

# Emerging Lessons of Public Funders in Branchless Banking

The potential of branchless banking services to fundamentally transform the way low-income people manage their money has generated tremendous enthusiasm in the financial inclusion world. This paper highlights emerging lessons from the public funders that have been engaged in branchless banking. The goal is to help other funders consider the role they might play in this area. Branchless banking offers the potential to fundamentally transform the way low-income clients can access financial services and to help them move forward to full financial inclusion. Technology (such as mobile phones) and nonbank retail agents can dramatically reduce transaction costs and facilitate the delivery of financial services outside of bank branches, thereby bridging the gap to reach lower income groups.

Public funders<sup>1</sup> can play several roles in branchless banking, namely to (1) advise policy makers, (2) invest in public goods, (3) support branchless banking providers through technical assistance, and (4) fund operations. Funders should carefully consider which roles they wish to play in which markets, based on their internal capacity and the stage of branchless banking and availability of private funding in a given market. In addition, each funder brings a unique set of instruments that it can use—such as grants, debt, equity, technical assistance, and advocacy—as well as its own relationships and experiences in the market. Before embarking on support to branchless banking, funders should carefully reflect on the additive role they can play and be willing to commit to building sustainable services over the long term.

This paper will be most relevant for funders that have a solid track record in microfinance and financial inclusion and are now considering

branchless banking. The paper assumes basic familiarity with branchless banking as well as good practice guidelines for funders in financial inclusion. Additional resources are available in Annex A.

## Introduction

After several decades of microcredit, more than 190 million people today have microloans,<sup>2</sup> yet a further 2.7 billion people still lack access to formal financial services (CGAP and World Bank 2010). Branchless banking offers new business models and delivery channels that can dramatically reduce transaction costs. The most striking example of this can be seen in Kenya, where M-PESA is not only used by more than half of the adult population but is also increasingly reaching down market; it is currently used by the majority of poor (51 percent) and rural (59 percent) households.<sup>3</sup> Moreover, now that M-PESA has such a high customer penetration and ubiquitous agent network, customers are using it to access a wide range of financial products, such as savings, insurance, and loans.<sup>4</sup>

Increasingly, branchless banking implementations seeking to replicate M-PESA's success are gaining traction. CGAP estimates there are 50 branchless banking implementations with active users and 22 with more than 1 million registered customers.<sup>5</sup> There is increasing evidence that branchless banking services are reaching the unbanked. A recent CGAP Focus Note found that 37 percent of customers (or an average of 1.4 million people each) across eight branchless banking implementations were previously unbanked (McKay and Pickens 2010).

The potential is increasingly clear, and public funders are eager to use their resources to help fulfill this potential in more and more countries.

1 Public funders are defined as publicly funded donors (bilaterals and multilaterals) as well as development finance institutions. This paper is aimed at public funders as well as private foundations.

2 Microcredit Summit Campaign, [http://www.microcreditsummit.org/news/record\\_128\\_million\\_of\\_worlds\\_poorest\\_received\\_a\\_micro-loan\\_in\\_2009/](http://www.microcreditsummit.org/news/record_128_million_of_worlds_poorest_received_a_micro-loan_in_2009/)

3 See <http://financialaccess.org/node/3593> and Jack and Suri (2010).

4 Eighty-one percent of M-PESA customers report using it for savings. For more information, see McKay and Pickens (2010).

5 See CGAP blog post at <http://technology.cgap.org/2011/05/11/the-state-of-the-branchless-banking-sector/>

Indeed, public funders have played a catalytic role to date. M-PESA was started with the support of a GBP 1 million grant from the UK Department for International Development (DFID). The CGAP Technology Program<sup>6</sup> used grant funding to seed other branchless banking implementations beginning in 2005, when the branchless banking concept was still nascent.

However, public funders are often unclear about their role in branchless banking. With significant momentum in branchless banking, including considerable private money,<sup>7</sup> what meaningful role can public funders play without crowding out private investment? The key players in branchless banking are multinational mobile network operators (MNOs), commercial banks, and, to a lesser extent, technology companies. For public funders to play a role in the development of branchless banking, should they give money to these institutions despite their lack of an explicit social mission?

Public funders can play an important and additive role in developing branchless banking services in several ways, namely by doing the following:

- **Extracting knowledge and learning that will benefit the entire industry.** This can be done at both a macro level (investing in public goods to understand issues such as customer adoption and regulatory obstacles) as well as at a provider level (extracting learning from specific implementations that can be shared widely).
- **Influencing the industry and specific implementations to develop products and services that are relevant for the low-income unbanked segment.**
- **Kick-starting development,** especially in smaller or post-conflict countries where providers struggle to obtain the capital and buy-in to make major investments.

If structured appropriately, public funding of private organizations has the potential to leverage

substantial private funding, extend outreach to the unbanked, and create public goods that the private sector would not otherwise support.

## Challenges

Despite the potential benefits that public funding could bring to branchless banking, however, funders should keep two points in mind before deciding to enter this growing market.

First, because funding for basic branchless banking operations is available through private investment, funding is not a primary obstacle to growth. Instead, the limiting factors in this area are challenges such as regulatory obstacles, low customer uptake, limited agent networks, and uncertain business cases. Public funders need to strategically use their knowledge, relationships, and money to tackle these challenges. This strategic process requires more creativity and technical expertise than, for example, funding loan portfolios to help microfinance institutions (MFIs) go to scale. Second, as a result of these challenges, not all funders will have the capacity to engage in this sector in a meaningful way. Only funders with both a long-term commitment to developing sustainable branchless banking services and the ability to develop strong internal capacity should become involved.

## Role of Funders

A funder's role in a given market depends on both the funder experience and tools available in the market as well as the stage of the branchless banking industry. Each market varies due to differing regulatory environments, market structure, and other factors. Even within a region, there is considerable variation. Looking at West Africa, for example, in Côte d'Ivoire, both major MNOs—Orange and MTN—launched mobile money services in 2009. They invested heavily in marketing; as a result, customer awareness

<sup>6</sup> CGAP is not a public funder. However, the Technology Program at CGAP has given grants to branchless banking implementations, and these experiences are reflected in this note. The Technology Program works to expand financial services for the poor using mobile phones and other technologies and is co-funded by the Bill & Melinda Gates Foundation, CGAP, and DFID.

<sup>7</sup> Private investors have provided about 80 percent of the estimated \$400 million in debt/equity investments that have been made in branchless banking. See blog post at <http://technology.cgap.org/2011/04/20/commercial-investment-landscape-in-mobile-financial-services-and-branchless-banking/>.

of mobile money is high. In contrast, in Nigeria, the largest market in West Africa, all activity was at a standstill while regulators decided on their approach. Finally, in December 2010, regulators gave 16 companies provisional licenses for branchless banking concurrently.<sup>8</sup> As a result, the race is on to launch branchless banking while in other countries in the same neighborhood—such as Gabon and Togo—no players have yet emerged.

Consequently, the role of funders will be completely different in a country, such as Togo, where the sector is yet to emerge, than in a country, such as Côte d'Ivoire, with active implementations. For funders, engaging in frontier markets, such as Togo, is a clearer process. For example, in new or nascent markets, funders can focus on creating a conducive regulatory environment for new entrants or on funding market research studies to help potential mobile money providers understand the market scope. In countries with more mature branchless banking systems, funders have to rely more on their influence than on their money. Funders with technical expertise in branchless banking can influence governments and businesses

to use new delivery channels to reach rural and low-income households. They can help improve agent networks to reach further down market. This involves a combination of advocacy and technical assistance.

Figure 1 shows a range of roles that funders can play in each of four areas depending on the stage of industry maturity.

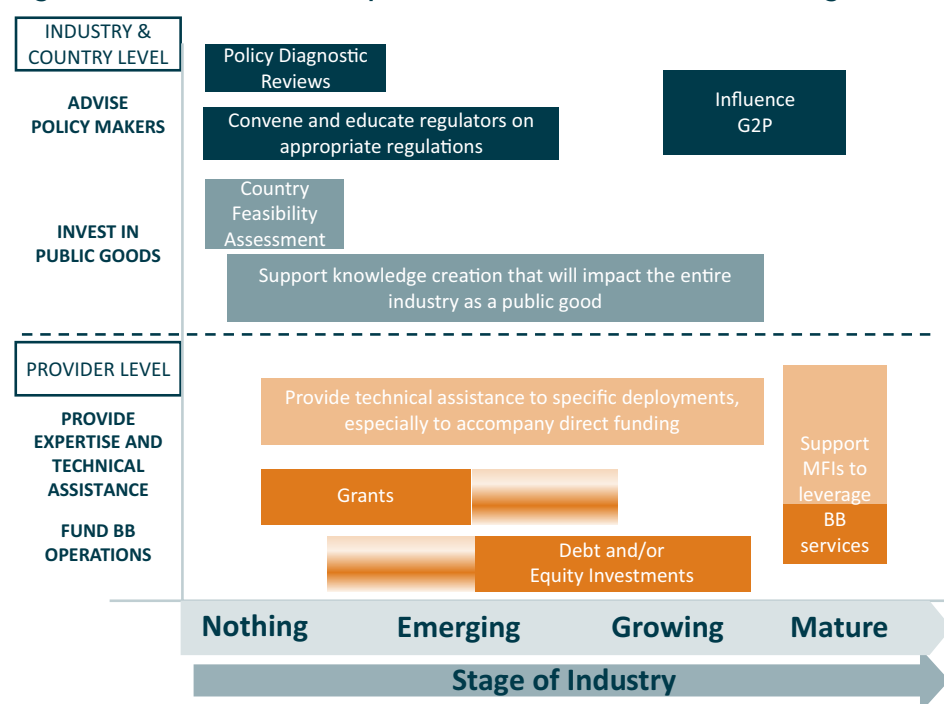
Funders have the potential to contribute by doing the following:

- Advising policy makers
- Investing in public goods such as knowledge creation
- Providing technical assistance
- Directly funding branchless banking operations

## Advise Policy Makers

As only a handful of countries have branchless banking or electronic money (e-money) regulations, regulatory issues remain unanswered in many countries, and regulators have many legitimate

**Figure 1: Potential roles of public funders in branchless banking**



8 For more information, see <http://mbanking.blogspot.com/2011/01/mobile-banking-revolution-nigerian.html>.

### Box 1: USAID'S Role in Influencing the Government of Colombia

The U.S. Agency for International Development (USAID) has been involved in branchless banking since 2004, when its country missions saw the potential of branchless banking in their markets. One of the agency's key focus areas is advising policy makers.

In Colombia, USAID was working to promote sustainable financial access in rural isolated communities when it learned about the tremendous success of branchless banking in Brazil. Due to the history of direct government involvement in financial services in Colombia (e.g., directed credit), USAID wanted to support the sustainable development of the Colombian branchless banking sector, with private providers taking the lead on service delivery. With this in mind, USAID worked as a broker between public and private entities to develop a shared vision between the two and ensure regulators fully understood this new approach. It also sent Colombian regulators to Brazil so they could learn first-hand about branchless banking. Subsequently, USAID experts supported the development of a sound regulatory framework for branchless banking. They also helped the newly established Banca de las Oportunidades—a public sector institution that came close to directly delivering branchless banking services—promote private sector-led branchless banking by proactively disseminating information and by providing temporary incentives for private banks to reach rural and underserved areas.

questions and concerns on practices that seem risky, such as using retail shops to conduct banking transactions. As a result, funders can play an important role by advising policy makers in developing appropriate regulations, by convening peer groups for learning and exchange, and by encouraging the use of branchless banking channels for government payments.

In the early stages of branchless banking in a country, a good first step is to conduct a diagnostic review of regulations and identify the main regulatory gaps. Central banks are not always well placed to do this diagnostic since branchless

banking cuts across several different regulatory domains.<sup>9</sup> In 2007, DFID funded CGAP to conduct diagnostic reviews of the regulatory environment in seven countries.<sup>10</sup> This led to several longer engagements and new or revised regulations in several countries.

Funders can also help central banks determine their policy and approach for regulating and supervising branchless banking. Eventually, every country with branchless banking will need a comprehensive regulatory framework that covers important issues, such as the treatment of agents, e-money, and know-your-customer (KYC) requirements. However, many funders and regulators believe that they need to spend a lot of time and money developing a comprehensive framework before any branchless banking service can begin. This step is not always necessary; in fact, it may be a misstep if it leads to a regulatory framework that is brought in from a different country and does not follow the local market dynamics. A different approach is to “test and see”—permitting some branchless banking services to start on an ad hoc basis, conditional on specific measures to mitigate identified risks.<sup>11</sup> Regulators can then observe how the market develops and will be better positioned to issue more detailed, customized, and effective regulation. This is how branchless banking regulations developed in the Philippines. The Filipino regulators expressly stated that they aimed to “follow the market.” Regulators approved the first two branchless banking services, GCash and Smart Money, on an ad hoc basis. After four years of observing the market's development, the central bank issued e-money regulations in 2009 that were carefully tailored to the Filipino market.

Many funders have substantial convening power. Perhaps their greatest contribution in this area is to help inform and train regulators, other government officials, and in-country influential organizations, such as other funders and embassies. In Colombia, USAID educated regulators through visits to Brazil and technical assistance (see Box 1). These

9 For a comprehensive diagnostic tool applicable to all branchless banking regulatory domains, see CGAP's Branchless Banking Diagnostic Template (available in English, Spanish, and French) at <http://www.cgap.org/p/site/c/template.rc/1.11.1772/1.26.12702/>.

10 These and CGAP's most recent country diagnostics can be found at <http://www.cgap.org/p/site/c/template.rc/1.11.1772/>.

11 See CGAP blog post at <http://technology.cgap.org/2010/02/09/branchless-banking-the-test-and-see-approach/>.

influential organizations should understand the advantages of branchless banking and give consistent messages on critical issues, such as allowing nonbank retailers to act as agents, implementing proportional KYC regulation for agent-level transactions, and addressing the important role of nonbanks.<sup>12</sup> Workshops and exchange visits with the right level and mix of attendees can also help educate and dispel some of the concerns about branchless banking risks. For instance, DFID played an important role early on in sponsoring regulators from around the world to learn from policy experts and exchange ideas through the Windsor Leadership Seminars. The Alliance for Financial Inclusion (AFI)<sup>13</sup> organizes policy forums and exchange visits. Also, funders that have influence over international standard setting bodies and initiatives (such as the Financial Action Task Force [FATF] and the G-20) should advocate and educate these institutions on appropriate enabling environment issues.

Channeling large volumes of payments through branchless banking channels can help these services gain traction. Hence, in addition to policy and regulatory assistance, funders can help catalyze branchless banking by influencing governments to leverage their payment flows through branchless banking channels. This is usually easier once a basic branchless banking service is up and running. Governments make government-to-person (G2P) payments—such as salaries or social transfer payments—to more than 170 million poor people worldwide, but just a fraction of these are paid through branchless banking channels. More money in the system means that providers and agents can rely on steady payment flows. It can encourage customers to register for and to learn how to use the service. In many countries, the branchless banking account is linked to a bank account, and customers gain access to a financially inclusive bank account. In addition, electronic delivery of payments can help the government cut costs and reduce leakage.<sup>14</sup> In Brazil, where branchless

banking has been widespread for almost a decade, nearly all G2P payments are made through agents; people are even paying taxes through agents.

Just as funders that wish to influence regulation should have prior relationships and experience in the regulatory arena, funders that are already financing G2P payments will be best placed to influence how these payments are delivered. Often, a consortium of donors will fund social transfer payments; this consortium may be able to influence the delivery channel. In Fiji, for instance, the United Nations Capital Development Fund (UNCDF) has been able to influence the Department of Social Welfare to gradually transition social payments from cash to branchless banking. So far, more than 17,000 people receive payments through no-fee transaction bank accounts accessible via 700 point-of-sale (POS) devices and 36 automatic teller machines (ATMs) throughout the country.<sup>15</sup> Incidentally, the same benefits apply to branchless banking channels used for payments by donors or nongovernmental organizations (NGOs). Donors and NGOs should consider which of their payments can be channeled through branchless banking.

### Emerging Lessons for Advising Policy Makers

- **Support policy makers in creating an enabling environment for branchless banking, especially through the “Test and See” approach.** Encouraging regulators to permit branchless banking services on a provisional basis, accompanied by rigorous monitoring and evaluation, can lead to regulation that is custom-tailored to market conditions.
- **Encourage governments to channel payments electronically.** G2P payments made through branchless banking channels are more efficient and less expensive for the government, help support the development of branchless banking infrastructure, and bring beneficiaries into the financial system.

<sup>12</sup> A number of CGAP publications cover this area in great detail. For a primer, see Lyman, Pickens, and Porteous (2008).

<sup>13</sup> Learn more about AFI at <http://afi-global.net>. AFI is administered by GIZ and funded by the Bill & Melinda Gates Foundation.

<sup>14</sup> See Pickens, Porteous, and Rotman (2009).

<sup>15</sup> For more information, see CGAP blog post at <http://technology.cgap.org/2011/06/02/g2p-starts-with-government-to-the-poorest-in-fiji/#more-4620>.

## Invest in Public Goods

Many branchless banking implementations are struggling with obstacles such as low customer uptake and usage, small and poorly managed agent networks, and uncertainty around the business case. Funders are well placed to contribute to knowledge creation that tackles these common challenges and disseminates lessons learned in the industry.

### Knowledge Generation

As most providers are in the private sector, they do not want to share lessons learned with their competitors. Against this backdrop, funders are well placed to address common challenges and to make their findings widely available for the broader public good. For example, DFID has contributed substantially to the sector through knowledge generation and dissemination (Box 2).

Knowledge creation begins with foundational research that tackles critical issues (e.g., what are the benefits to the end client of delivering financial services via branchless banking?) as

#### Box 2: DFID's Role in Knowledge Creation

DFID was one of the earliest donors to actively contribute to branchless banking, not only through direct funding, but also through knowledge creation. In 2005, DFID led a participatory process with regulators and providers that resulted in the report "The Enabling Environment for Mobile Banking in Africa" (Porteous 2006). Further research followed on regulations and other topics that were very influential in developing branchless banking in different countries.

DFID also developed strong national centers (Financial Sector Deepening [FSD] initiatives) in several African countries that have become research and development hubs on financial inclusion in their countries. For example, FSD Kenya plays an important role in helping coordinate different research projects around M-PESA; DFID has access to the information produced. Several FSD programs have attracted wider donor support and will continue beyond DFID's grant funding.

well as operational research that may be more useful to a particular player or market (e.g., what is the state of play of branchless banking in a given country?). Both types of research are important. For example, country feasibility studies are important for countries without branchless banking services. USAID has funded feasibility assessments in El Salvador, Ethiopia, Mexico, and Nigeria to assess the viability of introducing or supporting branchless banking. These publicly available studies are applicable mainly to in-country missions, providers, and development agencies. The Asian Development Bank (ADB) and UNCDF have conducted complementary studies in Papua, New Guinea.

Foundational research will be more broadly relevant. The following are examples of donor-funded, rigorous, field-based knowledge generation that has benefited the branchless banking field:

- USAID identified a gap in industry knowledge among both regulators and practitioners in quantifying and understanding risks in branchless banking. In July 2010, it released the USAID-Booz Allen Hamilton Mobile Financial Services Risk Matrix.<sup>16</sup> This included a detailed analysis of the risks involved in different models of branchless banking from the perspective of various stakeholders.
- CGAP's *Agent Management Toolkit* (Flaming, McKay, and Pickens 2011) is based on more than a year of research that yielded data on more than 16,000 agents in Brazil, India, and Kenya.

### Financial Infrastructure Projects

Another type of public good that is attractive to some funders are financial infrastructure projects that could lead to interoperable systems that benefit the broader market. (Box 3 provides an example from Ghana.) These projects often attempt to create both back-end infrastructure (e.g., national switch) as well as customer-facing infrastructure, such as POS devices and agents. The projects appeal to public funders because they have public good goals that serve the larger

<sup>16</sup> <http://bizclir.com/galleries/publications/Mobile%20Financial%20Services%20Risk%20Matrix%20July%202010.pdf>

population. As national scale projects, they also require large funding amounts that some funders can provide.

However, there are many challenges in developing these complex systems, such as in implementing these systems and in aligning the interests of all parties involved. Funders, such as the World Bank and the International Finance Corporation (IFC), play an important role in supporting the development of basic, critical, back-end financial infrastructure, such as an automated clearinghouse (ACH) and electronic funds transfer switch. However, issues arise when these projects attempt to change concurrently front-end, customer-facing services, such as interoperable POS devices and shared agent networks.

Lessons learned by funders include the following:

- **Business case and customer demand need to be clear.** The main motivation for donors to put such a system in place is national interest, such as full financial inclusion. Governments share these goals and are also concerned with reducing administrative costs. However, in most cases, these systems rely on private institutions, such as banks, and, as a result, there needs to be a clear business case or profit motive for them to participate. Heavy subsidies may be needed until a critical mass of customers is reached and the business becomes attractive.
- **Buy-in from the private sector.** These projects need strong commitment from the private sector to be successful. Banks and MNOs need to be part of the process from the very beginning and need to be able to influence the entire process to ensure that they benefit as well.
- **Timing matters when encouraging interoperability.** Effective interoperability across banks and branchless banking services benefits customers and is an important goal. However, mandating interoperability (e.g., shared agent networks) when a branchless banking market is just beginning to develop is likely to stifle industry development and do more harm than good. It is expensive to build an effective agent network, and private sector actors need to know that their efforts will not benefit their competitors—at least

### Box 3: Building an Interoperable Branchless Banking Service in Ghana

In 2007, the Bank of Ghana decided to implement a national, interoperable, biometric payment system called eZwich. KfW has been involved in the project since the outset and has pledged a concessional loan of 7 million euros for infrastructure, such as eZwich-enabled POS devices.

But eZwich has encountered many challenges. After several years, it has issued only a few hundred thousand cards, and only a fraction of these are active. Most of these customers are students that receive government grants through eZwich accounts.

The biggest challenge eZwich has encountered is the lack of a profit motive for banks; as a result, they are not interested in pursuing this type of business. Banks were mandated to purchase cards, POS devices, and ATMs at high prices and were restricted to charging only minimal fees to recover these costs. Not surprisingly, they have purchased the bare minimum and are not motivated to market these products.

for a period of time. Once branchless banking service is widespread, funders can experiment with funding shared agent networks.

### Emerging Lessons for Investing in Public Goods

- **Support knowledge creation that tackles the big questions around branchless banking.** Funders should direct resources to help solve big obstacles, such as quantifying the business case; ensuring customer adoption; and developing an effective, widespread agent network. They should encourage the industry to see these issues through the lens of the market opportunity and the large market share represented by reaching poor and unbanked people.
- **Be cautious of funding large-scale, interoperable systems prematurely.** Interoperable systems (especially on the front end) that are designed for full financial inclusion from the start are complicated. Instead, funders should focus on stimulating private sector development of branchless banking now and, as markets mature, consider how to encourage interoperability.

## Provide Expertise and Technical Assistance

Most funders will select one or more branchless banking providers to support directly. Funders should focus their efforts on providing expertise and technical assistance rather than on funding core operations.

Since only a small number of branchless banking services have reached some scale, there is no successful recipe for new services. Providers struggle with basic decisions around pricing, product development, and marketing messages. Funders should build in ample technical assistance to any branchless banking organizations they are funding. Knowledge of best practices to establish branchless banking is so limited that, in many cases, technical assistance will be more valuable than the funding itself. Funders do not need to be able to provide the technical assistance directly. However, they need enough capacity and knowledge to get the right expertise at the right time. And technical assistance does not end with the launch of the service. Reaching unbanked clients and offering appropriate services are ongoing processes. Service providers may need additional help to provide these services. Boxes 4 and 5 highlight IFC and GIZ technical assistance.

How can MFIs take advantage of branchless banking?<sup>17</sup> MFIs can benefit by linking into a branchless banking service that is already widespread to facilitate loan disbursements and repayments for their clients. In markets where branchless banking services have reached some scale, funders can play an important role in providing technical assistance (possibly combined with funding) to MFIs to help them link into the existing branchless banking service. They may require technical assistance with the MFI's management information system (MIS) as well as support to educate clients on the new service. For example, USAID provided a grant combined with technical assistance for the MABS project that linked rural banks in the Philippines with GCash.<sup>18</sup>

### Box 4: IFC Technical Assistance to WING

IFC's Access to Finance Unit provides advisory services to financial institutions and regulators to strengthen the financial sector. It has a few engagements in the branchless banking space, and it is hoped that these engagements will lead to investments (see Box 8).

IFC and WING Money, a mobile banking service in Cambodia, entered into a cooperation agreement under which IFC provided technical assistance on a 50-50 cost sharing basis. Together, they funded experts to help develop a customer care center, a merchant network, a strategy for technology uptake, and a financial literacy campaign.

IFC's *Mobile Money Toolkit*\* pools together many industry resources and offers new content. While parts of the toolkit are publicly available, the entire toolkit is used for engagements with clients, such as WING.

\*<http://www.ifc.org/ifcext/gfm.nsf/Content/MobileMoneyToolkits2>

When building technical assistance into projects, funders should make sure sufficient resources are allocated upfront to market research and business model development. The implementation must be structured to generate sufficient revenue to support all companies in the supply chain (e.g., the provider, agents, agent network managers, and so on). To date, several implementations have followed M-PESA's product and pricing model without understanding the specific customer and agent needs in their own market. Technical advisers

### Box 5: GIZ Technical Assistance in Indonesia

Technical assistance is the main tool GIZ uses to support the development of branchless banking. In Indonesia, GIZ supported a network of rural banks to understand the potential of mobile banking for their businesses. GIZ helped create a mobile banking working group for rural banks, organized field visits to the Philippines, and convened workshops with market players. A technology provider has been selected, and the project is awaiting the necessary license before launching.

<sup>17</sup> For a full discussion on the role of MFIs in mobile banking, see Kumar, McKay, and Rotman (2010).

<sup>18</sup> See [www.rbapmabs.org](http://www.rbapmabs.org) for more information.



can help providers look at the economics of the entire supply chain and make realistic business projections. The branchless banking service should be accessible to low-income and unbanked customers.

### Emerging Lessons for Providing Expertise and Technical Assistance

- **Ensure sufficient resources are allocated to technical assistance in every project.** Many providers will find technical assistance as essential as funding.
- **Help MFIs benefit from existing systems, not create their own.** Even if MFIs purchase the appropriate technology, most will not be well placed to develop agent networks and manage a payments system. Donors can play an important role in informing MFIs about branchless banking options and in helping them take advantage of existing systems.

### Fund Branchless Banking Operations

Funders in branchless banking can also play an important role in funding branchless banking provider operations. However, this area also offers the greatest risk of public funders crowding out private investors. Public subsidies for private branchless banking operations are justifiable when funders target their money and influence as much as possible toward the wider public good. They can do this in three ways:

1. **Ensure that, in return for subsidized funds, some knowledge and learning will be publicly disseminated.** Funders must be clear upfront that, in return for a grant or subsidized debt/equity investment, some knowledge and lessons learned must be more broadly shared. Ideally, this should be included in the initial contract. Private companies will be reluctant to share data, but emerging lessons from startup operations are very useful to others. Both sides should agree what experiences and data can be shared and in what timeframe.
2. **Steer providers toward viewing the poor and unbanked as a viable customer segment.**

Funders can influence the target market and help subsidize upfront costs to build infrastructure to reach the poor and unbanked. For example, UNCDF and AusAID provided additional funding to Digicel and Vodafone in Fiji to build a rural agent network, subsidizing the startup cost of setting up and capitalizing agents in remote island areas. And CGAP's grant to Orange Money in Mali included funds to hire and train Orange Money "Boys and Girls" to go to rural markets to increase customer adoption. As a result, the sales promotion force of 100 "Boys and Girls" accounted for 92 percent of new registrations in rural areas.

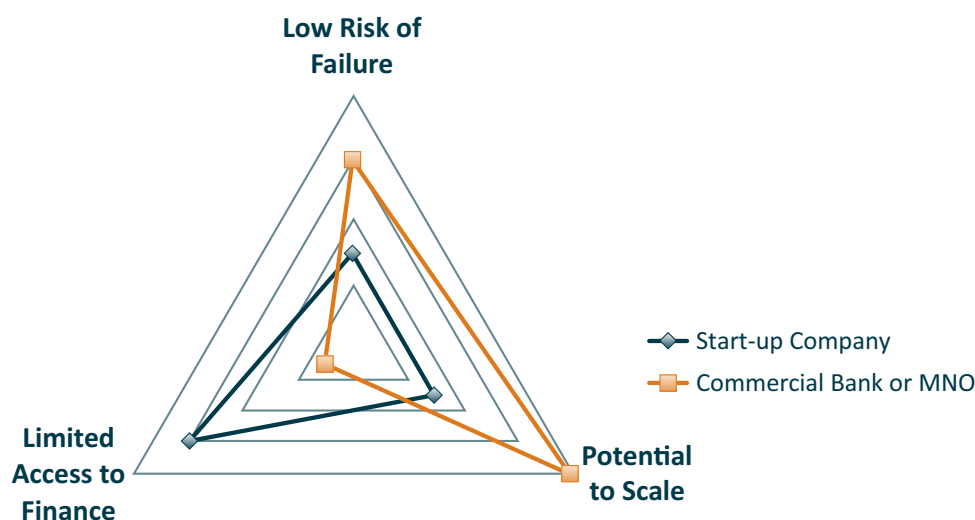
3. **Kick-start market development to speed private investment.** Funders can help providers kick-start operations in markets that are not yet mature. Providing a small, carefully targeted grant to a branchless banking project within a much larger organization helps to raise the project's internal profile and ensure that it is brought to market and tested. If the initial funding acts as a catalyst and early results are promising, the multiplier effect can be very large. For example, DFID donated GBP 1 million to support the launch of M-PESA. It is estimated that Safaricom (an MNO in Kenya) has spent more than \$20 million since then building the M-PESA brand and service—a substantial multiplier of DFID's GBP 1 million initial investment.

### Who to Fund

Start-up companies and established MNOs or banks are the main candidates looking for branchless banking funding. These two types of organizations are opposites in several ways. All else being equal, public funders would likely prefer to fund an organization with a low risk of failure, a high potential to scale, and limited access to private funding. Unfortunately, it is rare to find all three of these criteria within one organization. Figure 2 shows the tradeoffs between start-ups and established MNOs/banks along these three dimensions.

Many start-up companies tend to be very risky, and many will fail, especially when they are in

Figure 2: Tradeoffs in funding start-ups versus established companies



direct competition with large MNOs that have significant marketing budgets. Many start-ups in branchless banking are technology companies that work on back-end technology requirements or provide a service that works across any mobile network (MNO-agnostic). Companies such as EKO in India, WIZZIT in South Africa, and Mobile Transactions in Zambia all started from scratch and had some donor funding support. They offer a unique, MNO-agnostic proposition to customers. However, they face an uphill battle as they seek to come to market with a completely new product and limited marketing funds. If funders decide to invest in these types of organizations, they should be prepared for longer term horizons and some failure.

On the other hand, large and profitable MNOs or banks are driving the high potential implementations in most markets. At first glance, most public funders might assume that they do not need external funding. However, some public funders have decided that the benefits of influencing these MNO-led implementations toward the financial inclusion goal outweigh the potential sensitivity around giving public funds to large-scale, profitable institutions. Grants to MNOs have been given by CGAP (in 2009, to Orange Money), by UNCDF (in 2009, to Vodafone Fiji and Digicel Pacific), and by USAID (in 2011,

Digicel Haiti received \$2.5 million from USAID and the Bill & Melinda Gates Foundation). Similarly, the Bill & Melinda Gates Foundation gave at least one grant to a large commercial bank (United Bank Limited of Pakistan).

#### Box 6: UNCDF Experience Funding MNOs

UNCDF is funding Digicel to introduce a low-cost mobile wallet in Fiji, Samoa, Tonga, and Vanuatu. The grant will enable the company to develop a business plan for a broader Pacific rollout and to implement a pilot project before launching in these markets. Through this experience, UNCDF has learned that working with MNOs is very different than working with its traditional grantees.

Some differences noted include the following:

- **Intense sense of competition.** MNOs want to be first market movers. Funder neutrality and confidentiality with different private actors are crucial.
- **Technical assistance needed more than financial resources.** As discussed, providers often need expertise more than financial resources. This is particularly true for MNOs that do not have experience with financial products and customer education.
- **Funder role in influencing project toward financial inclusion.** UNCDF is involved in the project on a regular basis to ensure that the goal of financial inclusion to the unbanked remains relevant. Otherwise, this may not be a priority.

## Choice of Funding Instruments

As with microfinance, direct funding for branchless banking operations can be done via grants, debt, or equity investments.

**Grants** offer a lot of flexibility. Donors can consider giving grants to any type of organization to finance innovation. Currently, different funders approach grants in different ways. For example, the CGAP Technology Program has awarded relatively small, strategically placed grants in key markets to help “prove the concept,” with the idea that once one or two implementations are underway in a given market, the private sector can take over to help bring the project to scale. A challenge fund model that invites applications and supports the best based on specific criteria may be a good way to structure branchless banking funding. Funders making challenge fund grants include the Multilateral Investment Fund (MIF) at the Inter-American Development Bank (IDB), the African Enterprise Challenge Fund, and the Millennium Challenge Corporation. As always, donors should follow best practices and give smart subsidies (Morduch 2005) to ensure their grants are strategic and do not crowd out potential commercial investors, and that there is accountability for results. In particular, disbursing grants over several tranches helps to ensure milestones are met and funds are released only when targets are reached. Box 7 discusses a relatively new funding instrument—prizes.

**Debt financing** has been an important funding instrument for startup and growing MFIs. Once established, MFIs are able to revolve funds quickly, make a profit, and repay the loan. As they are in the lending business, there is a clear repayment source. In branchless banking, however, a longer time horizon is needed as companies are still figuring out how to grow and be profitable. Although branchless banking providers have received commercial bank loans, debt originating from public funders has not played an important financing role.

**Equity financing** is another way to invest in the industry. The private sector has been very active in investing equity in the branchless banking sector. An estimated \$340 million worth of equity deals have been completed since 2005, including a very large deal of \$140 million to Obopay.<sup>19</sup> While two public funders—IFC and the Overseas Private Investment Corporation (OPIC)—have been active, their investments together are less than 20 percent of the total (less than \$60 million). IFC is by far the more active of the two (see Box 8).

Almost all the investees are small to medium-sized technology companies, not MNOs and

### Box 7: Prizes: A New Funding Instrument?

Donors should carefully select their funding instruments based on both what they hope to achieve and how many players in the market have the ability to achieve these results. While grants are a common funding instrument, they may not always be the best tool. Grants guarantee effort, but not necessarily outcomes. Donors may spend a lot of money with no guarantee of success.

The branchless banking world has seen at least one very different approach—the use of prize money. A prize is paid only if a specific result is achieved. This may be useful when the objectives are clear, but the way to achieve them is not. The Bill & Melinda Gates Foundation and USAID offered a \$10 million prize to spur the development of mobile banking in Haiti after the earthquake. The MNO Digicel received the first \$2.5 million tranche for being the first provider to launch mobile banking services. The second operator to launch will receive \$1.5 million. To ensure that the services being built are scalable and sustainable, another \$6 million will be awarded after the first 5 million transactions occur, to be divided accordingly among those that contributed to the total number of transactions.

It is too early to predict whether this prize money helped bring about sustainable mobile money services in Haiti. However, it was a creative attempt to introduce more competition and to tie funds to results achieved. In DFID’s words, it is in the business of “starting races, not picking winners.” Funders should follow this approach and carefully consider the best mechanism to achieve the desired results.

<sup>19</sup> This is not a comprehensive number as not all deal sizes are made public. It does not include internal investments by corporations. The Obopay deal involves the following countries: India, Kenya, Senegal, and the United States. See CGAP blog post at <http://technology.cgap.org/2011/04/20/commercial-investment-landscape-in-mobile-financial-services-and-branchless-banking>.

banks. MNOs and banks tend to finance their implementations internally. From an investor perspective, it does not make sense to invest equity into a large, multinational organization since an investment of a few million dollars would buy only a tiny fraction of the company. Some implementations might be spun off into separate entities that eventually could take equity investment.

## What to Fund

Finally, funders need to consider what to fund. As noted, it is important to include ample technical assistance with any funded project. But there are two other considerations.

First, donor subsidies should focus on front-end, customer-facing issues, such as customer education and strong agent network development. These pose a bigger challenge in the industry than back-end technology platforms. There is a variety of technology platforms in the market, and most services can find the platform that suits them without public funding.

Second, public funders should ensure that projects target low-income and unbanked customers. For example, funders could ask implementers to measure clients' poverty level since this is not something that private providers are likely to do on their own. For instance, the Bill & Melinda Gates Foundation funded AudienceScapes to measure the poverty level of mobile money users in Kenya and Tanzania.<sup>20</sup> It found that, although early adopters in Tanzania have higher incomes, 36 percent of new users are living on less than \$2 a day.

## Emerging Lessons for Funding Operators

- **Determine your risk appetite.** Start-up companies are riskier than commercial banks or MNOs. However, the market development aspect of investing in start-up companies might fit better with a funder's organizational objectives.

- **Tailor funding instruments to the goal and project needs.** The size and type of funding instrument should be carefully selected as it influences the market in different ways. The instruments should be flexible to meet project needs and not vice versa.
- **Focus subsidies on customer-facing challenges, rather than on back-end technology.** Subsidies should be directed toward the bigger customer-facing issues, such as reaching poor and unbanked customers effectively, not to purchase technology platforms.
- **Ensure that the provider is targeting the poor and unbanked, and track this as part of the project.** One of the main unique contributions public funders can make is to keep the focus on reaching households with limited or no access to financial services.

### Box 8: IFC and Equity Investments

IFC has been involved in branchless banking since 2005. It invests in the sector primarily through equity deals. It has invested about \$50 million and has a current portfolio of six deals, making it the most active equity investor.

IFC sees a progression in the development of branchless banking in a country. It starts with the regulatory framework, then moves to early-stage funding of companies, and eventually to scaling these companies through mainstreaming. In this progression, IFC's role is in funding early/growth stage companies that have an initial track record but are not yet attractive to the private sector. While its average investment size is \$3 million to \$4 million, it wants to increase this. It primarily invests in technology companies since it cannot invest in large MNOs and banks. For example, IFC provided the technology company FINO in India with \$4 million in first-stage financing. This filled an immediate financing gap for FINO and enabled the company to reach a stage where purely commercial funding options were more widely available.

IFC sees the biggest industry gap in the funding of seed-stage companies or projects. These startups require small amounts (less than \$1 million) and are too small and risky for an IFC investment. There could be a role for a public funder with a higher risk appetite to create a fund to invest in seed-stage companies.

<sup>20</sup> For more information on the methodology, see MMU blog post at <http://mmublog.org/blog/mobile-money-in-tanzania-is-it-reaching-the-bop/>.

## Prepare the Organization for Branchless Banking Interventions

Before entering into the realm of branchless banking, funders must recognize that some internal changes and investments will be necessary to contribute effectively to the sector's growth. The following are emerging lessons that funders should consider:

- **Internally define branchless banking's important role in the broader financial inclusion agenda.** The full financial inclusion goal requires innovative ways to deliver financial services to poor people. Branchless banking holds great potential to become an important service. Explaining the public good element of this type of intervention is important for public funders that are less accustomed to working with the private sector.
- **Obtain buy-in to work directly with the private sector.** Public funders often face internal problems working with the private sector. Before heading in this direction, funders should define their impact model and seek buy-in to work with the private sector. This often requires working with competitors in the same industry. Funders must understand and respect the importance of partners' concerns over propriety information.
- **Develop an engagement strategy based on internal capacity.** For most public funders, branchless banking is a new arena. If there are resource constraints, consider being the junior partner of bigger projects, thus allowing the funding agency to influence programs with greater impact rather than funding discrete, small initiatives with low visibility and limited impact. DFID, for instance, has only one full-time equivalent staff working on branchless banking at its headquarters. However, as a partner of CGAP's Technology Program, DFID influences the branchless banking agenda worldwide. Also, consider pulling together internal resources into an interdisciplinary team and training staff. Understanding the necessary political, financial, and technical building blocks of a branchless banking ecosystem might require public funders to establish interdisciplinary teams. One model used by GIZ brought together information and communication technology, agricultural

development, and financial system development colleagues into a unified team at its headquarters.

- **Seek flexibility in investments.** Some public funders lend to governments as their main client. Funding branchless banking may not match this type of funding instrument. Seeking flexibility in the type, size, and recipient of instruments is key. If this is not possible, funders should perhaps not engage in this area at all. Funders should not try to fit the project to the lending instrument.
- **Think about pooling funding with others to share risk and leverage capabilities.** Pooling funds in a branchless banking investment facility might be a good strategy for funders with little expertise, limited funding, and low-risk appetite in this arena.
- **Evaluate and stay accountable.** If the funding organization decides to invest in branchless banking, it should develop systems that monitor and evaluate the programs to determine whether the funding is effective and to ensure a feedback loop.
- **Look for opportunities to leverage other programs already being funded.** Funders should look at how their grants are disbursed and understand that the same benefits of branchless banking G2P payments (decreasing leakage and corruption while supporting branchless banking infrastructure) apply to donor payments as well. For example, the World Food Program experimented with directing flood relief emergency payments in Pakistan through branchless banking.

## Conclusion

Considerable enthusiasm has surrounded branchless banking in both the private and public sectors in the past few years. There is indeed cause for optimism that branchless banking services can go to scale and offer efficient delivery mechanisms for financial services to poor people around the world. To achieve this potential, knowledge and capital are needed. There are many unanswered questions, such as what financial services poor people really want and what the business case is for different branchless banking models. Public funders can play an important role in helping to answer these questions and to support branchless banking by advising policy makers, investing in knowledge for the public good, providing technical assistance, and funding branchless banking operations.

Not all funders are well equipped to be involved in branchless banking. As with other aid, too much money given carelessly or in response to disbursement pressure will harm the industry. This is not an area for one-off solutions intended to show quick results. Funders who engage should have a long-term commitment to robust and sustainable branchless banking services. Those funders who are ready to dedicate significant resources to internal knowledge, to engage with the private sector, and to be creative in how they can bring all their resources—relationships, knowledge, and money—to the table can play an important role in supporting branchless banking services around the world and in advancing toward full financial inclusion.

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## Annex A: Resources

### Branchless Banking

Branchless Banking Database, <http://www.cgap.org/p/site/c/template.rc/1.9.49977/>

CGAP Technology Blog, <http://technology.cgap.org/>

Dermish, Ahmed, Christoph Kneiding, Paul Leishman, and Ignacio Mas. 2011. "Branchless and Mobile Banking Solutions for the Poor: A Survey." <http://ssrn.com/abstract=1745967>

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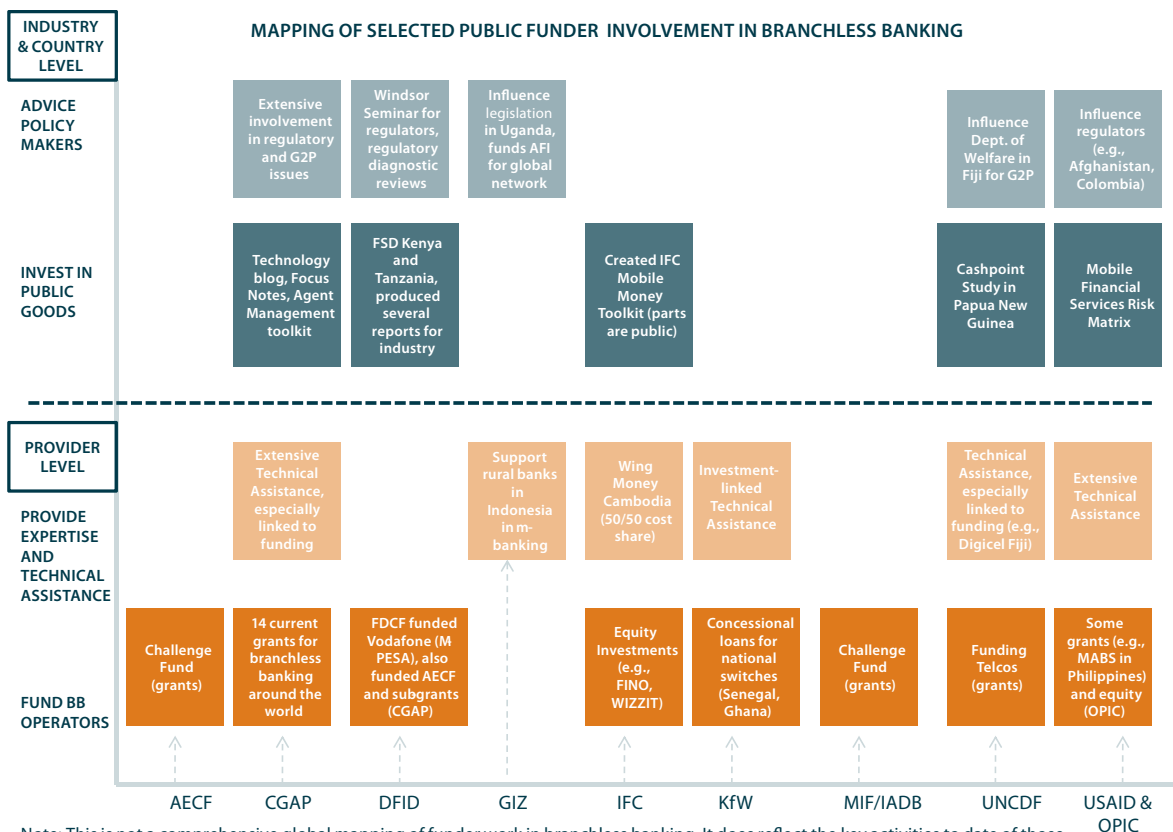
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## Annex B: Mapping of Selected Public Funder Involvement in Branchless Banking



Note: This is not a comprehensive global mapping of funder work in branchless banking. It does reflect the key activities to date of those funders researched for this publication.

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