



Universiteit van Pretoria
University of Pretoria



GORDON INSTITUTE
OF BUSINESS SCIENCE

Strategies for optimising financial inclusion in South Africa

Mindy Mloi

2860840

A research project submitted to the Gordon Institute of Business Science, University of Pretoria, in partial fulfillment of the requirements for the degree of Masters of Business Administration.

11 November 2009

ABSTRACT

An underlying premise of this study was that the formal financial sector has an important role to play in the process of assisting the development of South Africa's disadvantaged communities, especially those living in poverty. The study explored the construct of financial inclusion and sought to understand what measures are being taken by South African financial services institutions to optimise financial inclusion. Through secondary data analysis, the study investigated instances of the construct in other geographies and sought to compare and contrast what was being done in those geographies, with what is being done in South Africa. The study concluded that while the lower segments of the market are relatively uncharted territory for South African financial services organisations, the strategies that are being employed to service these markets seem to be a combination of strategies that are being employed in other geographies around the world.

Based on evidence from the analysis of the various geographies and face-to-face interviews with industry practitioners from some of the larger financial services organisations in South Africa, the study proposed some additions to the way in which product development processes are carried out within financial services.

DECLARATION

I declare that this research project is my own work. It is submitted in partial fulfillment of the requirements for the degree of Master of Business Administration at the Gordon Institute of Business Science, University of Pretoria. It has not been submitted before for any degree or examination in any other University. I further declare that I have obtained the necessary authorisation and consent to carry out this research.

Mindy Moloji

11 November 2009

ACKNOWLEDGEMENTS

I would like to acknowledge, with thanks, the support and encouragement of a number of people, without whom, this research report would not have been possible:

I would like to dedicate this report to the memory of my father, who always encouraged me to be the best I can be.

To my supervisor, Gavin Price, I would like to express my sincere gratitude for the many helpful suggestions that led to the completion of this research report. I would also like to thank Prof. Margie Sutherland, who helped me to determine my research topic.

To my family (my husband Seati, and my mom) thank you for the constant encouragement during the course of this undertaking. Without your love and support, the last two years would not have been possible.

A number of individuals helped provide contacts at the various companies – thank you for taking the time to help introduce me the interview candidates who made this research possible. To the organisations that were instrumental in the completion of this research report – thank you.

I would also like to thank Dotty Mantzel, who did the final proofreading of this text and whose contribution was indispensable.

TABLE OF CONTENTS

1.	Chapter 1: Introduction to research problem.....	1
1.1	Introduction	1
1.2	Banks' reluctance to serve the poor	2
1.3	The bottom of the pyramid in South Africa's banking sector	3
1.4	Scope of research.....	5
2.	Chapter 2: literature review	7
2.1	Financial inclusion.....	7
2.2	Unbanked and underbanked markets	9
2.3	South Africa's formal financial infrastructure	10
2.3.1	Institutional infrastructure	11
2.3.2	Organisational infrastructure	11
2.3.3	Support infrastructure.....	12
2.4	Strategies for serving the bottom of the pyramid.....	13
2.4.1	Mine and translate local market information.....	13
2.4.2	Adapt the business model to community realities	14
2.4.3	Change internal incentives and challenge cultural assumptions	15
2.4.4	Create partnerships and strategic alliances	15
2.4.5	Improve the enabling environment.....	16
2.5	The Mzansi Initiative	18
2.5.1	Reputational risk	19
2.5.2	Financial risk	19
2.6	Legal boundaries of collaborative action	21
2.7	The Grameen model	21
2.8	Mobile phone banking for meeting the needs of the unbanked and underbanked	23

2.8.1 Mobile as a gateway product	26
2.8.2 Mobile phone banking adoption framework.....	28
2.9 Correspondent banking arrangements for meeting the needs of the unbanked and underbanked	29
3. Chapter 3: research questions	32
4. Chapter 4: research methodology.....	34
4.1 Research Design.....	34
4.2 Unit of analysis.....	34
4.3 Population of relevance.....	35
4.4 Sampling method and sample size of relevance.....	35
4.4.1 Sample.....	35
4.4.1.1 Sampling method.....	36
4.4.1.2 Sample size	36
4.5 Data gathering process	36
4.6 Data analysis	36
4.7 Research limitations.....	37
5. Chapter 5: results.....	38
5.1 Secondary data – country studies of the unbanked and underbanked	38
5.1.1 South Africa’s unbanked and underbanked markets.....	38
5.1.2 Botswana’s unbanked and underbanked markets	40
5.1.3 Kenya’s unbanked and underbanked markets	42
5.1.4 Brazil’s unbanked and underbanked markets	44
5.1.5 India’s unbanked and underbanked markets	46
5.1.6 Europe’s unbanked and underbanked markets.....	48
5.1.7 The USA’s unbanked and underbanked markets.....	49
5.1.8 Mexico’s unbanked and underbanked markets.....	51

5.2	Mobile banking for the unbanked and underbanked	54
5.3	Interview results	56
5.3.1	The factors that have an impact on financial inclusion in South Africa.....	56
5.3.2	Enabling environment: The efficacy of the three components of the environment that exists in South Africa’s financial services market.....	59
5.3.2.1	Institutional infrastructure.....	59
5.3.2.2	Organisational infrastructure.....	62
5.3.2.3	Support infrastructure	63
5.3.3	Leveraging technology to optimise the provision of products and services to the unbanked and underbanked	64
5.3.4	Leveraging the retail store network to optimise the provision of products and services to the unbanked and underbanked	66
5.3.5	Optimising product design to meet the needs of the unbanked and underbanked....	68
5.3.6	Transaction versus credit products for meeting the needs of the unbanked and underbanked	71
5.3.7	The profitability and sustainability of service and product offerings for the unbanked and underbanked	72
5.3.8	Examples of service and product offerings for the unbanked and underbanked and the reasons for success or failure	75
5.3.9	Broadening of products and services	79
5.3.10	Emergent themes on financial inclusion	79
6.	Chapter 6: discussion of results	82
6.1	The factors that have an impact on financial inclusion in South Africa.....	82
6.2	Enabling environment: The efficacy of the three components of the environment that exists in South Africa’s financial services market.....	83
6.2.1	Institutional infrastructure	83

6.2.2	Organisational infrastructure	84
6.2.3	Support infrastructure.....	85
6.3	Leveraging technology to optimise the provision of products and services to the unbanked and underbanked	87
6.4	Leveraging the retail store network to optimise the provision of products and services to the unbanked and underbanked	88
6.5	Optimising product design to meet the needs of the unbanked and underbanked....	89
6.6	Transaction versus credit products for meeting the needs of the unbanked and underbanked	90
6.7	The profitability and sustainability of service and product offerings for the unbanked and underbanked	91
6.8	Examples of service and product offerings for the unbanked and underbanked and the reasons for success or failure	92
6.9	Conclusion	93
7.	Chapter 7: conclusion	95
7.1	Optimising product design.....	95
7.2	Suggestions for future research	97
7.3	Limitations of this study.....	98
8.	Reference list.....	99
9.	Appendices	106
	Appendix 1 – Discussion guide – phase 2 of research.....	106
	Appendix 2 – Examples of other private sector experimentation and innovation	109

TABLE OF FIGURES

Figure 1: The economic pyramid..... 4

Figure 2: Landscape of financial services available to South Africans..... 10

Figure 3: The 4 As..... 17

Figure 4: Cumulative net direct revenue from Mzansi and NEA (US\$) 20

Figure 5: The overlap of banking and mobile use 24

Figure 6: Percentage of South African adults with a bank account pre-Mzansi, 1994 – 2003 39

Figure 7: Segmenting South Africa's market for retail transactional, savings and banking 40

Figure 8: Financial Inclusion in Kenya, 2007..... 43

Figure 9: Unbanked and underbanked percentages of U.S. adults..... 49

TABLE OF TABLES

Table 1: Communication channels.....	24
Table 2: Comparison of banked profiles.....	40
Table 3: Major m-banking offerings in South Africa.....	55

1. CHAPTER 1: INTRODUCTION TO RESEARCH PROBLEM

1.1 Introduction

“Since the democratisation of South Africa in 1994, increasing pressure has been brought to assist the development of the disadvantaged majority of the community living in poverty. The formal financial sector has a critically important role to play in this process. It must somehow open up traditional banking services - deposit and credit facilities - to the poor” (Schoombee, 2000, p. 2). Commercial banks traditionally do not serve low-income earners, micro-entrepreneurs and the poor (collectively referred to as the unbanked), chiefly because the high costs involved make it unattractive (Schoombee, 2004, p. 581). Whether simply the consequence of material poverty, geographic isolation or as the result of being perceived as “non-creditworthy”, many of the world’s low-income earners (particularly in rural areas) find themselves “unbanked” and without any recourse to the benefits of credit or secure deposit-taking facilities (Sherbut, 2009, p. 8).

For emerging middle-income nations which are seeking to guarantee upward economic mobility for their poorest citizens, the presence of large numbers of unbanked people is particularly problematic. For governments in these states, the viability of their attempts to encourage home ownership, household savings plans and the expansion of small business as avenues for “pro-poor growth” are brought into serious question when national banks are unable (or unwilling) to extend their financial assistance to impoverished constituencies (Sherbut, 2009, p. 8). It is only since the early 1990s that South African banks have given serious thought to entering this market segment, in no small way influenced by the changes in the local political landscape (Schoombee, 2004, p. 581).

The objective of the research described in this report was to investigate the strategies that are being employed by South African financial services organisations to optimise

financial inclusion; and to compare these to financial services providers in other geographies where evidence of financial exclusion could be found.

1.2 Banks' reluctance to serve the poor

The failure of formal banks to serve the poor is due to a combination of high risks, high costs and low returns associated with such business (Schoombee, 2000, p. 3). The factors cited in (Schoombee, 2000) as reasons why banks do not serve the poor include:

- High risk: credit transactions are subject to high risk because of the delay involved before debt obligations are repaid. To mitigate this risk, banks screen potential borrowers to ascertain the risk of default; devise incentives for borrowers to fulfill their promises; and develop various enforcement actions to make sure those who are able to repay, do so (Hoff and Stiglitz, 1990: 237) in (Schoombee, 2000, p. 3). In the case of the poor, these actions are difficult and costly to undertake, largely due to scarcity of information.
- Lack of collateral: the poor seldom have sufficient forms of conventional title to submit as collateral. Due to South Africa's political past, conventional forms of collateral - the most common being title over fixed property – are not available in adequate numbers to the poor.
- Sustainability: banks run the risk that loans issued to the poor may not generate an adequate and sustainable flow of income to service the all-inclusive cost thereof. When lending to microenterprises, the transaction and mentoring costs and the provision for loan losses are high per unit of funds lent (Schoombee, 2000, p. 3). Banks avoid serving the poor because of the danger of small businesses generating insufficient cash flow to meet regular interest payments in times of adverse business conditions, and there not being any risk capital to act as a cushion. Banks also experience problems in finding viable microenterprises to lend to.

- High operating costs: high operating costs (e.g. salaries for highly skilled personnel, standardised procedures for transactions) relative to the size of transactions with the poor inhibit banks from serving them. The banks' poor clients also encounter substantial transaction costs (e.g. time and transportation costs) in dealing with them, because formal banks are often not conveniently located.

In addition to these factors, governments tend to establish institutional barriers which dissuade commercial banks from seeking to serve the underserved. "In most countries, finance ministers, treasury secretaries and reserve bank chairmen express regular concern about matters such as currency stability, investor confidence and related to these, the strength of national banking systems" (Sherbut, 2009, p. 8). In South Africa, these concerns have encouraged the South African Reserve Bank (SARB) to introduce disciplined banking regulations that guarantee fiscal and monetary stability, but which also make it difficult for the country's banks to adopt the underserved as clients. There seems to be a contradiction in that government encourages banks to provide credit to low-income and "high-risk" populations who often lack collateral, when doing so may subject these institutions to a large number of sub-prime loan defaults and a subsequent "run" on bank assets. For the SARB in particular, the broader aims of preserving macroeconomic stability must be seen as more important than the developmental necessity of pursuing poverty-reducing measures that could be introduced by serving the underserved (Sherbut, 2009, p. 8).

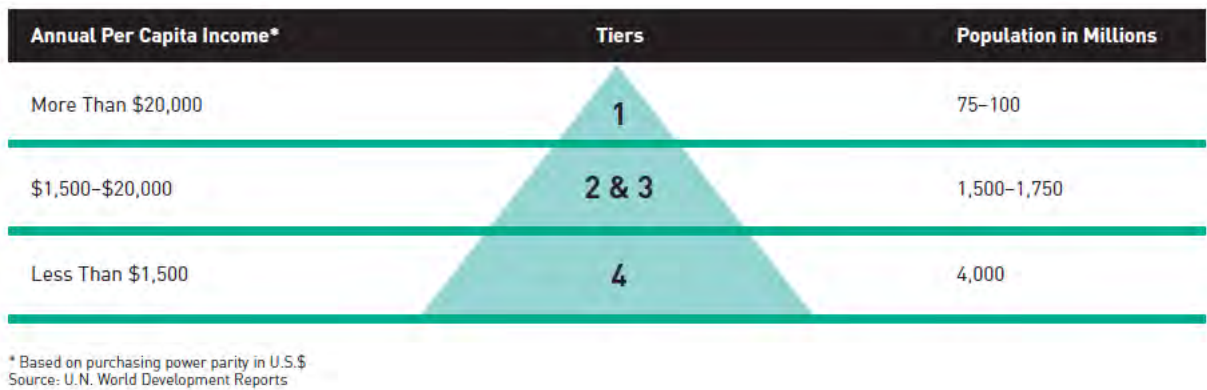
1.3 The bottom of the pyramid in South Africa's banking sector

The unbanked and underbanked markets in South Africa signify the bottom of the pyramid (BOP) for the country and represent a vast, untapped source of new customers and revenues for traditional financial institutions. C.K. Prahalad (2006) purports that if one stops thinking of the poor as victims or as a burden and starts

recognising them as resilient and creative entrepreneurs and value-conscious consumers, a whole new world of opportunity will open up.

Prahalad defines the bottom of the pyramid (as illustrated in Figure 1 below) as individuals earning the equivalent of less than \$1 500 a year, which constituted approximately 4 billion people worldwide in 2002 (Prahalad and Hart, 2002).

Figure 1: The economic pyramid



In South Africa, many traditional, well established organisations have adapted neither their products nor their distribution networks to the needs of low-income people. Instead, complex products and distribution methods designed for more affluent consumers have been pushed into a market that is characterised by different forms of behaviour, a less sophisticated understanding of financial products, and far lower revenue flows per customer (Moore, 2000).

The challenge for financial institutions is how to address the concerns of unbanked and underbanked customers and provide them with products that meet their needs within the context of the structure of each financial institution and the regulatory environment (Jacob and Tescher, 2005). New approaches are needed to capture the market including new ways of thinking about product and service offerings. Formal financial institutions can turn this market into a profitable venture in the long term (Prahalad and Hart, 2002).

It is impossible to understate the importance of access to financial services for population groups that lack the resources both to escape from poverty and to contribute to economic activity, social cohesion, and political stability. A population that plays an active part in the economic process is much more likely to identify with the rest of society and to have a sense of ownership and belonging, thereby contributing towards stability. “Belonging means having something to lose, and this sense is fundamental to social cohesion” (Moreno, 2007, p. 85). “Business now faces the challenge of both creating profits and meeting social needs. If business fails to meet this challenge, one is condemned to living in islands of wealth in a sea of poverty. If business succeeds, it can help to build a world that works for all” (Weiss, 2007, p. 37).

South Africa’s 2007 FinScope survey indicates that the proportion of the adult population (16 years and older) with a bank account reached 60% in 2007, implying that the unbanked market still constitutes 40% of the adult population. Additionally, the proportion of banked adults in the Living Standard Measure (LSM) 1–5 bracket saw a growth rate of 26% in 2007, bigger than any of the higher LSM segments. Entry level banking products remain at the top of the list of products used, with 55% of adults having an ATM card and 43% using a savings/transaction account. The FinScope 2007 data also reveals that use of a Mzansi account has increased from 2% in 2005 to 6% in 2006 and 10% in 2007. For the third year in a row, there has been a marked increase in the take-up and use of financial products in South Africa (FinScope South Africa, 2008).

1.4 Scope of research

The scope of the research was twofold. First, the research aimed to investigate South Africa’s financial services industry and determine how the industry is striving to achieve greater financial inclusion, by meeting the needs of the underserved. The strategies

currently employed by formal financial services institutions to optimise financial inclusion were investigated. Next, focus was directed at strategies being employed in other countries where evidence of financial exclusion could be found. In conclusion, the financial services product development stages were assessed, to identify areas for improvement, especially when designing products and services for underserved markets.

2. CHAPTER 2: LITERATURE REVIEW

2.1 Financial inclusion

Financial inclusion is defined as “a process that ensures the ease of access, availability and usage of the formal financial system for all members of an economy” (Sarma, 2008, p. 3). Ease of access is measured by proxies such as number of bank branches or number of ATMs per 1000 population. In the South African context, other factors that have an impact on the ease of access are transport costs to the point of access and the opportunity cost associated with travel time. Availability and usage are measured by the extent of utilisation as well as the size of bank credit and bank deposits, relative to the GDP of a country. An inclusive financial system should have as many users as possible as this gives an indication of how much the financial system has penetrated among its users (Sarma, 2007). The various dimensions of inclusion that are encompassed in this definition, together build an inclusive financial system. As banks are the gateway to the most basic forms of financial services, banking inclusion/exclusion is often used as analogous to financial inclusion/exclusion. It has been observed that even “well-developed” financial systems have not succeeded to be “all-inclusive” and certain segments of the population remain outside the formal financial systems. (Sarma, 2008).

The (Financial Services Authority, 2000) in (Carbo, Gardener and Molyneux, 2007) states that financial exclusion can come about as a result of a number of factors:

- Access exclusion: restricted access through the process of risk assessment;
- Condition exclusion: where the conditions attached to financial products make them unsuitable for the needs of some people;
- Price exclusion: where some people cannot afford the levels at which financial services are priced;
- Marketing exclusion: where some people are excluded by targeted marketing and sales; and

- Self exclusion: where people decide that there is no point in applying for a financial product because they believe their application would be refused.

Financial exclusion or constrained access to finance has negative, interrelated economic and social impacts. As stated in (Jefferis, 2007, p. 5), these consequences arise for a number of reasons:

- The lack of efficient financial service provision means that poor people are either forced to use inefficient provisions, often at high cost (for instance, with high transactions costs, excessively high interest rates on loans, or poor returns on savings) – thereby entrenching poverty – or they do not have access to certain financial products, either because of an absolute absence of suitable products or because available products are too expensive;
- This in turn tends to restrict the economic opportunities open to the poor. This is most obviously the case with credit, as almost all entrepreneurship activities need capital upfront, even if in small amounts, to fund investment;
- The poor are vulnerable to adverse events and financial loss (due to lack of insurance and secure savings products);
- The absence of savings products makes it difficult to build up capital;
- Poverty is entrenched, as the poor are faced with the high costs of accessing financial services, and are denied entrepreneurship opportunities that might provide them with a chance to earn an income; and
- Economic growth is below potential, as the level of investment is reduced.

Groups in society that are unable to access financial services are frequently unable to obtain other social provision and financial exclusion can often exacerbate other kinds of social exclusion (Carbo et al, 2007, p. 21).

As products get more complex, they have a greater potential to meet the specific financial needs of the poor—but they also become harder for clients to understand and manage. The key is to identify optimal combinations of all these dimensions by

determining which factors “sell” best to clients and by understanding the literacy required for a product to succeed (both in terms of take-up and proper usage). In offering products and services that assist the poor in accomplishing their stated goals, attention must be given to more than just the pure economics of the choices being offered. The way offers are presented can have just as much to do with take-up and usage as do the terms of the products and services. Given that the presentation of choice matters, choices in product design affect how the product is used, and by whom (Karlan and Morduch, 2009).

2.2 Unbanked and underbanked markets

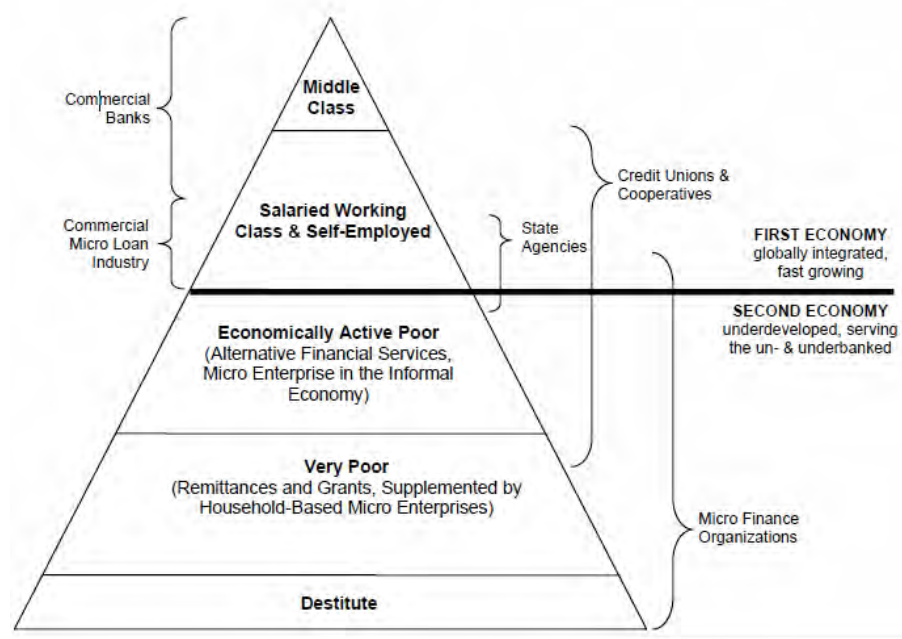
(Worthington, 2008, p.101) defines the unbanked as “those individuals without a traditional savings or checking account”. They are distinct from the underbanked, who have some limited relationship with a financial institution. (Sarma, 2008, p.8) defines the underbanked as people with bank account, but who make very little use of the services on offer. Sarma purports that merely having a bank account is not enough for an inclusive financial system; it is also imperative that the banking services are adequately utilised.

The underbanked tend to rely on alternative financial institutions even though they have bank accounts because they are not fully integrated into the banking system. As a result, these individuals may pay more for basic financial services. In addition, “the underbanked lack the tools they need to save and build assets which, according to the South African Reserve Bank, can enable poor and vulnerable households to protect themselves from negative economic shocks” (Dorsey and Jacob, 2005, p. 1). Underutilisation of the financial mainstream can have far-reaching effects. Communities with well-functioning financial markets are more resilient against economic downturns and can more readily take advantage of economic growth. Consumer participation in the financial mainstream can help stabilise and revitalise

local communities. Participation can also enhance credit flows to help facilitate residential and business financing (Sherrie, Rhine and Greene, 2006, p. 23).

The following diagram represents the landscape of financial services available to South Africans with the unbanked and underbanked tending to transact in the alternative financial services sector and informal economy (Sisulu, 2005 in Dorsey and Jacob, 2005, p. 2).

Figure 2: Landscape of financial services available to South Africans



Source: Dorsey and Jacob, 2005, p. 2

2.3 South Africa's formal financial infrastructure

The introduction of the two-economy discourse has been remarkable for the extent to which it has drawn attention to the subject of the persistence of underdevelopment in South African society (Synthesis of the 2005 Development Report). South Africa has a dual economy, with a sophisticated first world sector overlaid on what can be characterised as a developing economy (Arora and Leach, 2005). The percentage of population having bank accounts varies from 26% in rural areas to 34% in small urban areas and 64% in metros.

There are three critical components in the environment that surrounds any financial services market – institutional infrastructure, organisational infrastructure and support infrastructure (Arora and Leach, 2005, p. 1727). If any one of these components is dysfunctional, the financial markets are unlikely to work effectively.

2.3.1 Institutional infrastructure

Institutional infrastructure comprises policies, laws and regulations, which provide the foundation for any effective market (Arora and Leach, 2005). In the South African context, legislation such as the Financial Intelligence Centre Act (FICA), require banks to have evidence of pay slips and proof of residence from clients. This poses an inclusion challenge for people living in informal settlements who do not have proof of residence. Pay slips are also a concern in instances of low levels of formal employment. Another obstacle to increasing credit availability is the shortage of acceptable collateral at the bottom of the pyramid because of the historic lack of property rights. De Soto (2000) highlights the fact that any asset whose economic and social aspects are not fixed in a formal property system is extremely hard to move in the market. Property rights are thus a key prerequisite for facilitating access to capital.

2.3.2 Organisational infrastructure

Organisational infrastructure comprises the diverse providers of financial services having varying capacity and often being in competition with each other (Arora and Leach, 2005). In South Africa, the banking sector is highly concentrated, with four dominant local banks and other smaller players. The small number of participants is due to a lack of interest by foreign entrants under the previous regime, years of economic isolation and the departure of a number of small organisations in recent years such as Saambou Bank. Since 1995 the market has opened to outsiders and

foreign entities in the banking, insurance and securities industries (Goeller and Szymanski, 2005).

Most banks however, tend to focus on the profitable top quartile of the market, consisting mainly of high net worth individuals and large and medium-sized corporates. Though banks are aware of the commercial imperative in expanding their potential client base beyond this much sought after sector, they seem to be having some difficulty in finding ways to do so cost effectively and profitably (Arora and Leach, 2005, p. 1727).

2.3.3 Support infrastructure

Support infrastructure supports the other two components and includes professional services that are involved in the financial sector (Arora and Leach, 2005). Providers of financial services concentrate on gathering information about the top end of the market and often remain uninformed about the needs of the poor. Traditionally, providers have made assumptions about the part of the population that is presently unbanked, without attempting to establish the realities of the situation.

Evidence of the lack of focus on the bottom of the pyramid can be found in the 2009 FinMark report which comments on the insufficiency of collaboration between the banks, which “is now at such a low level that it can hardly be described as an “initiative” anymore. “Already it is hard to find reference to Mzansi products in private bank offerings” (Finmark report, 2009, p.87). Even the dispute that arose a year after the launch of the Mzansi initiative in October 2004, over Mzansi’s penetration rate is evidence of the lack of focus on the bottom of the pyramid. While the banks claimed that 2 million Mzansi accounts had been opened in that first year, the FinScope 2005 survey brought those figures into question by stating that “only 550 000 more people had bank accounts this year than last year” (Business Day, 24 October 2005). The

report further showed that 55% of the adult population had not even heard of the Mzansi initiative. The banks could not tell with accuracy, which of the accounts that were opened were by previously unbanked individuals. While the Banking Association estimated that 80% of Mzansi account holders were previously unbanked, the FinScope 2005 report indicated that only about 193 000 (or less than 10%) were first-time account holders.

2.4 Strategies for serving the bottom of the pyramid

It is necessary to find alternative methods of banking the unbanked and the poor which can provide essential products and services but that do not undermine the steadiness of commercial financing agencies or the wider economy (Sherbut, 2009, p. 8). There is both opportunity and risk in underserved markets and according to (Weiser, 2007), there are five key strategies for achieving success in these markets:

2.4.1 Mine and translate local market information

Information about the market and about organisation performance is critical in providing the knowledge needed to identify opportunities, avoid pitfalls, and take corrective action where necessary (Weiser, 2007). Bottom of the pyramid communities are different from their mainstream counterparts in that they tend to be more heterogeneous and diverse. Organisations serving these markets find that national information sources tend to have less accurate information on the particular communities by reason of it being harder to get individuals in these communities to participate in censuses and surveys. They may not be legally documented and may not have permanent homes. They may also be concerned that answering a census questionnaire will lead to potential problems with authorities. All these factors significantly hinder accurate surveying of consumers in the indicated communities compared with middle- and upper-income consumers (Weiser, 2007).

To address the above-mentioned complications, organisations have to change the ways in which they obtain information on BOP markets. Instead of using standard approaches to gather and analyse data for product development they have to use non-traditional sources. In South Africa, organisations such as the FinMark Trust specialise in gathering and analysing information on these markets. Some organisations also create internal “learning labs” – staff teams who spend extended periods of time living and working in BOP communities to gain a deeper and more exhaustive understanding of the needs, interests, and purchasing patterns of consumers in the particular communities (Weiser, 2007).

2.4.2 Adapt the business model to community realities

The business models that organisations use for their sales and marketing, may need to be adapted and extended for BOP markets. The first key differences between BOP and mainstream markets is that customers in BOP communities tend to prefer products with the lowest initial costs, even if the life cycle costs are higher and that they tend to buy goods in smaller units. This can dramatically change how organisations package and deliver products (Weiser, 2007). Although providing products in single-use sachets has been a very successful strategy in many BOP communities, delivering products in single use sachets to customers who buy small amounts at a time can drive up the unit cost of distribution. To address this difficulty, organisations look to find distribution channels already rooted in the community (Weiser, 2007). A fundamental challenge is the fact that the social networks in these communities are often disconnected from the social networks in which the organisations and their employees are embedded. This makes it difficult to find and attract employees from these communities. To succeed in these markets, an organisation may need to foster the development of social networks with residents in the indicated communities.

2.4.3 Change internal incentives and challenge cultural assumptions

Most organisations have a set of financial and social incentives that work to align the behavior of its employees with the strategic goals and objectives. Organisations need to acknowledge that incentives that work well to focus the behaviors of employees in mainstream markets can often be counterproductive when it comes to providing incentives for working with BOP communities. Incentives might have to shift, for example, from a focus on margins (that might be lower margins) to a focus on total profits in order to encourage managers to spend time and energy building business in these markets (Weiser, 2007).

Employees may have a tacit set of cultural assumptions or biases that need to be challenged if they include inaccuracies or biases concerning underserved individuals and communities. The core of strategies to address these assumptions often involves making these assumptions explicit so that they can be addressed and managed. Organisations may also engage managers with the communities, and the communities with managers, through projects, volunteer work, and mentoring activities so that each side can gain firsthand understanding of the other (Weiser, 2007).

2.4.4 Create partnerships and strategic alliances

In many BOP markets, there are barriers that prevent organisations from achieving profitable sales when working through their normal business networks. These barriers include cost structures that make it impossible to sell a product profitably or difficulties in aggregating demand – making the cost to acquire customers too high (Weiser, 2007). In the banking industry for example, the rolling out of products and services using the branch network is expensive and has an impact on product profitability.

There may also be political or bureaucratic obstacles to market entry. In addition, organisations can face considerable distrust from residents of BOP communities, which

reduces demand and increases scrutiny by community-elected officials and regulators. Creating partnerships and strategic alliances can help address both challenges. These partnerships help organisations reach customers, find workers, develop sources of supply, and create profitable new products and processes (Weiser, 2007). In the banking industry, the use of community bankers, who live and work in the communities and partnerships with local retailers are examples of such partnerships.

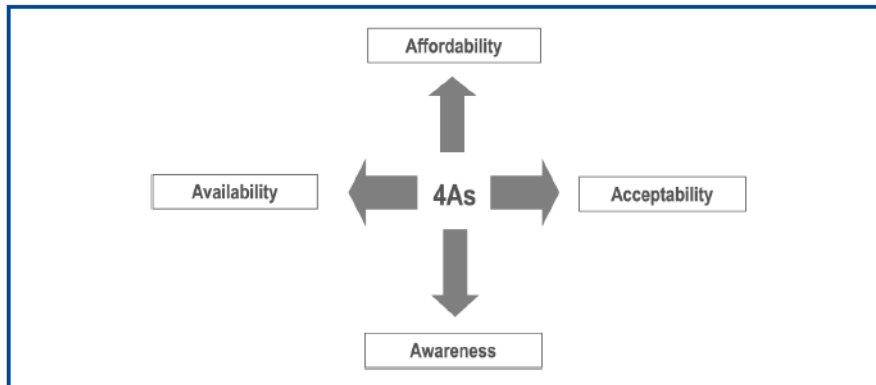
2.4.5 Improve the enabling environment

The enabling environment – the laws, institutions, and infrastructure that support (or hinder) business activity in a market – often need to be improved in order to do business profitably in BOP markets. Businesses can confront inadequate infrastructure or cumbersome regulations, which make it nearly impossible to provide high-quality products at affordable prices. A number of approaches can be followed in addressing these issues:

- Making investments in the infrastructure in the form of building roads and other infrastructure;
- Working in collaboration with other businesses and nonprofit advocacy groups to identify problems and develop the political will to bring about effective change; and
- Creating a self-regulatory structure that “raises the bar” for corporate participants in these markets, such as the Financial Sector Charter.

Serving populations at the bottom of the pyramid also requires solutions that deliver on the 4 As, as depicted in the figure below.

Figure 3: The 4 As



Source: Anderson and Billou, 2007, p. 16

Availability: the extent to which customers are able to readily acquire and use a product or service (Anderson and Billou, 2007, p. 14).

Distribution channels in BOP markets may be fragmented or non-existent and the task of getting products to consumers may be a major hurdle. Organisations therefore need to explore alternative methods of delivering their products and services to even the most isolated communities.

Affordability: the degree to which a firm's goods or services are affordable to BOP consumers (Anderson and Billou, 2007, p. 14).

Cash-flow is generally a significant problem for many low-income consumers. Organisations must therefore deliver offerings at a price point that enables consumption by even the poorest consumers.

Acceptability: the extent to which consumers and others in the value chain are willing to consume, distribute or sell a product or service (Anderson and Billou, 2007, p. 14). There is often a need to offer products and services that are adapted to the unique needs of both customers and distributors. Organisations need to respond to specific national or regional cultural or socioeconomic aspects, or to address the unique requirements of local business practices.

Awareness: the degree to which customers are aware of a product or service (Anderson and Billou, 2007, p. 15). With conventional advertising media being

inaccessible for many low-income consumers, building awareness can be a significant challenge for organisations wishing to serve these markets. Alternative communication channels therefore need to be explored.

2.5 The Mzansi Initiative

A Federal Deposit Insurance Corporation (FDIC) report states that “access to a basic bank account and financial services is fundamental to economic self-sufficiency” (FDIC report, 2008). It further found that banks need to do more in serving both the unbanked and underbanked of their communities. As financial institutions begin to consider how to move consumers along the credit path, basic barriers to entry must be overcome. In other words, it will be difficult for the underbanked to access credit products if they are denied access to basic transaction products in the beginning (Jacob and Tescher, 2005). The Mzansi account is one of South Africa’s answers to address the issue of financial inclusion for unbanked and underbanked markets. The account is an entry-level bank account, based on a magnetic strip debit card platform. The account was developed by the South African banking industry and launched collaboratively by the four largest commercial banks, together with the state-owned Postbank in October 2004 (FinMark Trust, 2009). “Mzansi” is an umbrella brand owned by the Banking Association of South Africa and it is used as an “endorser brand”. “Mzansi initiative” refers to the collaborative process of designing, launching and marketing the product within the context of South Africa’s Financial Sector Charter of 2003. While the Charter outlined a broad framework for the desired characteristics of a basic transactional and savings product, it did not specify the product design. An inter-bank task team, convened under the auspices of the Banking Association, was formed to undertake the task of designing the Mzansi product.

The Charter also did not prescribe collaborative action by the banks in launching the Mzansi initiative, but the major banks chose this route with the aim of mitigating perceived risk and achieving the bold access goals specified in the Charter. The risks

identified by the major banks in taking on the Mzansi initiative were put down as follows:

2.5.1 Reputational risk

The major banks faced a paradoxical situation in that if the Mzansi initiative was profitable, they could be faced with the reputational risk of being seen to be making money out of the poor. On the other hand, if the venture was not profitable, they could be accused of not trying hard enough. In the context of the politically charged environment in which the Mzansi initiative was conceptualised, the only way to mitigate reputational risk to any one bank was through collaborative action.

It could be argued that the high fixed costs of the big banks are a key factor that influences the profitability of an initiative such as Mzansi. Perhaps the way in which Teba Bank and Capitec are structured makes them better able to serve the Mzansi target market more adequately, because they do not have such a big footprint and have less fixed costs. Reputational risk for the big banks could have also manifested in the form of existing clients feeling that their bank's brand and service levels would be compromised by them taking on "large numbers of low income customers who might clog banking halls and ATM lines" (FinMark report, 2009, p.19)

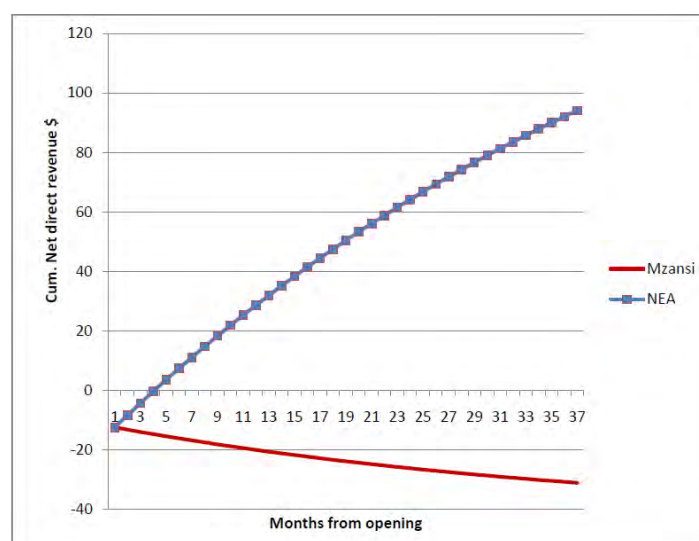
2.5.2 Financial risk

While the banks expected that their Mzansi operations would either break-even or incur limited and manageable losses, they still wanted to limit the downside by sharing at least some of the initial costs of product development and launch. Another financial risk was "the threat that a new low cost transaction account would cannibalize their lucrative revenue from existing transactional offerings in the event where existing customers would switch down to the lower fee option" (FinMark report, 2009, p.19). In hindsight, this fear of cannibalisation did not manifest.

A key benefit of the collaborative action was that it gave the initiative the kind of scale that it would not have enjoyed if each bank had launched an entry-level product independently (FinMark Trust Report, 2009, p.5). While the smaller participants in the financial services sector such as Capitec and Teba Bank were invited to join the Mzansi initiative and be Mzansi issuers, they turned the invitation down in favour of independently pursuing market opportunities and rolling out their own low-end transactional and deposit products designed for the marginally banked. Capitec and Teba Bank felt that they already had offerings for the segment of the market being targeted by the Mzansi initiative, so the perceived benefits of collaboration were lower for them. They also perceived that their collaboration would bring about higher costs. Capitec and Teba Bank, saw that “the mixed motivations of the big banks could result in poor product design and take-up which would taint their brands in their core market.” (FinMark report, 2009, p.20).

As illustrated in Figure 4 below from the 2009 FinMark report, Mzansi accounts are showing signs of increasing non-profitability, but because of the “anonymity” provided by the collaboration, no one bank’s reputation is at risk. NEA in the graph refers to “Nearest Equivalent Account”.

Figure 4: Cumulative net direct revenue from Mzansi and NEA (US\$)



Source: FinMark Trust, The Mzansi bank account initiative in South Africa – final Report, p. 72

2.6 Legal boundaries of collaborative action

South Africa's competition law unequivocally prohibits competitors from "directly or indirectly fixing a price or any other trading condition"; and no exception was provided for a Charter-like initiative such as Mzansi (FinMark report, 2009, p. 20). The extent and form of collaboration between competing major commercial banks therefore required careful consideration within the competition law framework. Moreover, in 2003, the National Treasury, supported by the South African Reserve Bank, commissioned a Task Group to undertake a study of "Competition in South African Banking", which expressly concluded that any national bank account initiative defined in terms of price-fixing and collusion would pre-empt competition and should be avoided. Consumers and policymakers had voiced increasing concerns over inadequate competition among the large banks manifesting in high retail bank charges, culminating in a full Banking Enquiry established by the Competition Commission (Finmark report, 2009, p.19). Appendix 2 is a snapshot from Dorsey and Jacob, 2005 and is an illustration of other private sector experiments and innovations in the area of facilitating financial inclusion, some of which no longer exist.

2.7 The Grameen model

The Grameen Bank is a microfinance organisation and community development bank that makes small loans to the poor without requiring collateral. The bank, which started in Bangladesh, is based on the idea that the poor have many underutilised skills that are potential community resources (Wilkins, 2007, p. 359). The Grameen Bank is an organisation of microenterprises for, of, and by the poor (Auwal, 1996, p. 28). The idea behind the Grameen model is that the poor obtain small loans to support income-generating activities, from which they can generate sufficient income to repay the loan. The lending is not collateral-based, but is based on the credit-worthiness of the group of co-borrowers. Prior to loans being granted, groups of borrowers are trained on the

bank's rules and regulations, as well as in the making of key decisions. Borrowers are also taught how to sign their names and how to use the loans (Wahid and Hsu, 2000).

The goal of Grameen Bank is to empower the poor, especially women, to “improve their socioeconomic conditions in an environmentally sound, sustainable manner” (Auwal, 1996, p. 29). The founder of Grameen Bank, Dr Muhammad Yunus argues that “if a person does not have economic resources, then he or she cannot realise the basic human rights of food, shelter, health and education. There must be some economic conditions that enable people to enjoy the benefits of these human rights” (Auwal, 1996, p. 30). Dr Yunus also argues that “in order to design systems that are more accessible to the poor, the institutions fighting poverty must understand the limitations faced by the poor and seek to work around them” (Yunus, 2007, p. 20). There is direct contact between bank employees and borrowers and the step-by-step lending rules mean that any issues can be identified and resolved timeously; and the small and frequent payments reduce the burden of debt on the borrowers (Wahid and Hsu, 2000).

“Grameen Bank starts with the belief that credit should be accepted as a human right, and builds a system where one who does not possess anything gets the highest priority in getting a loan. Conventional banking is based on the principle that the more you have, the more you can get. In other words, if you have little or nothing, you get nothing. As a result, more than half the population of the world is deprived of the financial services of the conventional banks. The overarching objective of the conventional banks is to maximize profit. Grameen Bank's objective is to bring financial services to the poor, particularly women and the poorest — to help them fight poverty, stay profitable and financially sound. The first principle of Grameen banking is that the clients should not go to the bank, it is the bank which should go to the people instead. There is no legal instrument between the lender and the borrower in the Grameen methodology. There is no stipulation that a client will be taken to the court of law to

recover the loan, unlike in the conventional system. There is no provision in the methodology to enforce a contract by any external intervention.” (Grameen Bank website, 2009).

2.8 Mobile phone banking for meeting the needs of the unbanked and underbanked

Mobile banking is defined as the provision of banking and financial services with the aid of mobile telecommunication devices. The scope of services offered includes information provision, transactions, and account management (Cain, 2009, p. 3). Transformational m-banking is the provision of banking services using a mobile phone in such a way that currently unbanked people are targeted. The term was coined to differentiate this type of offering from additive m-banking options, where the mobile phone is simply another channel. If m-banking extends financial access at sufficient scale to unbanked people, then the retail financial sector of a country is likely to be transformed (Porteous, 2007, p.6). While current adoption of mobile banking is relatively low, banks offering the service expect the adoption of the service to increase.

A significant percentage of the unbanked population comprises mobile phone users. The prevalence of the mobile phone makes it an ideal channel to reach customers who do not have access to financial services. There are numerous reasons why consumers are unbanked, and the mobile channel has the potential to address many of these by extending banks’ distribution capabilities through a new channel (Cain, 2009). As illustrated in Table 1 below, the number of mobile phone users has continued to rise over the period 2004-2006, and the number of m-banking (mobile banking) users has risen from a negligible figure in 2004 to around 450 000 by 2006. While this is a rapid increase from a near zero base, less than 3% of banked customers use the mobile channel for banking (Porteous, 2007, p.19).

Table 1: Communication channels

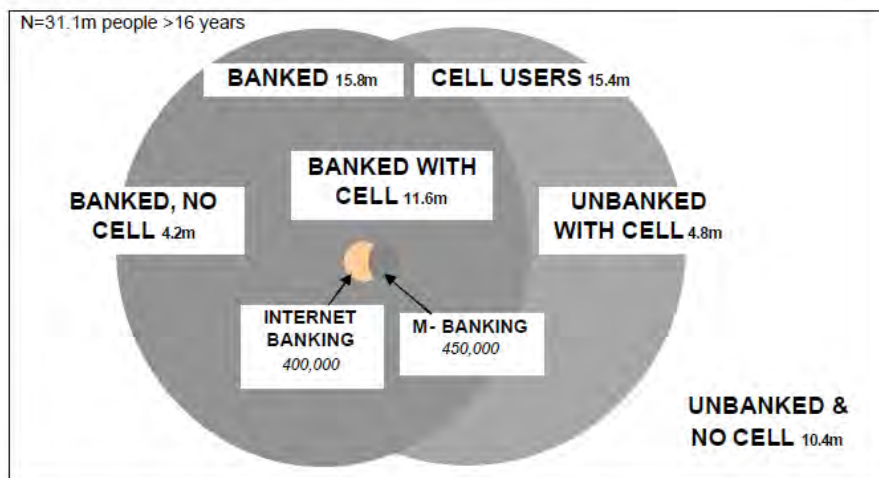
Category	2004	2006
Numbers/ % of all adults		
Personally use cellphones (2006: prepaid and contract combined)	11.4m 42%	16.4m 53%
Internet users at home	1.3m 5%	0.6m 2%
M-banking	Negligible*	0.5m 1.6%

Source: FinScope™ SA 2004, 2006

Mobile banking is allowing people who could never afford traditional bank accounts to send, receive, and save money. “Cheap and efficient m-banking services are cropping up and are the latest example of how the cell phone has transformed life in sub-Saharan Africa” (Africa Research Bulletin, 2009, 18167).

Figure 5 below is an illustration of combinations of being banked or unbanked, with or without a mobile phone. Of particular interest for the purposes of this study, are the unbanked people with cell phones since they would be the logical target group for transformational m-banking. Similar studies in other countries have also found this group to be large: in Botswana, for example, 36% of the unbanked have a cell phone (Porteous, 2007, p.19).

Figure 5: The overlap of banking and mobile use



Source: FinScope™ 2006

A unique characteristic of providing financial services through the mobile channel is the presence of the mobile network operators in the value chain, whose involvement varies from market to market. The extent of variation in involvement can be classified as follows:

- No involvement: the network operator acts in the same way as an internet service provider does for online banking;
- joint ventures between network operators and banks; and
- network operators provide the mobile banking service and banks act as utilities that provide regulatory compliance services and handle the funds behind the scenes.

The relationship between mobile network operators and banks is often characterised by tension and mistrust, with each player believing that the other is encroaching on their territory. The various forms of involvement can co-exist in the same market (Cain, 2009).

Mobile network operators are in many ways better suited than banks to provide financial services to unbanked demographics. One of the key reasons cited by the unbanked for not using banks is that they do not trust them, or they feel intimidated by them. By contrast, mobile network operators, often enjoy strong customer relationships with these demographics. The majority of unbanked customers are prepaid subscribers and are accustomed to handing cash to mobile network operator outlets in exchange for airtime. In many markets, mobile network operators also have stronger distribution capabilities than banks, with extensive networks of outlets and airtime resellers that can provide essential cash-in/cash-out services for mobile banking customers (Cain, 2009).

The dominant reason why the unbanked do not use banks is that they are not employed or do not have regular or sufficient incomes to make it worthwhile. Research

on mobile commerce in poor communities shows that mobile telephony can be a highly effective tool for economic empowerment by enabling the poor to participate in the economic system. By providing a secure and efficient mechanism for payments and saving, as well as enhancing access to information, mobile is a powerful enabler of commerce. This leads to a virtuous circle where mobile banking services improve social and economic well-being, which in turn increases the demand for banking services (Cain, 2009).

Gautam Ivatury, manager of the Consultative Group to Assist the Poor (CGAP) technology programme as cited in (Cain, 2009), points out that mobile phones have become the first communications technology in history to have more users in poor countries than rich ones. Those who do not own a mobile phone will often have access to one through friends or family. Less than one-fifth of Africans have bank accounts, and far fewer access the Internet. Africa, however, recently surpassed the United States and Canada with 340m mobile phone users and is adding another 70 million each year, according to *Wireless Intelligence*, a market research group (Africa Research Bulletin, 2009).

2.8.1 Mobile as a gateway product

Since unbanked customers do not yet have banking relationships, banks must attract them with so-called 'gateway products' which are designed to bring customers into a bank so that they can be persuaded, over time, to invest in a richer and more profitable suite of bank offerings. Mobile banking can deliver a number of such gateway products (Cain, 2009). These include the following:

- Airtime top-ups: giving prepaid subscribers the opportunity to quickly and easily top-up their mobile phones directly from a bank account represents a natural way of bringing them into the banking system.

- Remittances: as the remittance market involves regular transfers of funds between the unbanked, remittances are increasingly recognised as an effective gateway to bring people into the banking system.
- P2P payments: in many countries there are also large domestic remittance flows between unbanked people. Often these are migrant urban workers sending money home to family in rural areas. Mobile transfers of funds can provide a convenient and cost effective solution for these groups. Mobile P2P payment products can operate in the context of mobile banking in the strict sense in which the user's mobile phone is the channel used to access their individual bank account, or they can be 'mobile wallets' in which all funds in the system are stored in a pooled account.
- Low balance alerts: studies show that a significant percentage of unbanked consumers in developed countries were previously banked. A key reason for account closures is the fees and penalties associated with inadvertently going into overdraft. Charges for going into unauthorised overdraft can be high and these deterred this group from maintaining an account. SMS low balance alerts would give these consumers a greater ability to manage their accounts so as to avoid these high fees, thus encouraging them to resume and maintain a banking relationship.

Offering mobile banking as an additional distribution channel, on its own, is not sufficient to bank the unbanked. The offering must be part of a comprehensive approach which encompasses best practices in product design, pricing, marketing, customer services, financial education, and risk management, for the unbanked (Cain, 2009).

2.8.2 Mobile phone banking adoption framework

Tan and Teo (2000) in (Brown, Cajee, Davies and Stroebel, 2003) developed and tested a framework that identified factors that may influence the adoption of Internet banking. Mobile phone banking may be considered as an extension of Internet banking, and thus a similar set of factors can be derived for mobile phone banking by using this framework as a basis (Brown et al, 2003). Factors from the Internet banking study, which may apply equally to mobile phone banking adoption, include relative advantage, compatibility, complexity, trialability, banking needs, risk, self-efficacy, and facilitating conditions. A brief explanation of each of these factors follows:

- Relative advantage: the extent to which a person views an innovation as offering an advantage over previous ways of performing the same task (Taylor and Todd, 1995) in (Brown et al, 2003, p. 383).
- Compatibility: the degree to which an innovation is viewed as being consistent with the existing values of users (Agarwal and Prasad, 1997) in (Brown et al, 2003, p. 383).
- Complexity: the degree to which an innovation is considered relatively difficult to understand and use (Taylor and Todd, 1995) in (Brown et al, 2003, p. 383).
- Trialability: the extent to which users would like an opportunity to experiment with the innovation prior to committing to its usage (Agarwal and Prasad, 1997) in (Brown et al, 2003, p. 383).
- Banking needs: the variety of banking products and services required by an individual (Tan and Teo, 2000) in (Brown et al, 2003, p. 383).
- Risk: the perceived sense of risk concerning disclosure of personal and financial information (Tan and Teo, 2000) in (Brown et al, 2003, p.383).
- Self-efficacy: an individual's self-confidence in his or her ability to perform a behaviour (Taylor and Todd, 1995) in (Brown et al, 2003, p.383).
- Facilitating conditions:

- Technology support: the extent of technology support in the environment (Tan and Teo, 2000) in (Brown et al, 2003, p.383).
- Government support: Perceived government support for mobile commerce (Tan and Teo, 2000) in (Brown et al, 2003, p.383).

(Brown et al, 2003) found that a perceived sense of risk was a major factor inhibiting the adoption of mobile phone banking. By focusing on this factor, banks and mobile phone service providers may be able to increase the rate of adoption of mobile phone banking.

2.9 Correspondent banking arrangements for meeting the needs of the unbanked and underbanked

Correspondent banking arrangements refer to bank partnerships with non-banks, typically retail commercial outlets, ranging from lottery kiosks, pharmacies, post offices and retail outlets, to provide distribution outlets for financial services. These are private contracts where each contract determines the scope of services, fee paid and risk shared. Each financial institution decides the type of services it wants its banking correspondent to offer to the public in accordance with its strategic plan. (Kumar, Nair, Parsons and Urdapilleta, 2006, p. 1). Most businesses that enter into correspondent contracts with banks have pointed to benefits from an increase in clientele, an increase in revenue, differentiation from other competitors, an instrument that helps develop customer loyalty and a new source of revenue. Through the sharing of the point of service interfaces with retailers, the high variable costs of enhancing financial access can be reduced. Correspondent banking arrangements also reduce the high fixed costs associated with maintaining bank branches in remote areas where population density or economic activity is low. Benefits to the population include access to the financial system in a simplified form, flexibility with business operating hours, greater ease in transactions by combining banking services with shopping, easier receipts of social

benefits, and reduced travel and costs for accessing financial services (Kumar et al, 2006, p. 3).

In Brazil, correspondent banking is growing at a tremendous speed and has become the primary form of financial access in remote areas where the population would otherwise have to travel to a city to get social benefits or basic banking services. On the supply side, it allows outreach to the unbanked profitably, and allows risk sharing arrangements with retailers. Significantly lower initial investment and ongoing costs compared to traditional branch banking appear to be a prime driver. Perceptions among the lower income population that retail or service outposts are more “friendly” than traditional bank branches also appears to have contributed to the growth (Kumar et al, 2006, p. 37).

There are some regulatory issues that are very specific to Brazil that may have an impact on the potential for replicating the correspondent banking model in other countries. In particular, regulations regarding space and equipment for bank branches and agreements related to salaries of bank employees. Brazil’s success in correspondent banking however, suggests a channel for financial institutions to increase outreach profitably. It allows them to gain proximity to small and perhaps higher risk clients through a format that is friendly to this population segment, but with significantly reduced start-up investments and ongoing costs. Economies of scale allow this model to be successful, despite low balances and profit margins. Expansion beyond simple payment services to the provision of credit and more complex services however, remains a challenge (Kumar et al, 2006, p. 38).

In the United States, Wal-Mart offers basic money services to underserved customers. The offerings are limited to the range of services that Wal-Mart believes would appeal to this segment of the market. Wal-Mart, in collaboration with GE Money Bank and

Green Dot have launched the Wal-Mart Money Card, which is a “reloadable prepaid Visa Card” (Worthington, 2008, p. 102). Wal-Mart also has independent banks operating out of some of their stores, with store design that caters for an independent bank tenant. For Wal-Mart, offering financial services to the underserved is attractive for the following reasons:

- The market is large and overlaps significantly with their core retailing business;
- The pay-as-you-go nature of the financial services offered such as remittances and bill payments; and
- Emerging financial products such as prepaid cards lend themselves to the delivery of financial services for the unbanked (Worthington, 2008).

(Welch and Worthington, 2007) in (Worthington, 2008) purport that the diversification of retailers into financial services carries a risk for the retailers “and is only likely to be successful for a relatively limited range of financial services” (Worthington, 2008, p. 102).

3. CHAPTER 3: RESEARCH QUESTIONS

This research report was directed towards furthering an understanding of the measures being taken by South African financial services institutions to optimise financial inclusion.

The following research questions are investigated:

Research question 1:

What are the factors that have an impact on financial inclusion in South Africa?

Research question 2:

There are three critical components of the environment that surrounds any financial services market – institutional infrastructure, organisational infrastructure and support infrastructure (Arora and Leach, 2005, p. 1727). If any of these components is dysfunctional, the financial markets are unlikely to work effectively.

How are these three critical components of the environment in South Africa's financial services market geared towards optimising financial inclusion?

Research question 3:

How can technology be leveraged to optimise the provision of products and services to the unbanked and underbanked, thereby optimising financial inclusion?

Research question 4:

How can the retail store network be leveraged to optimise the provision of products and services to the unbanked and underbanked, thereby optimising financial inclusion?

Research question 5:

How can products and services targeted at the unbanked and underbanked be improved to optimise financial inclusion?

Research question 6:

What impact does access to basic transaction products versus access to credit products have on financial inclusion?

Research question 7:

How can the profitability and sustainability of products and services targeted at the unbanked and underbanked be improved to optimise financial inclusion?

Research question 8:

Examples of previous products and services aimed at the unbanked and underbanked and their reasons for success or failure.

4. CHAPTER 4: RESEARCH METHODOLOGY

4.1 Research Design

A qualitative research design, in two phases, was adopted for the study. The initial research topic exploration was conducted through secondary data analysis making use of published academic articles, books and periodicals. Information gathered through the secondary data analysis was used to formulate the interview guide and facilitate the direction of data analysis. The interview guide listed the questions or issues to be explored in the course of the interview and ensured that the same basic lines of inquiry were pursued with each person interviewed (Patton, 2002). The guiding interview questions can be referred to in Appendix 1.

Thereafter, the research questions were explored through the use of individual depth interviews with industry practitioners from established, South African financial services institutions. In-depth interviews employed a focused interviewing strategy in which questions were open-ended and non-directive, allowing the discussion to follow the subjects' responses and issues (Mariampolski, 2001). Qualitative interviewing began with the assumption that the perspective of the respondents was meaningful, knowable, and able to be made explicit (Patton, 2002).

4.2 Unit of analysis

The primary unit of analysis for the purposes of this research report consisted of practitioners who work with entry-level transactional banking products in South African financial services institutions. The secondary unit of analysis consisted of various country studies where evidence of the issue of banking the unbanked could be found, as well as literature on the subject.

4.3 Population of relevance

The population of relevance was formal financial institutions within South Africa, who offer personal finance products to the unbanked and underbanked markets (where personal finance products or services refer only to transactional or saving accounts and personal loans).

4.4 Sampling method and sample size of relevance

4.4.1 Sample

In choosing a sample of countries where evidence of financial exclusion could be found; various electronic databases were interrogated using search terms such as “financial inclusion”, “financial exclusion”, “banking the unbanked” and “unbanked. Websites used for the country studies include, amongst others, the FinMark Trust site, EbscoHost and Emerald.

The sample for this research report also comprised of large, established financial institutions in South Africa. The South African banking environment is highly concentrated, with the Big Four banks (ABSA, FNB, Nedbank and Standard Bank) accounting for some 85% of the industry’s assets (Goeller and Szymanski, 2005). In 2009, the Big Four banks had 34.5 million accounts and they are expected to have 42 million retail accounts by 2012, an increase of 22% (Metcalfe, 2009). Schoombee (2000) maintains that all of the Big Four banking groups have created divisions to serve the unbanked or underserved in the economy and since then, more initiatives have come to the fore, with the launch of products such as Mzansi. Niche players include, amongst others, Capitec Bank, Teba Bank, WIZZIT Bank, MTN Banking and Postbank (SA Financial Sector Forum, 2008).

4.4.1.1 Sampling method

A convenience sampling technique was applied in choosing the countries where evidence of financial exclusion could be found. A judgemental sampling technique was applied to determine interview respondents, in which the researcher selected interview members based on some appropriate characteristic (Zikmund, 2003). In the case of this research study, interviewees within the population of relevance were individuals working in financial institutions who have been directly involved in the implementation of products or services for the unbanked and underbanked markets of South Africa.

4.4.1.2 Sample size

Literature on eight countries with evidence of financial exclusion was reviewed; and between one and four individuals from each of the financial institutions, involved in the implementation of products and services for the unbanked and underbanked markets, was interviewed.

4.5 Data gathering process

For the secondary data, data collection occurred through the interrogation of various electronic databases, newspaper and magazine reports on financial inclusion. Data collection also occurred through direct participation by the respondents in the form of face-to-face interviews, as they could provide an efficient and accurate means of assessing information about the defined population (Zikmund, 2003). The researcher was guided by an open-ended interview guide (see Appendix 1) and the interviews were recorded.

4.6 Data analysis

Data from the research interviews was edited and coded in order to provide the input that produced the information required to answer the research questions (Zikmund, 2003). The data was analysed using a grounded theory building approach. Grounded

theory building is a general methodology of analysis linked with data collection that uses a systematically applied set of methods to generate an inductive theory about a substantive area (Glaser, 1992, p.16) in (Douglas, 2003). The process of generating grounded theory involves data being systematically collected through field observations, interviews, meetings and the inspection of documentation where appropriate or possible (Douglas, 2003). Secondary data was reviewed to identify common themes and knowledge gaps.

4.7 Research limitations

The following aspects are limitations to this study:

- Time constraints and issues of access did not permit a study of all financial institutions i.e. the four big banks, plus some of the smaller players such as Capitec, Teba Bank and Wizzit.
- Some of the smaller players declined to participate in the study, so the respondents who were interviewed for this study were only from large financial institutions. The results of the study are therefore not representative of a cross-section of views on the subject.

5. CHAPTER 5: RESULTS

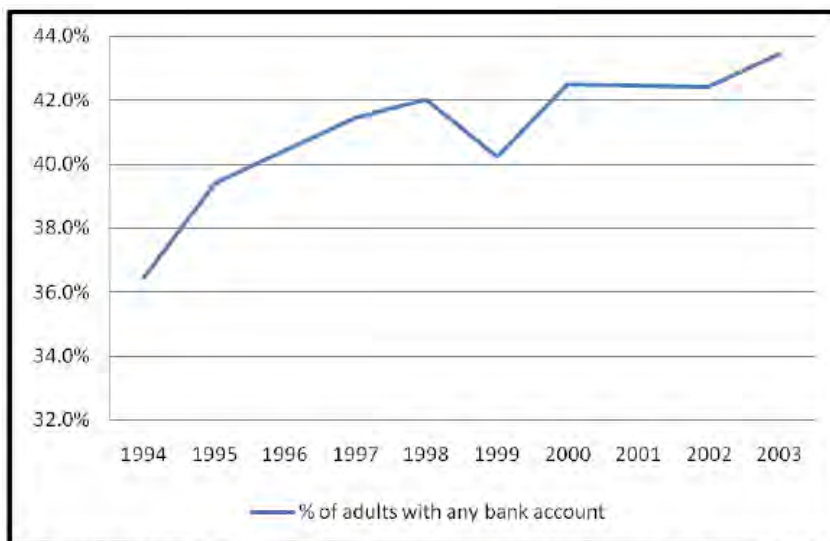
This chapter reports on the results of both the country studies and the face-to-face interviews that were conducted. It consists, firstly, of the findings from the secondary data analysis of various countries. It then proceeds to report on the results of the face-to-face interviews with industry practitioners

5.1 Secondary data – country studies of the unbanked and underbanked

5.1.1 South Africa's unbanked and underbanked markets

In South Africa, the issue of banking the unbanked is one which the financial services industry has been grappling with for many years. During the late 1990s, South Africa's Big Four banks (ABSA, FNB, Nedbank and Standard Bank) “developed and implemented different strategies to reach out to the black working class with basic banking products. These strategies often involved the development of new brands to appeal to and differentiate the offering from the rest of their mid- to upper-income market offerings” (FinMark Trust Report, 2009, p.15). The strategies were successful as is evident from the increase in usage of transaction bank accounts, illustrated in **Error! Reference source not found.** below (the graph is calibrated up to 2003 because the Mzansi initiative was launched the following year, in 2004). The approach used delivered the objective of banking previously unbanked, formally employed individuals. Growth started to slow down around 2002 however, with most formally employed individuals already having been banked.

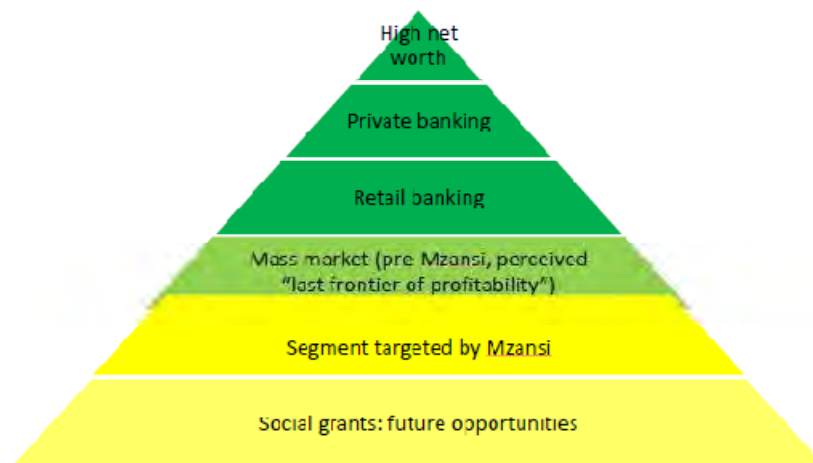
Figure 6: Percentage of South African adults with a bank account pre-Mzansi, 1994 – 2003



Source: All Media & Products Surveys (AMPS), as presented in Fig. 2.1 in Porteous, D., *Banking on Change*

In the early 2000s, South Africa’s financial institutions faced growing political pressure because of issues relating to a lack of access to financial services. It was in this climate that, at the Nedlac Financial Sector Summit of 2002, “the Chairman of Standard Bank, Derek Cooper, speaking on behalf of the entire financial sector, committed the sector ‘to working in partnership with Government, labour and the community to bring about...change’” (FinMark Trust Report, 2009, p.16). This assurance led to the development of the Financial Sector Charter, which committed financial institutions to among others – access to financial services. The interpretation of access is wide, but among other definitions, the Financial Sector Charter defines effective access as “a sufficiently wide range of first-order retail financial products and services to meet first order market needs, which are aimed at and are appropriate for individuals who fall into the All Media Product Survey (AMPS) categories of LSM 1-5”; “appropriate and affordably priced products and services for effective take up by LSM 1-5; and “structuring and describing financial products and services in a simple and easy to understand manner.” (Financial Sector Charter, 2004, p. 3). These Charter commitments led to the development of the product umbrella called Mzansi – an avenue to banking the next tier of South Africa’s unbanked. The segmentation position of Mzansi is illustrated in **Error! Reference source not found.** below.

Figure 7: Segmenting South Africa's market for retail transactional, savings and banking



Source: FinMark Trust, The Mzansi bank account initiative in South Africa – final Report, p. 23

FinMark 2006 data (Porteous, 2007, p.9) shows that some progress had been made in increasing the number of banked individuals in South Africa, as illustrated in Table 2 below:

Table 2: Comparison of banked profiles

Category	2004	2006
1. Currently banked	13m (48%)	15.9m (51%)
Unbanked Made up of:	14.1m (52%)	15.3m (49%)
2. Previously banked	3.6m (13%)	3.6m (11.5%)
3. Never banked	10.5m (39%)	11.7m (37.5%)

Source: FinScope™ SA 2004, 2006

5.1.2 Botswana's unbanked and underbanked markets

The biggest concerns about financial coverage in Botswana relate to geographical and income-related exclusion. The structuring of banking products and services seems to reflect a belief that there is little or no profit to be made from serving low-income and/or rural and peri-urban/semi-urban communities. As a result, the use of banking is relatively low among the rural population, the unwaged, the young and the elderly, and those with less education.

The FinScope™ 2004 survey revealed that Botswana had a relatively low demographic penetration of bank branches; with 3.8 branches per 100 000 people - ATM availability was better, with nine ATMs per 100 000 people. Around 45% of the population in Botswana lives in settlements with a permanent banking presence, but many large population centres have no local access to banking services. The survey also investigated why the unbanked do not have bank accounts. The results showed that the main disincentives to having a bank account were unemployment and low incomes. In addition, the requirement to pay service fees, the expense of maintaining an account, and distance from banks are cited as important barriers to banking.

The FinScope™ 2004 study showed that nearly half of the population was financially excluded, in that they did not use any financial institutions, and that over half of the population was unbanked. This suggests that this portion of the population is largely restricted to cash-based transactions and does not experience the benefits that various types of financial services (transactions, savings, insurance and credit) can bring. It is also unlikely that the extension of the branch banking (“bricks and mortar”) network to cater for especially the unbanked, would be commercially viable. Innovative approaches are therefore needed if banking services are to be extended to the unbanked, with the potential benefits for economic growth and poverty reduction. These solutions will most likely need to be based on “branchless banking”.

The FinMark report suggests that strategies to make the financial sector more inclusive could follow a number of different courses (or a combination of them) and suggests four main approaches:

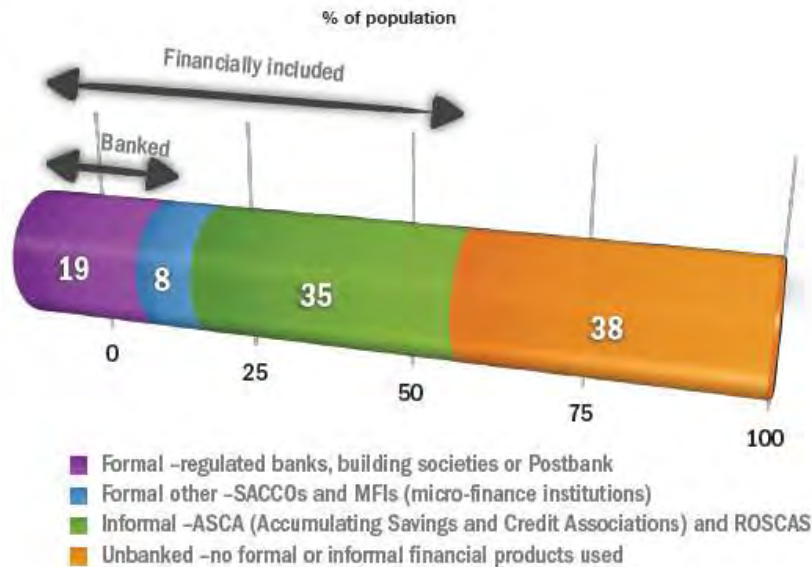
- Encouraging institutions that already deal with the low-income market (e.g. the Botswana Savings Bank) to broaden their services;

- Encouraging private sector/market-led solutions, especially those that take advantage of emerging technological opportunities to provide low-cost banking services, perhaps making use of agents, such as retail stores;
- Changing the bank licensing regulations to provide more flexibility in the provision of banking services; and
- Pushing the banks (whether by moral suasion or more formal pressure) in the direction of greater social inclusiveness (Jefferis, 2007).

5.1.3 Kenya's unbanked and underbanked markets

According to a 2007 survey by The Financial Services Deepening Trust, only 19% of Kenyans had access to formal financial services (Retail Banker International, 2009). The survey reported that a further 43% had access only to informal financial services such as savings associations and microfinance institutions. Some 38% was entirely unbanked. About 27% of Kenyans owned a mobile phone and a further 27% had access to one via family or friends. Less than 20% of unbanked consumers, or those making use of informal financial services, had a mobile phone. With only 450 bank branches servicing a population of about 39,8 million (UN, 2009), a mobile channel holds great promise as a way of extending financial services to Kenya's unbanked and underbanked (Retail Banker International, 2009).

Figure 8: Financial Inclusion in Kenya, 2007



SACCO = Savings and Credit Cooperatives; ROSCA = Rotating Savings and Credit Association

(Source: FSD)

M-Pesa is a mobile phone-based money transfer service, owned by Kenya’s largest telecommunication services provider – Safaricom. The service was launched in March 2007 and has about 5 million subscribers. The service allows Kenyans to send and receive money via SMS messages and collect or deposit cash at any of the network of 4000 Safaricom outlets and other agencies around the country. To open an account, Safaricom subscribers present their Kenyan national identity card and complete a simple registration process. The account identifier is the mobile phone number (Retail Banker International, 2009).

M-Pesa can also be used to pay for goods and services if the merchant accepts this form of payment. To make a deposit, customers purchase a “mobile money” scratch-card which is similar to a prepaid airtime card and enter the code into their phone. To withdraw funds, the recipient takes the text message to any agent in the network and “cashes-in” by entering a secret code and presenting identification. M-Pesa fees are significantly lower than those charged by other money transfer agencies and compares favourably to fees charged by local banks. M-Pesa funds are also not held in individual bank accounts, but in a central account held by the Commercial Bank of Africa. M-Pesa

has a full transaction tracking and reporting systems as well as money-laundering measures (Retail Banker International, 2009).

Safaricom says that the secret to its success is keeping things simple, focusing on what customers want and getting early visibility and adoption. A key challenge going forward is the continued support of regulatory authorities. M-Pesa is classed as a mobile payments system and does not require a banking license. Some banks argue however, that M-Pesa operates like a bank and should be regulated as such. M-Pesa does not however, pay interest on deposits or charge transaction fees. The potential for M-Pesa to provide financial services to the unbanked depends on whether the benefits of the service are compelling enough to persuade potential users to acquire mobile phones to use the service (Retail Banker International, 2009).

5.1.4 Brazil's unbanked and underbanked markets

Brazil is one of the most unbalanced countries in terms of wealth distribution, with about 40 million of a population of 194,2 million (UN, 2008) Brazilians either unbanked or underbanked. The use of retail agents by existing banks to deliver financial services through supermarkets, pharmacies and lottery kiosks has transformed the availability of banking services throughout the country. Much of the potential of this type of service stems from the availability of information and communication technologies that can be used to record and transmit transaction details quickly and reliably, and mobile phones and smartcards have the potential to provide stores of value (Jefferis, 2007, p. 24).

Since around 2000, there has been an unprecedented growth in the outreach of Brazil's banking system. Most striking has been the huge expansion in correspondent banking outlets; more than 32 000 new correspondent outlets were added from 2000 to 2004. In Brazil, 74 financial institutions (57 banks and 17 financial companies) had over 38 000 formally recognised correspondent outlets by the end of 2004, and an

estimated 90 000 formal and informal correspondents by end 2005 (Kumar et al, 2006, p. 1). Many financial services are offered through correspondents without the need to open an account. While only 43% of the adult urban population had a bank account, almost twice that proportion had access to some bank services through the use of the correspondent outlets. With the use of correspondent bank outlets, the number of municipalities with no financial services has shrunk to zero. Financial services became available to many in geographically remote regions and to poor people, who had been chronically underserved. Brazil's correspondent bank arrangements appear to illustrate a model of achieving scale.

Brazil's government has developed alternative service payment systems and regulations to encourage access to savings. Measures taken by the government in 2004 follow a model based on the U.S. Community Reinvestment Act in requiring Bank disclosure of location and income levels of clients. At the same time, the government has introduced certain regulatory requirements to encourage the offering of affordable savings accounts, to extend micro-credit, and initiate a housing subsidy credit-linked scheme to reduce the risk that banks perceive in working with the poor, while working with the judiciary to enforce legal dispositions to customers of all income classes. Recent improvements include the use of banking services in the administration of conditional cash grants, whereby families below a certain income level receive monthly allowances provided their children attend school regularly and get vaccinated (Bolsa Familia and Bolsa Escola). These grants, targeting women in particular, are dispensed through very simple ATMs that do not require literacy skills, or previous banking experience. Moreover, the ATMs have a tremendous impact on increasing the familiarity of the population in using banking technology and improving their self esteem and sense of social and economic inclusion (Solo, 2005, p. 3)

5.1.5 India's unbanked and underbanked markets

Initiatives by Indian policy-makers to improve the outreach of both credit and savings services to rural households can be traced back to the late 19th century (Fisher and Sriram, 2002) in (Arora and Leach, 2005). During the first phase, which continued up to the 1960s, the focus was on delivery of agricultural credit through cooperatives, while during the second phase the focus shifted to commercial banks. The Integrated Rural Development Programme, the largest state supported small loans programme in the world covered over 50 million households during 1980-99. The twenty years starting with the nationalisation of the ten largest commercial banks in 1969 and ending with the onset of financial liberalisation in 1990, marked the heyday of the Indian social banking program. At the point of bank nationalisation, the Indian central bank committed to increasing bank presence in rural areas and to equalising population per bank branch across Indian the states. In 1977, as part of this endeavour, the central bank imposed a 1:4 branch license policy which required banks to open four branches in rural unbanked locations for every branch opened in an already banked (typically urban) location. As a result, a network of Regional Rural Banks (RRBs) was established, leading to a rapid expansion of bank branches in rural areas. This policy was discontinued in 1990, with the onset of financial liberalisation (Burgess, Pande and Wong, 2005).

An analysis of the Indian social banking program shows that rural branch expansion has been associated with a reduction in the levels of rural poverty. Bank borrowing was also higher among rural households in states that saw higher rates of rural branch expansion. These findings suggest that regulation of the Indian banking sector played a key role in directing bank credit towards the poor, and that easier access to bank credit and saving opportunities was associated with a significant decline in rural poverty (Burgess, Pande and Wong, 2005). To achieve this reduction in poverty however, the Indian state invested substantial resources in the development of a state banking

sector. The third phase of economic liberalisation and financial sector reforms was triggered by the financial crisis of the early 1990s (Fisher and Sriram, 2002) in (Arora and Leach, 2005). Post 1990, the main performance indicator for the central bank was bank profits and after the policy of nationalization was disbanded, rural branch expansion into unbanked locations ended.

With 27 public sector banks, 30 private banks, 36 foreign banks, 196 RRBs, 5 local area banks and over 66 000 cooperative banking institutions, India has an extensive banking infrastructure. Despite the extensive infrastructure, there are still wide gaps in the quality and outreach of financial services. Sinha and Patole (2002) in (Howard, Jones, Williams, Nilsson and Thorat, 2007) note that despite the vast bank network in India, the financial needs of the poorest are largely unmet. The All India Debt and Investment Survey in 1991 found that 36% of rural households depended on the informal sector, with only occasional evidence of transactions with the formal financial sector (Rutherford and Arora, 1997) in (Arora and Leach, 2005). Banking statistics also show shrinkage in small loan services over the years. “The proportion of bank credit to small borrowers (below Rs 25,000) has come down from 18.3 per cent of total scheduled bank credit in 1994 to 5.3 per cent in March 2002. During the same period, the number of small borrower accounts has reduced from 55.8 million to 37.3 million. Considering that India has nearly 110 million farms and nearly 35 million non-agricultural enterprises, the banking system should have been striving to increase its base to 145 million borrower accounts, rather than reduce the number of accounts to 37.3 million” (Mahajan and Ramola, 2003:2) in (Arora and Leach, 2005). Basu (2006) in (Howard et al, 2007) says that apart from a financial climate which is not conducive to rural lending, banks are reluctant to serve the rural poor because of uncertain repayment capacities of the borrowers and high transaction costs of rural lending.

5.1.6 Europe's unbanked and underbanked markets

Financial exclusion is an important dimension of social exclusion and it represents a key dimension that European policy-makers seek to address. Structural and strategic developments in the financial services industry have served to exacerbate financial exclusion in Europe. The liberalisation of financial services and subsequent intensification of competition among banks, serves to explain why financial exclusion has become more evident. The rise of customer value concepts has resulted in increased customer segmentation and the pursuit for more affluent customers has been especially significant. In an effort to maximise shareholder value, banks have implemented standardised and rigid practices in screening customers (credit scoring) and formulating profitable financial contracts (loans, deposits). This has made it difficult for certain population groups to access financial services and has caused the exclusion of those whose profile does not fit within the current standards (Carbo, Gardner and Molyneux, 2007).

The profile of those who are excluded incorporates people who are less well-off, less educated, or unemployed, as well as women, older and younger members of society, and ethnic minorities. The consequences of financial exclusion are becoming more serious in an environment where an increasing volume of payments are made via bank accounts. The financially excluded borrow from non-status lenders who charge high prices and the loans are often secured on the borrower's property. The consequences of non-repayment are therefore especially serious.

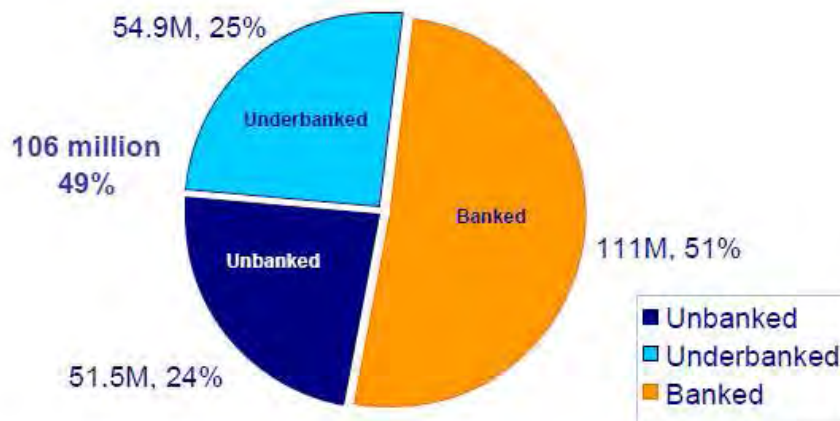
A related issue is the practical relevance of local knowledge and presence by financial services firms. As financial services firms desert certain geographic localities and customer segments, information for assessing respective risks is reduced. Without a local presence and the customer knowledge that results from such presence, financial institutions may become more risk averse in their lending. While the benefits of

financial liberalisation and increased competition continue to be sought, the free market alone does not seem to be capable of solving the issue of financial exclusion. Historically, in many European countries, “public models” and social responsibility have been emphasised. Yet the Horter study quoted in (Carbo et al, 2007) states that shareholder value will increasingly drive European financial services firms. The implication is that financial exclusion is likely to become more widespread and a policy response will be required. To date, the position of the European Commission on financial exclusion is unclear. The European Union has also not played a role in encouraging banks to offer low-income bank accounts.

5.1.7 The USA’s unbanked and underbanked markets

The figure below is an indication of the unbanked and underbanked percentages of the United States adult population in 2008, from the Centre for Financial Services Innovation (CFSI) underbanked consumer study.

Figure 9: Unbanked and underbanked percentages of U.S. adults



Population demographics in the United States are undergoing significant change and between 2000 and 2030, the U.S. population is projected to increase by 29%. During the same period, the total minority population may increase by 79% (Robbins and Contreras, 2006). People of Hispanic origin are the largest minority group in the United States, equalling more than 14% of the U.S. population. Hispanic/Latino immigrants

constitute a large portion of the unbanked and as this population increases, so will the number of unbanked. As Hispanic populations grow, so does their importance to retail-oriented financial institutions.

Immigrants typically migrate to the United States seeking better employment or lifestyle opportunities for themselves and their families than are available in their home countries. From the worker's perspective, the ability to deposit one's salary into a transaction account helps ensure safety against theft or loss. It also accommodates other financial transactions such as account payments and transactions drawn on a deposit account. Unbanked workers must find other ways to accommodate their financial needs (Caskey 1994; Dunham 2001; Rhine, Greene, and Toussaint-Comeau 2006) in (Sherrie, Rhine and Greene, 2006). Moreover, households that forego a relationship with a financial institution are unable to easily establish credit worthiness, often resulting in limited credit access or relatively more expensive credit available (Sherrie, Rhine and Greene, 2006, p. 23).

Understanding variation among unbanked Hispanic consumers' needs and the barriers they face may assist financial institutions in developing products that better suit this customer segment. While many of the survey respondents in the Robbins and Contreras study (2006) indicated that they maintain some type of deposit account with a financial institution, the remaining survey respondents noted the foremost reasons for remaining unbanked as the lack of necessary identification documents, with the language barrier a close second. Identification requirements may differ across financial institutions and some consumers are discouraged by these requirements. The survey found that respondents who have resided in the U.S. for shorter periods were very unlikely to have multiple identification documents.

Other reasons for remaining unbanked include distrust of financial institutions and financial literacy issues. Additional studies have shown that unbanked householders tend to be less educated and younger, tend to have lower income, and tend to be members of a minority group (Rhine, Greene, and Toussaint-Comeau 2006; Hogarth and O'Donnell 1997; Kooce-Lewis, Swagler, and Burton 1996) in (Sherrie, Rhine and Greene, 2006, p. 23). Building relationships with Hispanic consumers is important in order to overcome distrust of banks. Financial education and partnerships with community-based organisations are vital to reaching Hispanic consumers and developing relationships. Furthermore, in order to overcome misconceptions about bank products, banks need to educate consumers on their product availability (Sherrie et al, 2006).

From a regulatory perspective, the United States employed affirmative action in the form of the Community Reinvestment Act of 1977, which aims to encourage banks and other deposit-taking institutions to help meet the credit needs of the communities in which they operate, especially in low and moderate-income communities. This Act requires that each bank's record of helping to meet the credit needs of its community be periodically reviewed. This record is taken into account by the authorities when banks apply for regulatory approval to expand their activities (Carbo et al, 2007).

5.1.8 Mexico's unbanked and underbanked markets

This section of the report is based on the results a 2002, World Bank survey of Mexico City's unbanked to profile the unbanked and to explain why they are unbanked; as well as a 2005 nationwide survey. The results showed that the unbanked population in Mexico was somewhat less educated than the banked population, was less likely to be working, and had a lower household income. Only about 10% of GDP was held in savings accounts at commercial banks and just 15 - 25% of the urban population and 6% of the rural population had a savings account in a formal financial institution

(Klaehn et al., 2006) in (Djankov, Miranda, Seira & Sharma, 2008) Bank branch penetration in Mexico was low, with 7.6 bank branches per 100 000 people. The low rate of penetration was exacerbated by recurrent currency crises and a weak regulatory environment. There were few practical alternatives for people to cash cheques, other than to go to a bank. Banks in Mexico commonly cash cheques for people who do not have deposit accounts and they do not charge a fee for this service (Caskey, Durán & Solo, 2004).

Unbanked individuals in the World Bank survey were asked why they were unbanked and most (72%) responded that they had not tried to open an account because they either did not have enough money, or that the minimum balance requirement was too high. Only 3% of the respondents reported that bank location was a barrier. Almost 9% of the unbanked survey respondents said that they did not trust the banks, which reflects the turbulent history of Mexican banks over the past 20 years.

In recent years, banks have introduced new products that could benefit a significant share of the unbanked. For example, 12 of the 45 commercial banks in Mexico City offer payroll debit cards which enable a worker who does not have a traditional deposit account to be paid electronically. The worker can use the card to withdraw funds from an ATM or to purchase goods at a store that accepts debit cards. The card is linked to an electronic account that keeps track of the remaining balance. The account is not a true bank account, however, since the worker cannot make independent deposits into the account or write cheques on the account.

Another initiative came from a non-bank. A large department store chain, Elektra, with a largely working-class clientele, applied to obtain a banking charter, which the authorities granted. Elektra named its bank “Banco Azteca” and located many of its offices within its department stores. The bank structured its products, both deposit

accounts and loans, to meet the needs of moderate and middle-income households. Banco Azteca appears to be very successful, which could encourage other banks to start serving this market. Banco Azteca opened its first office in 2002 and by mid-2003; it had over two million deposit accounts and 836 branches. Part of the basis for such rapid growth was that the bank could market to households that had been credit customers of Elektra, and by opening small branches within existing stores, the bank could keep its facilities costs low (Caskey, Durán & Solo, 2004).

Other non-bank initiatives to attend the unbanked include institutions that make loans but do not take deposit accounts. Formally, these non-bank financial institutions are known as “Sociedades Financieras de Objeto Limitado” (SOFOLAS). They are also called “specialised” banks since they are exclusively dedicated to one sector (for example: construction, automobile, etc) or activity (for example, credit cards). They finance their assets by selling debt securities or by obtaining financing from other financial institutions. Their main activity consists in granting loans for the acquisition of specific assets such as cars or houses, or issuing credit cards. SOFOLAS have become the main source of financing for new auto purchases, making it possible for many people to buy cars who might not be able to obtain bank financing for this purpose (Caskey, Durán & Solo, 2004).

The gaps left in the market by commercial banks have, to some extent, also been filled up by informal microfinance institutions. However, these informal institutions were, insecure places to keep money because of a lack of regulatory oversight. In 1994, the Mexican Congress modified the law to allow for the legal existence of the Savings and Credit Cooperatives, and by 2000 there were more than 600 of these organisations, known as “Cajas Populares”. Since the Cajas had already developed lending relationships with clients, the Mexican authorities decided to use their existing structure to broaden financial access and to regulate the existing Cajas in 2001. Despite the

Cajas and their electronic links to Bansefi, the development bank, the problem of lack of physical access to banking services remains acute, with 43% of municipalities in Mexico having no commercial bank, Bansefi, or registered microfinance institution (Djankov, Miranda, Seira & Sharma, 2008).

Banks in Mexico are profitable in serving low-income markets and this is attracting the participation of new entrants. The 2008 national survey highlighted that while the unbanked in Mexico are poorer than their banked neighbours, the corresponding differences in wealth are smaller, with education being another important correlate of the decision to open a bank account. The study found no evidence of prohibitively high bank account costs, and given that in the sample, the distribution of income across the banked and the unbanked was similar, this suggests that it is not a simple transactions cost-benefit calculation alone. The findings of the study seem to imply that education and other unobserved households traits play a significant role in the decision to use banks (Djankov, Miranda, Seira & Sharma, 2008)

5.2 Mobile banking for the unbanked and underbaked

Mobile phones have evolved to become tools of economic empowerment for the world's poorest people. The phones compensate for inadequate infrastructure such as bad roads and slow postal services, allowing information to move more freely, and making markets more efficient (The Economist, 2009). The GSMA, a worldwide consortium of mobile industries, and the Bill & Melinda Gates Foundation have teamed up to found the "Mobile Money for the Unbanked" (MMU) initiative, to promote mobile banking in developing countries. The Foundation has donated US\$12.5 million and will support twenty projects in Africa, Asia and Latin America. The goal is to supply 20 million unbanked people with mobile financial services by 2012 (Africa Research Bulletin, 2009).

Mobile money services allow small retailers to act like bank branches (The Economist, 2009). In South Africa, a new Amendment Act to RICA (the Regulation of Interception of Communications and Provision of Communication-Related Information Act) came into effect on 1 July 2009. The Act is intended to assist law enforcement agencies with tracing criminals where mobile phones are used to commit major crimes; however, this new regulatory requirement has had the unintended consequence of making it more difficult for customers to register for mobile services, including mobile money (Mobile Money for the Unbanked website, 2009).

To date, only two m-banking offerings in South Africa bundle the opening of a new bank account together with access to m-banking in a way that has the potential to be transformational - MTN Banking and WIZZIT. Both are alliance banking models in which a telco (MTN) or a third party (WIZZIT) ally with a bank (Standard Bank and Bank of Athens respectively) to provide a separately branded and marketed basic transactional bank account with a debit card. Both rely heavily on existing channels such as ATMs or branches for top-up or cash withdrawals; while offering the functionality of balance requests and making person-to-person payments to any other South African bank account holder. Table 3 below is a summary of the major m-banking offerings in South Africa, and it illustrates that there is little difference in functionality.

Table 3: Major m-banking offerings in South Africa

	FNB	MTN Mobile Money	Wizzit
Bank at which account is held	FNB	Standard Bank	Bank of Athens
Account also linked to a debit card for ATM/POS use	Yes	Yes	Yes
M-banking functionality			
1. Informational (balance enquiry, SMS alert, etc)	Yes	Yes	Yes
2. Payments (inter-account transfers, P2P transfers, bill pay, airtime purchase)	Yes	Yes	Yes

	FNB	MTN Mobile Money	Wizzit
3. Cash access (deposit and withdrawal via ATM or branch)	Yes	Yes	Yes
Cost per month	R46/R41	R33/R29	R29/R23
Category of m-banking	Bank-led	Hybrid: JV	Hybrid: non-bank driven

While WIZZIT is the cheapest of the offerings, it is still more expensive than a basic Mzansi account, which comes with a debit card but without mobile access. It is clear that current mobile offerings do not significantly alter the affordability of basic bank accounts, and that their transformational potential must lie in other characteristics.

“Mobile money presents a shining opportunity to start a second wave of mobile-led development across the poor world. Operators, banks and regulators should seize it” (The Economist, 2009).

5.3 Interview results

Interviews were conducted with six industry practitioners from three large financial services institutions in South Africa. The industry practitioners are all involved in the provision of products and services to underserved markets. Four of the respondents occupy middle management positions, while the other two occupy senior management positions. The respondents were asked to express themselves in their own words and minimum control was maintained over their responses. A list of guiding questions was used and thematic analysis was used to report the results.

The respondents were initially asked to provide insight into their understanding of the concept of financial inclusion. This afforded a useful point of departure, from which the discussions could continue.

5.3.1 The factors that have an impact on financial inclusion in South Africa

The influencing factors cited by the respondents can be summarised as follows:

- Financial factors
 - The use of informal financial offerings, especially in the rural areas where the lack of access to formal institutions leads to the increased usage of informal channels;
 - Affordability and unemployment: due to limited income and the “high” cost of banking services as a percentage of total income. FinMark research suggests that that to be affordable, the cost of banking services needs to be no more than 2% of total income. In addition, accounts could previously not be opened without a regular income; and
 - Accessibility: lack of banking infrastructure within close proximity, which translates to long distances that people have to travel to access services, at added cost. Access does not only relate to the extension of services to more physical locations, but also to making services more appropriate to the needs of people, so that products address the specific needs of the market; as opposed to having generic products that are actually middle-market products, being imposed on the unbanked and underbanked.
- Cultural and social factors
 - Poverty;
 - Low levels of education have an impact on financial literacy. In addition, banking products and services tend to be complex and therefore do not facilitate easy understanding;
 - Low levels of financial literacy and a lack of understanding about banking and how it works;
 - Lack of awareness and low levels of comfort with financial services offerings;
 - The process of opening an account is intimidating, especially the documentation requirements (as a result of FICA legislation) and may lead to people doing without bank accounts;

- Lack of a trusting relationship with the formal financial system. “Knowing who you are dealing with influences levels of comfort and knowing what banking is all about” (Interview respondent, 2009);
- Dignity: “Financial services need to take people’s social reality into account and interact with them in a dignified way. Financial institutions must deal with them as human beings with specific needs as opposed to just consumers and take into account where they are in the financial development continuum. This must be accompanied by sufficient support services and education to enable them to use the right products appropriately and to understand what they are getting themselves into” (Interview respondent, 2009). Barriers associated with issues such as language, complexity and access must therefore be removed;
- Lack of cost-effective distribution mechanisms; and
- Lack of awareness about innovations in the payments arena, associated with low levels of penetration of alternative payment mechanisms.
“If my life is 99% cash, I probably won’t be attracted to a bank account because where will I use a card?” (Interview respondent, 2009)

Informal and irregular income in this segment of the market means that minimum balances and monthly fee requirements do not work - the pay-as-you-go model is preferable. The way in which revenue models are viewed therefore needs to change. It is inaccurate to say that this market does not want to pay for services. FinMark research supports the view that clients are willing (whether consciously or not), to spend about 2% of income on obtaining financial services. This fee however, must be all-inclusive. It then becomes a volume game, where if one has sufficient transactions, very small profits can be made per transaction. As a service provider, it is important to keep in mind what clients can afford and then target high volumes.

While looking for financial offerings that will empower the unbanked and underbanked and improve their lives, it is important to be cognisant of the fact that such offerings come at a price. Driving cost down may mean driving inferior products into the market, and if recipients do not see the benefits of products, they may revert to informal financial services offerings. A delicate balance must be maintained between the level of customer sophistication, the needs of the customer and product features.

5.3.2 Enabling environment: The efficacy of the three components of the environment that exists in South Africa's financial services market

5.3.2.1 Institutional infrastructure

While the Financial Services Charter helped to set the ball rolling, the banks are now on board and it is because the regulatory environment is conducive to serving the unbanked and underbanked, that products like Mzansi have emerged. "South African laws and policies are highly developed and are some of the best in the world" (Interview respondent, 2009). Current regulation is already very focused on servicing the needs of the unbanked and underbanked, so more regulation is not required. Banking regulation in particular, allows for the effective functioning and stability of the South African financial services system, which is why the country was able to avoid the severe impacts of the recent financial crisis. The strong and healthy oversight role of the regulator has served to shield South Africa from the recent financial crisis.

While efficient regulation means high levels of professionalism in the industry, it also means high levels of detachment from the market i.e. regulation has kept banks away from the market. Direct engagement with the market is required, instead of through the banking ombudsman. In preference to regulation, it would be better to let the banks innovate on their own about how best to service the unbanked and underbanked in a customer-centric and cost-efficient manner. It would be preferable to let market forces prevail and let the banks voluntarily serve the various market segments, especially in

light of the fact that they are reaching saturation points with the other segments. By necessity, banks need to diversify into the unbanked and underbanked markets.

Regulation removes efficiencies and hinders innovation, which means that the best customer/product match is not always achieved. When institutions are observing a compliance requirement, then only the bare minimum is provided and this stifles innovation. Business should be allowed to innovate freely, driven by a solid business case and market requirements. Regulation does not promote long-term solutions as it forces the financial services organisations to focus on the present, rather than the future.

Commentary provided about specific pieces of legislation was as follows:

The Financial Services Charter acted as a trigger to financial inclusion, but most banks were already starting to look at that particular segment of the market. Regulation served to make the banks look at that segment of the market differently, and to create win-win solutions. Regulation raised the necessary attention and influenced the process of change.

The Financial Advisory and Intermediary Services Act (FAIS) requires that people must have certain levels of knowledge before giving financial advice. When attempting to address the needs of low-income communities, it is preferable to get bankers from the community in question, who understand the issues and are able to speak the local language. A significant amount of training is required to meet FAIS requirements and do justice to the products being sold.

Consumers at the lower end of the market do not always have proof of residence as they do not have water, electricity or telephone bills that could be used to confirm residential addresses. For this reason, the Financial Intelligence Centre Act (FICA)

legislation was initially problematic for service providers trying to serve the lower segments of the market. This requirement has been mitigated by Exemption 17, which now only requires customers to provide their identity documents. Such exemptions should be more common because of complexities around certain identification requirements at the lower end of the market. FICA is less of a problem for account-based interactions because there are multiple-opportunities to create a history and recoup the cost of acquiring the client. For single transactions such as remittances, clients still need to fulfil FICA requirements and this represents significant inefficiencies because although there is a single transaction, there is still the same cost of identifying the client.

What is useful in South Africa's regulatory environment is that there are no restrictions in terms of the use of technology, if the technology is an extension of what a financial services provider already does. There might otherwise have been issues with the use of mobile phones. The Regulation of Interception of Communications and Provision of Communication-Related Information Act (RICA) does not have the equivalent of Exemption 17, so there is a requirement to get details from clients such as proof of residence and an identity document. The unintended consequence of the legislation is that it has the impact of increasing the complexity associated with serving the poor by requiring proof of residence. Unlike FICA, RICA does not have a regulatory authority linked to it such as the Independent Communications Authority of South Africa (ICASA), but is a tool of the Department of Justice and Constitutional Development, whose only interest is in complying with the letter of the law. With FICA, it was possible to negotiate certain aspects, through the relevant regulatory authority, and with sufficient justification.

The RICA requirements have dictated that businesses whose operational models for serving the unbanked and underbanked involved giving away SIM cards, change their

operating model – at significant cost. In order to reduce the SIM dependency, other technologies have had to be explored, e.g. the use of USSD technology. This illustrates the point that the cost of compliance can be heavy and banks need to be innovative in the way that they address regulatory requirements. Some practitioners were of the belief that regulation should be minimised to improve ease of access to financial services.

5.3.2.2 Organisational infrastructure

High levels of concentration mean that between them, the four big banks have a fair depth of knowledge and capability and will provide proficient people, good training and make sure that regulation is complied with. The challenge is that the Big Four offer comparable products and services, and do the same things. Innovative approaches to market engagement are required.

It is the internal mindset, rather than the highly concentrated nature of the industry structure that inhibits the provision of financial services to the unbanked and underbanked. The way in which banks interact with one another, by default means that there is an availability of a national footprint and this allows any bank to deal, on a national level, with any other bank. The sharing of infrastructure drives down the cost of providing services on that infrastructure. Extending the use of the infrastructure to include as many people in the population as possible should not be difficult. The banks' current models however, are aimed at the middle and business classes. A break in the mindset is required to serve a wider audience.

Another respondent was of the opinion that the nature of South Africa's organisational infrastructure gives consumers choice because it is not only the Big Four banks that are available for use, but other options are also available, depending on the consumer's needs. South Africans are very innovative, so over and above the formal

options, there are also the informal channels, which work very well and give more choice.

Two respondents were of the opinion that the nature of South Africa's organisational infrastructure limits consumer's options and affects the underbanked because it limits offerings. As supported by the competition commission findings, dominant players disenfranchise smaller players. If there were more players, there would be more differentiation. High levels of concentration in the industry have negative impacts on consumers. People tend to trust bigger banks, but smaller banks are making inroads into the market, especially with mobile offerings and efforts that are being made to go to the customers, in the environments in which they live and work. Having distinctive brands also seems to play a role in terms of differentiation and because the Big Four have stronger brands and better infrastructure, they seem to be in a better position to attract customers. The smaller banks' processes are however simpler and because of their size, are easier to change. Smaller banks are also more nimble, while changes in the bigger banks take longer – causing them to lose valuable time-to-market. Smaller banks have lower cost bases and lower overheads and can therefore offer more to customers in this segment of the market. Big banks have complicated cost structures and are multi-channel, multi-segmented organisations. They also tend to prioritise more profitable clients because of the good returns on these investments. Most bank costs are fixed, not variable. The cost of delivery is therefore high. Some of the smaller banks are using pricing as a strategy, but the sustainability of pricing as a strategy is questionable.

5.3.2.3 Support infrastructure

Direct engagement with the market is necessary in order to get a feel for their unexpressed needs of consumers in that particular market segment. While research in this area has expanded through initiatives such as the FinMark Trust, the larger banks

have only recently started to get in touch with communities in the places where they live. The appointment of community bankers, who live and work in the communities that they serve, is one way in which data is being gathered about the unexpressed needs of the market. Be that as it may, feedback mechanisms must be formalised. In-house research capabilities are also being formalised in order to get information that will enable the various financial services institutions to fine-tune their offerings. Products can therefore be targeted per market segment and increasingly, organisations will be able to match products to customer needs. Internal expertise and customer insights also play a crucial role in trying to understand the lower end of the market. In some organisations, focus mechanisms have been created, with supporting organisational structures.

Some practitioners said that not enough is being done to gather information about the lower end of the market. The FinMark Trust is nonetheless, a valuable source of information. The low levels of information about this segment of the market is a factor of the high levels of concentration in the market. Traditionally, the few market players could pick and choose their customer base, but the market is becoming saturated diversification strategies increasingly have to be explored. The unbanked and underbanked are becoming the next area of growth for financial services organisations, in order to create shareholder value. This change is out of necessity as banks realise that people do not stay in same market segment permanently

5.3.3 Leveraging technology to optimise the provision of products and services to the unbanked and underbanked

Technology is an enabler, but not a fit-all solution. It cannot change structure of the market because other components such as knowledge and capital input are necessary to accomplish such changes. Once the essentials are in place, putting the products and services into operation through the use of technology is fairly easy. Financial services

institutions must start with identifying the hindrances to providing services, and then understand how technology can be used. There is a case for the adoption of alternative channels because they help to deal with access and cost. However, face-to-face interactions are, still necessary because of a general lack of financial understanding in the market. One of the respondents was of the opinion that while alternative channels are useful, they will not eliminate feet from the branch.

The mobile phone is an important development in the provision of financial services because it allows reduced cost transaction capabilities, but it must be interoperable with existing systems. If the functionality is kept simple, then the mobile handset is a wonderful extension to financial services. If it is made complex, or requires specific models of handsets to work, then it will not be adopted, regardless of how it is packaged. For technology to be successful in serving the lower end of the market, it must be intuitive, meet a real need and must be familiar in some way. For example, although ATMs were not known when they were first introduced, they were successful because they met a real need of people not having to stand in queues in branches and of providing the convenience of unlimited operating hours. If technology works in a similar way to what people are already used to, such as buying airtime, the adoption is more likely to be successful and its use may be broadened to include uses such as remittances. "Technology must be a natural extension of a device's current use" (Interview respondent, 2009). Technology allows for low-cost augmentation of the range of services that organisations already offer. While technology does not provide a sustainable advantage, there is an advantage to being consistently first to market. There is high mobile phone use and ownership in South Africa, but retaining contact with the customer is difficult because mobile phone numbers change frequently.

5.3.4 Leveraging the retail store network to optimise the provision of products and services to the unbanked and underbanked

Most banks have formed alliances with retailers as a way of increasing coverage, access and value-add i.e. a retailer plus components of banking services under one roof. Leveraging the retail store network allows for the matching of where people shop and where they want to do their banking transactions. The retail network offers an advantage because customers already go there and relationships are already established. It is therefore easier to penetrate the market in this way.

Alliances with retailers are a critical, but challenging way to extend financial services. If banks wish to promote financial inclusion however, they cannot do so by using the current branch-model alone. The infrastructure and the way that banks currently interact with customers (the branch network) is expensive. Affordability is a significant issue in the lower end of the market. Financial services institutions report that the nature of transactions in the lower segments is characterised by high volumes and low margins, which makes the branch model very expensive. It would therefore be difficult to use that particular model to improve financial inclusion. Banks need to engage in a sustainable way with their customers and they cannot make the assumption that extending financial services to a further 25% of the population, for example, will necessarily mean that these 25% will become a feeder market into the middle market. There will be a large percentage of that market segment that will want to have access to financial services where they are, but that will remain in that segment without moving up into the middle market.

Banks need to engage with the market in a way that is at least marginally profitable. This requires a change in the current operational model and can be achieved through the use of third party transactional networks to enhance access and reduce cost. The most important third party transactional networks include retailers, mobile network

operators and state-owned organisations such as the Post Office. If alliances with retailers are adopted, the benefit for banks would include lower levels of dormancies and lower levels of closure.

Issues associated with alliances with retailers include:

- The provision of sufficient financial training to meet regulatory requirements.
- The protection of both brands, which is tricky to achieve because it means seeing the bank “through” the retailer.
- The sharing of revenue i.e. what the retailer is paid to provide the service. The model adopted must be flexible enough to change with consumer needs and behaviour. While the initial set-up is not too difficult; the trick is in sustaining the model in response to changing consumer needs.
- Alliances may lead to the deepening of relationships with customers and they also present the potential for co-branding opportunities for the alliance partners. The enhanced customer relationships which come about as a result of the alliances often motivate retailers to demand exclusive arrangements i.e. if a retail financial services provision agreement is signed with one retail chain, it may preclude a similar arrangement with the same bank at a competitor. While such an agreement may be beneficial to the retailer, the consumer loses out on the benefit of a choice of retailers with similar benefits.
- From the perspective of the banks, there needs to be a change in mindset and an ability to see retailers both as clients and as partners. Banks make significant margins out of retailers, due to the risks associated with the handling of cash. “It is not uncommon for banks to charge retailers up to 1% of each deposit” (Interview respondent, 2009). For food retailers, whose operating models are based on low margins, a 1% fee per deposit is significant. The change in mindset that is required is that it is acceptable for retailers to make money out of banks and their customers as well.

- Advantages can be attained from alliances between financial services providers and retailers, if the right retailers are used.
- Retailers can work with their customers to determine deposit and withdrawal times, thereby making cash management more efficient.

5.3.5 Optimising product design to meet the needs of the unbanked and underbanked

The issue of the complexity of financial services cuts across market segments. To optimise the provision of products and services to the unbanked and underbanked, interview respondents proposed the following:

- Adding complexity to products adds cost, which then has to be recovered from the customer. Products should therefore be kept simple and focus on the most common transactions e.g. remittances, withdrawals, deposits, airtime and other purchases. “Complexity elicits lots of migration within the banking system because of needs not being matched by the product” (Interview respondent, 2009).
- Solutions for the lower end of the market need to eliminate fees (minimum balance and monthly management fees) to comply with the affordability requirement.
- Transaction fees lead to the suboptimal use of transaction accounts because they become “money-in” and “money-out” vehicles, thereby exposing consumers to cash-risk.
- Consumers in the lower segments of the market are price-conscious, so products and services should be priced appropriately. “Consumers attach price to value” (Interview respondent, 2009).
- Products must deliver on their promises and on customer needs, without the frills. If the basic customer requirements are not fulfilled, the products will be subject to high levels of dormancies, which have an impact on acquisition costs.
- Matching products and services to customer needs is important and it leads to higher customer retention as opposed to dormancies. In the telecommunications

industry for example, understanding different customer requirements meant having to reduce the denominations of pre-paid airtime. Previously, pre-paid airtime came in set denominations, with the lowest being about R29. When the denominations were reduced, sales increased because the product suddenly catered to more needs.

- Trust is a key issue and can be achieved through being able to identify with the brand offering the product or service. The backing of a strong partner is also helpful.
- It became evident with MTN mobile money product that self-service does not work. Assisted models, using cheaper channels such as mobile are preferable and community bankers can provide most of the services.
- In enabling the retail network, all of the basic service transactions should be offered, not just purchase transactions such as the purchasing of airtime. Retailers need to be able to take deposits, enable withdrawals and balance enquiries. “Enable the withdrawal of money through avenues such as spaza shops” (Interview respondent, 2009).
- Financial services providers should pay attention to how customers are serviced and ensure that service is provided with respect and dignity.
- Education on product use is essential because in many instances, a lack of education leads to accounts being money-in-money-out vehicles. Such behaviour is a result of a cash-based mentality as opposed to awareness about point of sale and other electronic channels. “Economic upliftment and literacy levels are key to optimising financial inclusion” (Interview respondent, 2009).
- Products and services must be easy to use, easy to understand and accessible – “simple, but not patronising” (Interview respondent, 2009).
- It is prudent to develop products that can be distributed using low-cost channels such as mobile phone banking. It is also easier to deliver products through mobile

phone banking because the customer does not bring cost to the bank i.e. using banking halls and personnel.

- Products and services should increase awareness of the need for a cashless society because of the high cost of cash and the risk of cash.
- Banks already share infrastructure such as POS, ATMs and internet banking. To serve the underbanked and unbanked, it makes sense to extend and share infrastructure to include retailers.
- Financial services organisations ought to develop a coherent, recognisable and appropriate service proposition to bank this segment of the market.
- While collaboration is necessary to drive down costs, especially relating to infrastructure, each financial services organisation must approach the market independently. Financial services providers must compete in their value propositions to the various markets.
- The model for product and service provision should not be constrained by simply looking at South Africa, but should consider the whole of Africa as one market and employ the same model everywhere. While deployments may be different in different countries, the business model should be consistent and share operational capabilities.
- Service providers should also keep in mind that the aim is not to eliminate the unbanked, but to reduce the numbers by understanding the financial requirements of these customers. The cross-subsidisation of lower income products by higher income products is not sustainable and is what is happening with Mzansi at the moment. In addition, there needs to be an acknowledgement that conversion-rates from low income to high income products are not as high as may be desired, which implies that either products are offered to people who were not ready to grow in banking services, or the model used is not suitable to enable progression to other products.

5.3.6 Transaction versus credit products for meeting the needs of the unbanked and underbanked

Should financial institutions primarily use transaction products or credit products that are specifically targeted at the unbanked and underbanked in order to attract lower-income customers? This long-standing debate informs what service providers consider to be their primary relationship with their clients. It should not be one or the other, but the matter is influenced by the customers' context at a particular point in time, and is also driven by life events and economic cycles. The anchor product is driven by the cycle and what customers need. "Business models can develop with a certain flavour, but they must re-invent themselves and be driven by client needs, otherwise, they stagnate" (Interview respondent, 2009). The transactional model comes from a certain era, but banks must be flexible and constantly reinvent themselves.

A transactional account establishes an on-going relationship with a client and the customer will use it repeatedly. Through the agency of the transactional account, trust is established and the financial services provider becomes the first place that clients go to for other needs such as savings products, funeral plans, insurance and loans. The attraction to other financial services is built through transactional products. It also becomes easier and cheaper to "graduate" a transactional client to lending products because the client is already known to the financial services provider and they have a relationship. The financial services institution therefore does not have to price for risk.

While entry to banking should ideally be through transactional products, the two schools of thought cannot exist independently and the models are not mutually exclusive i.e. acquiring wealth vs. seed capital. The key is to understand the primary needs of the target market. If customers are entrepreneurial, they may require seed capital i.e. lending products to make them economically active. Transactional products imply that there is some money coming in the form of social grants or remittances for

example. Transactional products also provide opportunities for awareness campaigns and education.

5.3.7 The profitability and sustainability of service and product offerings for the unbanked and underbanked

Profitability should not be a key strategic reason for serving the lower end of the market. The motivation should rather be about life-time potential. Entry-level products offer a means to enter banking services. While evidence from industry shows that the upward migration into other accounts has not happened in great numbers, products such as Mzansi are a feeder stream to other bank accounts. Mzansi is not the only product that addresses this market segment though, and there has been a broadening of products and services for that end of the market. Some products have had good uptake and are breaking-even, while others are actually making small profits.

Some respondents were of the view that in order to serve the lower end of the market successfully with a full-service bank, a thriving and sustainable business must already be in place. The full spectrum of banking services must first be created, and only once the top end is stable, can the lower end of the market be tackled. While certain aspects of serving the low income market are profitable, profitability can only grow to a limited degree. Businesses must therefore always first target the middle or higher end of market, and then move downwards.

The big issue in serving low income markets is the cost to serve, so technology must be used to drive down costs. At high volumes, the model is profitable both in the transactional and lending spaces. Higher interest rates can also be charged in the lending spaces due to increased risk. It is necessary to capture a sufficient chunk of the market, to drive volume and be profitable. An additional benefit of increased financial inclusion would be a more accurate estimate of the Gini-coefficient, a measure of

income inequality. Financial institutions would then be better positioned to assess the relative size of the lower-end market

To serve the lower end of the market, a micro-banking model should be used, with a defined set of services. However, the service offering should not be too wide lest it becomes dysfunctional in terms of the market. A national footprint could then be established through third-party service providers such as the retail store network and mobile providers. There must be sufficient market engagement in terms of direct engagement, education and support and if priced appropriately; it will be hard to not make money in this market. A few elements also need to be in place:

- Before a financial services institution starts lending, providing savings products or selling shares, it needs to invest in a transactional network and transactional products. The institution needs to understand that it will probably not make money through transactional products, but they are the “glue” or financial infrastructure. Allowing retailers to handle those transactional accounts is beneficial because that is how the banking network and trusting relationships are built-up.
- A financial services institution that is prepared to invest in creating a transaction network through third parties and to engage with the market, followed by the introduction of additional products, while keeping the service charges appropriately low, is certain to make a profit. It may not be as much money as investment banking, but perhaps closer to the middle market. If financial services institutions extend the current operating model and build branches, failure is guaranteed.
- Profitability is possible, but it ties in with infrastructure. Cheaper channels must be found to service customers.
- To succeed, a bank must identify by when they want their products to be profitable and understand that profitability may be delayed and may only happen at later stages of the customer life-time value. Different measurements mechanisms are also required because if current methods of measurement continue, then financial

exclusion will continue. Current models of profitability do not take into account the needs of the unbanked and underbanked.

- It is important to take a cue from the customer, as opposed to punting products that may not be suitable. If different models of banking are explored, then it is possible to be profitable in servicing the unbanked and underbanked. Alternatively, it would be possible to serve this market by keeping the current delivery model, but changing the profitability model.
- The bundling of products e.g. funeral product, plus transactional product, often promotes customer retention and contributes towards profitability.

The low-income market is a low-value, high-volume business and solutions must be found that service that value proposition. Pricing is not a lever in this market because the margins are low, with average balances of about R200. Constant innovation is required to finance this market efficiently. Efficiencies can be achieved through the reduction of customer's touch-points and through the use of technology or alliance partners. While there is still a lot of work to be done, there is definite potential in serving low-end markets. Through encouraging a culture of education, these markets can become more sustainable. For banks, the proposition can be split into high technology clients i.e. self service customers, whose needs are mostly electronic; and high relationship clients, who need education and support. If banks are able to split their customers in this way, they can free-up some branch capacity, with increased capacity, comes an increased ability to explore different offerings such as serving low-income and other clients. Banking infrastructure costs are fixed and include rentals, staff etc, so the ability to segment customers according to their needs, would go a long way towards being able to service more clients. The challenge lies in the ability to service low income customers profitably.

“A complementary offering for corporate and investment banking clients would be the ability to offer low-end banking products for their employees this would allow an expansion of bank offerings” (Interview respondent, 2009).

5.3.8 Examples of service and product offerings for the unbanked and underbanked and the reasons for success or failure

Product or service	Outcomes/lessons learnt
<p>Mzansi: entry-level transactional banking product</p>	<p>Conceived before the signing of first Financial Services Charter and a bank-initiative to extend banking services.</p> <p>Successes</p> <ul style="list-style-type: none"> • Raised awareness and provided education about banking in the communities because it was a joint initiative and was promoted considerably for about three years. • It highlighted regulatory hindrances that were perpetuating financial exclusion, prompting solutions like “Exemption 17” for FICA. • It served as a simple introduction to banking. • Forced the banks to focus on the lower end of the market. • Raised levels of trust among people who had never interacted with financial services before. • Direct engagement by the banks. • Drove down cost and increased affordability because of no monthly fees, minimum ATM transaction cost etc. <p>Failure</p> <ul style="list-style-type: none"> • It does not address the issue of accessibility. • It has not led to a significant drop in the underbanked population because of the transaction costs. • The solution uses existing infrastructure, so it could not be as affordable. Distribution is an important component in determining product cost. • Stigma of it being a “poor man’s account”. • Innovation was constrained by it being a joint venture between banks <p>Summary:</p>



Product or service	Outcomes/lessons learnt
	<ul style="list-style-type: none"> • Broadened the market, but did not lead to a change in the business model. • Drove down cost, but did not engage the market sufficiently in terms of the extension of services and education. • Limited innovation. • On the surface, Mzansi looks unprofitable, but costs must be allocated differently for the product to be profitable. • Use of different channels e.g. mobile, could make product more profitable. • High levels of dormancies and closures suggest that there is a need for more education both on the part of the consumer and the branch people selling the products. • Dormancies present opportunities for other products e.g. remittances.
<p>Mobile centres and Sekulula for social grants</p>	<p>Successes</p> <ul style="list-style-type: none"> • Rurally based, heavy usage of ATMs for cash withdrawals, but, <p>Failures</p> <ul style="list-style-type: none"> • Deposits are over the counter
<p>Cash-send – remittance solution</p>	<p>Successes</p> <ul style="list-style-type: none"> • Sending money with a number and a pin, but no card needed. This solution reduces cash risk.
<p>The original MTN mobile solution aimed at MTN subscribers</p>	<p>Successes</p> <ul style="list-style-type: none"> • Very low costs <p>Failures</p> <ul style="list-style-type: none"> • Relied purely on the use of the hand-set and a self-registration process i.e. consumers could go through the registration process and end-up with a bank account. • The market requires assisted use of financial services because of the low levels of awareness and education about financial services.



Product or service	Outcomes/lessons learnt
Revised MTN mobile money	<p>Successes</p> <ul style="list-style-type: none"> • The solution has now been changed to an assisted sign-up process, while the technology remains the same. • Allows transactions through the retail-network . • Uses community bankers, who understand the communities and speak the local languages. Traditional branch banking is charged at Mzansi rates. • A 1% ad-valorem pricing structure is used to prevent cannibalisation. Fees are based on transaction value, not a fixed cost.
Mzansi money-transfer: remittances solution estimated as a R13bn a year industry in terms of the estimated volumes being transmitted. (5 years ago)	<p>Successes</p> <ul style="list-style-type: none"> • Reduced the cost of remittances through bank and Post Office distribution networks. The going rate at the time was about R50 through taxi drivers or other channels, so the aim was to reduce the R50 cost to perhaps under R20. <p>Failures</p> <ul style="list-style-type: none"> • Competition Commission, who stopped the banks from talking to each other about product design and cost. For the money-transfer product to work, it would have required wide access to infrastructure such as ATMs and the banks had wanted to talk to each other about issues relating to increasing access, product features and maybe reducing initiation fees through the use of the internet for the initiation component. The Competition Commission intervention meant that this ended up as a branch-to-branch solution, which inevitably became inconvenient and expensive, and did not meet the needs of the market. • Branch-based solution which did not work because of distribution mechanism. • Due to time delays and the Competition Commission intervention, the initiative ran out of



Product or service	Outcomes/lessons learnt
	steam.
Zimele insurance product	<p>Successes</p> <ul style="list-style-type: none"> • Industry-wide initiative <p>Failures</p> <ul style="list-style-type: none"> • Unlike Mzansi, there was not much hype created around the product. • The pricing was too expensive.
Community banking	<p>Successes</p> <ul style="list-style-type: none"> • Use of retailer network that customers can use. • Cell-phone based, therefore lower costs. • Mobile banking is a better solution for unbanked and underbanked because branches are not always positioned at the point of need and they have time restrictions. <p>Failures</p> <ul style="list-style-type: none"> • Lacked the necessary support structure in terms of awareness and education in terms of showing the community the benefit of banking products.
E-plan: transaction product	<p>Successes</p> <ul style="list-style-type: none"> • Managed to bank a large portion of employed, pre-Mzansi consumers. <p>Failures</p> <ul style="list-style-type: none"> • Previously not segmented properly and is currently being mined for up-sell and cross-sell opportunities.
Wizzit: cell phone banking	<p>Successes</p> <ul style="list-style-type: none"> • Use of low cost channel. <p>Failures</p> <ul style="list-style-type: none"> • Banking is about trust and trust is expensive because it requires a relationship. The flaw in the Wizzit model was not matching the people selling the product with the intended consumers in terms of age and where the Wizz-kids came from. The Wizz-kids could therefore not be effective brand-ambassadors. Wizz-kids are also techno-savvy and may not necessarily relate to the target audience.

5.3.9 Broadening of products and services

Ever since Mzansi started, there has been a deepening of penetration of financial services, but the product-set has remained constant: transaction accounts, funeral plan and consumption loans – every financial services institution offers this range of products. The range of options has not been expanded. When considering the introduction of new products and services, it is important not to make the product range too wide, because some products could become unprofitable because of limited usage caused by low volumes. In-depth needs assessments are required before offering products.

The financial services industry has fallen short in terms of the support structures to keep the deepening penetration going, especially with regards to education about the use of services. Micro-business loans are an area that is not adequately addressed, but financial services providers need to ensure that the right environment exists for the utilisation and re-payment of these loans. Apart from the informal structures that exist in communities, the financial services industry has not been able to extend savings capabilities sufficiently.

Banks have fixed costs, but banking this market requires new thinking such demonstrated by Wizzit, which capitalised on high mobile phone penetration, thereby addressing issues of access and cost.

5.3.10 Emergent themes on financial inclusion

There are two economies in South Africa and financial inclusion has to have an element of bringing two economies closer to each other by extending existing financial services in whatever form is possible, to more clients, beyond the current distribution. Even if a financial services institution thought of alternative models, there would always

be people whose needs do not warrant the use of a bank account. Financial services organisations need to think differently about these peoples' needs because of low levels of economic activity. Banks cannot by themselves bring about economic development, but they can enable it by bringing financial services to those have been excluded because of geographic isolation and socio-economic conditions.

The levels of cooperation between banks must go beyond driving down cost. They should formulate consistent banking models with different market engagement models. It does not matter if one bank does exactly what another bank does in terms of transaction processes on mobile handsets for example. From the consumer's perspective, this is in fact positive. There will still be room for competition in terms of pricing and market engagement. "What is important is to build the trust and to build the ease with which people interact with the system" (Interview respondent, 2009). An example is the way in which petrol is dispensed, which is the same, regardless of who the service provider is. By the same token, some product offerings in the financial services sector could be the same. "In financial services, it seems that sometimes things are done with the consumer in mind and other times not" (Interview respondent, 2009). Serving the lower end of the market is about more than Mzansi – there is a bigger proposition and it can be profitable. "Mzansi alone should not equal a bank's entry-level strategy" (Interview respondent, 2009).

Banking has already changed and cash may become even less prevalent, with the use of other payment channels and other innovations in the payments arena. Education is essential for increasing financial awareness, but can be informal such as at the points of sale. Education campaigns could be part of corporate social investment budgets and not priced into the products cost which must then be recouped. Trying to reach customers using a model that has never accommodated them will never be successful.

Account closures have nothing to do with product design, but rather with a mismatch between customer requirements and available products. Sometimes the need is for remittances, but because of limited product offerings, customers open bank accounts. Alternatives are being sought such as transmission wallets. The low-income business is a volume-based business and alliances with other service providers such as retail outlets are key in terms of enhancing access. If this is done, banks will notice lower levels of dormancy and lower levels of account closure.

6. CHAPTER 6: DISCUSSION OF RESULTS

This chapter comprises the interpretation and discussion of the results presented in the previous chapter taking into account the literature review in Chapter 2, and the eight research questions outlined in Chapter 3.

6.1 The factors that have an impact on financial inclusion in South Africa

Literature on the factors that have an influence on financial inclusion suggests that financial exclusion can come about as a result of lack of access, prohibitive terms and conditions of use, costly charges, ineffective marketing and self exclusion (Carbo et al, 2007). Access in this context, relates to prohibitive risk management practices that serve to exclude certain segments of the population; while marketing refers to campaigns that fail to include underserved populations. These factors have the effect of resulting in self-exclusion, as potential customers do not even try to gain access to the financial system because they believe they would be refused entry.

Evidence from the various country studies suggests that the factors that have an impact on financial inclusion include geographical and income-related factors; as well as factors related to gender, age, and levels of education. Other factors include levels of access, where appropriate access refers to the availability of products and services, that are easy to understand and suitably priced. Industry practitioners classified the factors that have an impact on financial inclusion into three categories viz. financial, cultural and social. Financial factors included the use of informal financial offerings and expensive distribution channels, while the cultural and social factors included issues relating to low levels of trust in formal financial services, low levels of financial literacy, the complexity of processes and the need to treat consumers with dignity.

Based on the findings, this research report concludes that the factors that have an impact on financial inclusion are diverse and range from environmental, to social and economic to personal. While it could be argued that the construct of financial inclusion affects on the economic well-being of individuals above all, the factors that have an impact on inclusion are varied and cannot be confined to economic factors alone. Similarly, that the causes of financial exclusion are not restricted purely to economic factors; and its effects also tend to have an impact on other spheres of an individual's well being.

6.2 Enabling environment: The efficacy of the three components of the environment that exists in South Africa's financial services market

The subject literature purports that for a financial market to operate effectively, three components within the financial services market need to be in place. The three components are institutional infrastructure, organisational infrastructure and support infrastructure (Arora and Leach, 2005).

6.2.1 Institutional infrastructure

In the country studies, evidence of the role of institutional infrastructure in optimising financial inclusion could be found in countries such as the United States and Brazil, who introduced the Community Reinvestment Act and adaptations of the Act. This Act requires banks to disclose the location and income levels of their clients and the record is taken into account by the authorities when banks apply for regulatory approval to expand their activities. In India, the integrated Rural Development Programme was an initiative aimed at combating geographical exclusion by encouraging the provision of financial services to rural communities. In Brazil, the government has introduced additional regulatory requirements to encourage the offering of affordable financial services.

Overall, the interview respondents were of the opinion that South Africa's institutional infrastructure is conducive to serving the needs of the unbanked and underbanked populations. They cited laws such as FICA and regulations introduced through the FSC to illustrate the effective functioning of South Africa's institutional infrastructure and the focus that exists on low-income markets. "South African laws and policies are highly developed and are some of the best in the world" (Interview respondent, 2009). Some respondents pointed out that while efficient regulation meant high levels of professionalism in the industry, regulation also had the effect of keeping banks away from the market. They argued that instead of regulation, it would be better to let the banks innovate on their own in a customer-centric and cost-efficient manner about how best to service the unbanked and underbanked.

What seems evident is that financial exclusion would be far more pronounced if the free market system prevailed without any oversight role from the state. This is apparent from the fact that in South Africa, at the time when there was no concerted regulatory effort on the matter, the issue was largely ignored by financial services institutions, as they preferred to interact with the more profitable segments of the market. Perhaps, as was suggested by some industry practitioners, with the saturation of the more profitable segments of the market, it is out of necessity that financial services organisations are beginning to find more innovative and even profitable ways of serving the underserved. Advances in technology, especially technology related to payments, have also been a major contributing factor in enabling the provision of products and services to the underserved. An effective institutional infrastructure is however, essential in ensuring the provision of products and services to the underserved.

6.2.2 Organisational infrastructure

While high levels of banking industry concentration are evident in the South African economy, countries such as Brazil and India have more diverse providers of financial services, with varying capacity and in competition with each other. Literature on Brazil

points to 74 financial institutions that have over 38 000 formally recognised correspondent outlets (Kumar et al, 2006). In India, there are 27 public banks, 30 private banks and 36 foreign banks (Howard et al, 2007). In the United States and Europe, where banking is deregulated, the high levels of competition have led to bankers to chasing high net worth business. The high levels of competition in these geographies are therefore a key contributing factor to financial exclusion.

Some interview respondents commented that high levels of concentration mean that between them, the four big banks have a fair depth of knowledge and capability and provide skilled people and good training while ensuring that regulation is complied with. The challenge is that the Big Four offer comparable products and services and do the same things. Innovative approaches to market engagement are therefore required.

While organisational infrastructure is an essential component in the effective functioning of the financial services system, it alone is not the only element that has an impact on the extent of financial exclusion. This is evident from the fact that financial exclusion still manifests itself, regardless of whether an economy is highly concentrated such as in South Africa, or is deregulated and highly competitive such as in the United States and Europe. In all instances, it seems that the pursuit for high net worth clients is the primary contributing factor to financial exclusion. Some interview respondents pointed out that it is the internal mindset, rather than the highly concentrated nature of the industry structure that inhibits the provision of financial services to the unbanked and underbanked.

6.2.3 Support infrastructure

Subject literature about financial inclusion in Europe highlights the relevance of local knowledge and discusses the fact that as financial services firms desert certain geographic localities and customer segments, information for assessing specific risk is

reduced. The literature draws attention to the fact that without a local presence and the customer knowledge that results from such presence, financial institutions may become more risk averse in their lending (Carbo et al, 2007).

Interview respondents stressed the need for direct engagement with the market in order to get a feel for the unexpressed needs of customers. While research in this area has expanded through initiatives such as the FinMark Trust, the larger banks have only recently started to get in touch with communities in the places where they live. The appointment of community bankers, who live and work in the communities that they serve, is one way in which data is being gathered about the unexpressed needs of the market; however, feedback mechanisms must be formalised in future. In-house research capabilities are also being formalised in order to get information that will enable the various financial services institutions to fine-tune their offerings. Products will therefore be targeted per market segment and organisations will increasingly be able to match products to customer needs. Internal expertise and customer insights play a crucial role in trying to understand the lower end of the market. In some organisations, focus mechanisms have been created, with supporting organisational structures.

Evidence from literature and from face-to-face interviews highlights the importance of customer intimacy. As the sources of information about the needs of the poor begin to diversify and as financial services organisations become more aware of the fact that to serve these markets segments successfully, business models and paradigms need to change, so the market will continue to witness more effective matching of customer needs to product features.

6.3 Leveraging technology to optimise the provision of products and services to the unbanked and underbanked

In terms of technological developments, the mobile phone is arguably the most significant development in the provision of products and services to the underserved. A significant percentage of the unbanked population being mobile phone users makes mobile banking an ideal channel to reach customers who do not have access to financial services (Cain, 2009). The 2009 Africa Research Bulletin states that mobile banking is allowing people who could never afford traditional bank accounts to send, receive and save money.

Interview respondents pointed out that while technology is an enabler, it is not a fit-all solution. Once the essentials of providing financial services are in place, operationalising them through the use of technology is fairly easy. The one condition that the respondents said should be accepted by the financial institutions was that due to the relatively low levels of financial literacy amongst the underserved populations, one-on-one presence is still necessary in the provision of financial services to the underserved. Self-service channels without human interface do not work in this market.

Based on these findings, this research report concludes that the use of technology is an important development in the provision of financial services to underserved markets, especially from the perspective of decreasing costs and increasing access. There is however, no way to counter the need for the human interface. This is partly due to the factors influencing financial inclusion stated in the first research question, which included issues of trust and low levels of financial literacy. Both of these can be countered through the human interaction. This research report also concludes that functionality is an important determinant of technology adoption. To improve the chances of successful adoption, technology must be kept simple, should not require

specific models of handsets to work and be intuitive and meet a real need. “Technology must be a natural extension of a device’s current use” (Interview respondent, 2009).

6.4 Leveraging the retail store network to optimise the provision of products and services to the unbanked and underbanked

Leveraging the retail store network to provide products and services to the underserved is a trend which this study found to be most prevalent in Brazil. This has become the primary form of financial access in remote areas where the population would otherwise have to travel to another city to get social benefit payments or basic banking services. Evidence of this trend was also found in the United States, with Wal-Mart providing basic financial services to the underserved. Most businesses that enter into correspondent contracts with banks have pointed to benefits such as an increase in clientele, an increase in revenue, differentiation from competitors, conditions that help develop customer loyalty and a new source of revenue (Kumar et al, 2006). Literature on the utilisation of the retail store network cites benefits to the community as including access to the financial system in a simplified form, flexibility with business operating hours, greater ease in transactions by combining banking services with shopping, easier receipt of social benefits, and reduced travel costs for accessing financial services. Interview respondents agreed that alliances between banks and retailers are a way of increasing coverage, access and value-add. This is achieved by matching where people shop to where they do their banking transactions. Another advantage, which addresses a factor cited as a hindrance to financial inclusion, is that relationships have already been established between customer and retailer.

Affordability is a significant concern at the lower end of the market and banks need to engage with the market in a way that is at least marginally profitable. Based on the evidence cited above, this research report concludes that alliances between financial services institutions and retailers offer a win-win solution for both parties. These alliances facilitate the effective provision of products and services to the underserved,

at reduced costs, and they have the potential of increasing customer volumes at the retail outlets. Forming the alliances is however, not an easy process and agreements must be set up in ways that are flexible enough to accommodate changing customer requirements.

6.5 Optimising product design to meet the needs of the unbanked and underbanked

The factors cited in the first research question as having an impact on financial inclusion are the ones that require attention in optimising product design to meet the needs of the underserved. Among others, these factors include issues such as low levels of financial literacy, the complexity of financial services offerings, and access and affordability. Interview respondents reported that the complexity of financial services is a concern that is prevalent across market segments. To optimise the provision of products and services to the underserved, interview respondents proposed optimising product design by matching products and services to customer needs, pricing them appropriately, using alternative distribution channels to drive down cost, and staying away from self-service solutions.

This research report concludes that while financial services providers should take all the necessary measures to cut costs for this price-sensitive segment of the market, this ought not to be done at the expense of matching customer needs to product offerings. Financial services institutions also need to be mindful of factors such as low levels of financial literacy and the importance of relationships that are based on trust when devising distribution strategies. Products and services aimed at this segment of the market therefore need to balance the use of alternative distribution channels such as mobile phones and the retail store network; with the need for education and the process of building relationships; while keeping product design simple and easy to understand. To be profitable, scalability is important, bearing in mind that the low

income market is a high volume and low margin business. Financial services institutions furthermore need to be mindful of the fact that while there has been a deepening of the penetration of financial services, there has not necessarily been a widening of offerings for this segment of the market. The key word to bear in mind in the provision of products and services for this segment of the market is “balance”, i.e. attaining a balance between the design and implementation aspects of products and services, and satisfying the need for profitability and sustainability. In summary, solutions for the lower segments of the market must deliver on the four A’s, viz. availability, affordability, acceptability and awareness (Anderson and Bilou, 2007).

6.6 Transaction versus credit products for meeting the needs of the unbanked and underbanked

While the Grameen model advocates small loans to support the income generating activities from which loanees can repay the loans (Wahid and Su, 2000), there is another school of thought which suggests that it will be difficult for the underbanked to access credit products if they are denied access to basic transaction products in the beginning (Jacob and Tescher, 2005). Practitioners advised that the decision as to whether to use transaction products versus credit services is influenced by the customer’s context at a particular point in time, and is driven by life events and economic cycles.

This research report concludes that a customer’s choice of his or her anchor product is driven by the customer’s economic cycle and what they need at that particular time. While transactional accounts allow for on-going relationships to be established with clients, lending products cater for entrepreneurial needs in the form of seed capital. The report concludes that the two schools of thought cannot exist independently and that the models are not mutually exclusive. The key is to understand the primary needs of the target market.

6.7 The profitability and sustainability of service and product offerings for the unbanked and underbanked

(Sherbut, 2009) highlights the need to find methods of banking the unbanked that provide essential products and services, but which do not undermine the stability of commercial financing agencies. (Weiser, 2007) outlines strategies that can be employed to achieve success in the lower income markets and these strategies range from mining and translating local market information; to creating partnerships and strategic alliances. Once financial services institutions understand that the low income market is a high volume, low margin business, it becomes possible to formulate profitable and sustainable value propositions for serving the lower segments of the market. Industry practitioners noted however, that profitability should not be a key strategic reason for serving the lower end of the market and that the motivation should rather be about life-time potential.

Some interview respondents were of the view that prior to being able to successfully serve the lower end of the market with a full-service bank, a thriving and sustainable business must already be in place. The full spectrum of banking services must first be created, and only once the top end is stable can the lower end of the market be tackled. While certain aspects of serving the low income market can be profitable, profits can only grow to a limited degree. Financial services institutions must therefore always first target the middle or higher end of market, and then focus on the lower end of the market because there will be a need for cross-subsidisation. The cost to serve must be considered in the provision of products and services for the underserved, and so technology and alternative distribution channels should be used to drive down costs. At high volumes, the model is profitable both in the transactional and lending spaces.

This research report concludes that pricing is not necessarily a sound strategy to be employed in this market because of the low margins. Constant innovation is required to continuously drive costs down, while increasing customer volumes. This said, it also needs to be acknowledged that financial services, in the traditional sense of transactional accounts, are not suitable for everyone. The scope of possible solutions therefore needs to expand beyond bank accounts and include alternative options. Evidence of such new options is already starting to emerge in the market with remittance solutions such as payment wallets and other innovations in the management of payments.

6.8 Examples of service and product offerings for the unbanked and underbanked and the reasons for success or failure

When examining examples of products and services for the underserved markets, it becomes evident that the success or failure of a product depends on the adherence or non-adherence to the design principles outlined in research question number 5. Distribution channels are a major factor influencing product profitability, as is the matching of customer needs to the features of the products and services. Industry practitioners commented that ever since Mzansi started, there has been a deepening of penetration of financial services, even if the product-set has remained constant: transaction accounts, funeral plans and consumption loans is still what most financial services institutions offer. The range of options has not been expanded very much. The financial services industry has also fallen short in terms of setting up the support structures needed to keep the deepening penetration going, especially with regards to education about the use of services.

This research report concludes that Mzansi was essential in terms of enhancing awareness about financial services, but more work needs to be done towards the effective provision of products and services for the underserved. Financial services

organisations have to acknowledge that due to insufficient levels of economic activity, there will always be people whose needs do not warrant the use of bank accounts and banks ought to think differently about these peoples' needs. "What is important is to build the trust and to build the ease with which people interact with the system" (Interview respondent, 2009). Serving the lower end of the market is about more than Mzansi – better strategies can be implemented and they can be profitable. "Mzansi alone should not equal a bank's entry-level strategy" (Interview respondent, 2009). The risk of handling cash is a key driver of innovation in the management of payments and needs to be built into solutions for the lower end of the market.

6.9 Conclusion

This research report concludes that financial inclusion has an impact on multiple aspects of an individual's well being. Advances in technology have been a major contributing factor in enabling the provision of products and services to the underserved. This is especially true with respect to decreasing the cost of service provision and increasing access. The functionality of technology is however, an important determinant of technology adoption and efforts must be made to keep functionality simple.

Trust is an important component of service provision in this market, so it is difficult to counter the need for the human interface. This need is aggravated by low levels of education and awareness about financial offerings. The report also supports the premise that the three components of financial markets must function effectively to enable the provision of financial services to the lower segments of the market. Specifically, this report advocates that the state should play an oversight role and ensure that the needs of the underserved receive appropriate levels of attention. While organisational infrastructure is an essential component in the functioning of an effective financial services system, it is not the only factor that has an impact on the extent of

financial exclusion. It is equally important to gather sufficient information about the lower segments of the market and use this to provide more appropriate products and services. Information about the customer is what will ultimately drive the decision about the nature of a customer's anchor product, i.e. whether they gain entry to the formal financial system through a transaction or a lending product. To ensure sustainability, there needs to be a change in paradigms and business models to ensure the profitable provision of products and services.

Affordability is a significant issue that affects the use of formal financial services and FinMark studies have shown that consumers at the lower end of the market are not willing to spend more than 2% of total income on financial services. Financial services providers need to be cognisant of this fact and strive to implement whatever measures are necessary to drive down the cost of service. Financial services institutions also need to be mindful of the fact that while there has been a deepening of the penetration of financial services, there has not necessarily been a widening of offerings for this segment of the market. While a product such as Mzansi was essential in terms of enhancing awareness about financial services, more work needs to be done towards the effective provision of products and services for the underserved. There also needs to be an acknowledgement that due to insufficient levels of economic activity, there will always be people whose needs do not warrant the use of a bank account and financial services organisations need to think differently about these peoples' needs.

7. CHAPTER 7: CONCLUSION

A key theme that has emerged from this study relates to the effective design of products and services for the underserved. This chapter starts with a discussion about gaps that exist in the product development processes within the financial services industry and based on the findings discussed in the previous chapter, goes on to propose enhancements to the product development processes.

7.1 Optimising product design

Studies have shown that a strong market-driven new product process with thorough execution impacts positively on the market performance of new products (Edgett, 1996, p. 508). An assessment of new product development processes showed that many financial services organisations do not follow a systematic development process, instead, ad-hoc processes are deployed (Edgett, 1996). What was also evident was that organisations that had spent more time in the pre-development stages produced better results. (Alam, 2007, p. 51) suggests that not all the stages of the service innovation process are equally important and that service managers should pay more attention to the initial stages of idea generation and idea screening.

The product development process becomes more expensive with time and as complexity is added to the design process. (Alam, 2007, p. 51) purports that customers should be involved extensively in the idea generation and idea screening stages because they can help develop service concepts and evaluate the overall service delivery blueprint and final offerings. Institutions that enter the more advanced stages of development with “more complete information on markets, competition and financial viability” should have “tighter specifications, thus producing better end products in a more timely fashion” (Edgett, 1996, p. 514). Lessons for financial services institutions include the following:

- Organisations with more complete and better processes achieve better execution and have a higher percentage of successful products. More successful new products translate to competitive benefits.
- Higher success rates are related to a better job being done during the early stages of product development. A strong pre-development phase includes:
 - Idea screening: the process of filtering ideas in a well-timed manner
 - Preliminary market and technical assessment: high-level checks of technical and market requirements. “These steps allow an institution to assess the degree of synergy with existing technology, markets and business directions (Edgett, 1996, p. 515).
- Detailed market study: A detailed analysis of the market, contributes input to the business case and project scope definition.
- Quality execution: To be effective, the well thought-out plan must be well executed by applying consistent standards.
- Success is manageable: Solid processes in the development phase enhance the probability of product success.

For practitioners involved with new service development, the (Alam, 2007) study highlights the importance of understanding cultural differences and idiosyncrasies when developing new services. The matter of employees who may subscribe to a set of cultural assumptions or biases that need to be challenged if they include inaccuracies or biases concerning underserved individuals and communities, has already been addressed in this thesis. Matching products to customer needs emerged as a strong theme from the interviews with industry practitioners. Keeping the above-mentioned in mind, this research report proposes that it is important to understand the socio-economic and other differences that exist in underserved markets, especially in a dual-economy country like South Africa, before developing new products and services for lower-income communities.

The following strategies are proposed for inclusion in the design of products and services for underserved markets:

- Strong market engagement to understand the socio-economic and other factors that influence customers;
- Strong product process, with specific focus on the early stages of development. This should include assumptions about profitability, how it will be measured and when it is anticipated;
- Strong customer involvement, especially in the early stages of product development;
- Effective execution; and
- Continuous customer education.

“Poverty is caused by our inadequate understanding of human capabilities and by our failure to create enabling theoretical frameworks, concepts, institutions and policies to support those capabilities” (Yunus, 1998, p. 47).

7.2 Suggestions for future research

A number of areas in which additional research could be conducted were identified during the analysis of data for this report. Mobile phone banking emerged as a strong trend in terms of service provision for the underserved. Given the widespread adoption of mobile phones and the relatively slow uptake of mobile phone banking, more information about the factors that influence on mobile phone banking adoption would be useful as a way of assessing the future viability of mobile phone banking.

Additionally, with most innovations in the management of payments moving towards cashless solutions, an exploratory study into how the lower end of the market is dealing with the dematerialisation of money might be useful.

Lastly, (Cooper and Edgett, 1996) in (Edgett, 1996) state that the estimated failure rate of new services is almost 50 percent. An analysis of product failure in various segments of the market would be useful for determining whether there is a “one-size-fits-all” formula for product and service development or whether there are segment-specific nuances.

7.3 Limitations of this study

- Interview input for this study was only garnered from large banks in South Africa and can therefore not be generalised. It would be useful to find out whether the same sentiments would be expressed by practitioners from the smaller banks.
- This study focused exclusively on banks and did not explore the strategies being employed by other financial services organisations, such as insurance companies.

8. REFERENCE LIST

Alam, I. (2007) New service development process: emerging versus developed markets. *Journal of Global Marketing*, 20 (2/3), 43 - 55

Aliber, M., Maharajh, R., Kirsten, M., Nhlapo-Hlope, J. & Nkoane, O. (2005) *Overcoming underdevelopment in South Africa's second economy*. 2005 Development Report, Chapter 4

Anderson, J. & Billou, N. (2007) *Serving the world's poor: Innovation at the base of the economic pyramid*. *Journal of business strategy*, 28 (2), 2007, 14 - 21

Arora, S.S & Leach, J. (2005) *Towards building an inclusive financial sector: Lessons from South Africa*. India: Economic and political weekly, April 23, 2005

Auwal, M. A. (1996) *Promoting microcapitalism in the service of the poor: the Grameen model and its cross-cultural adaptation*. *The Journal of Business Communication*, 33 (1), 1996, 27 - 49

Brown, I., Cajee, Z., Davies, D. & Stroebel, S. (2003) *Cell phone banking: predictors of adoption in South Africa – an exploratory study*. *International Journal of Information Management*, 23, 381 - 394

Burgess, R., Pande, R. & Wong, G. (2005) *Banking for the poor: evidence from India*. *Journal of the European Economic Association*, April – May, 2005

Cain, R (2009) *The business case for mobile banking*. VRL Knowledge Bank Ltd.

Carbo, S., Gardener, E.P.M., and Molyneux, P. (2007) *Financial exclusion in Europe*. Public Money & Management, February, 2007

Caskey, J. P., Durán, C. R. & Solo, T. M. (2004) The unbanked in Mexico and the United States. Available from http://collab2.cgap.org/gm/document-1.9.27602/28356_file_2.pdf (Accessed 20/07/09)

Centre for Financial Services Innovation (2008) *Highlights from the 3rd annual underbanked financial services forum: new approaches, new understanding, new relationships*. Available from <http://www.cfsinnovation.com/research-paperdetail> (Accessed 25/07/09)

De Soto, H. (2000) *The mystery of capital*. Great Britain: Bantam Press.

Djankov, S., Miranda, P., Seira, E. & Sharma, S (2008) *Who are the unbanked?* Available from http://www.doingbusiness.org/documents/Mexico_unbanked_june08.pdf (Accessed 20/07/09)

Dorsey, D. & Jacob, K. (2005) *Financial services trends and recent innovations in South Africa: lessons for the United States*. Centre for financial services innovation, October 2005

Douglas, D (2003) Inductive theory generation: *A grounded approach to business inquiry*. Electronic Journal of Business Research Methods, 2 (1), 47-54

Edgett, S. J. (1996) *The new product development process for commercial financial services*. Industrial Marketing Management, 25, 507 - 515

The Federal Deposit Insurance Corporation (2008) *Banks' Efforts to Serve the Unbanked and Underbanked*: data from Dove Consulting. Available from <http://www.fdic.gov/unbankedsurveys/> (Accessed 28/04/09)

Financial Sector Charter (2004) South African Financial Services Industry. Available from http://www.fscharter.co.za/page.php?p_id=1 (Accessed 27/04/09)

Finmark Trust (2009) *The Mzansi bank account initiative in South Africa – final Report*: data from Bankable Frontier Associates

Finmark Trust (2009) *The Mzansi initiative in South Africa – Launch presentation*: data from Bankable Frontier Associates

FinScope™ South Africa (2008) *Big increases in banking and burial society membership – an overview of facts and figures from FinScope™ South Africa 2007*. Press release. March 2008

Goeller, G. & Szymanski, M. (2005) *Banking environment – South Africa*. South African Banking Survey, KPMG

Grameen Bank (2009) *Is Grameen bank different from conventional banks?* Available from http://www.grameen-info.org/index.php?option=com_content&task=view&id=27&Itemid=176 (accessed 08/09/09)

Howard, J., Jones, M., Williams, M., Nilsson, E. & Thorat, Y. (2007) *Training to address attitudes and behaviour of rural bank managers in Madhya Pradesh, India: a*

programme to facilitate financial inclusion. Journal of International Development, 19, 841 - 851

Jacob, K & Tescher, J (2006) *Highlights from the inaugural underbanked financial services forum*. Chicago: The center for financial services innovation [Internet]
Available from: http://www.cfsinnovation.com/research-paperdetail.php?article_id=2665 (accessed 14/06/09)

Jefferis, K. (2007) *Enhancing access to banking and financial services in Botswana*.
Finmark Trust

Karlan, D. & Morduch, J. (2009) *Access to finance*. Handbook of development economics, 5 (2), June 2009

Kumar, A., Nair, A., Parsons, A. & Urdapilleta, E. (2006) *Expanding bank outreach through retail partnerships: correspondent banking in Brazil*. World Bank Working Paper No. 85

Mariampolski, H. (2001) *Qualitative Market Research – A comprehensive guide*. Sage Publications, Inc., London

Metcalfe, B. (2009) *Strategic and Emerging Issues in South African Banking*. Price Waterhouse Coopers

Mobile Phone Banking: Banking the Unbanked (2009) Africa research bulletin. Economic, financial, and technical series [0001-9852] yr:2009 , 46 (2), 18167

Moore, D. (2000) *Financial services for everyone*. The McKinsey Quarterly, 2000(1), 124-131

Moreno, L.A. (2007) *Extending financial services to Latin America's poor*. The McKinsey Quarterly, 2007 special edition: Shaping a new agenda for Latin America

Patton, M. Q. (2002) *Qualitative research and evaluation methods*. Sage Publications, Inc., London

Porteous, D. (2007) *Just how transformational is m-banking?* FinMark Trust. Available from http://www.finmark.org.za/Documents/transformational_mbanking.pdf (accessed 30/07/09)

Prahalad, C.K & Hart, S (2002) *The fortune at the bottom of the pyramid*. Strategy + Business, Issue 26, 2002

Prahalad, C. K. (2006) *The fortune at the bottom of the pyramid: eradicating poverty through profits*. New Jersey: Wharton School Publishing.

Retail Banker International (2009) *M-Pesa: Kenya's revolutionary new bank*, 15

Robbins, E. & Contreras, P. (2006) *Strategies for Banking the Unbanked: How Banks are Overcoming Entrance Barriers*. Federal Reserve Bank of Kansas City – Financial Industry Perspectives, January 2006

Sarma, M. (2007) *Index of financial inclusion*. Indian Council for Research on International Economic Relations, Dehli, November 2007

Sarma, M. (2008) *Index of financial inclusion*. Indian Council for Research on International Economic Relations, Dehli, June 2008

Schoombee, A (2000) *Banking for the poor: The successes and failures of South African banks*. DEVNET conference on 'Poverty, Prosperity and Progress'. New Zealand: Victoria University of Wellington

Schoombee, A. (2004) *South African Banks and the unbanked: progress and prospects*. South African Journal of Economics, 72 (3), 581 - 603

Sherbut, G. (2009) *Responding to new pressures: Ithala Limited's changing role in serving the "unbanked" and the poor in KwaZulu-Natal*. School of Development Studies Research, No. 79. Available from www.sds.ukzn.ac.za/ (accessed 31/07/09)

Sherrie, L., Rhine, W. & Greene, W. H. (2006) *The determinants of being unbanked for US immigrants*. The Journal of Consumer Affairs, 40 (1), 21 - 40

Solin, M. (2009). New regulatory change in South Africa affects mobile money [Internet] Available from <http://mmublog.org/> (accessed 20/08/09)

Solo, T. M. (2005) *Financial exclusion: a new angle to urban poverty in Latin America*. World Bank, En Breve No. 77, September 2005

The Economist. (2009) *The power of mobile money*. 23 September 2009. Available from www.economist.com/printedition/PrinterFriendly.cfm?story_id=14505519

Wahid, A. N. M. & Hsu, M. K. (2000) *The Grameen Bank of Bangladesh: History, Procedures Effects, and Challenges*. Journal of the Royal Society for Asian Affairs, June 2000

Weiser, J. (2007) *Untapped: strategies for success in underserved markets*. Journal of business strategy, 28 (2), 30 - 37

Wilkins, J. (2007). Journal of Nutrition, Education and Behavior, 39 (6), 359

Worthington, S. (2008) *Financial services for the unbanked in the U.S. – why, who and what?* Journal of financial transformation, 101 – 105

Yunus, M. (1998) *Poverty alleviation: is Economics any help? Lessons from the Grameen Bank experience*. Journal of International Affairs, 52 (1), 47 - 65

Yunus, M. (2007) *Credit for the poor: poverty as a distant history*. Harvard International Review, Fall 2007

Zikmund, W.G (2003). *Business Research Methods (7th edition)*. Ohio: Thomson

9. APPENDICES

Appendix 1 – Discussion guide – phase 2 of research

These questions will serve as guides to elicit information from interviewees. The bullet points will serve as a checklist to ensure that required areas are covered and to prompt respondents.

Interview Question	Research question
<p>What do you think are the issues that influence the use of financial services by the unbanked and underbanked markets?</p> <ul style="list-style-type: none"> • Comment on the complexity of financial offerings for the lower end of the market • Thoughts on making financial services available through the retail-store network • Thoughts on whether there is sufficient regulation or whether more regulation is required to improve financial inclusion • The impact of fees, costs (e.g., minimum balance requirements and fees), and documentation requirements in limiting financial access 	<p>Factors that influence financial inclusion (research question 1)</p>
<p>Please tell me about the products and services within your organisation that that are targeted at the unbanked or underbanked market.</p> <ul style="list-style-type: none"> • Why do you think that this product/service has or has not been successful? • Differences in usage among rural vs. urban populations • Comment on whether there has been a broadening of product and service offerings at the lower end of the market? • What changes would you make to this product/service offering if you were given the mandate to make any changes that you wanted? 	<p>Factors that influence financial inclusion (research question 1)</p> <p>Factors that improve access (research question 5)</p> <p>Products for the underserved (research question 8)</p>
<p>What are your thoughts on the role of technology in</p>	<p>The role of technology in</p>

Interview Question	Research question
<p>serving the unbanked and underbanked markets?</p> <ul style="list-style-type: none"> • Thoughts on a “bricks and mortar” presence vs. the use of technology to serve the underserved • The role of technology in influencing industry structure i.e. industry rivalry (new entrants, substitute products or services, bargaining power of suppliers and buyers) • Ways in which technology might create competitive advantage • In what ways can information technology be used to improve access to financial services? 	<p>serving the underserved (research question 3)</p> <p>Factors that improve access (research question 5)</p>
<p>There are three critical components of the environment that surrounds any financial service market – institutional infrastructure, organisational infrastructure and support infrastructure. If any of these components is dysfunctional; the financial markets are unlikely to work effectively.</p> <p><i>(Institutional infrastructure comprises policies, laws and regulations, which provide the foundation for any effective market.)</i></p> <ul style="list-style-type: none"> • Please comment on the efficacy of South Africa’s institutional infrastructure in promoting access to financial services for the unbanked and underbanked. <p><i>(Organisational infrastructure comprises the diverse providers of financial services having varying capacity and often in competition with each other. In South Africa, the banking sector is highly concentrated, with four dominant local banks and other smaller players.)</i></p> <ul style="list-style-type: none"> • How do you think this situation affects the provision access to financial services for the unbanked and underbanked? <p><i>(Support infrastructure supports the other two layers and includes professional services that are involved in the</i></p>	<p>Factors that influence financial inclusion (research question 1)</p> <p>Enabling environment (research question 2)</p> <p>Profitability and sustainability (research question 7)</p> <p>Transaction vs. lending products (research question 6)</p>



Interview Question	Research question
<p><i>financial sector. Providers of financial services concentrate on gathering information about the top end of the market and often remain uninformed about the needs of the poor.)</i></p> <ul style="list-style-type: none"> • Please comment on measures that are being taken or can be taken in gathering information about the unbanked and underbanked. • Comment on the use of transactional product information to build a history that can lead to access to credit products. 	
<p>Do you mind telling me about an idea for the unbanked or underbanked market that seemed good at the time but that didn't work out?</p> <ul style="list-style-type: none"> • Why do you think that this idea wasn't successful? • What would you have done differently given another chance? 	<p>Factors that influence financial inclusion (research question 1) Previous products to serve the underserved (research question 5) Profitability and sustainability (research question 7)</p>
<p>Please comment on the profitability and long term sustainability of providing financial services to the unbanked and underbanked.</p> <ul style="list-style-type: none"> • Is this profitable, and if not, what can be done to make it more profitable? • Please comment on whether you think it is possible to build a business model that focuses exclusively on the unbanked and the underbanked or does an organization need to focus on a wider segment of the market to survive. (why?) 	<p>Factors that influence financial inclusion (research question 1) Factors that improve access (research question 5) Profitability and sustainability (research question 7)</p>

Appendix 2 – Examples of other private sector experimentation and innovation

August 2003: portable banking device to open accounts and issue Sekulula debit cards for social welfare recipients

- Joint venture between ABSA and its subsidiary AllPay
- Use of smart card technology,
- Allows the Gauteng Province to distribute benefits to low-cost bank accounts of social welfare recipients.
- Recipients can withdraw funds at any ATM or use the card at POS terminals.
- Recipients may make two free ATM transactions per month after receiving the card
- Accounts have no maintenance fees
- The real innovation is in the portable device that complements the debit card.
- The system provides almost one million social welfare recipients access to low-cost bank accounts with ATM and POS access
- Innovation has cut pension payment costs from R24 to R15 for the Gauteng province
- System can provide payments in remote areas where there are no electricity or telecommunications facilities since the card relies on smart card technology.

1994: E-Plan

- Standard Bank's E-Plan, offering electronic transaction and savings products through E-centres that didn't handle cash but provided hands-on training and support in the use of ATM's.
- Relied primarily on ATM technology rather than personnel, thereby lowering the cost of providing accounts to customers who were traditionally viewed as unprofitable because of their small account balances and low transaction volume.
- E-Centres cost the bank nearly 30 percent less than traditional branches

- The E Plan experience suggests that it may be profitable to serve the unbanked, but the key is looking beyond low-cost products to appropriateness of services and fees while exploiting technology and creative distribution channels.

October 2004: Capitec Bank's Pre-Authorized Debit Card on the Global Chip Card (EMV) Standard

- A type of stored value card (SVC), serving as a cheque or cash alternative to link customers to transactional services and broader financial opportunities.
- Conforms to the international EMV (Europay, MasterCard, and Visa) standard for chip-based payment cards.
- Debit card is designed to provide a straightforward, low-cost banking product with easy access to the mass market.
- Unlike magnetic stripe cards, chip-based debit cards do not depend on the need for 'always online' telecom infrastructure.⁴⁶
- This is because retailers can accept a guaranteed payment directly from the chip without needing an online authorization.
- In a country with high telecommunications costs, the ability to process purchases once a day rather than numerous times during the day saves retailers time and money. Moreover, in a country with high crime rates, it is important that Capitec Bank cardholders can avoid carrying large amounts of cash to buy goods and services.
- Cardholders can load the chip with funds from their bank account, allowing retailers to deduct purchase amounts from the preauthorized amount without being online. The cardholder continues to use the card in an off-line mode until the amount requested exceeds the card's open-to-buy counter.
- Since the chip keeps up with the balance, the card cannot be overdrawn and can be reloaded at any Capitec Bank branch or POS terminal.

- Customers pay 50 cents per transaction with no fees to issue the card or for loading funds. In addition, a personal card reader suitable for a key ring is issued for cardholders to check the balance on the card.
- In South Africa, the financial services industry has focused on smart cards as a means of avoiding high telecommunications costs associated with using magnetic stripe cards at retail locations.

October 2004: Mzansi Accounts

- Big four banks plus Post Bank
- Collective launch cost of between R25 and R35 million
- Basic bank account targeted at low-income consumers
- About 35 - 60% cheaper than other entry-level products
- Pooled ATM infrastructure

January 2005: FNB's million-a-month account

- Effort to encourage a culture of saving
- 32-day investment product with a minimum opening balance of R100 and no maximum account balance.
- No fees or transaction costs, but the account does not pay interest.
- Account replaces interest payments with a chance of winning R1 million, R100,000, R20,000, or R1,000.
- Account with a low minimum opening balance, no transaction fees, and a risk-free chance to win up to R1 million, they will be able to attract unbanked and underbanked South Africans who like the excitement of the lottery.
- Unlike the lottery, Million-a-Month account holders do not risk losing any of their investment contributions.
- Potential to provide insights into the role of rewards in facilitating asset building

January 2005: Standard Bank's satellite terminals

- Internet protocol-based (IP-based) broadband satellite terminals to power ATMs in remote areas
- Broadband satellite links used in conjunction with prefabricated ATM concept to coordinate faster and more cost efficient services.
- Help Standard Bank meet the objectives of the Financial Services Charter by providing banking services to South Africans in poor and rural communities,
- Satellites deployed in low-traffic and low-volume areas, allowing Standard Bank to serve areas where branches are not commercially sustainable. In addition to being less expensive than branches
- Projected set-up cost per unit: R2000

August 2005: MTN Banking

- Uses an interactive voice response system in conjunction with prepaid cell phones.
- Customers open accounts using software downloaded over the air or already embedded on their SIM cards.
- Customers can also receive MobileMoney CashCards, which enable withdrawals at Standard Bank Autobanks and branches, for free from Standard Bank branches or identified MTN Service Providers.
- No monthly service fees or minimum
- CashCards can be upgraded to MasterCards.
- Transactions include person to person payments, account transfers, ATM withdrawals, as well as bill payment options and other limited purchase options.

Other Innovations with Potential for the Unbanked

- Pick n' Pay Go Banking, a division of Nedbank, is offering a cheap way to transact from a supermarket banking platform by providing bank account information packets on the grocery store shelves

- Standard Bank's PureSave, a card-based savings account with no monthly management fees and some transactional functionality
- Teba Bank provides cost-effective financial services to miners and others in rural areas, including savings vehicles and remittance services
- First National Bank offers a direct deposit payroll card to reduce crowding in their branch lobbies on paydays
- ABSA's 28-ton mobile bank, which can be lifted by crane onto a truck and transported anywhere it is needed
- ABSA has cellular network phone booths where the unbanked can open accounts remotely
- Standard Bank's pilot that used fingerprint scanning in ATMs beginning in 1996, which was the first live installation of biometrics on an ATM
- African Bank has a loan program where every customer is granted a loan. The type of loan and repayment terms depends on risk profile and the bank takes credit risk only
- Home Loan Guarantee Company has developed a product that will enable banks to deal with the HIV/AIDS risk when providing housing finance to low-income borrowers
- Insurance companies and banks have developed funeral insurance partnerships, including cross-selling products
- Development finance institutions (DFIs), which are alternative financing agents and are government-controlled parastatals. These bodies are tasked with the responsibility of financing commercially "non-viable" (or at least unprofitable) development initiatives, and can serve the "unbanked" and low-income markets while having the risks associated with doing so underwritten by guaranteed government funding and support. As such, their financing activities are disassociated from market mechanisms and any sub-prime lending activities they

pursue will bear little weight on either banking system stability or wider economic health (Sherbut, 2009).