What Can Branchless Banking Do to Advance the Field, and What Can It Not Do? From Mobile Banking to Point of Service

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Introduction

Today, less than 10% of the 2.5 billion people living with less than 2$ per day have access to a financial services of any kind\(^1\). As a consequence, the poor have to spend a great amount of energy and time to manage their finances. For instance in Haiti, it can take up to 4 hours simply to initiate a transfer of money\(^2\). Even saving for school fees becomes a challenge. These resources could be spent on productive activities and help these people get out of poverty.

Access to water, electricity or good transport networks are often referred to as indispensable to development. There is no doubt that financial services should be added to the list. 10% is a confounding number for such an essential infrastructure. The question is what prevents financial institutions from serving this market adequately?

Unsurprisingly, part of the answer has to do with costs: the cost to serve people outside of the main urban centers is too high. Another part relates to business models: small balances are unattractive to intermediation focused institutions. For those and for other reasons, the vast majority of poor people see their access to financial services limited to informal or semi-formal providers. They have no choice. The situation is slightly different for microcredit, although costs remain high.

This is starting to change, thanks to the pervasiveness of mobile communication services and their fast adoption by customers and businesses across developing markets. There are

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currently more than 1 billion people without an account but with a mobile phone.

Distances between people get reduced, distances between places matter less. Mobile services can take financial services outside bank branches, closer to where people live and work. The road to financial inclusion may not be straightforward but the fast adoption of mobile communications gives strong signal that progress could accelerate its course.

Branchless banking holds the promise of addressing two major hurdles to financial inclusion: lack of proximity and high costs. Building on the sustained development of mobile communications, it makes it possible for the banking sector to embrace indirect distribution via agents and for new mobile money services to reach otherwise unbanked customers. Branchless banking is therefore essentially about facilitating access to financial services (i.e. loans, savings, insurance), not about replacing these services.

This paper explores what branchless banking can bring to the field, as well as what it cannot. Let’s be clear about our focus: it is financial services. No more, no less. Financial services play an important part in development and branchless banking can help poor people take control of their financial lives, which are complex. This is not an option they have today when they predominantly use cash.

The main contribution of branchless banking is to offer poor people the ability to conduct conveniently and at an affordable price, their basic financial transactions at a retail point close to where they live and work. The main two approaches, agent banking and mobile money, rely on mobile connections for real-time communications, and often on mobile phones too.

Branchless banking offers a gateway to a population which has never engaged with financial institutions. It provides much greater access to essential financial tools in the formal sector. Usage shows those new customers trust their new micropayments services, which is essential for sustainable impact.

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Creating new points of service and offering new transactions capabilities is the opportunity. Delivering it brings challenges. It is unsettling both for the incumbent providers, the banks, and for the disruptive new comers, retailers and mobile service providers. Banking beyond branches essentially entails the unbundling of existing financial services. It requires the right enabling environment to be sustainable at scale.

The power of branchless banking goes well beyond providing access to financial services for the poor. By effectively connecting them to the rest of the economy, it puts the poor on a wider web of opportunities, through which they can expect to lead more productive lives. Other stakeholders benefit from branchless banking, among which governments and large organizations: it becomes easier for them to reach the poor with micropayments, expanding further the windfall for this otherwise ill-served part of the population.

1 – Complex financial lives

Financial services are essential for people to manage their lives; this statement is as valid for the poor as it is for the wealthier readers of this paper. Actually, it may be even more important to the poor, who need to get by with very little means. Portfolios of the Poor shows how poor people spend a great amount of resources to manage their limited financial assets. They creatively combine different financial instruments and thereby leverage a whole portfolio of solutions for their financial needs: they pay people, goods or services, save small amounts they are sometime able to accumulate, lend to and borrow from their relatives or neighbors. The average number of financial instruments used by the 250 or so poor households documented in the book is 10 in Bangladesh and South Africa, 8 in India and at least 4 across all households.

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5 Ibidem.
The main difference between the way poor and wealthier people manage their financial lives, is that the former can only resort to cash and physical assets while the latter have other options. Cash reduces poor people’s horizon to their nearest community: it is useful in an environment they trust (no risk of theft) and where they can physically be (sending cash to distant parties or locations is onerous). This drastically limits poor people’s opportunities. Cash also inevitably favors the present or very near future: holding cash is difficult and costly in inflation ridden and unsecure environments. It is also (too) easy to spend, including by demanding family members. Cash is therefore more of an impediment than an effective instrument to build a better future. Ideally, poor people should use cash by choice, not by default.

For the rest of us, most transactions within the formal banking sector are movements of electronic money, not of cash. A savings account stores electronic value. Even an ATM withdrawal entails an electronic component. It is therefore difficult to envisage how financial inclusion can be effectively addressed without helping the poor accessing that electronic world. To take a stepped approach to a complex problem, facilitating access to electronic transactions is a good starting point. Poor people may have small balances, but they transact frequently. Compared to wealthier customers, their transactions may be smaller, but they are more numerous. The turnover of funds in poor households is many times the value of their financial assets: 15 times in rural areas and 8 times in urban areas\(^6\). This is because the main financial goals of poor households are to manage their daily cash flow against irregular income, as well as to accumulate small, frequent lump sums to be able to resist shocks and to build up investments capacity.

Relying on cash to manage one’s financial life also means having little privacy in doing so: physical assets are visible, hiding money aside not necessarily discreet and travelling to a bank branch rarely unnoticed. The story of this woman in Eastern Africa who reported on the opening of an agent of a savings bank close to her home started as we would all expect it to: she could now go directly from her plot of land to the local agent to deposit or withdraw money instead of travelling to the bank branch and enjoyed the

\(^6\) *Ibid.*
proximity and saving on transport costs and time. This was not the reason for her sharing her story though. To her, there was another benefit, both simpler and much greater: she did not have to dress up nicely to conduct her financial transactions anymore, she could go to her local agent in her working clothes. She gained much privacy – and safety - as a result: no one noticed she was depositing or withdrawing. There is little doubt many other women who manage the financial lives of their households would enjoy having the same opportunity.

2 – Proximity at low cost

Branchless banking enables people to make those small transactions outside of bank branches. It saves them the inconvenience of travelling to a location, which is often far away from where they live and work: Burundi has 107 bank branches for about 8 million inhabitants. Branchless banking means that financial institutions can reach their customers through retailers and points of services located outside their normal branches.

Agent banking is one dimension of branchless banking. This ability for a financial institution to delegate customer facing activities to an agent who represent it, is not new. What is new is the tremendous opportunity to connect those agents in real-time to the financial institution they represent. This is the result of the phenomenal progress in communication technologies and in particular mobile communications which can now connect remote locations in an efficient way. It means electronic registration to new services can be processed instantaneously. It means customer depositing cash on their account at these locations can see their accounts credited securely and immediately, reducing thereby any credit risk.

Mobile communication is also essential to the other dimension of branchless banking: mobile money. This new service enables unbanked customers to open an account which they manage from their mobile phone, on which they can store electronic value and from which they can transact: receive money from others, make payments, check balances, among other functionalities. They can register for the service at small local stores, close
to where they live and work. They can also deposit or withdraw cash at these ‘cash merchants’. The service can be managed by any retail organization which can satisfy the requirements of the financial services regulator. Smart and G-Cash in the Philippines were the first mobile money services to be launched and to reach some scale\(^7\). M-PESA in Kenya is the most successful to date\(^8\). Joseph Kinyua, the Permanent Secretary Treasury in the Kenyan Government, was referring to its usage in the result of an audit done less than two years after its launch\(^9\):

“Today, many Kenyans are using the M-Pesa service to conveniently transfer money safely, efficiently and effectively. They use it for paying field staff their allowances and expenses so that they do not need to travel to the Head Offices for payment, sending a long haul truck driver money for spare parts, sending money to family members for consumer purchases, school fees payment, sending pocket money to students in schools, and sending emergency medical payments among other purposes. A taxi driver wishing to be offered prepaid services due to security reasons could request for payment via M-Pesa service. In many instances today, Kenyans traveling up-country deposit cash before the start of the journey to pick it up upon arrival to their destination thus avoiding the risk of loss through theft or robbery that has increased in Kenyan highways today”.

The mobile money provider can be a bank but not necessarily – knowing that in all cases, the funds are held by a prudentially regulated bank\(^10\). It can be a retailer; it is often a mobile network operator. First and foremost, it is a retail organization with a strong brand, a recognized competence in marketing and solid experience in distribution.

Brand, marketing and distribution are essential to both agent banking and mobile money. Contrary to what many assume – or fear - technology is not the difficult component to implement. It does matter but the service does more. Branchless banking combines the

\(^8\) Ignacio Mas and Dan Radcliffe Mobile Payments Go Viral: The Story of M-PESA
power of real time communications to the convenience and efficiency of existing local retail outlets. This is why mobile banking is very different to branchless banking and unlikely to advance the field. Mobile Banking is essentially only a mobile channel, it refers to using a mobile device to access information from or send information to an existing bank account. It adds value to banked customers. It does not help the unbanked.

By relying on existing retail outlets and deployed technology, branchless banking provides a new infrastructure with great capillarity and at low cost. It does not replace banks but adds a larger presence which helps them reach more poor customers and provides more opportunities for poor people to access financial services.

3 - Gateway to financial inclusion

To effectively move from the cash world of informal financial services to the electronic ecosystem which underpins formal financial services, poor people need to be able to convert cash into electronic money and the other way round. The objective is not to get rid of cash but to provide, conveniently and at an affordable cost, the conversion mechanism without which poor people cannot participate in formal services. This is the most difficult part of branchless banking as it is the one which requires the local points of service.

The opportunity is there, as cash is already exchanged for goods in retail stores. Merchants exchange rice, soap or oil against cash which goes in their till. They can act as cash merchant in the same way as they are also rice merchants and soap merchants. A customer cashes-in and receives electronic money from the merchant, another cashes-out and the opposite happens. The critical point here is that the merchant is more than a till: it is an entrepreneur who invests his/her own working capital in soap and rice inventory and in the shop. They do no different when they trade electronic money – they buy it in advance, as they do with rice and soap, so that they can resell it. When they take cash from a customer who wants to make a deposit they do not accept it on behalf of a third
party, i.e. a financial institution, they do it because they see an opportunity to sell something they own (electronic money) and get remunerated for providing that service. Thus, they are not an agent of that financial institution to any greater degree than they are an agent of the rice company when they sell their rice.

Once cash is converted into electronic money, it can move around electronically, cheaply across large distances. Today, poor people have to travel with their cash or use informal transfer mechanisms if they need to send money to relatives who live far away. Branchless banking allow customers to send electronic money to each other, to make payments, and for the more mature solutions to shift money between different accounts, all this without having to travel to a bank branch. When coupled with the use of a mobile phone, it also means transactions can be initiated and received at any time or from anywhere – there are no constraints of opening hours.

A third essential element of branchless banking can make a real difference to poor customers: it is the transactional account. Electronic rails on which people do single transactions, such as Western Union exist already. They are not terribly efficient. Transactional accounts give customers choices in how to manage their financial life. The simple option to keep part of the amount on the account, rather than having to withdraw everything as cash, already provides convenience and safety. It is a convenient means to store value to face short term needs and assist in managing cash-flow uncertainties. By facilitating electronic transactions, these accounts become the first step into the formal financial service sphere, where everything is stored and handled as electronic money.

Some initiatives recognize the role of the account for financial inclusion purposes, such as the Mzanzi ‘no frills’ account in South Africa. Their success is however limited. They often build on the assumption that the poor cannot afford financial services and mandate the account for free. In reality, the poor struggle with fixed price structures (i.e.

11 A minority of these accounts is used regularly and the balances remain very low. See page 3: http://www.cgap.org/gm/document-1.9.51476/CGAP_Technology_Program_Country_Note_South_Africa_Public.pdf
opening or monthly fees, minimum balances) while variable ones (i.e. per transactions) would be more appropriate.

Beyond the role of mobile in branchless banking, the uptake of mobile services shows how a population with low education and high illiteracy rates can fast embrace innovative services. It does not matter that the service is electronic. And it does not require any specific standalone education program. Educating customers is the role of the service provider, it is what they call marketing. The only requirement is that the new service meets their needs in a way that can be communicated easily and understandably. Mobile did just that in the communications space, especially with the prepaid option to reload a phone in very small increments (as low as 20 cents in Pakistan). The same thing can take place with financial services: poor customers will adopt financial services which meet their needs.

This is what happened in Kenya with M-PESA. The simple proposition to ‘Send money home’ which was launched in March 2007 by Safaricom is now used by more than 15 million customers. By the end of 2009, over 70% of households in Kenya and more importantly over 50% of the poor, unbanked and rural populations used the service\(^\text{12}\). The marketing campaign of Safaricom did a great financial education work to the point that in June 2010, 70% of the electronic transactions in Kenya were done on M-PESA. Interestingly, it represented only 2.3% in value, pressing the case further for the huge demand for very small transactions\(^\text{13}\). This possibility to use small amounts means that new customers are willing to try. The familiarity with the mobile phone helps them build trust in the system faster.

A new trusted mechanism to store and move electronic money is meant to replace storage and movements of cash, but not the relationships and organizations built to make and manage those decisions. If people have elected to join savings groups for instance, they can continue to do so at the same time as they take advantage of the efficiency of

\(^\text{12}\) http://www.mit.edu/~tavneet/M-PESA_Update.pdf
\(^\text{13}\) Central Bank of Kenya.
Branchless banking. M-PESA in Kenya for instance has a functionality for savings groups which adapted the otherwise individual account to allow the group account be managed by a few individuals. Kim Wilson explains in Jipange Sasa how it is used by a group in Kibera, Nairobi: “To withdraw cash in preparation for the meeting, the group management committee visits an M-PESA agent; each committee member punches in a PIN that only he or she knows”14. Scalable mobile money can support small community-based activities.

4 - Unbundling financial services

Financial inclusion requires a new branchless infrastructure to solve the proximity and costs problems faced by banks today. It means finding ways for the banks to reduce the cost of providing their services. They need not be behind all aspects of their services, they can let other entities do that for them. For instance the access part could be managed by a third party. It is the essence of what agent banking or mobile money is about: cash and electronic value can be exchanged in retail stores (the small cash merchants) and agents can sell basic financial services. Small transactions can be done from/to transactional accounts opened via a bank agent or with a mobile money provider. Cash is inefficient for the poor but also for banks and its customers: it is the main reason behind overcrowded bank branches. Customers have to wait a long time, whether they come for simple cash transactions or for more sophisticated operations, such as buying structured products. The bank branch should not have to deal with all the cash and the small services. It should concentrate on complex operations and sale of structured financial service, which are its core business.

Branchless banking has the potential for great efficiency gains for the banking industry. It effectively unbundles the provision of financial services. It introduces the idea that more specialization and more cooperation between specialists should be explored further if costs are to go down and financial inclusion progressed. Few other industries remain so

integrated and offer all the elements of the value chain, in a vertical manner, including distribution. It may not be a coincidence that few other sectors only serve 10% of a market.

The changes go beyond the banks and impact the entire financial service ecosystem. The prospect of having 100% of the population with access to electronic value and able to transact across distances opens up opportunities for even the smaller financial services providers. MFIs can use mobile money accounts to disburse their microloans but also to collect the repayments. MFIs are mostly about issuing small loans. Why should they worry about disbursing or collecting cash. Others can do it for them, probably better, faster and cheaper.

The unbundling approach to financial services on the supply side also means a new regulatory stance. Branchless banking does not seek any exemption from regulation and advocate instead for service-based regulation (rules vary depending on the type of the service provided, not the type of institution which provides it). It supports risk-based approaches which create an enabling and sustainable environment for all the parties involved.

Such a regulatory framework should allow branchless banking providers to open account for their customers instantly. The easier the opening of accounts, the more likely their take-up and usage. How do you open accounts instantaneously? By allowing service providers to defer strict ‘Know Your Customer’ (KYC) based on account activity thresholds. While the accounts are limited to a small balance/transactions and all transactions can be monitored and frozen in case of fraudulent use, the risks are indeed limited.

The regulatory framework should also let branchless banking providers sell services to their customers through agents which act on their behalf and/or by rolling-out a network

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15 Claire Alexandre, Ignacio Mas, and Dan Radcliffe Regulating New Banking Models that Can Bring Financial Services to All, Challenge, May/June 2011.
of cash merchants which do cash in and cash out only. In most cases today, service providers cannot operate beyond their branches or are limited to agents. Cash merchants are often regulated as agents, despite their different set up and incentives. Both categories should be recognized, regulated differently and service providers should be able to chose the retail branchless strategy they prefer.

The regulatory framework needs to enable entities, including non-banks, to get licenses to operate ‘only’ as payment service providers, e-money issuers and/or money transfer providers. These institutions would not be allowed to invest or intermediate the funds they receive and can therefore be regulated differently than a credit issuing institution (a bank). They should be regulated depending on the type of services they offer, in a manner proportionate to the specific risk of the service. A more open (but level) playing field can help spark some more competition and innovation in financial services.

5 – A new web of opportunities

Branchless banking builds on the wide adoption of mobile communications by an ever growing segment of the poor population and by all types of businesses. The core contribution is financial access. Being able to conveniently and affordably move from cash to electronic, poor people can start using a wide range of financial services provided by a broader range of financial institutions. For instance, in addition to visiting the few providers located close to where they live, mobile money users can solicit business from other providers further away, thereby increasing competition on the supply side and their chance to get a good service or product. Poor people get a wider range of opportunities, far beyond the few kilometers around where they live.

Services which were difficult for the poor to access and use are now within reach. Savings is one obvious example. People are unlikely to travel to a bank to deposit a small

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amount every week or couple of days. If they can send the sum electronically, or deposit it in cash at their local banking agent, then distances do not matter anymore. Some M-PESA customers have started to do just that since mid 2010 when M-KESHO was launched\textsuperscript{17}: Equity Bank offer them a savings account which they can fund through their M-PESA account. If the market has been good and a seller has made a bit more money than usual, he or she can send the little extra from their M-PESA account onto their M-KESHO savings account for safe storage, earning interest. No need to go to an Equity branch and wait for it to open, M-PESA works day and night.

Enabling payments across distances, especially in time critical situations, can have an important impact on people’s lives. In Tanzania where Vodacom offers a mobile money service also called M-PESA, the staff of an NGO (CCBRT) “locate people requiring medical help and alert CCBRT, which transfers the money to pay for the person’s bus fare by M-PESA”. Since the start of the scheme, “they have quadrupled the number of cleft lip surgeries and more than doubled the fistula surgeries in less than one year\textsuperscript{18}”.

Branchless banking also represents an opportunity for large organizations, private and public, which need to make micropayments to poor people. They too have to rely on cash today. And they too would love to find other options and use electronic means to pay. Within the development community, conditional cash transfers programs usually comes to mind but the point is here much wider. It is all government payments (salaries, pensions, safety nets…), all large employers’ salary payments, etc. Being able to make all these payment electronically has great benefits. A study made in India about the benefits of e-payment to Indian Society concluded that “an electronic platform for government payments to and from individual households could save an estimated USD 22.4 billion a year – almost 10 per cent of the total payment flows between the government and households” and adds that E-payments may well ensure that every poor household in India – approximately 80 to 100 million – will have unparalleled access to secure and convenient benefits directly from the government, and without the interference of

\textsuperscript{17} www.equity.co.ke
\textsuperscript{18} http://www.cbm.org/programmes/CCBRT-275774.php
intermediaries.” Electronic payments can be more efficient for the sender but also for
the recipient, who is more certain to get the whole sum, and to receive the funds faster.
The mobile network operator Roshan is offering the mobile money service M-Paisa in
Afghanistan. In 2010, they started a project in which the Afghan National Police
disbursed salaries using M-Paisa. Many policemen received their full salary for the first
time and assumed they had got a salary raise.

Conclusion

The contribution of branchless banking to the field is multifaceted and offers solutions
for both clients and providers. By focusing on access, these new platforms have the
potential to be real springboards for the poor to effectively manage their financial lives in
a safe and efficient environment and more realistically aspire to more productive lives.
By providing access to financial services as well as choice, branchless banking can
impact financial inclusion. It can also contribute to progress on financial security and
integrity by bringing more people into the formal and electronic sphere and reducing the
usage of cash which is difficult to oversee.

This exciting potential cannot hide the fact that branchless banking is very hard work and
no silver bullet has been found yet. No matter the thrilling examples of impact and
progress distilled throughout this paper, the current status of branchless banking in April
2011 is not brilliant. We are still in the proof-of-concept stage. Except in East Africa
where Kenya’s neighbors Tanzania and Uganda are showing now promising signs of
success in their mobile money deployments and in some Latin American where agent
banking is making some progress, the picture is pretty blurred. On the policy front,
awareness for financial inclusion has never been as high on the global agenda, however
congrete regulatory progress at national level are scarce. The point here is not to give up

but to stress that branchless banking is difficult and requires a bit more than a few mobile handsets.

Branchless banking won’t solve all the problems of the poor or the problems of all the poor but it deserves some credit for putting this segment of the population center stage, within a connected network open to all customers, not only poor ones, and by giving them choices to decide for themselves.

Branchless banking is fundamentally about access and creating new channels. It is a very important infrastructure for developing countries. Equally, we should not lose sight of the financial products which can be reached through these channels and recognize that lots of work still needs to be done on that front.
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