Digital Financial Inclusion, Scope and Policy

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ITU Arab Regional Workshop on "Digital Financial Inclusion": Policies and Regulation
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AGENDA

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What is Financial Inclusion?

ITU:

The financial inclusion means the sustainable provision of affordable financial services that bring the poor into the formal economy

ACCESS

- Availability of formal regulated financial services;
- Physical proximity;
- Affordability

USAGE

- Actual usage of financial services and products;
- Regularity; Frequency;
- Duration of time used

QULAITY

- Products are well tailored to client needs
- Appropriate segmentation to all income levels

Source: Alliance for Financial Inclusion (AFI)-2011)

What is Mobile Banking?
What is Digital Financial Inclusion?
What is Digital Financial Services?

Mobile Banking

Banking services delivered through a mobile phone. Need a bank account.

Digital Financial Inclusion

The use of ICTs and non-bank retail channels to extend the delivery of financial services to unbanked.

- Bank account not needed.
- Use of agents for cash in and cash out.
- Use mobile handsets and other digital means for transactions

What is Digital Financial Services

The use of a mobile phone to access financial services (WITH/WITHOUT bank account) and execute financial transactions. Mobile money, Mobile insurance, Mobile credit and Mobile savings are mobile financial services.

2. Mobile Money as a driver of Financial Inclusion

Access to financial services is a crucial enabler of economic and social development. Until recently, policy efforts to develop financial services focused on the formal banking sector and its intermediating function in converting savings into investment. This meant that the urban population enjoyed access to financial services while financial institutions neglected low income population segments (who generated low or negative returns) and rural areas users.

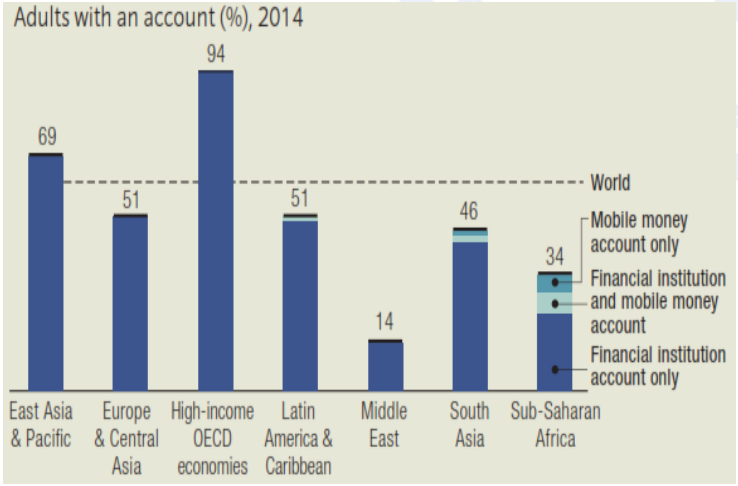
Barriers to financial inclusion on the demand side include:

- ***Affordability***, such as high interest rates on loans, high premiums on insurance products, and minimum balances on accounts;
- ***Awareness and understanding***, both as to availability of products and how they are structured, priced and used;
- ***Accessibility***, with financial products typically offered in urban centres and near high income users, and subject to heavy bureaucratic processes; and
- ***Desirability***, with many products not designed for the needs of low income users.

Source: World Bank, 1989, *World Development Report: Financial systems and development*

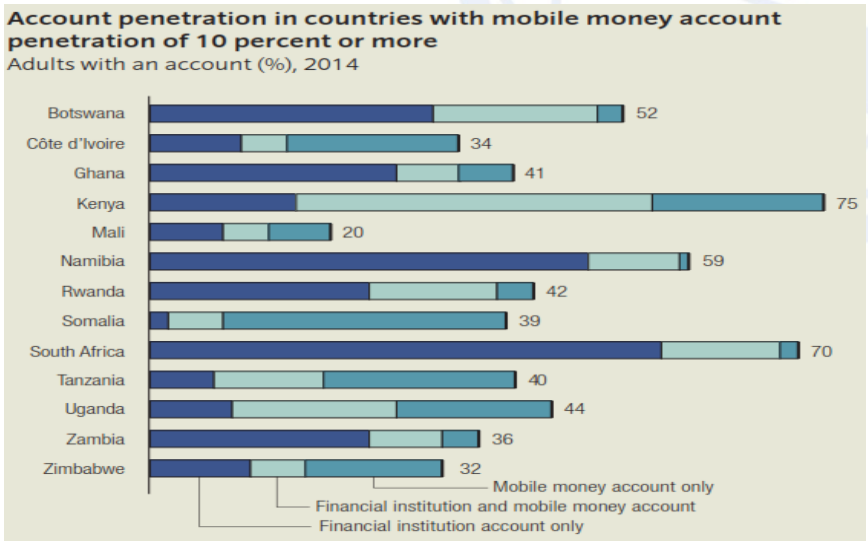
Statistics:

- The Global Findex database revealed that in 2014, 62% of adults had an account with a formal financial institution, i.e., bank, microcredit institution or mobile money provider.
- Many developing countries have very limited penetration of traditional financial services, particularly bank accounts and the range of services to which they provide access, such as transfers, payments, savings and loans.
- Between 2011 and 2014, 700 million adults worldwide became account holders and the number of adults with no account dropped by 20% to 2 billion. The establishment of mobile money accounts has been a major driver of the increase in account penetration.
- The number of mobile money accounts reached 411 million globally in 2015, having increased by about a third from 2014 (Source: GSMA, 2015).
- Mobile money is today available in 93 countries
- The figure below shows the adults with account around the world as of 2014:



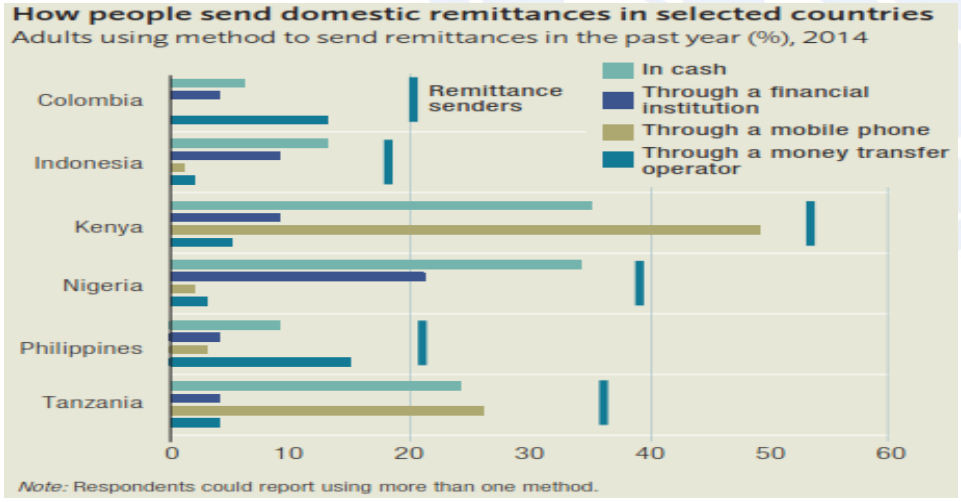
Source: Global Findex database 2014

- Mobile money accounts are making financial services available to people who previously had no access to formal financial institutions.
- Six out of seven countries where less than 20% of the population has access to formal financial institutions (such as banks) have mobile money services. More than a third of countries with mobile money services had ten times more registered mobile money agents than bank branches.
- The largest number of mobile money transactions are person-to-person (P2P) transfers (71.5% of total volume of transactions) and airtime top-ups (66%). However, only 3.6% of the value of all transactions was airtime top-ups. The use of mobile money to make airtime top-ups reduces agent commission costs for top-ups (Source: (GSMA, 2015).
- The figure below shows the account penetration by type of account:



Source: Global Findex database.

- Mobile money has been most successful in replacing cash transactions for domestic remittances, such as urban workers sending money to rural families. The fastest growing mobile money service is cross-border, led by remittances but with potential to support trade and regional integration. In Central America, Colombia, Kenya, Mexico, Philippines and Tanzania, more remittances are sent by mobile phone than in cash.
- The World Bank found that 90% of Kenyans sending remittances in 2014 did so over a mobile phone (Source: World bank, 2014).
- The figure below shows the methods of sending domestic remittances in selected countries:



Source: Global Findex database.

3. DFI-Policy and Regulation

- Policy and regulation refer to the regulatory framework within a country that governs the delivery of DFS. A regulatory framework involves several different aspects, typical services for the poor, and policies and guidelines to govern and supervise specific aspects of and guidelines ultimately govern **what types of institutions** can offer DFS, to **what extent** and in **which contexts**.
- In order for mobile money providers to continue to offer valuable services and contribute to financial inclusion, an enabling regulatory environment (a regulatory framework) is critical. In particular, having an enabling regulatory approach has a dramatic impact on both the development of a mobile money market and financial inclusion in general. Mobile network operators continue to play a leading role in delivering mobile money and deepening financial inclusion—69% of services launched in 2015 are operationally run by MNOs, and 58% of all live services are MNO-led.
- In 2015 empirical study of 22 countries found that regulation plays a key role in the success of mobile money.
- A harmonized regulatory framework for DFS is typically issued by the regulators.

The importance of good REGULATION

- The successful development of mobile financial services in the future will have a major impact on financial inclusion. For those countries still to launch services or in the early stages of doing so, a number of factors explain whether such services will take-off rapidly or flounder. One of these is regulation.
- Mobile financial services, like telecommunications, face 'network effect' dynamics common to 'platform' services. Network effects exist where the utility derived from consuming a service increases as the number of users increases. This applies both in telecommunications and payments markets. Positive feedback loops often apply so that as the number of users increases, even more are attracted to the platform.
- Furthermore, mobile money services are what economists call a 'two-sided platform'. A two-sided platform brings together two groups who need each other to generate mutual value from the collaboration. The utility of a mobile money system depends not only on the number of people to transfer and receive funds, but also on access points to the system itself for putting the cash in and taking it out (in addition to a safe and reliable transfer system). For traditional banks, these are branches and ATMs, and in mobile money they are agents.

4. DFI-ECOSYSTEM and its Stakeholders

- The mobile money ecosystem includes mobile money providers and all third-party organizations which can benefit from mobile money, either by using it as a payment mechanism or leveraging mobile money accounts.
- The mobile money ecosystem facilitates transactions from different sectors such as retail, utilities, healthcare, education, agriculture and transport, as well as insurance, savings, and credit.
- Stakeholders: International Organizations, Central Banks, Telecom Regulators, Mobile Money Operators, Payment Service Providers, DFS Platform Providers and Standards Development Bodies

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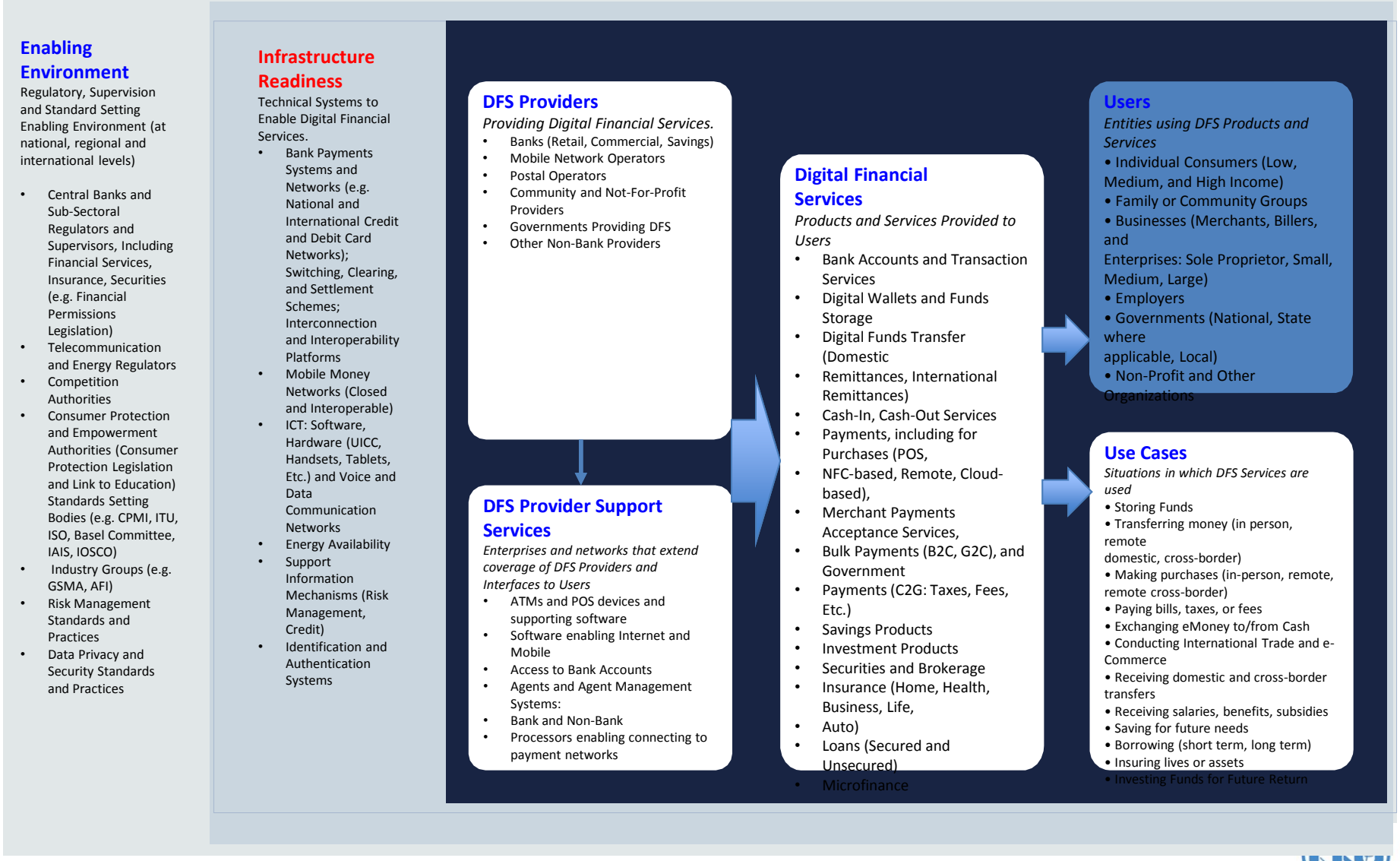
Digital Financial Services Ecosystem



Source: DFS Ecosystem Working Group – ITU DFS Focus Group

5. DFI: Key Success Factors and Challenges

Key Success Factors:

- Interoperability
- Technology impact on ecosystem
- Regulatory Dialogue (The regulatory framework is a key success factor)
- Consumer Risks
- Security Issues
- User Friendliness

Challenges Facing DFS

Unprecedented cases e.g Thin SIM for Mobile Money

Managing Competition

Dynamic Innovations requiring Dynamic Regulations

Cyber Security Threats & Fraud

6. ITU and the Digital Financial Inclusion (DFI)

- The ITU-T has a number of activities relevant to digital and mobile financial services.
- In June 2014, ITU-T set up a Focus Group on Digital Financial Services (FG DFS) for financial inclusion to foster dialogue between telecommunications and financial services regulators, and the private and public sectors (International Organizations, Central Banks, Telecom Regulators, Mobile Money Operators, Payment Service Providers, DFS Platform Providers and Standards Development Bodies), in collaboration with the Bill and Melinda Gates Foundation.
- The work of the Focus Group on Digital Financial Services (FG-DFS) is looking at four main areas: DFS Ecosystem, Technology Innovation & Competition (TIC), Interoperability and Consumer Experience and Protection. The FG DFS, incorporating 60 organizations from some 30 countries provides a unique platform bringing together regulators and stakeholders from both telecommunications and financial services to share best practices and their experience in DFS. The deliverables of the Focus Group will address a range of issues in digital financial services such as interoperability, consumer protection, competition issues, security measures for DFS applications, quality of service, big data, merchant payments acceptance, digitization of payments, DFS platform features, data protection, regulatory framework for DFS, agent exclusivity and digital identity.

ITU and the Digital Financial Inclusion (DFI)-Cont'd

- The FG DFS is expected to complete its work at the end of 2016 and transfer its key deliverables to the study groups for implementation as international standards.
- ITU-T SG3 will fold the outputs of FG DFS into its ongoing work on developing international standards in the areas of competition policy, costing and charging, and digital identity.
- ITU-T SG17 will work on the recommendations of FG DFS to develop international standards in the fields of security and digital identity. The deliverables of FG DFS on quality of service issues will be transferred to ITU-T SG12 to develop key performance indicators (KPIs) for quality of service and experience for digital financial services.
- In May 2016, the ITU-D had organized the Global Dialogue on Digital Financial Inclusion (GDDFI). The GDDFI had come up with a Collaborative Guiding Measures for Inclusive Digital Financial Services.

7. GSR-16: Best Practice Guidelines on Collaborative Regulation For DFI

Digital inclusion is one of the major challenges brought about by the digital age and it requires an inclusive dialogue across the sectors. Banking the unbanked, like connecting the unconnected, is a major milestone towards universal growth and prosperity. Leveraging on both technology and finance, digital financial inclusion through collaborative regulation can be a powerful drive towards achieving the Sustainable Development Goals.

Mr Brahima Sanou,
Director, Telecommunication
Development Bureau (BDT), ITU

➢ Unleashing the potential of two-sided markets:

We recognize that the introduction of m-payments creates a significant opportunity to spread useful and responsible services for the unbanked or underbanked people.

Innovative two-sided platforms enable digital financial services such as mobile banking, mobile money micro finance, mobile commerce and international remittance services. While regulation is not a goal in itself, various regulatory measures can be considered to leverage the potential of such platforms for digital financial inclusion.

➢ Coining new regulatory approaches:

We believe that adopting suitable regulatory framework and policies related to digital financial services will encourage services providers to reach out to the unserved and underserved.

New regulations for digital financial services should be based on a functional approach. The regulatory agencies involved in the various aspects of such services need to reassess their regulatory objectives and examine how they can best be achieved, regardless of technology or legacy market structures.

- **Addressing overlaps between sectors:**

We believe that the various regulators need to collaborate to tackle issues related to digital financial inclusion, from their inception to adoption to ensuring consumer redress.

The ICT regulator and the authorities regulating financial services as well as the dedicated competition and consumer protection authorities should know and fulfill their respective powers and responsibilities. Where their mandates overlap, specific mechanisms could be considered to ensure the interplay (such as memoranda of understanding or less formal agreements).

Good governance principles and practical solutions should be leveraged for a truly collaborative approach to regulation.

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8. Outcomes of the Global Dialogue on DFI

We, the **stakeholders** participating in the 2016 **GDDFI**, recognize that targeted collaborative approaches can go a long way towards fostering access, availability, and up-take of robust, secure and affordable digital financial services. Therefore, we have identified the following policy, regulatory, and business collaborative guiding measures to move forward the digital financial inclusion agenda by building synergies at the national, regional and global levels:

1. Develop an inclusive ECOSYSTEM for Digital financial services

Telecom/ICT and financial services regulators need to collaborate to develop consistent and proportionate regulatory frameworks in order to develop a competitive and innovative digital financial ecosystem where different providers have the possibility to lever their unique assets and capabilities to serve the bottom of the pyramid…etc

2. Encourage INTEROPERABILITY

The possibility for users worldwide to make electronic payment transactions with any other user in a convenient, affordable, fast, seamless and secure way via a single transaction account is likely to further promote financial inclusion while increasing efficiencies and competition in the marketplace.

Telecom/ICT and financial regulators and market players have a role in driving interoperability and also encourage shared access to digital platforms aimed at promoting financial inclusion. We encourage interoperability at different levels such platforms, access points, agents and customers.

3. **Encourage public private PARTNERSHIPS**

Collaboration and partnerships are critical due to the broadening of the value chain and the participation of an increasing number of actors in the digital financial ecosystem such as banks, telecom/ICT operators, agents, processors, aggregators and merchants. We call for collaborative approaches between the telecom/ICT and financial public and private actors. Public-private partnerships have the power to build synergies, foster collaboration, extend reach and enhance competition. Consequently, digital financial inclusion can expand, leverage on existing infrastructure, and lower barriers for new entrants.

Source: ITU-GSR-16 Global Dialogue on DFI

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Cont'd

4. Enable access to INFRASTRUCTURE

Financial services provided over ICT infrastructure, and in particular mobile networks, have the potential to reach in a faster and more cost effective way the underserved and unbanked, especially in rural areas. More importantly these networks can also support the provision of financial services beyond digital payments such as loans, savings, insurance that can help low income people stay/lift themselves out of poverty.

Given the importance of the ICT infrastructure, the public and private sectors need to ensure business critical technology is offered under fair terms and conditions and that to the ICT infrastructure provided is reliable, secure and of high quality to ensure a proper customer experience

5. Protect CONSUMERS and enhance consumer experience

We recognize that consumer trust is the foundation for the uptake and adoption of digital financial services. Policy makers and regulators need to ensure those services are provided in a responsible manner by putting consumers at the center of discussions and enhancing consumers experience. This may be done by adopting regulatory measures to: protect client data, provide recourse and redress mechanisms, mandate proper disclosure and transparency, require fair treatment of customers, fair cost of services, protection of customer funds, and agents.

6. Address lack of IDENTITY

We recognize that the lack of formal identity (ID) is one of the biggest barriers preventing low income people from accessing formal financial services. Governments can play a key role by determining how national (or industry specific) identity systems should be used by the digital financial services ecosystem and define how emerging biometric-based and other digital identity systems can be utilized to simplify and make more cost efficient the current "KYC" (know your customer) processes for providers

7. Promote a collaborative regulatory approach

We believe that regulatory intervention should happen only when necessary. A light touch approach should be preferred as it allows to define a framework within which the nascent DFS industry can grow organically.. Given the role played by both the financial services and telecommunications/ICT regulators it is also important they develop tools and mechanisms to ensure proper communication, consultation and collaboration. **Tools to strengthen a collaborative approach can include a memorandum of understanding (MoU) between regulatory and supervisory authorities, and the establishment of joint and multi-sectorial committees.** This collaboration and cooperation will not only benefit end users but will also impact economic growth by enabling the unbanked to take part in the digital economy.

Source: ITU-GSR-16 Global Dialogue on DFI

9. Conclusion

- Mobile Money is now available in 93 countries via 271 services (GSMA report,2015).
- More regulators are recognising the importance of creating an open and level playing field for mobile money services, although policy improvements are still required to ensure mobile financial services reach the full addressable market and achieve financial inclusion.
- In order for mobile money providers to continue to offer valuable services and contribute to financial inclusion, an enabling regulatory environment is critical.
- In 2015, 51 of 93 countries have an enabling regulatory framework.