REGULATORY ENABLERS FOR ACHIEVING UNIVERSAL FINANCIAL ACCESS

Ivo Jenik, Max Mattern

April 24, 2019

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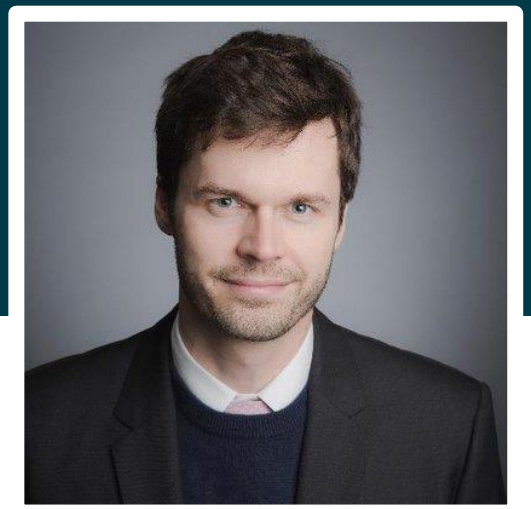
Speakers



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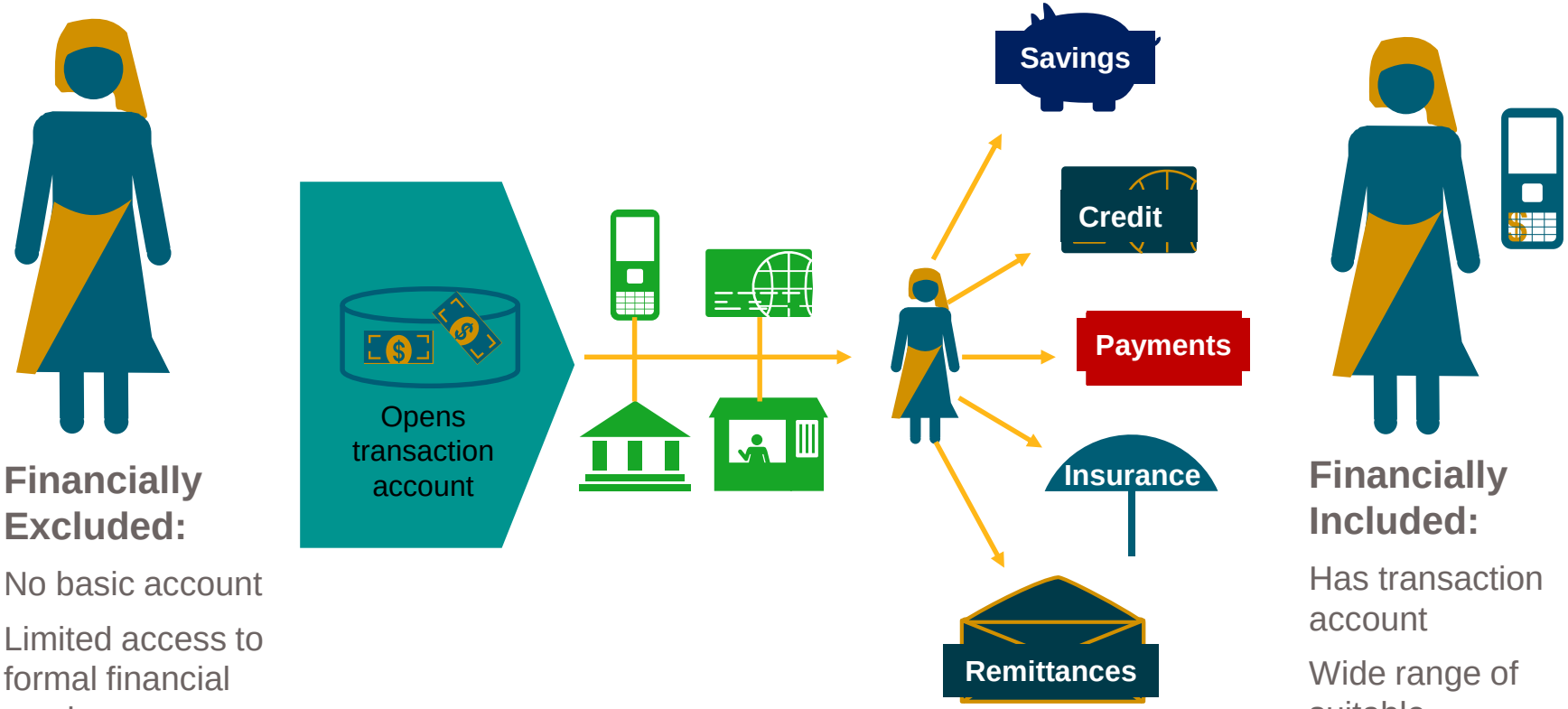
Poor people can access and use the financial services they need to advance their lives



Financially Excluded:

No basic account

Limited access to formal financial services

Cash economy

Financially Included:

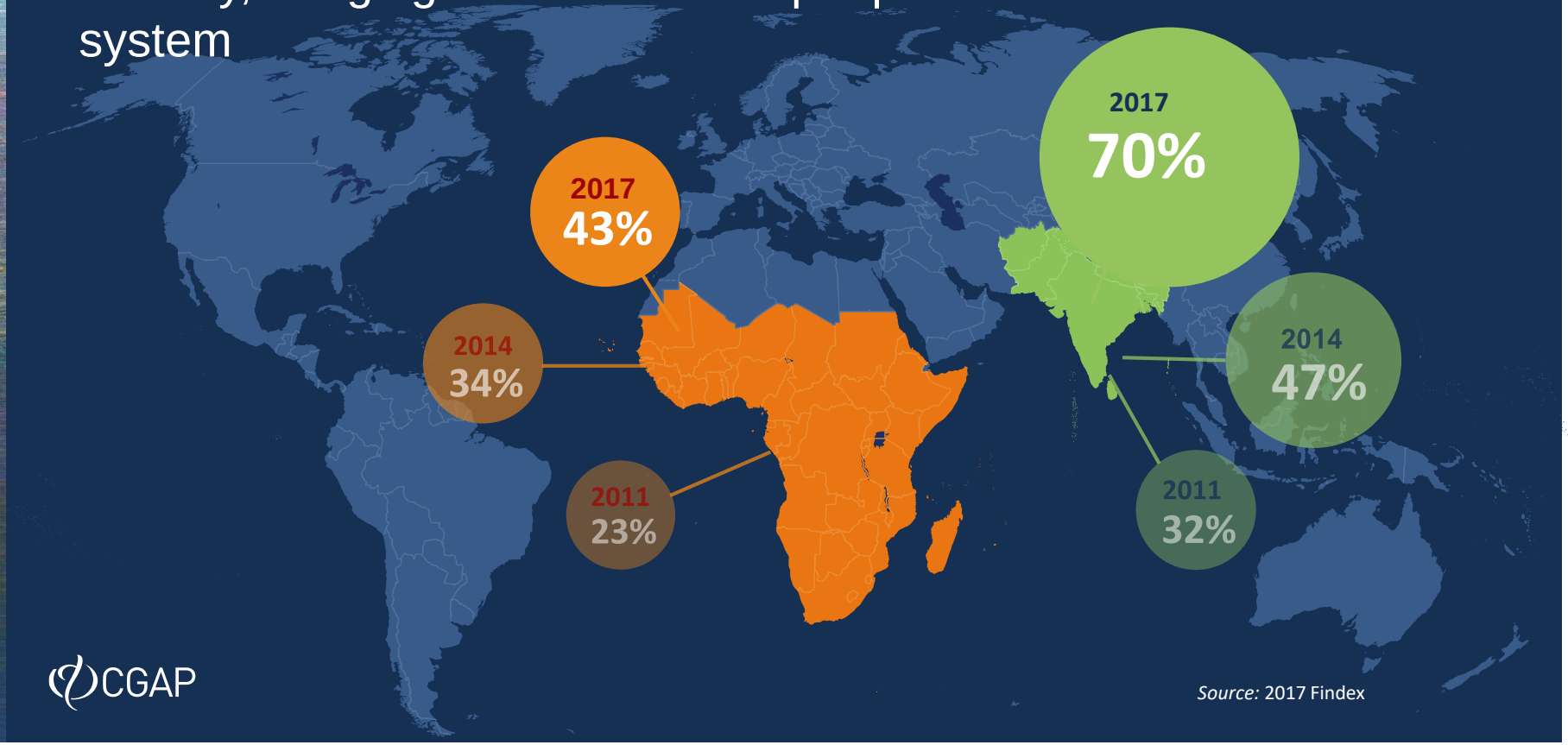
Has transaction account

Wide range of suitable financial services

Can seize opportunities and build resilience

ACCESS

Since 2011, the share of adults with an account has grown steadily, bringing 1.2 billion more people into the financial system



Source: 2017 Findex

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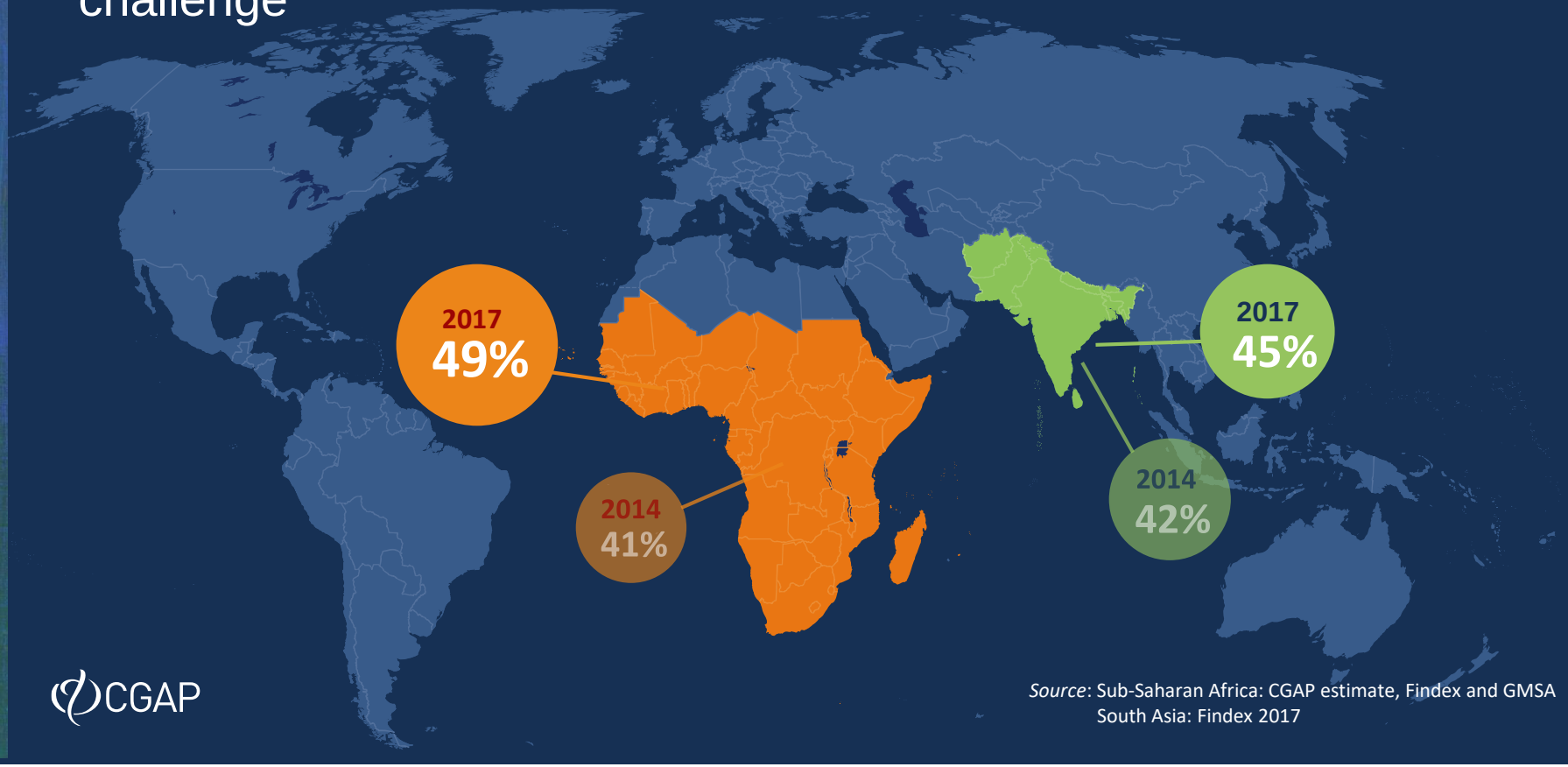
USAGE RATES LAG

Although access is growing, high account dormancy remains a challenge



Source: Sub-Saharan Africa: CGAP estimate, Findex and GMSA
South Asia: Findex 2017

To improve account usage, financial services need to be:

Convenient

Responsibly delivered

Meet the needs of customers

Affordable for customers

Sustainable for providers

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Digital financial services offer new ways to bridge the financial inclusion gap by …

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But DFS poses new challenges for policymakers:

Customer profile
Financially excluded and underserved customers are first-time users of financial services, which makes them vulnerable

New providers & business models
Services are provided by new financial institutions such as: non-banks, FinTechs and BigTechs. The services are provided through new business models, such as: crowdfunding, ICOs, and lenders using BigData analytics

Intensive use of digital technology
Financial service providers extensively rely on technology to improve speed, convenience, accuracy, access, affordability and security

Use of agents
Agents represent a significant distribution channel and physical point of contact (compared to traditional branches and ATMs)

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“What are basic regulatory enablers for digital financial services for financial inclusion to emerge and thrive?”

CGAP’s Learning Question

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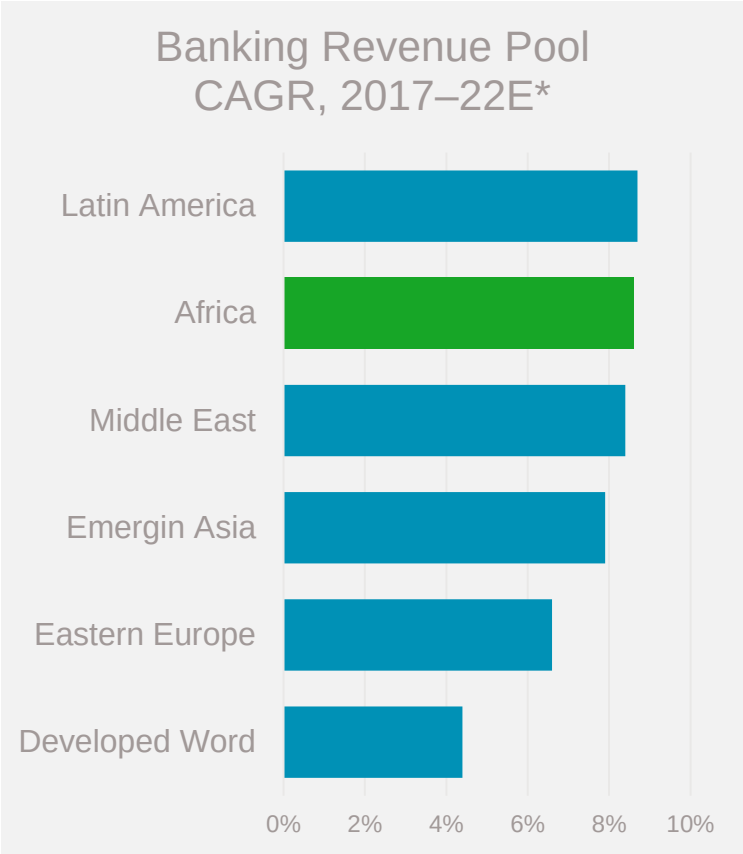
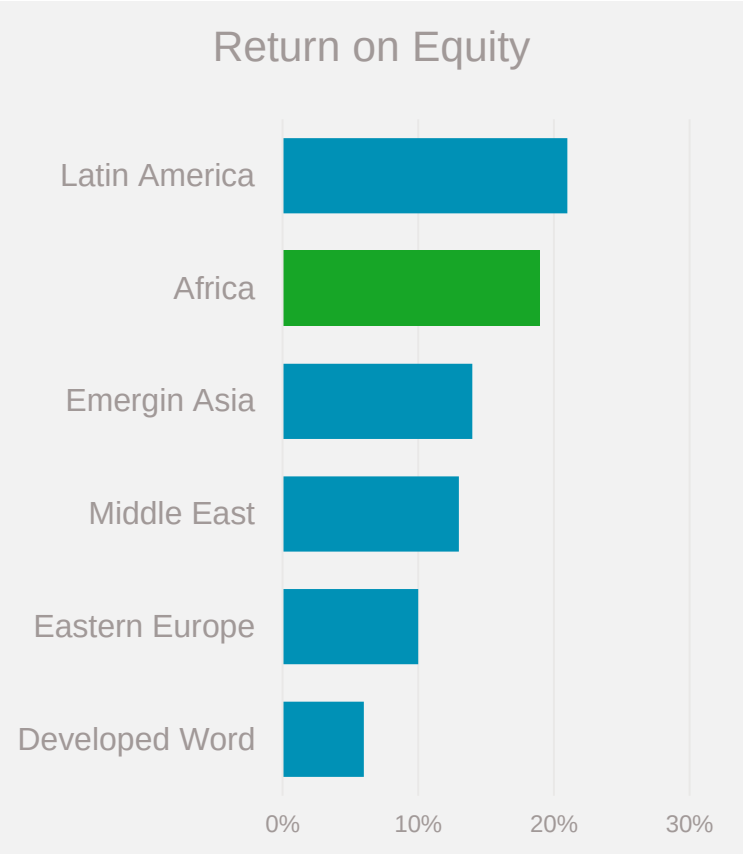
Four Basic Regulatory Enablers for DFS

CGAP identified these four regulatory enablers based on its work in 10 countries in Africa and Asia and in consultation with leading DFS providers and policy makers.

Four Basic Regulatory Enablers for DFS

Africa's banking market is 2nd fastest growing globally and 2nd most profitable

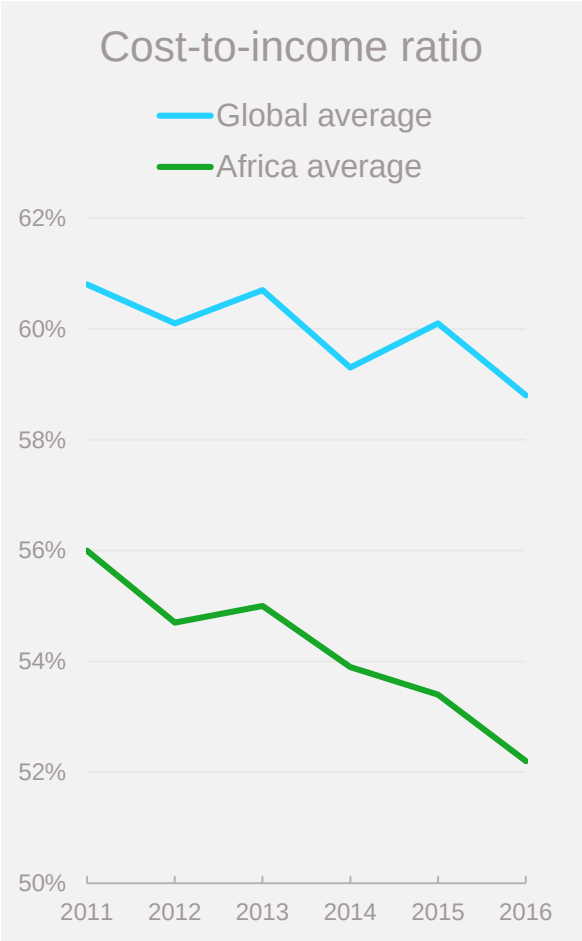


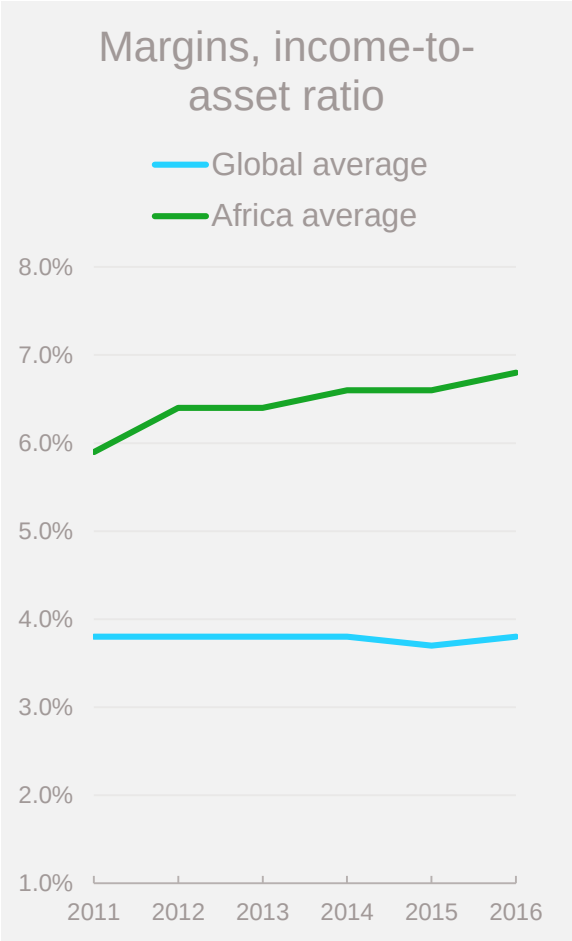


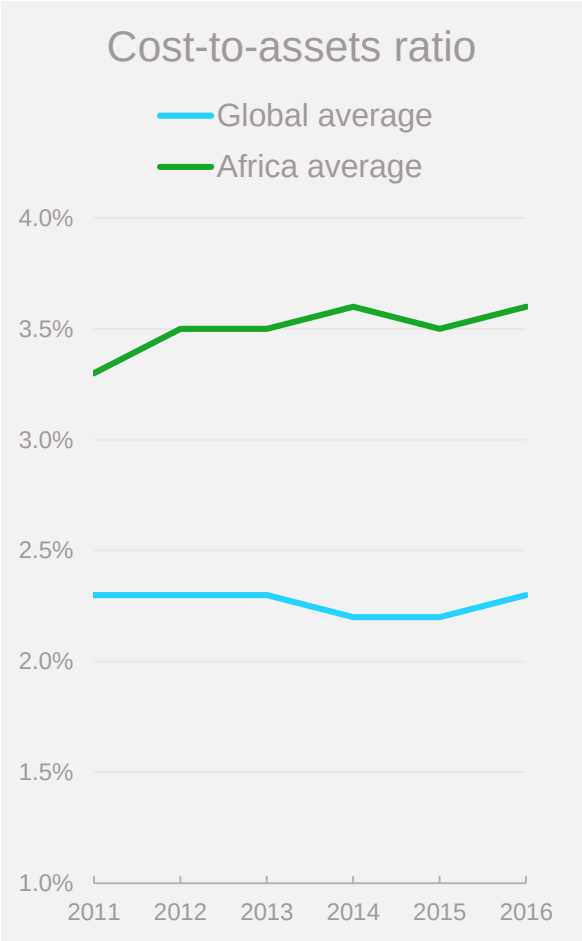
*Client-driven revenues before risk cost; constant 2017 exchange rates;
Source: McKinsey Global Banking Pools

African banks also are among the least efficient globally

The decline in cost-to-income ratio is due to rising margins rather than improvements in cost-to-assets



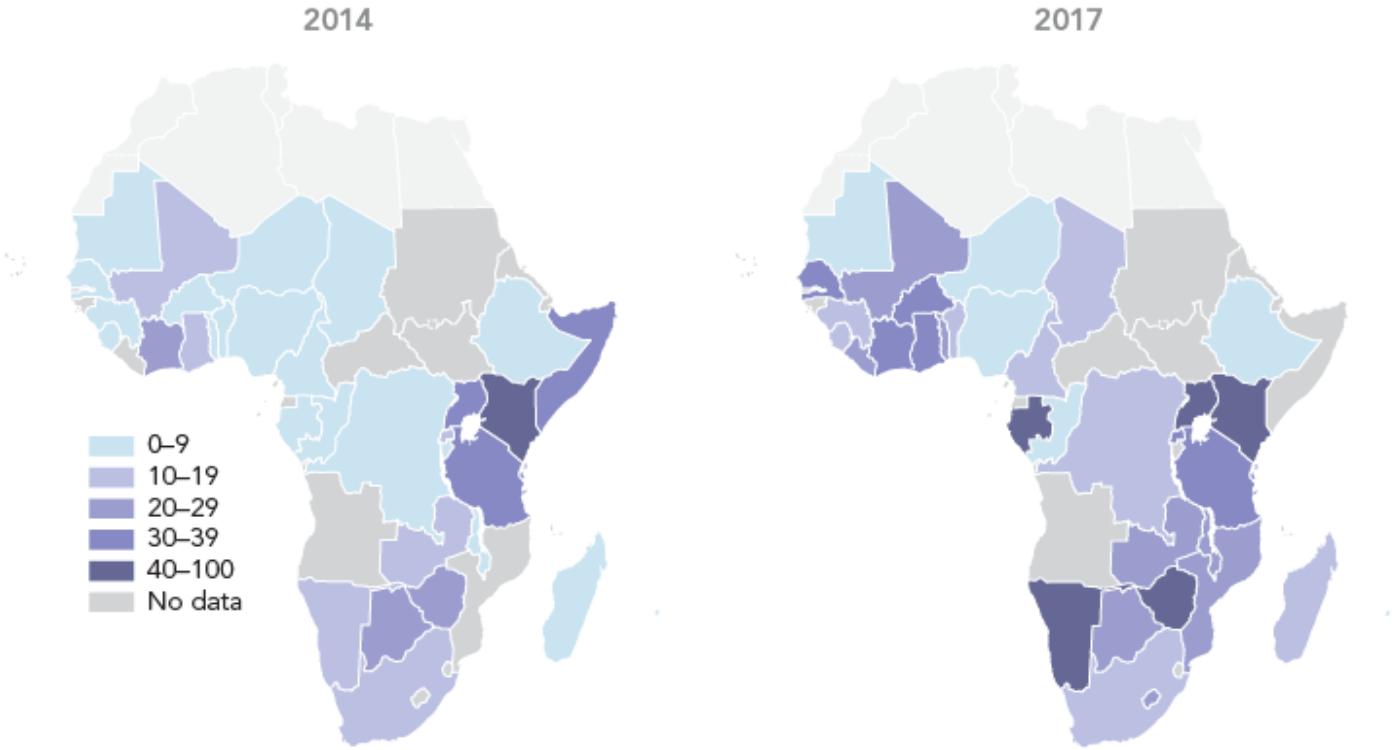




Sources: SNL; McKinsey analysis

No wonder mobile money drives progress in financial inclusion across Africa

Mobile money accounts have spread more widely in Sub-Saharan Africa since 2014
Adults with a mobile money account (%)



Source: Global Findex database.
Note: Data are displayed only for economies in Sub-Saharan Africa.

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This illustrates why e-money issued by non-banks is key to digital financial inclusion

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Regulatory frameworks for non-bank EMIs typically focus on the following areas

Legal definition of function and nature of e-money:

- Facilitates payments
- Stores value electronically
- Differs from other deposits

Authorize and regulate e-money issuers:

- Eligibility
- Capital requirements
- Permitted activities
- Protection of customer assets

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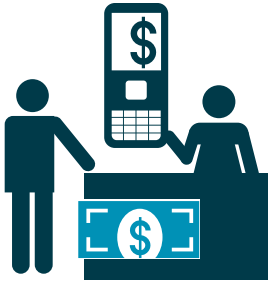
Regulators need to take into account different types of risk posed by non-bank EMIs

BANK

Balance sheet

Loan operations

NON-BANK EMI



E-money issuer

Balance sheet

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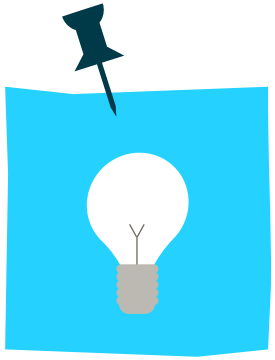
Key Points To Remember



- Non-bank e-money issuers are real game changers
- Regulation should ensure a level playing field proportional to the risks

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Four Basic Regulatory Enablers for DFS

Agents solve the distribution challenge

- Countries that allow bank and non-bank EMI agent networks have financial inclusion rates 11.8 percentage points higher than those without regulations.
- 85% of jurisdictions permit FSPs to contract with agents.

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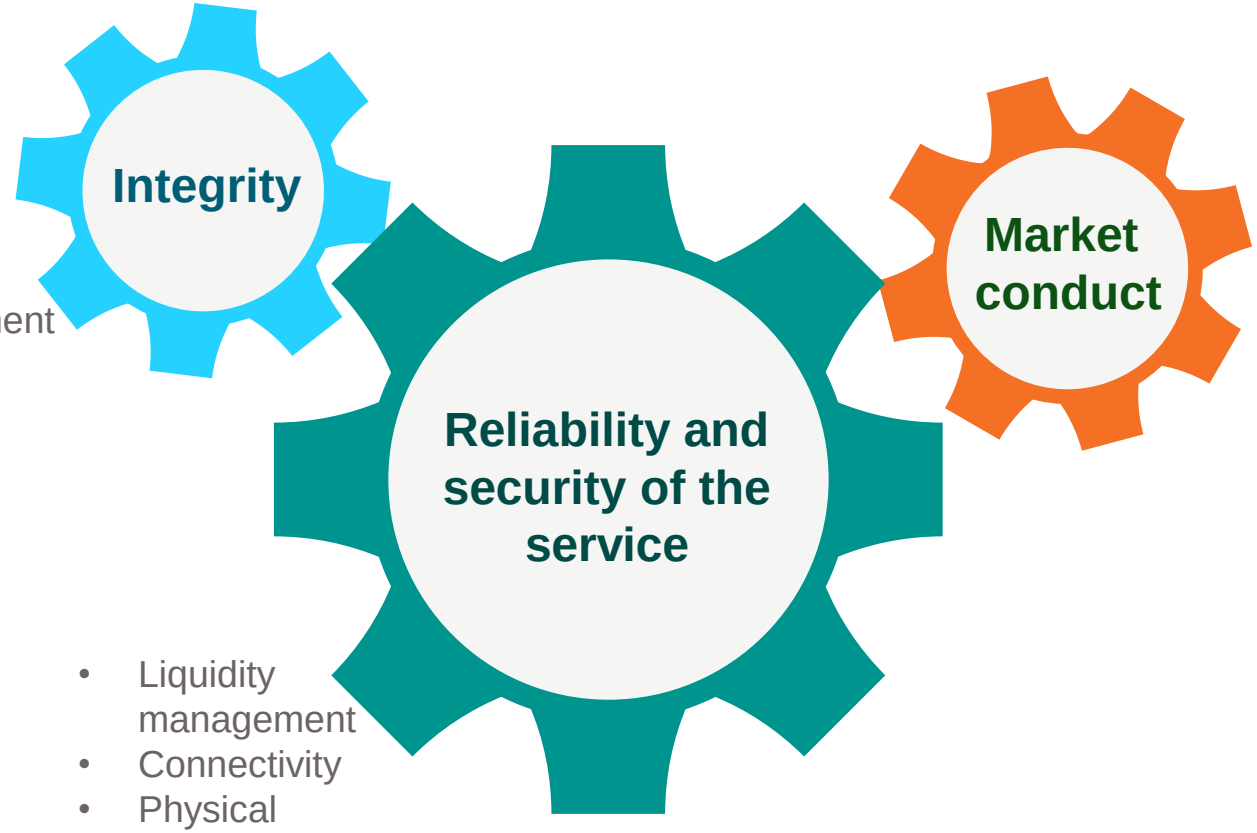
The nature of the agent-principal relationship determines three primary areas of regulation



- Fraud management
- AML/CFT

- Liquidity management
- Connectivity
- Physical security of agent
- Cybersecurity

- Consumer protection
- Transparency
- Complaint handling
- Exclusivity
- Fair treatment

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Key Points To Remember

- Agents solve the challenge of costly bricks-and-mortar branches and ATMs
- A wide spectrum of FSPs allowed to use agents works best
- Regulators may need to intervene against exclusive dealings that cause significant market distortions

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Four Basic Regulatory Enablers for DFS

Reminder of DFS characteristics that policymakers need to be aware of:

Customer profile

New providers & business models

Intensive use of digital technology

Use of agents

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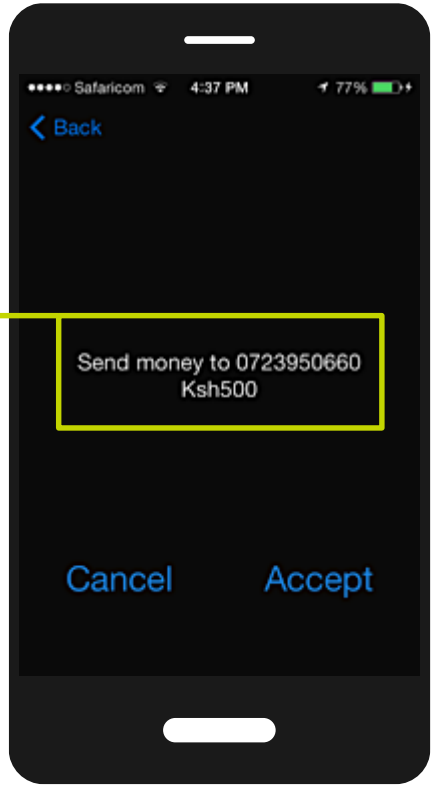
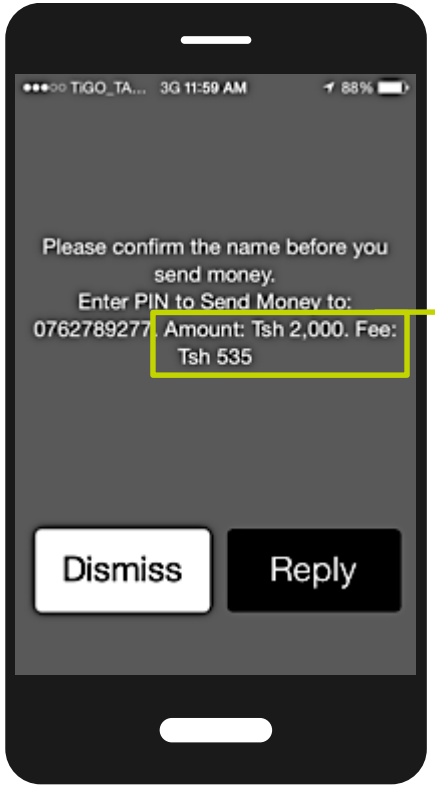
Transparency over terms and conditions for DFS

Disclosure of fees

No disclosure of transaction fee





Transaction fee clearly disclosed

Four main areas to consider for protecting consumers in digital finance

Transparency & disclosure

Protection against fraud

Data protection and privacy

Consumer recourse

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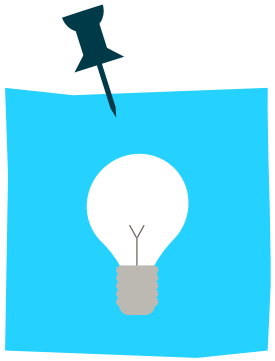
Key Points to Remember



- Effective consumer protection helps build trust in DFS
- Multiple DFS channels, products and actors introduce unique challenges
- Technology offers new ways to deal with traditional consumer protection issues

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Four Basic Regulatory Enablers for DFS

Overly restrictive CDD can hinder financial inclusion

Unnecessarily excludes customers → Grows the cash economy → Makes transactions harder to track (vs DFS) → Hinders consumer protection efforts → Undermines combatting of financial crimes → Worsens financial exclusion

AML/CFT and inclusion policy objectives are aligned with enabling everyone to use secure financial services

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Simplified CDD reduces compliance burden in line with level of risk

SIMPLIFIED REQUIREMENTS:

Full name, address, state, date of birth and gender

Information only, no physical copies

Account opened at branch, banking agent or electronically

Mexico uses tiered approach

Level 1: US $225 maximum deposits per month – no ID required (individuals only)
Level 2: US $900 maximum deposits per month – SDD (individuals only)
Level 3: US $3,000 maximum transactions per month – SDD (individuals and firms)
Level 4: No ceiling, but US $9,000 per month deposit cap where account is opened by video conference – full CDD (all).

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Key Points to Remember

- Risk-based approach to AML/CFT is essential
- Inadequate controls may allow criminal abuse, while over-designed controls may undermine inclusion and integrity
- ID systems and digital technology (e.g., eKYC) play an important enabling role

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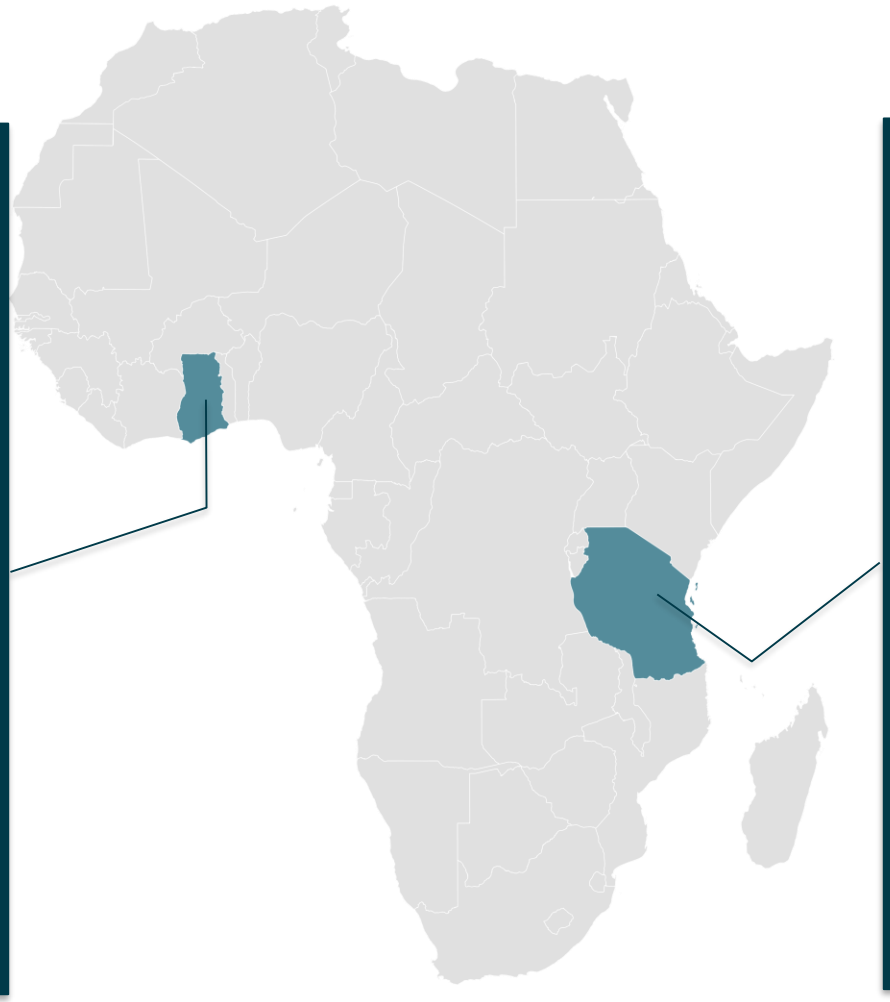
Tanzania and Ghana: Two paths to enabling regulations

Ghana

- Early regulatory framework fails to spur DFS investment
- 13% of adults have a mobile account in 2014
- Regulations revised in 2015, drive uptake of mobile accounts
- 39% mobile account ownership by 2017



Tanzania

- Early regulatory approach provides space for investment
- 32% of adults have a mobile account by 2014
- Regulations formalize enabling approach in 2015
- 39% mobile account ownership in 2017

Data Source: Global Findex


Wim Opmeer, CGAP Photo Contest

The Case of Tanzania

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Tanzania adopts enabling regulations early

- Non-banks allowed to become E-Money Issuers (EMI)
- Non-banks can build agent networks

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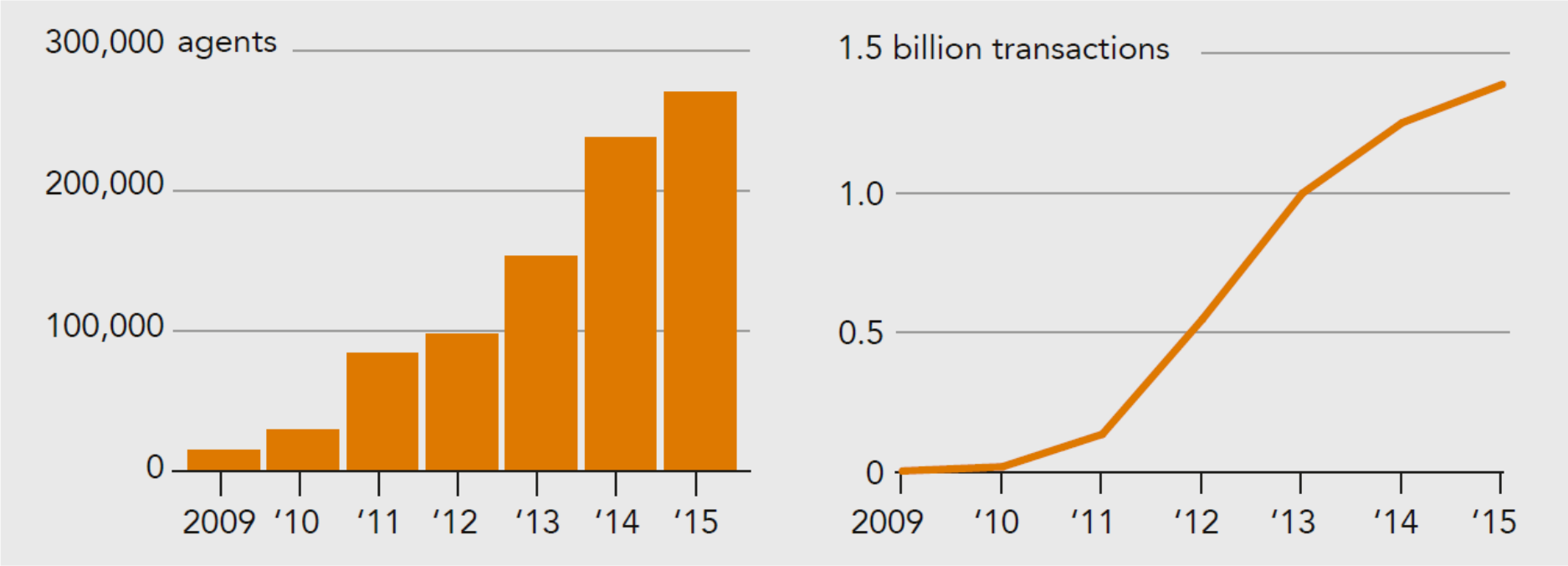
Tanzania's approach encourages early investment



Source: Bank of Tanzania

Tanzania codifies best practices in 2015

- Nonbank E-Money Issuance
- Use of Agents
- Risk-Based Customer Due Diligence
- Consumer Protection

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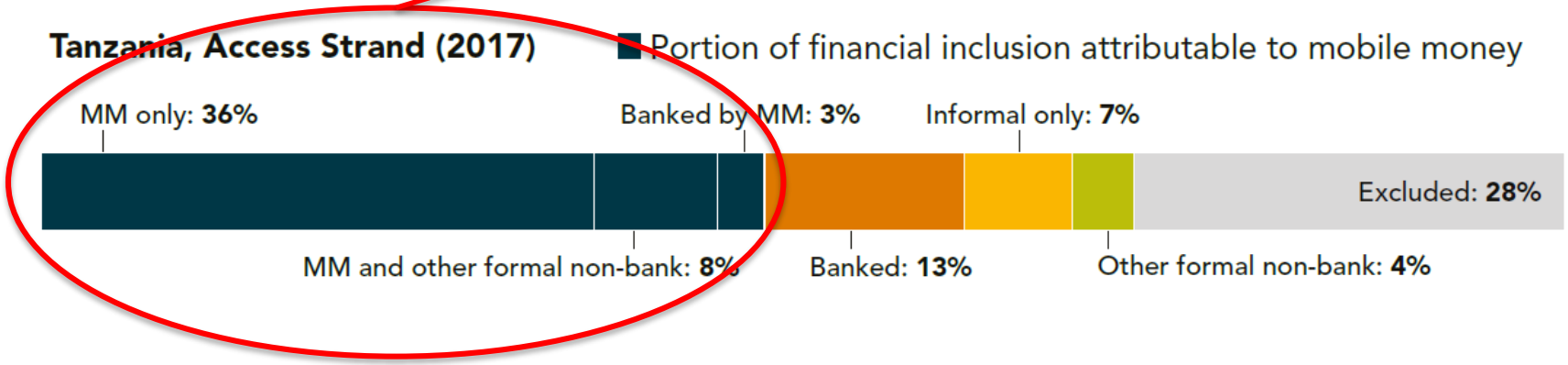
Mobile money responsible for most financial inclusion in Tanzania by 2017

Financial inclusion attributable to mobile money



Source: Finscope 2017


Brandon Smith, CGAP Photo Contest

The Case of Ghana

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"Mobile money was viewed, at best, as a channel for use only by banks and deposit-taking financial institutions."

Elly Ohene-Adu, Former Head of Payments Systems Division, Bank of Ghana

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Ghana's 2008 branchless banking guidelines fall flat

Only banks permitted to become EMIs, use agents

EMIs must consist of a partnership between at least 3 banks

MNOs serve as agents of banks, but no dialogue with Central Bank

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Mobile money struggles to gain traction in Ghana

By 2011, there were **only 100,000 active mobile accounts**

3 key problems:

- **Passive Partners:** Banks decline to take responsibility for services, invest in agents/marketing
- **Cost to MNOs**: Absent bank investment, MNOs are forced to pick up the slack but do not technically own the services
- **Communications Gap:** With no license from the central bank, MNOs have no seat at the table when discussing regulations or other issues

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"The banks were supposed to recruit the agents, they were supposed to promote the product... We were operating, but we were not operating fully."

Carl Ashie, Former Head of M-Commerce at Zain

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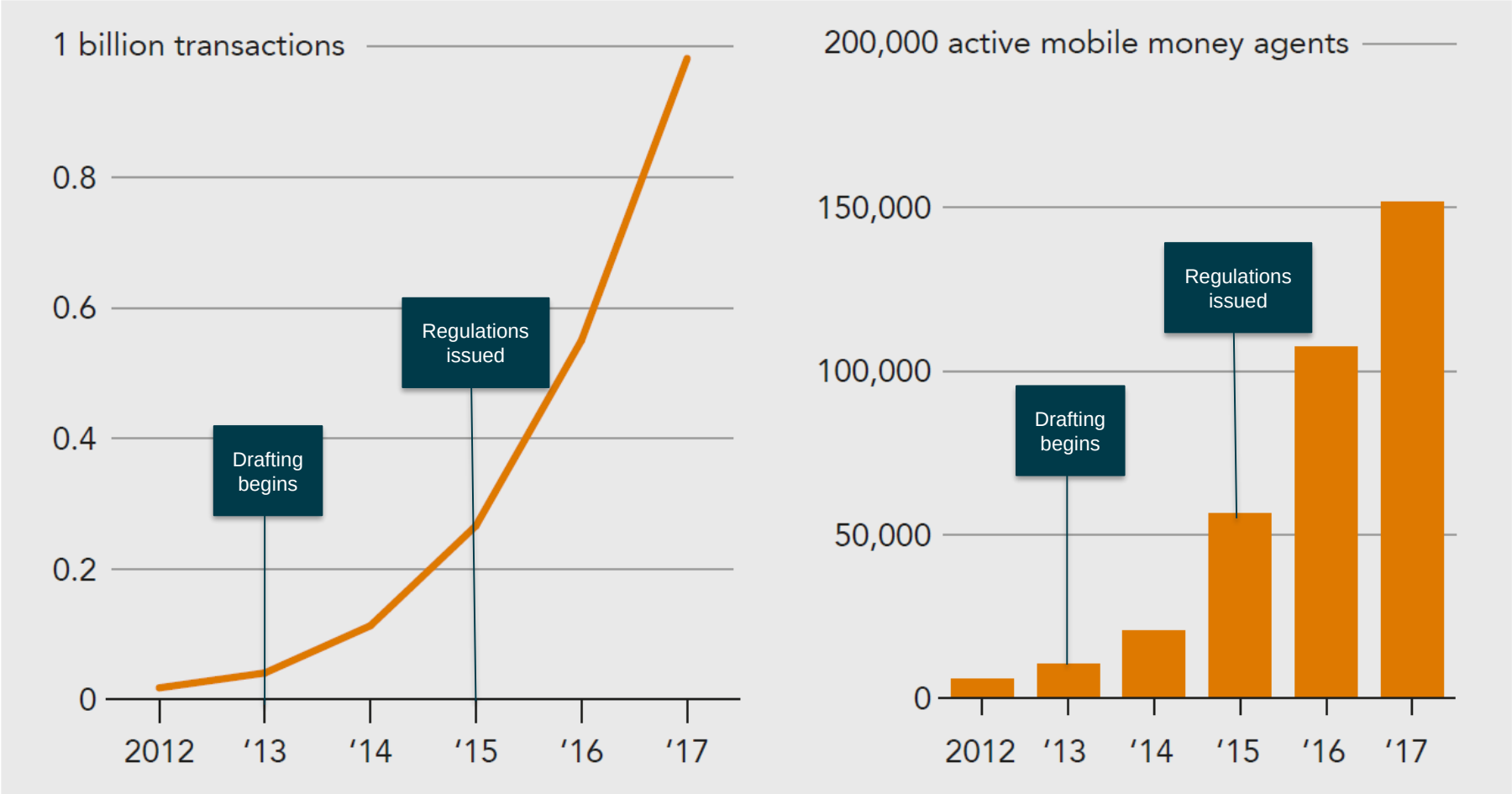
Ghana's central bank signals new approach in 2013, spurring investment and growth



Source: Bank of Ghana

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“This was what the telcos were waiting for… they just spread their wings.”

Elly Ohene-Adu, Former Head Payment Systems Division, Bank of Ghana

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Ghana issues new EMI guidelines in 2015

- Nonbank E-Money Issuance
- Use of Agents
- Risk-Based Customer Due Diligence
- Consumer Protection

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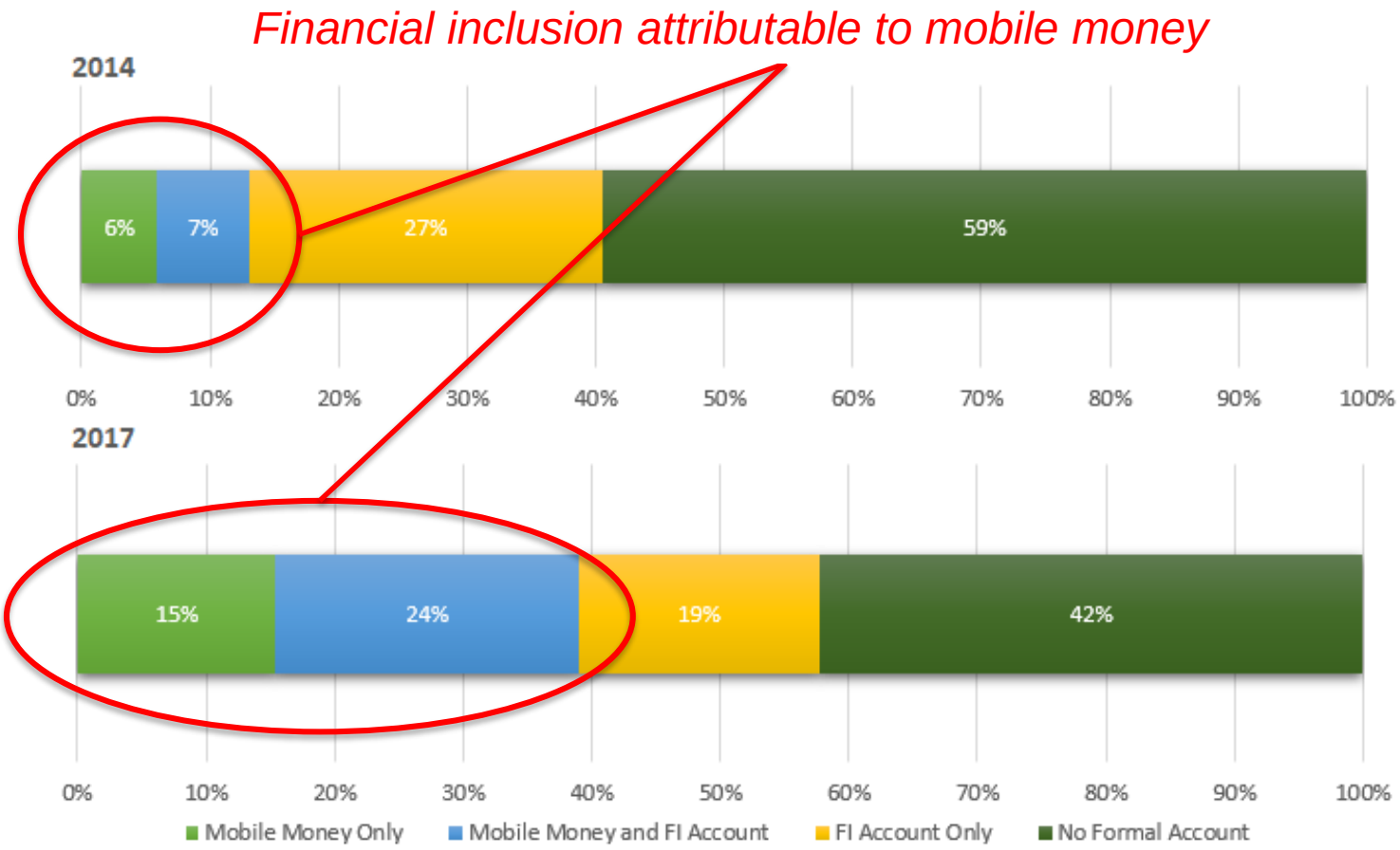
Mobile money emerges as most important driver of financial inclusion in Ghana by 2017



Source: Findex 2017


Photo Credit: Corinne Riquet, CGAP

Another example: Côte d'Ivoire

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Like Ghana, early regulations stifle investment

- 2006 e-money regulations prevented non-banks from becoming EMIs
- MNOs forced to partner with banks, expected to drive investment in services but have no control over services or communication channel with central bank
- Revision in 2015 implements regulatory enablers, allows non-bank EMIs

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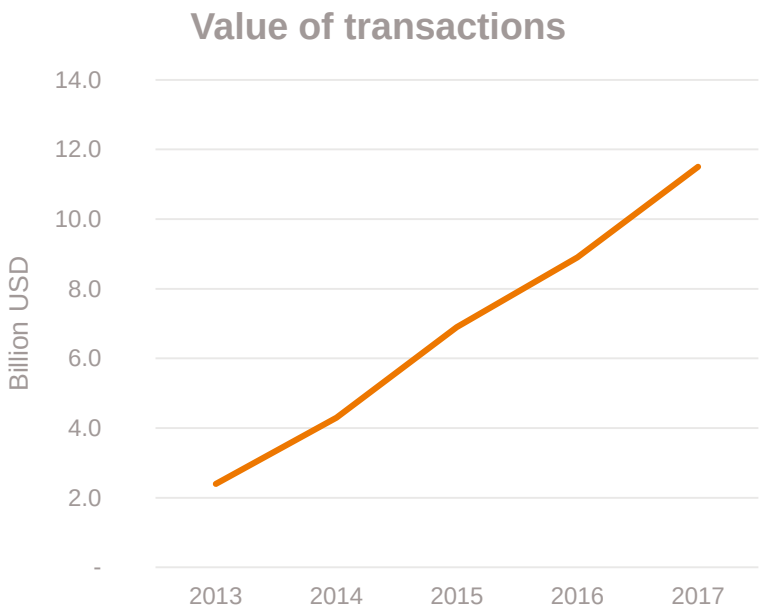
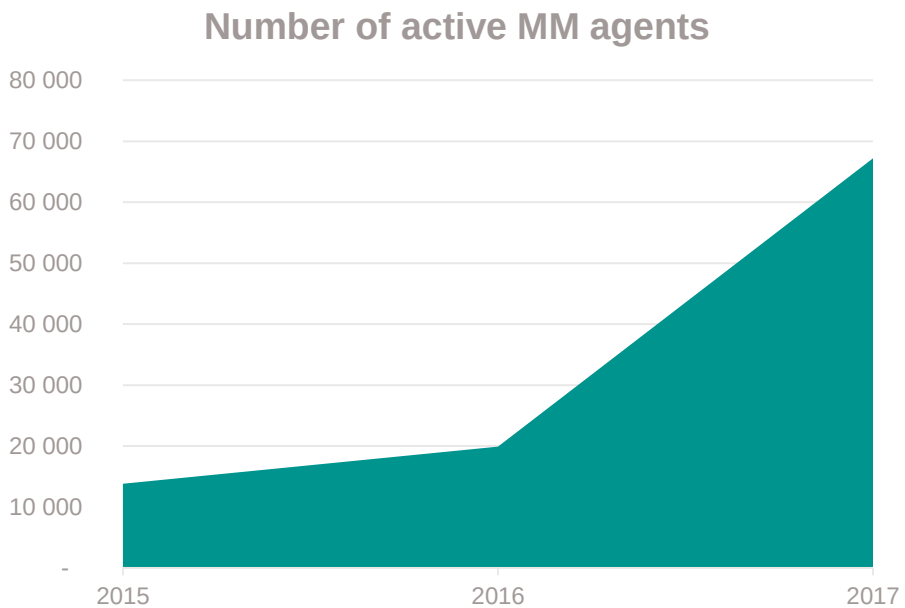
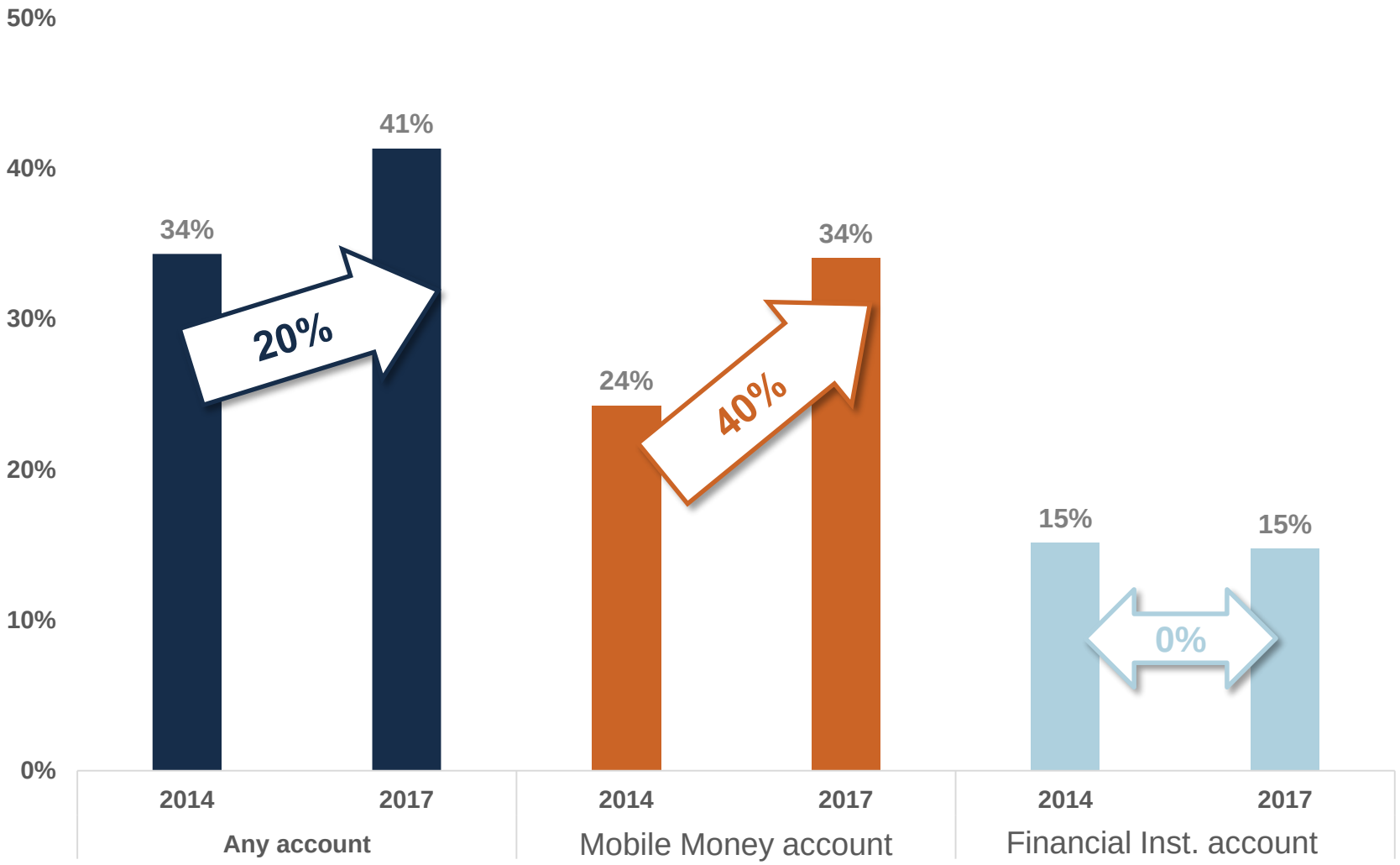
2015 regulations drive transactions, investment in agents





Source: BCEAO

Mobile money drives financial inclusion in Côte d'Ivoire



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Enablers beyond regulations

Enabling Regulatory Approach:
Regulators foster dialogue with industry and are proactive in addressing shortcomings

Executive Commitment and Investment:
Provider leadership believes in the business case and are committed to investing even in the face of early losses

Competitive Landscape:
A dynamic market exists in which a range of players compete to offer innovative services at affordable prices

Interconnected Services:
Customers can use payments accounts to transact with a broad range of account types and providers

Compelling Use Cases:
Digital products and services respond to customer demand, incentivize use

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FOCUS NOTE

No. 109
May 2018

Stefan Staschen and Patrick Meagher

Basic Regulatory Enablers for Digital Financial Services

Executive Summary

Digital financial services (DFS) differ from traditional financial services in several ways that have major implications for regulators. The technology enables new operating models that involve a wider range of actors in the chain of financial services, from design to delivery. The advent of DFS ushers in new providers such as nonbank e-money issuers (EMIs), creates a key role for agents in serving clients, and reaches customers who have otherwise been excluded or underserved. This in turn brings new risks and new ways to mitigate them.

For many years now, CGAP has been interested in understanding how these new models are regulated, and how regulation might have to adapt to enable DFS models that have potential to advance financial inclusion. This Focus Note takes a close look at four building blocks in regulation, which we call basic regulatory enablers, and how they have been implemented in practice. Each of the enablers addresses a specific aspect of creating an enabling and safe regulatory framework for DFS. Our focus is on DFS models that specifically target excluded and underserved market segments. We analyze the frameworks adopted by 10 countries in Africa and Asia where CGAP has focused its in-country work on supporting a market systems approach to DFS.

The four basic enablers are as follows:

1. **Nonbank E-Money Issuance.** A basic requirement is to create a specialized licensing window for nonbank DFS providers—EMIs—to issue e-money accounts (also called prepaid or stored-value accounts) without being subject to the full range of prudential rules applicable to commercial banks and without being permitted to intermediate funds.
2. **Use of Agents.** DFS providers—both banks and nonbanks—are permitted to use third-party agents such as retail shops to provide customers access to their services.
3. **Risk-Based Customer Due Diligence (CDD).** A proportionate anti-money laundering framework is adopted, allowing simplified CDD for lower-risk accounts and transactions. The latter may include opening and using e-money accounts and conducting over-the-counter (OTC) transactions with DFS providers.
4. **Consumer Protection.** Consumer protection rules are tailored to the full range of DFS providers and products—providing a necessary margin of safety and confidence.

Why the focus on these four elements? They arise consistently in CGAP's experience working on DFS frameworks, and their importance underscored in research and policy discussions. There is wide agreement that the four enablers are necessary (though not sufficient) conditions for DFS to flourish. This is not to deny that DFS has emerged in some markets where one or more of the enablers are weak or missing. It is also not to say that in certain cases other enablers such as healthy competition or interoperability might be equally important. But experience strongly suggests that, in any given market, DFS is far more likely to grow responsibly and sustainably and achieve its full potential when all four elements are in place. (Empirical research confirms some of these correlations.)

Through our research, we aim to understand how a range of countries has addressed the four enablers in their regulatory frameworks and to see what lessons can be learned from their experience. The countries covered are Kenya, Rwanda, Tanzania, and Uganda in East Africa; Côte d'Ivoire and Ghana in West Africa; Bangladesh, India, and Pakistan in East Asia; and Myanmar in Southeast Asia.

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FOCUS NOTE

No. 110
June 2018

Max Mutten and Claudia McKay

Building Inclusive Payment Ecosystems in Tanzania and Ghana

Over the past decade, financial services for the poor have undergone a dramatic transformation. For years, financial institutions like banks and microfinance institutions (MFIs) struggled to sustainably serve the world's poor. But advances in technology have led to innovative business models, and with them, new opportunities for expanding the reach of financial services. At the heart of this financial transformation is the rise of digital payments services through which nearly any individual or business can send or receive money in real time for almost any purpose and from nearly anywhere in the country—an inclusive payment ecosystem.

Much of this transformation can be attributed to an explosion in mobile phone ownership. According to the World Bank's World Development Indicators (2018), mobile phone subscriptions per 100 people living in low- and middle-income countries increased from just 40.61 in 2007 to 96.89 in 2016. As mobile technology has found its way into the hands of those excluded from the formal financial system—about 1.7 billion people worldwide in 2017—they have increasingly leveraged this newfound connectivity to gain access to financial services (Demirgüç-Kunt et al. 2018). Mobile money, a service that allows users to send and receive payments using their mobile phones, is perhaps the most notable example of how technology has expanded the reach of financial services. In Sub-Saharan Africa alone, there were 121.9 million active mobile money accounts in 2017 (GSMA 2017).[1] Since 2014, the share of adults with a mobile money account has grown roughly twice as fast (9 percentage points) as the share of adults with an account at a formal financial institution (4 percentage points) (Demirgüç-Kunt et al. 2018).

Because mobile money services can reach customers and maintain accounts at a lower cost than can banks or MFIs, these payments platforms have revolutionized the economics of providing financial services to the poor. Today, a range of services providers are taking advantage of mobile money networks to reach new customers and enable the provision of innovative financial and nonfinancial products and services. Banks, MFIs, and FinTechs are using mobile money rails to offer savings , loan, insurance, and other products that can deepen financial inclusion.[2,3] Organizations from outside the financial services industry, such as off-grid solar companies and agribusinesses, increasingly rely on key features of mobile money, including real-time transactions and the ability to leverage existing infrastructure, such as agent networks and mobile telephone towers, to serve low-income customers and those living in remote areas.

Despite the strong potential of inclusive payment ecosystems to drive greater financial inclusion, progress in developing these ecosystems has been uneven. In 2016, only eight countries in the world had over 40 percent of their adult populations actively using mobile money (GSMA 2016).[4,5] This raises questions as to why success has been uneven across countries. Of these eight countries, five are in Sub-Saharan Africa, underscoring the outsized importance of mobile money as a means for increasing financial inclusion in this region.

1 Active mobile money accounts are defined as having been used in the past 90 days.
2 FinTech refers to companies and businesses that leverage emerging technologies to deliver financial products and services.
3 Over 20 percent of mobile money services offer a savings, pension, or investment product (GSMA 2017).
4 The eight countries are Kenya, Tanzania, Zimbabwe, Ghana, Uganda, Gabon, Paraguay, and Namibia.
5 The number of active mobile money users is only one metric for identifying successful inclusive payment ecosystems. While this study uses active mobile money users as a proxy metric for success, CGAP also defines inclusive payments ecosystems using indicators that include activity rates among those living on less than $2/day, the ratio of male to female active users, the existence of basic regulatory enablers, supportive government policies to drive DFS use, population living within 5 km of a financial access point, and the level of competition among DFS providers.

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