Branchless Banking for Inclusive Finance: Challenges & Opportunities

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Agenda

- CGAP and CGAP Technology Program
- Branchless banking: overview
- Regulatory Diagnostics (Jan. – June 2007)
- Models of Branchless Banking
- Fostering market development
CGAP: Who we are

- Global resource center on access to finance issues
- Established 1995
- 33 members, housed at World Bank
- Incubate innovations, set standards, convene stakeholders
- Four year Technology Program
Technology Program

Systematic, strategic research through large-scale experiments with financial services providers

- $26m program (over 4 years) with Gates Foundation co-funding
- Incubate new approaches through advice and support to 20-30 banks, telcos, MFIs
- 10-15 “branchless banking” policy diagnostics
- Communicate lessons learned broadly to stimulate the market
What are the factors that limit access?

- High distances / low population density
- Low income relative to cost of service
- Low education and illiteracy
- Lack of credit history
- Poor product / channel design
- Narrow range of products offered

Technology approaches may overcome these constraints
CGAP Technology Program focus areas

**Regulation**
- 7-country study (DFID, GSMA)
- Follow-up with local champions

**Business models**
- CGAP projects (Gates)
- Advising market actors

**Customer adoption**
- Customer demand profiling
- Client interface research
Branchless banking: what do we mean?

Use of information technology to deliver financial services to low income people beyond traditional banking channels and making use of non-bank retail agents.

Sample withdrawal transaction

1. Agent balance
2. KYC docs
3. Cash + receipt
4. Settle accounts

Benefits along the value chain

**Bank**
- Leverage agents’ infrastructure: minimize capex to expand
- Change economics of serving poorer clients, remote areas
- Enables rapid drive to high-volume required for profitable payments business

**Agent**
- Increase walk-in business
- Decrease cash-on hand
- Fee revenue from bank
- Differentiated service offer
- Bank brand strength rubs off

**Client**
- Proximity of service point: saved time and cost
- Comfort of dealing with corner merchant
- Low-income prize safety: access to services via regulated entity

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Diagnostics (Jan. – June 2007)

- Joint DFID-CGAP-GSMA template
- 20 GSMA “level 1” reviews
- 7 in-country reviews: Brazil, Kenya, India, Pakistan, Philippines, Russia, South Africa
- In-country interviews with industry, MFIs, regulators, policymakers, consumer advocates
- Understand and advocate for balanced regulatory approach
- Notes on Branchless Banking
- Feedback already to regulators (Pakistan Notes & Roundtable, Kenya Banking Bill)
Questions to date

- Which approach(es) will endure?  Business models
- Which have potential for A2F?  Client uptake
- How should regulators respond?  Regulation

Diagnostics aimed at three questions:

How are regulators responding?
Are these responses effective?
What can we recommend?
Which technology approaches?

- Mobile phone banking and agents
- POS agent network for banking
- Deploying ATMs
- Statistical scoring model for credit
- Issuing payment cards
- Data collection thru PDAs
- Joining a shared IS
- Computerized MIS

Institutional Capacity Needed

Potential to Expand Access
Branchless Banking for the Poor

Bank-based

- Leveraging agents
- Account opening

Nonbank-based

- Leveraging agents
- Account opening
  
  and...

- E-money
- Payment systems

Other issues: Consumer protection, Data security, Competition, Taxation, FX controls, Telco regulation

Transformative vs. additive models
Bank-based model

Banking regulations amended (over time) to permit contracts with virtually any kind of retail agent

Wide range of activities to be outsourced: Cash-in/out, KYC, even loan underwriting

Customers protected because bank is liable for its agents’ actions

Supervisor has authority to inspect agents (in theory)
Business model Brazil: Bank-based

**Market impact of BCs**

- Reach all 5561 municipalities
- 12 mil accounts opened ’02-’05
- US$ 90 billion in transactions
- 1.5 billion transactions
- Replaced branches as #1 service pt
Regulatory concerns when using agents

- New risk structure:
  - Credit risk
  - Operational risk
  - Liquidity risk
  - Legal risk
  - Reputational risk

- Consumer protection against losses caused by retail agent structure (e.g., fraud, negligence, bankruptcy)

- Anti-money laundering and combating of financing of terrorism

- Supervision of banking agents
Business models Philippines: Bank-based and nonbank-based

**Smart Money**
- Launch Dec. 2000, ~ 4 mil clients
- Facilitator, not competitor, to banks
- Mastercard debit card + mobile
- 2800 “fulfillment centers” + MC merchants and ATMs
- GMT pilot with mobile remittances

**GCash**
- Nonbank-based, with e-wallet and pooled deposits
- Launch 2004, ~ 1 mil clients
- GXI regulated as remittance provider and via letters w/ BSP
- 6000 cash-in/out merchants regulated as remittance agents
- Partnership with rural banks

*Source: interviews with GXI, Smart, April 2007*
Regulation: Philippines

- Regulator engaged, but flexible
- But don’t deal w/ e-money
- KYC a potential bottleneck

- GXI: remittance agent
- Smart: broad outsourcing
- 1:1 match, funds use
- <1% of potential agents

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Business model Kenya: Nonbank-based

- 250,000 clients, 400 agents, >500m deposit/withdrawals after four months of operations
- ½ the cost of Western Union
- CBK didn’t raise objections
- Largely unregulated as
  - not regarded as banking business
  - no payments law
  - no AML/CFT law covering non-banks
Fostering market development

- Balance openness to innovation with adequate protections for consumers and financial system
- Engage providers, understand risks and how provider proposes to mitigate them
- Avoid prescribing a particular model, rather analyze models presented from the market
Fostering market development

- Competition in retail payment systems
- Pricing structure can affect expansion of network and access
- Lack of interoperability hinders expansion
Market development: what decides the future?

Biz factors decide the initial slope but…
Regulation adjusts it up or down

Biz factors:
- Technology penetration
- Competition
- Risk profile of players
- Literacy
- Language
- Familiarity with mobile

Source: CGAP analysis
Regulation: fostering and sustaining growth

**Pioneer Phase**
- Who can participate?
- Transformative models possible?

**Liftoff**
- Clients can meet KYC requirements
- Interoperability
- Consumer protection & data privacy

Source: CGAP analysis
Some conclusions

1. Regulators have interest in BB to improve access
2. Existing regulation is over- and under-protective
3. Regulation should balance openness to innovation with adequate protections for consumers and financial system (open and safe)
4. Engage providers, flexible and hands-on responses
Theme 2: Existing Regimes

Existing regulation is both over- and under-protective.

*Overprotective*
- Tight control over deposit taking (sometimes payments)
- Rules-based and law-enforcement orientation to AML/CFT

*Underprotective*
- Lack of payment system law
- Lack of e-commerce laws
- Lack of coordination mechanisms among policymakers
Theme 3: Rapid and Safe

Regulation should promote **rapid** and **safe** scaling-up of branchless banking

**Rapid:** Provide space for experiments to scale-up into durable offerings that shift the access frontier

**Safe:** Prevent avoidable disasters which damage credibility of BB with public and regulators.

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Theme 3: Rapid

For BB to scale-up rapidly…

Understand *appetite for innovation*

- Appetite: in many markets weak among traditional banks, stronger among MNOs and banks with social dimension
- Attraction is new clients, reduced costs

Law and regulation *open* and *clear* on key features of BB:

- Use of electronic channels
- Outsourcing to agents
- Client acquisition by new avenues, using risk-based KYC
- Appropriate role for nonbanks
Theme 3: Safe

For BB to scale-up **safely**...

Safeguard *confidence*: the public (and regulators) must have for BB models to become trusted ways to pay and bank.

Preventing the *avoidable disaster*:
- Highly publicized loss of funds
- Large-scale breach of data privacy
- Botched prosecution due to non-recognition of e-signatures
- Low-level but systemic fraud or theft at agents
Theme 4: Hands-on but flexible response

Developing appropriate regulation likely to be iterative, learning process

- **Value of engagement with providers:** New business models come with new or heightened old risks, and new ways to manage both.
- New players, new models and new risks call for *flexible responses* moving towards *clear guidance*
- Avoid “*over-protection*” that blunts the business case
CGAP

Building Financial Systems for the Poor

Thank you!