctions such as the wealth and income of the other clients in the bank, the behaviour of the staff, and the language of the application documents and the product materials. Even for literate customers, the simple unavailability of application forms, signs/instructions, or product materials in the local spoken language could signal that he/she is not a desirable customer. Kleven and Kopczuk (2011: 66) incorporate stigma and language[5] uncertainty into a model of targeting and efficiency of social programmes; they find that stigma as well as language barriers are "pure ordeals" that impose pure deadweight costs on the applicants and improve neither targeting nor efficiency.

Although the role of stigma in non-participation has been studied more extensively in social programmes than in banking contexts, there is evidence that low-income banking customers seek out providers with a more inclusive environment. One of the reasons for the success of expensive, "fringe" banks among low-income households in developed countries is the poor and inconsistent service provided by formal banks (Buckland et al., 2010) and the more inclusive and welcoming atmosphere of "fringe providers" (Servon, 2013). In a recent survey in Tamil Nadu, customers with experience at different bank types felt that despite the increased time requirements, cost, and effort, a private or foreign bank account was most desirable, in large part due to the "more polite staff" (Mowl, 2013).

[4] According to Cohen and Steele (2002), for members of historically disadvantaged groups, past treatment "gives them grounds to mistrust authority figures."

[5] Language is a powerful factor "in social identification and stratification, an important index for according or withholding respect (McDougal et al., 1976: 157)." Other studies have documented how the use of the former colonial language in administrative and bureaucratic settings is "characteristic of contexts where explanations, deliberation, and ultimately, consent, are not really required" (Graeber, 2012: 114).

## 2.4 Transaction costs

Although information, cognitive bias, and stigma constitute important explanations for under-saving, they cannot be the only barriers. To an individual deciding whether or not to participate in a programme, more concrete transaction costs could play a larger role than lack of information or stigma.[6] In addition, since many of these barriers can be framed as more traditional economic variables (such as time), "the basic cost benefit/framework has remained the basis for empirical investigation into participation in social programs" (Currie, 2004: 6) as well as for the investigation of financial decision making.[7]

### 2.4.1 Direct and indirect costs

Transaction costs as a barrier to savings may be more salient to low-income households, simply because they are more resource-constrained. For a client, direct transaction costs would include the service charges (such as minimum balance fees or application fees) levied by the provider. These costs reflect some of the broad market frictions and infrastructure costs faced by the financial institutions. For fixed transaction costs that are independent of the size of the financial transaction, serving clients who require small and frequent transactions can be costly (Beck and De La Torre, 2007). Studies of microfinance institutions (MFIs) that deal with small savings revealed that MFIs rarely recover the bank's fixed cost(s) and have high operating costs; these costs can be overcome only by cross-selling loans and other products and by charging fees that are derived from the savings accounts themselves (Westley and Palomas, 2011). As Barr et al. (2008: 15) note, "market forces weaken or break down entirely with respect to saving for low income households…the administrative costs of collecting small value deposits are high in relation to bank's earnings on the small amounts saved, unless the bank can charge high fees. With sufficiently high fees, it's not clear that utilising a bank account makes economic sense for

[6] As Currie (2004: 11) notes, these are not entirely separate explanations. Incentives to obtain information about the programme increase with the size of the benefit, and a person who is required to complete an application that asks for a great deal of information may feel stigmatised.

[7] Studies on the transaction costs of formal and informal credit include Ahmed (1989), Cuevas (1988), Guia-Abiad (1993), and Houseini et al. (2011). The transaction costs of the group lending model in India have been examined by Dehem and Hudon (2013), Karduck and Seibel (2006), and Swamy and Tulasimala (2011). Gopinath et al. (2010) is a relatively recent study of the transaction costs of using formal and informal money transfer products. A recent study by Schaner (2011), which uses a field experiment to examine the role of ATMs on take up and account use, includes innovations in measuring transaction costs for savings.

a low income household." Indirect transaction costs include explicit costs such as transportation, photocopy, and documentation charges, as well as the implicit costs related to the opportunity costs of lost wages (Mowl, 2013). These reflect the underlying infrastructure and regulatory environment (for example, the quality of roads and the number of documents required by the financial regulator).

The principle behind many supply-side initiatives in expanding access is that by lowering direct and indirect costs for the user, take-up will increase. There is evidence from some countries that lowering the client transaction costs works to encourage both take-up of accounts as well as increased overall savings. The expansion of national savings programmes in Mexico increased the savings rate by 7 percentage points for low-income households (Aportela, 1998); similar positive results in savings bank expansions were reported in India (Burgess and Pande, 2005) and Thailand (Kaboski and Townsend, 2012). However, the results from India's drive to push "No Frills Accounts" were less successful and failed to increase the intended savings among the beneficiaries (Ramji, 2009). In Kenya, a randomised experiment (Dupas et al., 2012) providing vouchers for free savings accounts to a random subset of women was successful, with more than 60% of the women opening an account within one year of receiving the offer. However, fewer than 30% of those who opened an account made two or more deposits within one year. The India and the Kenya findings suggest that opening costs and minimum balance requirements are not the only constraints to meaningful use of formal savings.

### 2.4.2 Hidden costs

A more careful accounting of direct and indirect transaction costs reveals that even supposedly "free" goods impose hidden costs on the user; further, small costs can have a disproportionate impact on decision making that would not make sense in a standard economic model. These hidden costs are typically not well understood or well documented; yet the magnitude of their effects can be substantial.

For example, even a slight hassle involved in travelling to the bank—even if the distance is small—may be enough to discourage a person from opening an account or following through on an application.[8] According to Mullainathan and Shafir (2009: 141), "whereas most programs focus on options that are available…an otherwise beneficial program with small channel blockages may be *de facto* a program that is not available."

### 2.4.3 Role of institutions in mitigating transaction costs

Institutions, both public as well as private, play a role in affecting the choices of consumers via their design and impact on transaction costs. One of the contributions of psychology to economics is "a new appreciation for the impact and responsibilities of financial institution" (Mullainathan and Shafir, 2009: 128).

***Institutions can increase costs*:** Since financial institutions have a commercial disincentive to serve low-balance accounts, it is possible that the low take-up and use are the results of strategic bank behaviour. Several recent studies examined the quality of information and products offered by financial service providers; they found that firms often fail to de-bias clients, fail to market mandated products, and withhold key information on product features when it is against the firm's commercial interest. Firms, as actors, respond to regulatory incentives (Barr et al., 2008), and the firm, "often in a position to deal directly with customers and operating after regulations have been set, is well situated to circumvent regulatory intent" (Mullainathan and Shafir, 2009: 15).

In a randomised experiment of the quality of financial advice given to trained auditors posing as potential clients presenting different portfolios in the U.S., Mullainathan et al. (2012) found that financial advisors fail to de-bias clients and push for active funds with higher fees, even when the client presents a strong, well-diversified portfolio with low fees. In a study of the provision of basic savings products in Mexico (Gine et al., 2013), participants in focus groups reported losing a significant amount of their account balance due to avoidable charges that they were not informed about when the account was opened. In the same study, a randomised experiment using trained auditors revealed that potential customers were rarely offered the cheapest product, with the nationally mandated basic checking account offered in less than 5% of visits. In addition,

[8] Seemingly trivial effort costs have been demonstrated to derail the adoption of life-saving health technologies (Kremer et al., 2009) and prevent the adoption of farm technologies that yield high rates of return (Duflo et al., 2011).

bank staff provided just enough information to open the account, but withheld key information on avoidable charges and fees; further, the written materials that were provided lacked sufficient detail to compare products. The vast differences in annual returns for the basic checking account (-0.8%) compared to other current accounts (-7.4%) helps to explain why providers have little incentive to market these basic products (Gine et al., 2013: 7).

In an audit study of commission-based insurance agents in India, Anagol et al. (2013: 33) found that agents recommend highly unsuitable products and "hiding information is an important part of the agent's sales strategy." In a household survey in Kolkata, Fischer (2011: 12) found that the clients' "beliefs about product terms and restrictions is substantially less favorable than posted terms…banks have little incentive to correct misconceptions. This information gap extends far beyond the divergence between posted and perceived fees. Many households reported forfeiting their savings at banks when the account was classified as inactive after as little as six months, despite an RBI prohibition against this practice."

In addition to the commercial disincentive to reduce costs for clients, poor administration and operations by the provider can increase transaction costs. While institutions are ideally assumed to be organised to reduce transaction costs and increase efficiency, clients may feel the opposite to be true.[9] This feeling could be justified, as the front-line staff who represent institutions in their face-to-face interactions with clients are typically given substantial discretionary authority (defined as the ability to influence outcomes), while also dealing with unreasonable caseloads with ambiguous goals and lack of adequate resources.[10] Evidence from prior research shows that front-line staff use three common strategies in order to deal with the pressures they face on the job, namely, oversimplification or routinisation of complex tasks,[11] increasing the complexity for

[9] "Despite their self-representation as rational and efficient…for many people, bureaucracy signifies slowness and delays, unnecessary paperwork, and complicated protocols" (Hoag, 2011: 81).

[10] "This analysis may help place in some perspective the apparent paradox that some community groups, in good faith, insist that bureaucrats are biased and discriminatory, while at the same time members of these bureaucracies insist in good faith that their members do not engage in discriminatory and biased practices" (Lipksy, 1969: 30).

[11] A number of authors have shown how staff manage stress by "establishing formulae for rapid decision-making" (Hoag, 2011: 85). These shortcuts, routines, and simplifications allow front-line staff "to make quick decisions and thereby accomplish their jobs with less difficultly--perhaps freeing scarce resources through time-saving" (Lipksy, 1969: 12)

the client,[12] and manipulation of waiting time.[13] While this self-protective behaviour of the front-line staff imposes a cost on all clients, these behaviours are most salient to low-income clients and minority groups. This is because low-income individuals are more dependent on institutions than wealthier individuals are to provide access to basic services, and they have fewer resources to bear the additional costs.

***Institutions can lower costs*****:** Seemingly trivial changes in the contexts, constraints, and costs can have large positive effects on reducing barriers to access. Recent experimental evidence provides clear examples where changes to the default options, simple institutional design, and staff behaviour can dramatically change outcomes. In one randomised evaluation of expanding access to unbanked persons in the U.S., simply having a representative of the bank available for assistance with completing application forms had a positive impact on the likelihood that an individual would open an account; it was also positively correlated with the person's use of other bank services such direct deposits and ATMs (Bertrand et al., 2006). Similarly, Devoto et al. (2011) found that small administrative barriers had a surprisingly large effect in preventing households from taking loans to connect to piped water. When a subset of households were offered simple assistance in completing forms, 69% of the assisted households accepted the loan and water, compared to just 10% in the group that was not offered assistance.

In this section, we presented evidence related to the overall benefits of saving and the importance of small savings products for low-income households. This section also reviewed the theory and empirical evidence on four broad types of barriers to savings—eligibility, information and cognitive bias, stigma, and transaction costs—each of which is particularly salient to the savings decisions of low-income households. This section further highlighted the role of regulation, institutional design, and staff incentives in raising or lowering these barriers and in shaping individual savings decisions.

[12] This would include developing "procedures for effectively limiting client demands by making the systems irritating to use and financially or psychologically costly" (Lipksy, 1969: 18).

[13] Nichols et al. (1971) provide an extensive review of the literature on the waiting time to ration public goods.

# 3. Research Methodology and Design

## 3.1 Methodology

This study examines the range of hidden burdens and constraints imposed by the formal financial sector on individuals seeking to save and invest, as well as the extent to which these constraints can explain the savings decisions taken by low-income households. If these burdens and constraints are not reflected in the "sticker price" of the savings product, the persistent preference for physical or non-financial assets may be explained by the hidden costs of the formal banking sector. Tracking the full set of costs faced by customers purchasing a simple deposit product is, therefore, an important first step in designing better-targeted policies and products.

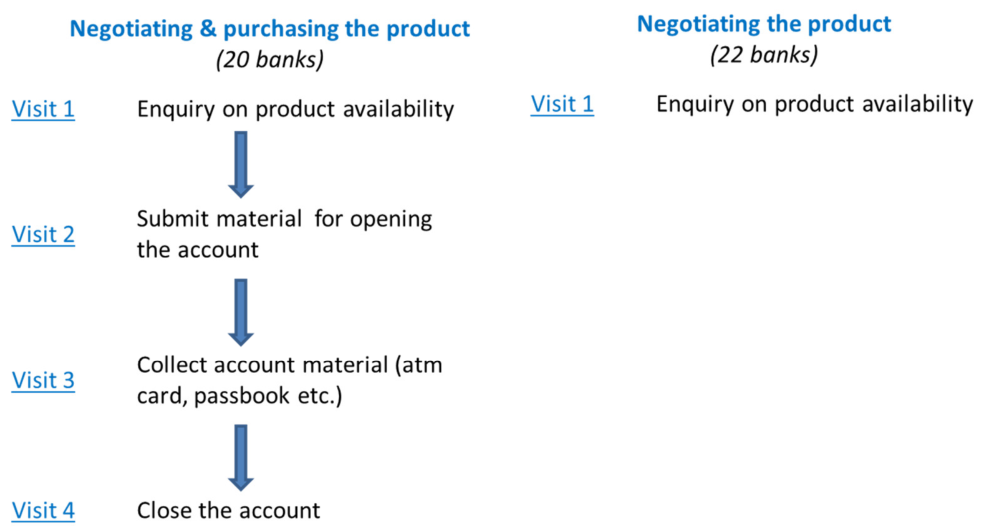
We utilise a framed field experiment and mixed-methods approach to measure the direct, indirect, and hidden costs faced by customers purchasing basic or low-cost deposit accounts. The research tools include modified mystery shopping techniques, repeated visits to the bank by trained auditors to open an account in the auditor's name, facility audits of the banking sites, qualitative analysis of audio recordings of interactions with bank staff and managers, and analysis of written materials and information provided to the auditor.

An alternative methodology such as an analysis of household surveys was considered. For instance, earlier work by one of the authors (Mowl, 2013) used household surveys to measure the transaction costs of users. However, while household surveys provide more detailed information about the individual characteristics (age, education, occupation, financial literacy) of financial services users, they can suffer from respondent recall and measurement error, which are especially problematic when attempting to address hidden costs. On the other hand, using mystery shopping techniques would allow us to directly record and analyse bank behaviour such as microaggression.

A large-scale audit of bank offers that were stopped when the product was offered or the negotiations were completed was also considered, similar to what was done in other recent audit studies measuring the performance of providers (Anagol et al., 2013; Gine et al., 2013; Mullainathan et al., 2012). However, this method is unable to accurately measure the complete set of costs to the customer, since it does not take into account every step of the process required to obtain a functioning product. Further, this approach does not capture the potential difference(s) between the stated offer and the final product.

Therefore, we decided on a mixed approach that involved (i) negotiating the hypothetical or "offer" contracts for half of our sample, and (ii) taking this one step further by completing the purchase and closing the account (following a short period of time) for the other half of the sample. Opening and closing an account involved a series of additional visits to the bank, as is highlighted in Figure 1. In these cases, an account was declared "complete" when (1) the account was opened and fully operational (i.e., the customer was included), or (2) the bank rejected the customer on the basis of KYC/AML eligibility or because it failed to market a low-cost product (i.e., the customer was excluded).

**Figure 1: Study Design and Sample Frame**




## 3.2 Product

Our study exploits the existence of a standard, full-service savings product that is available at all banks and has universal eligibility. In August 2012, the "No-Frills Account" (NFA) was revised as a full-service "Basic Savings Bank Deposit Account" (BSBDA),[14] "with a view to doing away

[14] Customers looking to open accounts based on simplified KYC protocols can still obtain bank accounts through the "Small Accounts" programme (Das, 2013).

with stigma associated with the nomenclature ‘no frills’ account and making the basic banking facilities available in a uniform manner across the banking system” (RBI, 2012). All scheduled commercial banks in India (including foreign banks) were advised to offer a BSBDA. Table 1 presents a list of the key product features of a BSBDA. The BSBDA was designed to remove one of the key demand-side barriers to savings—costs; by advising all banks to offer the product, a near limitless supply was guaranteed.

**Table 1: Key Features of Basic Savings Bank Deposit Account (BSBDA)**

| Features | Details |
|---|---|
| RBI policies | The BSBDA was subject to RBI policies on KYC/AML for opening of normal bank accounts. |
| Restrictions | The BSBDA would be considered a normal banking service available to all: banks were to impose no restrictions such as age, income, and amount criteria. However, the holders of a BSBDA would not be eligible for opening any other savings account in the same bank; they could have other deposit accounts, such as term/fixed deposits and recurring deposits. |
| Minimum facilities offered* | No minimum balance requirement.<br>No initial deposit required for opening a BSBDA.<br>The services available include deposit and withdrawal of cash at bank branch as well as ATM usage; receipt/credit of money through electronic payment channels; deposit/collection of cheques drawn by government agencies and departments.<br>No limit on the number of deposits in a month. Account holders will be allowed a maximum of four withdrawals per month, including ATM withdrawals.<br>Passbook and an ATM card or ATM-debit card will be provided free of charge. Chequebook would not be provided as a minimum facility.<br>The minimum facilities would be provided free of charge, and no charge would be levied for non-operation or for activation of inoperative BSBDAs.<br>Beyond the minimum facilities, banks could set their own pricing structure for fees and services. |

* Source: Reserve Bank of India (2012a, 2012b)

We recruited experienced investigators for the survey, all of whom had extensive experience in audit studies and mystery shopping exercises. Our auditors were given specific scripts for requesting a BSBDA account if the account had not been initially marketed by the bank staff. The instigation for a BSBDA was made using a minimum of three prompts suggesting the preference for such a product including: (i) using the word “basic”; (ii) asking for an account with no charges; and (iii) suggesting that the client would not be able to maintain a minimum balance at all times. While the BSBDA was chosen as the target product for investigation, if this product was not marketed by the bank agent, the auditor was authorised to purchase whichever account had the smallest initial deposit requirements (capped at a maximum of INR 1000).

The two key elements behind our product choice are: (i) requiring full KYC/AML documentation, and (ii) allowing some flexibility in the purchased product's characteristics (i.e., amount of initial deposit required). Using a product that requires robust KYC/AML compliance allows us to identify whether banks are more supportive of customers with such documentation. If they are, using Aadhaar[15] for both ID as well as address proof would potentially solve the documentation barriers associated with savings behaviour. Further, allowing the purchase of low-cost accounts (while keeping this amount [INR 1000] within the reach of low-income clients) would give us a good approximation of what banks would offer without government mandates and would allow us to verify whether the services provided on these accounts are of better quality. If this is indeed the case and banks are more inclusive of low-income customers with regard to the products they sell covering basic costs, it might warrant a reconsideration of the zero-cost decree on the BSBDA. Lastly, allowing for a two-stage negotiation process when opening the account (wherein the client indirectly requests a BSBDA and negotiates for a low-cost account if the former was unavailable) would allow us to measure how much the salesperson steers away from the optimal product enquired by the client.

## 3.3 Customer profiles

In order to test the response from banks related to the socio-economic status and level of financial literacy of new customers, we introduced two slightly different customer profiles. Both profiles used a nearly identical script and requested the same type of account, but differed on two dimensions: (i) the customer's self-description and documentation signalled his status as a formal or informal sector worker, and (ii) the customer would signal his level of financial literacy by prompting (or not prompting) for basic account features such as interest rates and fees. In order to reduce individual auditor bias, auditors were randomly assigned a profile and a bank branch. The only restriction to this random assignment was that the auditors could not be allocated to a branch in which they currently have or previously had an account. During the interview process, care was taken to ensure that accounts would not be rejected because of inadequate ID or address proof. As such, all auditors had at least one major ID proof (e.g., voter's ID) and address proof

[15] The Aadhaar card is the Unique Identification card currently promoted as the main form of ID for all individuals across India.

(e.g., ration card); all were middle-aged, male heads of their household. Ethical concerns about recruiting individuals from marginalised communities for intensive participatory research as well as the difficulties in recruiting non-professionals for the exercise led us to restrict our customers to professional investigators with survey experience.

## 3.4 Sampling

Using RBI data (which lists all bank branches and their exact location in Chennai), we created our primary sampling units (PSUs) as separate geographical zones of the city. These zones were mapped based on the postal code (i.e., zip code) of the bank address. Each zone generally included up to three postal codes, including neighbourhoods with both residential as well as commercial activity. This was to take into account the assumption that when a customer is looking to open a bank account, he/she would be most likely to choose a bank close to his/her residence or place of work so as to reduce travel costs. Hence, we decided to sample zones of mixed residential and commercial activity so as to closely mimic a natural setting. During the course of the study, we collected data across two urban zones.

From the five major bank categories—nationalised, State Bank of India (SBI) and associates, private, foreign, and regional rural banks—that are required to provide the BSBDA as per the RBI guidelines, we randomly sampled in proportion to the share of savings accounts in Tamil Nadu by bank type.[16] This sample was verified to approximately match the bank branch density in Chennai (also by bank type). Our final bank sampling frame was restricted to 27 banks that covered 80% of the branches in Chennai; this restriction was based on the assumption that a new customer aiming to open a bank account would most likely visit a recognised or known bank rather than an unfamiliar one. Our final sample included 20 branches for which accounts were purchased and 22 branches for which only an initial account enquiry was completed.

[16] Scheduled commercial banks in India are categorised into five groups according to their ownership and/or nature of operations: (1) State Bank of India and Associates (SBI and Assoc.), (2) nationalised banks, (3) private sector banks, (4) foreign banks, and (5) regional rural banks. Both SBI and nationalised banks are public sector banks, but are categorised separately by the RBI. Thus, our sample and analysis take these categories into account. Due to the urban nature of this survey, no regional rural banks were included in our sample.

## 3.5 Protocols

The auditor's scripts and scenarios were not deceptive and followed best practices related to research on human subjects. Information that could be used to potentially identify banks, branches, or staff was removed from all data and reports. In addition, we did not open an account at more than one branch of a bank in order to minimise costs to the financial institutions. Quality was assured through a series of measures, including extensive piloting, verification of questionnaires against audio data, frequent debriefings, and triangulation of data. Auditors were counselled that the purpose of the study was to measure the marketing of basic and low-cost accounts offered at banks as well as the transaction costs of opening accounts. Auditors were trained with regard to the written policies for KYC/AML and the minimum common features provided under the BSBDA in order to guide their conversations. However, the auditors were not given information about the savings products or policies of any specific bank.

## 3.6 Data and survey instruments

To explore our hypotheses, we used four data sources.

### 3.6.1 Primary data collection

***Account-level data:*** Immediately following their visit to the bank, auditors had to record account-level information using a detailed questionnaire that included specific questions about all verbal exchanges with bank staff, written materials provided, and observations related to the bank environment during the visit. For cases where the product was purchased, this information was captured for all the visits that were required. Audio recordings for each visit were taken in order to verify the auditor's self-reported data as well as to provide a rich source of information for qualitative analysis of the bank staff's language and tone.

***Branch-level data:*** During the first visit to a bank, the auditor was asked to report about the branch characteristics including the presence of a help desk, banners, brochures, and identifiable bank representatives. This information was independently verified during a separate visit by a different auditor, who collected more detailed observational data such as specific products advertised, display of informational banners, infrastructure, and layout of the banking hall.

### 3.6.2 Secondary data collection

***Bank-level data:*** To compare the information provided by the branch-level bank staff member about the actual products offered by the bank, we collected bank-level data from the bank's website. This included the advertised availability and specific features of the BSBDA, as well as the standard savings products intended for customers seeking to maintain low-balances or low initial deposits.

***Regulator data*****:** To determine the bank branch sample, we utilised RBI data on the number of savings accounts in Tamil Nadu by bank category, the bank category with the largest proportion of branches in Chennai, as well as the list and location of all bank branches in Chennai.

# 4. Results and Interpretation

## 4.1 Marketing of savings products by banks

When approached by an auditor posing as a potential low-income customer requesting to open a savings account, none of the banks offered a BSBDA product as the first suggestion (see Table 2). Further, while 67% of nationalised and SBI/associate banks suggested accounts with a low initial deposit (less than INR 500), 88% of private and all foreign banks proposed an account that required a high initial deposit (above INR 500) ranging from INR 1000 to INR 3 lakh. Assuming that low-income customers will not open an account with an initial deposit and monthly minimum balance requirement over INR 1000, we found that 12 out of the 42 banks visited (i.e., 28%) had excluded clients by marketing unaffordable products.

Following the initial marketing suggestions made by the bank staff, the auditors specifically asked for a BSBDA product using a minimum of three prompts indicating the preference for such a product, including (i) using the word "basic," (ii) asking for an account with no charges, and (iii) suggesting that he would not be able to maintain a minimum balance at all times. Despite such direct instigation, only 14% of the banks revealed the existence of such an account. When banks admitted that the BSBDA product was available, the admission was generally followed by verbal disincentives about opening such an account mainly by informing the client (incorrectly) that the BSBDA was only available to the extremely poor, disabled, "uneducated," or those in rural areas, or by informing the client (incorrectly) that the BSBDA had severe limits on functionality, such as no ATM card (see Box 1, Type 5 and 6 for examples of discouragement related to purchasing BSBDA).

**Table 2: Accounts Marketed During Initial Enquiry (By Bank Type)**

| | Nationalised | SBI & Assoc. | Private | Foreign | All banks |
|---|---|---|---|---|---|
| Offered a zero balance account (BSBDA) | 0 | 0 | 0 | 0 | 0 |
| Offered a low balance account (=< INR 500) | 0.67 (0.48) | 0.67 (0.50) | 0.12 (0.35) | 0 | 0.50 (0.51) |
| Offered a high balance account (> INR 500) | 0.33 (0.48) | 0.33 (0.50) | 0.88 (0.35) | 1.00 (0.00) | 0.50 (0.51) |
| Offered multiple products | 0.29 (0.46) | 0.22 (0.44) | 0.12 (0.35) | 0.75 (0.50) | 0.29 (0.46) |
| Offered a BSBDA when instigated | 0.09 (0.30) | 0.22 (0.44) | 0.12 (0.35) | 0.25 (0.50) | 0.14 (0.35) |
| *Number of observations* | 21 | 9 | 8 | 4 | 42 |

**Box 1: Marketing strategies by bank staff to deny or discourage the purchase of BSBDA**

| | | |
|---|---|---|
| **Type 1: Clear denial of BSBDA accounts** | | |
| Case 1 (Nationalised) | Client | *My colleagues told me about the basic savings account and that I could open one without minimum balance.* |
| | Manager | *There's nothing like that here sir, in [NAME OF BANK]. Maybe banks like [NAME OF LARGE PRIVATE SECTOR BANK] offer. We don't have like that.* |
| | Client | *Can you open for me an account with a zero balance or a small deposit?* |
| | Manager | *We don't have a zero balance account at all.* |
| | Client | *Really?* |
| | Manager | *You can check with [NAME OF SBI AND ASSOC. BANK]. It may be available there.* |
| | Client | *Have you offered it here before?* |
| | Manager | *We've never had it.* |
| Note: At the entrance of the bank, hanging over the threshold, there was a prominently displayed banner advertising the host of savings products available, including the basic savings deposit account (BSBDA). | | |
| **Type 2: BSBDA is no longer active or bank does not participate** | | |
| Case 1 (SBI & Assoc.) | Client | *Is there an account called the basic savings account, madam?* |
| | Staff | *We haven't received the (RBI) circular here for basic savings account.* |
| Case 2 (Private) | Staff | *Normally, till now, we have not done it. Now it seems like they have announced something.* |

| | | |
|---|---|---|
| **Type 3: Misrepresented the BSBDA as the bank's "regular" or "normal" account** | | |
| Case 1 (Nationalised) | Manager | *[Basic account] is the normal savings account. That's all.* |
| Case 2 (Private) | Staff | *You can even check with [NAME OF OTHER PRIVATE BANK] or [NAME OF OTHER PRIVATE BANK]. Everywhere the minimum balance requirement is INR 10,000. This is decided by the RBI.* |
| **Type 4: Misrepresented the BSBDA as the banks "Corporate Salary Account"** | | |
| Case 1 (Private) | Staff | *Only a salary account is available with zero balance. Whichever the bank you go to, that will be the response.* |
| Case 2 (Private) | Staff | *The (Basic Account) is the 'corporate salary account'. You can open that account only in the bank where your company has an account.* |
| **Type 5: Misrepresented client eligibility** | | |
| Case 1 (Nationalised) | Staff | *That [No Frills Account] may be opened only if you have no income.* |
| Case 2 (Private) | Staff | *If you see, only persons with salary less than minimum INR 4000 are eligible for that. We will need some proof documents for that. Moreover, there will also be charges.* |
| Case 3 (Nationalised) | Manager | *The zero balance account may be offered…only for exceptional cases like students, delivery cases [of government services]. Then for ATP,*[17] *blind persons, deaf persons, other special categories.* |
| Case 4 (Nationalised) | Manager<br>Client<br>Manager | *[The basic account] is for poor families in poor areas, like the uneducated people.*<br>*In this branch you don't offer this account?*<br>*Not only in this branch, sir. NO metro branch will give this account.* |
| **Type 6: Misrepresented BSBDA account features** | | |
| Case 1 (Nationalised) | Manager | *Go ask that madam, [BSBDA] can be opened. You can deposit and withdraw, but every time you will have to come in-person and transact. There is no ATM card.* |

Given that the investigators specifically asked for the BSBDA while making inquiries about opening low-cost bank accounts, the bank staff often gave very specific denials. These were not only inconsistent with RBI guidelines, they were inconsistent with their bank's own written policies, inconsistent across different members of the staff within the same banks, and even inconsistent with the product marketing in the branch itself. For example, during two separate bank visits, bank representatives vigorously denied the existence of the BSBDA product despite the presence of large banners at the entrance of the banks, which advertised the BSBDA and displayed its product features (see Box 1, Type 1–4 for examples related to the denial of the

[17] Translator's note: the manager used the term "ATP" or "Alternate Talent Pool" to refer to people with disabilities.

existence of the BSBDA). Other common ways of denying access were by marketing the bank's "regular" account as the "basic account" (even when the bank's standard product started with an initial deposit of INR 10,000) or by stating that the only account with "basic features" was an employer-linked salary account.

While these results demonstrate that banks fail to market appropriate products to low-income customers, we can also relate this poor marketing to the lack of customer information acquired by the bank staff. As shown in Table 3, out of seven relevant customer characteristics—address, occupation, salaried worker, other savings account, with which bank, purpose of savings, and frequency of transactions—on average, a bank representative asks the customer for information regarding only two of these. More specifically, only 5% of the banks asked for frequency of transactions, and 19% asked about the purpose of the account, both of which are crucial information in the context of what type of product would be most appropriate. However, we also find that while foreign banks were consistently the most likely to enquire about customer characteristics, they were the also the ones offering the most expensive products. This could reflect the use of better customer relation protocols by foreign banks, while still attempting to exclude certain customer segments by building barriers to enrolment into the products themselves.

**Table 3: Information Asked About Client Prior to Marketing During Initial Enquiry (By Bank Type)**

| | **Nationalised** | **SBI & Assoc.** | **Private** | **Foreign** | **All banks** |
|---|---|---|---|---|---|
| Occupation | 47.6 (0.51) | 0.56 (0.53) | 0.63 (0.52) | 0.75 (0.5) | 0.55 (0.50) |
| Purpose of account | 0.2 (0.41) | 0.11 (0.33) | 0.25 (0.46) | 0.25 (0.5) | 0.19 (0.40) |
| Frequency of transactions | 0.05 (0.22) | 0 (0.00) | 1 (0.00) | 0.25 (0.5) | 0.05 (0.21) |
| Index of information requested (0-7)[1] | 1.85 (1.9) | 2.22 (1.39) | 2.25 (2.05) | 3.0 (1.15) | 2.11 (1.75) |
| *Number of observations* | 21 | 9 | 8 | 4 | 42 |

[1] Index of information acquired about client includes: address, occupation, salaried, other savings account, with which bank, purpose of savings, frequency of transactions

## 4.2 Know Your Customer requirements imposed by banks on new clients

Our results revealed that of the six key documents allowed under the KYC rules as proof of identity (passport, PAN card, voter ID, driver's license, letter from recognised/approved authority, and Aadhaar card), a bank representative suggested at least two of these on average (see Table 4). However, 83% of the banks suggested bringing a PAN card—an identity card most commonly associated with salaried workers in the formal sector—as one of these two documents, despite the clients indicating their relatively low income status as workers. Nevertheless, 62% of the banks also did suggest a voter ID card—a much more suitable document for low-income customers—as a potential document for the application. In terms of proof of address, out of the six permitted documents—gas bill, electricity bill, phone bill, ration card, letter from approved authority, and bank statement—bank staff would suggest at least one of these, with the ration card being the most commonly suggested document.

**Table 4: "Know Your Customer" Documents Suggested to New Clients (By Bank Type)**

| | Nationalised | SBI & Assoc. | Private | Foreign | All banks |
|---|---|---|---|---|---|
| Voter ID card suggested | 0.62 (0.49) | 0.67 (0.50) | 0.63 (0.52) | 0.50 (0.57) | 0.62 (0.49) |
| PAN card suggested | 0.76 (0.44) | 1.00 (0.00) | 0.86 (0.35) | 0.75 (0.50) | 0.83 (0.37) |
| Aadhaar card suggested | 0.14 (0.36) | 0.33 (0.50) | 0.25 (0.46) | 0.50 (0.57) | 0.24 (0.43) |
| Ration card suggested | 0.76 (0.44) | 1.00 (0.00) | 0.63 (0.52) | 0.75 (0.5) | 0.79 (0.42) |
| Index of ID documents suggested (0-6) [1] | 2.33 (1.06) | 3.11 (1.90) | 2.38 (1.06) | 3.25 (1.71) | 2.59 (1.34) |
| Index of address documents suggested (0-6) [2] | 1.19 (1.28) | 2.11 (2.20) | 1.13 (1.24) | 1.50 (1.00) | 1.40 (1.49) |
| Introductory letter required | 0.43 (0.51) | 0.11 (0.33) | 0.13 (0.35) | 0.0 (0.0) | 0.26 (0.45) |
| Visibility of KYC norms at bank branch | 0.33 (0.48) | 0.78 (0.44) | 0.38 (0.52) | 0.0 (0.00) | 0.41 (0.49) |
| *Number of observations* | 21 | 9 | 8 | 4 | 42 |

[1] ID documents include passport, PAN card, voter ID, driver license, letter from approved authority, and Aadhaar card.

[2] Address documents include gas bill, electricity bill, phone bill, ration card, letter from approved authority, and bank statement.

There was little variation in the documents that were suggested across bank type, reflecting a general trend towards lack of transparency about KYC requirements. This is emphasised by the fact that less than half the banks visited had KYC norms visibly posted in their hall, which is an easy and efficient way of promoting customer knowledge and imposing pressure on bank staff to follow regulations. Further, the analysis of the transcripts showed that the communication of KYC requirements was not only misrepresented but also confusing for the client to follow. For example, staff often listed a variety of potential documents without specifying them as alternatives (see Box 2).

**Box 2: Poor communication of KYC documentation requirements**

| | | |
|---|---|---|
| **Case 1 (Private)** | Staff | *For ID proof PAN card is mandatory. PAN card or voter ID. But PAN card is definitely needed. For address proof: ration card, Aadhaar card, driving license, passport, gas bill.* |
| **Case 2 (Nationalised)** | Staff | *2 photographs, address proof are needed. For address proof: ration card, your voter ID, passport, LIC, gas bill, telephone bill, etc. For ID proof, with photograph. This means once again PAN card, voter ID, driving license or passport. Also, one existing account holder of this bank, not necessarily this branch, should introduce.* |
| **Case 3 (Nationalised)** | Staff | *One person has to give an introduction. Then you must give two photographs. Then one ID proof, and one address proof…PAN card, voter ID, driver license.* |
| **Case 4 (Private)** | Staff | *PAN card is compulsory. Apart from that we require ID and address proof. For the address you may produce your ration card, or something like that…if we need any clarifications we may ask for three additional proofs of identity and address.* |
| **Case 5 (Private)** | Client<br>Staff | *You asked for my passport. May I know the reason?*<br>*Passport is the main proof. If you can provide it, no introduction is required.* |
| **Case 6 (SBI & Assoc.)** | Staff<br>Client<br>Staff | *You have to open the account at the branch nearest to you.*<br>*I need to visit [NAME OF AREA] very often. It will be convenient for me to open the account here.*<br>*(Your home) should be in this area. If you have a local ID proof and local address proof in this area then you can open here. So, whichever the [NAME OF BANK] branch nearest to your home is where you must open the account.* |

The requirement of introductory letters indicated the use of excessive and misrepresented documentation as a tool to exclude undesired customers. According to KYC protocols, a customer is only required to submit an introductory letter if he/she does not have the permitted proof of ID and/or address. However, we find that despite the auditors presenting complete identity and address proof, 11 out of the 42 banks (i.e., 26%) required them to submit a letter of introduction. This was especially the case in nationalised banks, with 43% of the nationalised banks requesting this time-consuming and unnecessary document for opening an account. It is worth noting that the 11 banks that rejected clients on the basis of documentation (mainly nationalised banks) were different from those that discouraged clients by marketing unaffordable products (mainly private banks), suggesting that banks use either of the two strategies to exclude unwanted clients. Further, some banks created an additional barrier by requiring that customers can open accounts only in the branch nearest to their home. Although this was initially presented as a KYC requirement, it could have been designed to reduce administrative costs for the banks (see Box 2, Case 6).

## 4.3 Written and verbal communication by banks

In terms of products offered, we found that 37 out of 42 (i.e., 88%) banks first suggested a product that they called a "Regular Savings Account." This product had very similar features on average—4% simple interest rate, an ATM card and passbook, regular charges, as well as some restrictions on transactions. The main difference among the products offered was the monthly minimum balance. As can be seen from Table 5, the average minimum balance was INR 18,553, with the median balance as INR 500. However, the average minimum balance is significantly skewed by two banks requesting over INR 2 lakh as minimum balance.

The figures in Table 5 indicate the information that was verbally transmitted to the customer without any instigation. The second column of Table 5 includes the proportion of banks that voluntarily revealed this information, highlighting the significant lack of verbal communication about key product features. Regarding charges and fees in particular, only 5% of the banks revealed the presence of any charges on the account. When they did, the only charges mentioned refer to ATM/cheque book charges and/or minimum balance charges. None of the banks informed the customer about closing charges, inactivity fees, and so on, which are generally charged on most savings accounts.

**Table 5: Verbal Information Provided About Marketed Product During Initial Enquiry**

| | Average account feature | Declared without instigation |
|---|---|---|
| **Interest** | | |
| Interest rate | 4% | 0.02 |
| Type of interest | Simple | 0.02 |
| **Minimum balance** | | |
| Minimum monthly balance | INR 18553 | 0.36 |
| **Banking material** | | |
| ATM card provided | 1.00 | 0.29 |
| Passbook provided | 1.00 | 0.29 |
| Chequebook provided | 0.67 | 0.29 |
| **Charges and fees** | | |
| ATM/Chequebook charges | 0.70 | 0.05 |
| Minimum balance charges | 0.44 | 0.05 |
| **Transaction restrictions** | | |
| Unlimited transactions | 0.38 | 0.09 |
| Limited transactions | 0.63 | 0.09 |
| *Number of observations* | 42 | 42 |

While verbal communication clearly lacked transparency, suitable written documentation was entirely absent at every stage of the process. In response to inquiries about which account to open, none of the banks were able to provide brochures or pamphlets about the product marketed, despite the customer specifically requesting for this. Similarly, at the time of filling out the application form, none of the banks were able to provide the customer with a form in Tamil (the local language) even though the customer clearly indicated that he did not know how to read/write in English. Further, the bank staff were often very dismissive of the clients' requests for material in order to better understand what product they were purchasing (see Box 3, Case 1 and 2). This also applied to queries related to redress procedures that should be followed in case a problem arose (see Box 3, Case 3).

In terms of the written material provided when the account was opened, we found that most banks provided two pieces of printed material on average, one of which is always a passbook; the other could range from a guide to using the ATM card, to the schedule of service charges, to health tips for the customer. Looking specifically at the written information provided with the account material related to charges and fees, only 1 out of 15 banks gave the customer written proof of all account charges (this included fees related to minimum balance, ATM card, cheque book, account maintenance, inactivity, and closure).

**Box 3: Lack of Written Communication About Product Features, Application Form, and Redress Procedure**

| | | |
|---|---|---|
| **Case 1 (Private)** | Client | *May I have this form in Tamil?* |
| | Staff | *No, sir. If you want, you can write in Tamil.* |
| | Client | *If it was in Tamil, I can read and better understand it. You might have used technical words.* |
| | Staff | *It's not like that. You can read it easily.* |
| **Case 2 (Nationalised)** | Client | *Can I have a brochure for this savings account, madam? I can refer to the applicable charges.* |
| | Staff | *Nothing like that, sir.* |
| **Case 3 (Private)** | Client | *Suppose there is some problem who should I meet? If like you say, my account is not activated in 2 days or if there is some delay or problem…* |
| | Staff | *No problem will arise like that, sir.* |

## 4.4 Transaction costs involved in opening an account

Before having a completely functioning account, a customer is required to visit the bank at least once each for the following activities: acquiring information about the account and application procedure, submitting the application, and finally, collecting the banking materials once the account has been activated. Therefore, a minimum of three visits is required, although some customers had to make up to six visits.

As can be seen from Table 6, customers need to incur a great deal of indirect costs (in terms of time spent travelling, waiting at the bank, and collecting documents) as well as direct costs—measured as the cost of transportation and documentation. Measured as the total number of minutes spent during each visit before having a functioning account, we found that the process could take 7 hours on average, which is more than a normal working day in formal sector employment. Travelling was the most time-consuming activity during the whole process (on average, 3.5 hours in total), followed by the collection of documents required for the application (nearly 2 hours per customer). Further, when splitting up the total time spent in the bank for each visit, we found that approximately one-third of this time was spent waiting for the bank representative. This amount of time and the activities to which most of this time is dedicated to indicate the huge disincentives for customers attempting to open an account.

**Table 6: Average Costs and Time Spent Across All Visits**

| | **Initial enquiry (Visit 1)** | **Opening account (Visit 2)** | **Collecting material (Visit 3)** | **All visits** |
|---|---|---|---|---|
| Time travelling (min) | 68.45 (14.63) | 72.33 (15.79) | 71.42 (10.99) | 212.20 |
| Cost of travelling (INR) | 21.38 (3.78) | 20.2 (3.27) | 19.85 (3.88) | 61.43 |
| Time waiting (min) | 7.19 (5.88) | 11.2 (12.84) | 12.92 (12.77) | 31.31 |
| Time talking (min) | 17.55 (8.57) | 19.46 (13.7) | 22.85 (18.98) | 59.86 |
| Time for collecting documents (min)* | - | 114.67 (133.98) | - | 114.67 |
| Cost of documents (INR)* | - | 77.13 (15.94) | - | 77.13 |
| Time filling in the form (min) | - | 19.66 (9.76) | - | 19.66 |
| Number of visits | 1 (0.0) | 1.13 (0.35) | 1.21 (0.69) | 3.34 |
| Total time (min) | 93.19 | 237.32 | 107.19 | 437.70 |
| Total cost (INR) | 21.38 | 97.33 | 19.85 | 138.56 |
| *Number of observations* | 42 | 15 | 15 | 72 |

* Documents included photos and photocopies of documents required for application (e.g., PAN card, ration card).

## 4.5 Channel factors, "small costs," and stigma

The negative experiences imposed on a potential customer may be seen as part of an institutional process (which is largely discretionary) designed to discourage the take-up of a product or service that is less profitable for the firm. A sample of relevant observations from our findings that indicate this behaviour is presented in the following subsections.

### 4.5.1 Discouragement on arrival

Customers reported that during their first visit to the bank to enquire about savings products, they were greeted on arrival in only 7% of the cases. In addition to the fact that new clients are not greeted or guided on arrival, there are very few visual cues as to where to go and whom to approach for information/assistance. A designated help desk was present in only 11% of the banks visited. Partly due to this lack of visual guidance, a new client faces a nearly 35% chance of being redirected to another staff member at least once on his/her first visit.

### 4.5.2 Discouragement through time and effort

A client is asked to return to the bank on multiple occasions, taking between 3–6 visits before having a functional account. Revisits were especially common when collecting documents, with some customers making up to three visits, often for small tasks involving paperwork that could have been completed in a single visit or potentially via post. The bank could be demonstrating a lack of interest in the customer's value of his/her time (as can be seen from Case 1 in Box 4), or it could be a strategic way to discourage follow up and completion of the purchase. Further, during each visit, a client needs to spend 10 minutes on average waiting to speak to a bank representative. While this average waiting time is similar across the different visits, it can range from 0–33 minutes for the initial enquiry, to 0–42 minutes for submitting the application, and 0–50 minutes for collecting the documents. This suggests that banks are most attentive to customers when they want to sell a product, but then disregard their time on following visits. It is important to note that this waiting time is not necessarily related to the level of work activity in the bank, as customers reported that at least one bank representative was free in 47% of the cases during their first visit.

**Box 4: Discouragement through staff behaviour**

| | | |
|---|---|---|
| **Case 1 (Nationalised)** | Client | *Good morning, madam. A few days ago, I collected information to open a savings account. Here is my application form.* |
| | Staff | *You wait. I will call you.* [Note: Client waits for half an hour.] |
| | Client | *Hello madam, I've been waiting 30 minutes. I am getting delayed for my office.* |
| | Staff | *Actually, we are also busy. Otherwise, come tomorrow.* |
| | Client | *Can I wait for 5 minutes?* |
| | Staff | *I cannot give you 5 minutes. You wait. I call you.* |
| **Case 2 (Nationalised)** | Client | *Can I have this (application form) in Tamil, madam?* |
| | Staff | *It's not there in Tamil. Only English and Hindi.* |
| | Client | *There may be some terms that I don't understand. If I bring my documents, is there someone here to help me complete the form?* |
| | Staff | *There is nobody here. There is nothing else in this. Just fill it and put one sign here and one sign on the back. On this card 2 signatures. Everything else is only name, address, number that is all.* |

| | | |
|---|---|---|
| **Case 3 (Nationalised)** | Staff | *Don't pester me with your questions, I'm finding it difficult to work. Go sit there, read and fill it. I'm done talking. You have to pay INR 500. That's all. Go sit there, fill it up and then bring it. Even then, it won't get done today.. see how many people are waiting!* |
| | Client | *Once I fill in the form, who should I give it to?* |
| | Staff | *Bring [*the form back to me*].. Actually I should have given you the form only after receiving all the proof documents from you... but what to do, I have already given it. Don't keep talking, I have to work. If I don't finish the work given to me I will have to face complaints.* |
| **Case 4 (Private bank)** | Client | *[Is a basic account] not offered in your branch? My friend told me that basic savings accounts are available in all banks. I wanted to open the account because you offer good service at this bank.* |
| | Staff | *We don't offer anything like that, sir.* |
| **Case 5 (Nationalised)** | Staff | *What sir, you have become a big pain. Here my accounts are also not tallying!.* |

### 4.5.3 Discouragement through language cues and refusal to assist

As mentioned earlier, none of the banks made materials (brochures, pamphlets) in Tamil available even upon request; there was also very limited visible information, with only 2 out of the 42 banks displaying banners in Tamil about the savings products offered. Further, none of the banks where an account was opened were able to provide the client with an application form in Tamil,[18] despite the customer clearly specifying his/her inability to read or write in English. More disturbingly, when the customers asked the staff member for help with filling out the application form, only 2 out of the 15 banks where an account was opened agreed to assist the client (see Box 4 Case 2 for an example of such rejection).

### 4.5.4 Discouragement through microaggression

The results presented in Table 7 show that on their first visit to enquire about savings products, the customers rated the staff member's level of interest as "interested" in only 5 of the 20 banks and the staff's level of friendliness as "friendly" in only 7 of the 20 banks. In addition, the

[18] The RBI's 2011 Master Circular on Customer Service in Banks states: "In order to ensure that banking facilities percolate to the vast sections of the population, banks should make available all printed material used by retail customers including account opening forms, pay-in-slips, passbooks etc., in trilingual form i.e., English, Hindi and the concerned Regional Language" (Reserve Bank of India, 2011).

customers never reported an experience where the staff member was "very friendly" or "very interested." When we analysed the transcripts, we found numerous examples of insulting behaviour on the part of the bank staff (see Box 4 Case 3 and 4 for examples). The overall rating of behaviour is relatively similar across different bank types, with the foreign banks being rated relatively higher across all measures. However, the clients were also least likely to recommend foreign banks to a friend or to open an account in a foreign bank themselves, most likely due to the banks' marketing of highly unsuitable products (despite the staff behaviour being rated as relatively friendly and pleasant).

**Table 7: Rating of Staff Behaviour During Initial Enquiry Across Bank Types**

| | *Nationalised* | *SBI & Assoc.* | *Private* | *Foreign* | *All banks* |
|---|---|---|---|---|---|
| Index of staff behaviour (0-12)[1] | 6.62 (2.13) | 7 (2.5) | 7.75 (1.39) | 8.25 (2.98) | 7.1 (2.17) |
| Likelihood of recommending the bank to a friend (1–5)[2] | 2.95 (1.2) | 2.44 (1.2) | 2.48 (1.06) | 1.75 (1.5) | 2.6 (1.2) |
| Likelihood of opening an account (1–5)[2] | 3.04 (1.2) | 2.56 (1.2) | 2.13 (0.83) | 2.0 (1.4) | 2.7 (1.2) |
| Staff friendliness (1–5)[3] | 3.4 (0.93) | 3.11 (0.93) | 3.38 (0.74) | 3.75 (1.26) | 3.4 (0.91) |
| Staff explanation (1–5)[3] | 2.76 (0.83) | 2.78 (0.97) | 2.87 (0.64) | 3.5 (1.0) | 2.85 (0.84) |
| Staff interest (1–5)[3] | 3.14 (0.85) | 3 (0.87) | 3.25 (0.71) | 3.5 (1.0) | 3.2 (0.82) |
| *Number of observations* | 21 | 9 | 8 | 4 | 42 |

[1] Index of staff behaviour: 1: *staff greeted me*; 2: *staff addressed me respectfully*; 3: *staff made eye contact*; 4: *staff replied politely*; 5: *staff did not hold other conversations on the side*; 6: *staff did not leave during our conversation*; 7: *staff let me ask questions*; 8: *staff did not interrupt me*; 9: *staff answered all my questions*; 10: *staff offered further information*; 11: *staff offered advice*; 12: *staff offered help*

[2] Likelihood measure: 5 = very likely; 4 = likely; 3 = neutral; 2 = not sure; 1 = definitely not

[3] Staff rating is measured as: 5 = very friendly/explained very well/very interested; 4 = friendly/explained well/interested; 3 = neutral; 2 = not friendly/did not explain well/not interested; 1 = not at all friendly/did not explain well at all/not at all interested

## 4.6 Closing the account

Once the account was opened, the customers attempted to close these accounts after having performed only one transaction, i.e., withdrawal of the initial deposit. Surprisingly, closing an account proved just as challenging as opening it was. The customers had to make two visits on average for this purpose, with some banks requesting up to three visits. Further, the time spent talking to a staff member on these visits was 33 minutes longer on average than on any previous visit. The main explanations given by the bank staff for the complications faced in closing the account ranged from the fact that the accounts could not be closed before the end of the financial year due to quotas on financial inclusion, to the fact that banks required customers to pay closing charges.

Although none of the banks had mentioned closing charges during the entire process and only 17% of the staff members were able to justify the closing charges mentioned in the bank documentation when asked by the customer, only 3 out of the 15 banks did not charge the clients and returned their full initial deposit. As shown in Table 8, the amount retained by the banks was INR 202 on average, though this ranged from INR 0 to INR 450. Further, as a percentage of the initial deposit made, the amount kept was 22% on average, ranging from 0% to 51%. In the case of one bank, no initial deposit had been made, but the bank asked the customer to pay INR 281 for closing the account. These findings provide a clear understanding as to the high levels of account inactivity among savings products on the part of low-income households. It is evidently easier and financially wiser for an individual to simply withdraw all the money from his/her account and to not mention to the bank that they wish to close it.

**Table 8: Account Closing Procedures and Charges**

| | **Closing account (Visit 4)** |
|---|---|
| Number of visits | 2 (0.75) |
| Total time in bank at each visit (min) | 42.53 (15.25) |
| Initial deposit returned in full | 0.2 (0.41) |
| Average amount kept by the bank (INR) | 202.67 (102.91) |
| Closure charges shown by bank staff on material | 0.17 (0.39) |
| Given a proof of closure for the account | 0.87 (0.35) |
| *Number of observations* | 15 |

# 5. Conclusion

Our study set out to examine the range of costs and constraints faced by customers attempting to purchase low-cost savings accounts in order to explore whether or not these costs could partially explain the Indian households' persistent and rising preference for informal and physical savings instruments.

Our first key finding relates to the costs and constraints in accessing the Basic Savings Bank Deposit Account (BSBDA). This product is a cornerstone of India's recent financial inclusion efforts and is part of a national financial inclusion policy that is re-orienting towards a savings- and payments-led approach. Despite the BSBDA being a straightforward product with clear rules and (near universal) eligibility, in our study of the largest banks in two zones in Chennai (one of India's largest cities), we found nearly *zero effective* access to the BSBDA. Our results suggest troubling gaps between policy intention and policy implementation, which deserve close examination in other settings.

Our second key finding relates to the barriers to access for other low-cost savings products. We find that under optimal conditions—i.e., for highly motivated, employed males, with complete address and identity proof—the costs and effort necessary to purchase a basic deposit product are unreasonably high. In addition to the size of the costs, they are of a special nature. Most of the costs can be classified as "ordeals": they are pure deadweight cost on the applicant and are unrelated to the bank's efforts to match the client with suitable products. In addition, most of the costs are arbitrary, imposed at the discretion of the bank's representative, and are only tangentially related to regulatory policy or the bank's own written policies. Our findings suggest that the individual choices being made to "opt out" of formal financial savings and save in financial assets could be partly due to these costs.

Given the existing theory and the empirical evidence related to the benefits of formal savings and the role of lowered transaction costs as well as institutional bank behaviour in increasing household savings, there is a strong case to be made for policy intervention to reduce implicit costs and bank noncompliance for improving the welfare of the individuals who currently lack access to savings.

Our findings suggest a more urgent need for intervention, for two reasons. First, individual-level decisions to "opt out" are draining the financial markets of important savings that could be used for productive investment by firms and the public sector. Second, there is a "contagion effect" of misinformation and poor service that extends beyond any individual bank's behaviour (Campbell et al., 2011). These two reasons imply significant negative externalities of the “hidden costs” imposed by banks and are a strong argument for immediate intervention.

Our findings highlight multiple failures in implementation; thus, any intervention will require multiple approaches and policy tools. A complete analysis of the policy options requires further research and a detailed review. However, we would like comment on three tools that are often recommended to address the specific failures highlighted in this study. Although these three tools are an important part of a comprehensive financial inclusion policy, we do not recommend them as primary approaches to the specific problems identified in this study. First, as a primary approach, we do not recommend lightening penalties for KYC violations or lightening documentation requirements, since the evidence suggests that selective application of the rules to unwelcome clients is a greater barrier. Second, as a primary approach to the specific failures observed in this study, we do not recommend a rapid shift to direct benefit transfers (DBT), where providers receive a commission for individual transactions. Although an incentive-based scheme for banks would be part of an intermediate and long-term solution to make serving low-income customers more attractive for providers, successful government-to-person (G2P) payments require the existence of well-functioning accounts and payment infrastructure that is *effectively* accessible to low-income households, at reasonable costs. A recent review of G2P payments in four low-income countries found that implementation challenges were severely underestimated (Bold et al., 2012); a premature switch could lead to a temporary loss of the safety net coverage for a subset of households, which would weaken political will for direct benefit transfer and the digital financial inclusion agenda. Third, as a primary solution for the failures observed in this study, we do not recommend focusing on gaps in client redress and complaint systems, which would require clients to bear additional time and effort costs.

We do recommend that any set of interventions should begin with targeted monitoring and the enforcement of existing policies that are determined to have a high impact on financial access outcomes, beginning with those policies (1) that are designated high priority, (2) for which banks have a clear mandate, and (3) for which financial institutions have little discretion in implementation. One example of a high-impact policy could be the compliance of banks in accepting the minimum documentation requirements to open a bank account. Successful monitoring will involve different tactics, such as the use of independent auditors approved by the regulator and bank associations. Any successful enforcement strategy would require specific and escalating penalties for violation. Given the likely opposition by banks to monitoring and enforcement—particularly to financial penalties for noncompliance—this would be the least popular of all approaches. However, we believe the system-wide benefits will trounce the potential opposition.

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