Central Bank
of Kenya

Policy Reflections
Leveraging the success in Mobile Financial Services to expand financial inclusion

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1.Background
Cellular technology has exploded into the African market, providing an effective and cheap communication tool to the African people. The wide-spread use of mobile phone technology has opened new markets across the region, most notably in the financial sector with mobile phones widely used to provide financial services. In Kenya, these services have rapidly grown, giving opportunity to individuals and business that were left out of the traditional banking system. However, despite the potential for increased financial inclusion for the region's poor, these services have not found widespread success elsewhere in Africa.

It is with this background that the African Growth Initiative (AGI) of the Brookings Institution, the Central Bank of Kenya (CBK) and the Alliance for Financial Inclusion (AFI) organised and co-hosted a public forum and private roundtable on Mobile Phone Technology: Spurring Financial Inclusion and Growth, at the Brookings Institution, Washington DC, from May 16-17, 2011. The specific focus of the workshop was on the innovative technology of mobile financial services and its critical role in pushing the financial inclusion frontier forward in developing countries, and more so in Africa.

Regulators from the Reserve Bank of Malawi, Bank of Tanzania, Central Bank of Nigeria, Bank of Uganda, the Bank of Zambia, Bank of Ghana, and the Central Bank of Kenya represented African countries at varying stages of adopting mobile financial services. They were also joined by critical players from the private sector, research institutions, donor agencies, and other advisory bodies. With this powerful mix of discussants, the conference served as a think tank for ideas to push forward the financial inclusion & mobile financial services agenda for the benefit of the majority who are unbanked in the developing countries, especially in Africa.

2. Reflections
Through its focused dialogue, practical lessons for regulators looking to advance mobile financial services could be distilled. The participants shared insights on a number of key issues including the role of mobile financial services in financial inclusion as well as the successes and challenges. The following are key insights from the discussions.

Broadening mandate of Regulators: The Majority of the population in the African continent have no access to affordable and sustainable financial services. The Central Banks in African nations, therefore, have an important role to play as partners and agents of financial sector development and ensure financial inclusion is expanded. Central Banks further have a role to improve the regulatory environment in order to enhance innovative solutions that utilise new technology.

Take calculated risks: Innovation must not be stifled because of fear of perceived risks. Policy makers in Africa and financial sector regulators must have the courage to take calculated risks and grow financial inclusion through use of new technology. For example, in Kenya, the rollout of mobile financial services was initially piloted without a fully fledged regulatory framework, but with courage from the government, the private sector and goodwill from the regulator. What is needed most for this to happen is the courage to explore innovation and its potential benefits and risks, and it can be done as the Kenyan example illustrates.

Regulation lags behind innovation: Innovations by providers respond to market needs. Regulations follow thereafter in order to protect consumers and ensure safety and financial stability. Monitoring and understanding financial sector innovations by policy makers and regulators is therefore critical, to enhance efficiency and access as well as ensure a sound and stable sector. We should not consider lack of legal infrastructure as an impediment

Towards sound branchless banking: Banks and payments systems are converging and they need to be led to convergence in a sequenced way. Payments are systems that deal with payments and when they develop traction, we move to the next level and introduce intermediation and provision of a full suite of financial services, i.e., savings, credit, and insurance among others. This is the point where mobile financial services become more helpful.

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Enabling technology to reach its full potential: Mobile technology has the potential to reduce the cost of financial services and expand the outreach of financial services particularly to those hitherto excluded from formal financial services. However, although new technology is very important, it is not the only solution to enhancing financial inclusion. A number of issues must be addressed, for instance, how to scale up financial services in a safe and sound manner; and how to increase market uptake, particularly second generation uptake, of providing financial services, e.g. translating savings into investments. The experiences captured in the discussions at Brookings revealed the following as elements needed to scale up:

- **Pervasive cash handling points.** This calls for massive investment in developing wide networks of agents.
- A large majority must have an **electronic store of value** (whether it’s a bank account, e-money account, mobile wallet, etc) - it has to be electronic.
- **Payment instruments** that are affordable and reliable. Mobile money is a payments product – lower costs of electronic transfers should be passed on to all users.

Critical question on interoperability: Interoperability remains a sticky issue in the debate of mobile financial services. Questions around it include: whether interoperability should be enforced by regulators; what can governments do to stimulate interoperability in the long run; and how does one encourage interoperability while ensuring proprietary rights are protected?

Financial literacy to enhance usage: Financial literacy is required for regulators, service providers and consumers. Financial literacy is key in increasing the uptake of mobile financial services.

Monetary theory: Growth in use of mobile financial services has implications for the conduct of monetary policy. There is a need to understand, therefore, the extent to which the shift to e-money impacts conduct of monetary policy.

Leveraging development partners: Development partners can work with financial sector policymakers to play a significant role in several ways:

- Assist in infrastructure development and support continued innovation.
- Work through public-private partnerships and identify market niches into which financial services providers can move into and invest.
- Provide information to address market information gaps and use their convening power to create and coordinate platforms to enhance dialogue amongst regulators and policy makers.
- Support the development of appropriate regulations that enhance safe, sound and effective systems; consumer protection; inclusiveness and efficient oversight of mobile platforms.

Addressing our common regional challenges: What are the major impediments to the spread of mobile phone financial services in Africa? Is it lack of political will by governments not being informed enough or that see the risks involved only? Is it a challenge to regulators of the financial sector? Is it lack of courage or pervasive financial illiteracy?

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3. Outlook

The changing role of government: The financial sector is moving into a paradigm shift where the barriers of financial services are being removed completely. The roles of the government and financial sector regulators must be redefined within this paradigm shift, and the following roles have emerged for government:

- **As Convenor** – At all levels of government, financial inclusion must form a key agenda. At the G20 meetings this is already a reality and financial inclusion is one of the key themes. Governments thus play a critical role in eliciting buy-in from all players in enhancing financial inclusion.
- **As Regulator** – The regulator must embrace a broadening mandate. Consumer Protection, Financial Stability, Innovation and Scale are current issues that warrant attention in today's financial sector development. Regulators can impress on International Standard Setting bodies to continue to research on these areas and provide guidance on how to maintain financial stability as well. Policy that promotes better tools and better mechanisms is what is now required.
- **As Enabler** – For the mobile phone financial services, the governments as enablers are doing it better and doing it right. Governments around the world have a vision to attract the poor to formal financial services through models that use mobile phones. Along with development partners, which catalyze change, the government is supporting the model through complementary initiatives such as using mobile financial services to deliver government to person transfers. There must be open government partnership – a joint initiative to ensure transparency, accountability and openness.
- **As Driver of Monetary Policy** – New tools and probably new targets for monetary control will become necessary. A network of think tanks needs to design a research project that will understand how growth in use of mobile financial services will impact monetary policy.
- **As a Facilitator of Market Development** – Central Banks must seek to scale up financial inclusion as a sustainable way of dealing with poverty. They need to manage these developments and monitor how the micro and macro environments are changing.

New regulatory responsibilities: Regulation has a unique responsibility and opportunity to provide clarity in pushing forward the financial inclusion agenda. Regulators must:

- strive to understand and mitigate risks inherent from the innovations without stifling them. They must undertake research to determine the effects of the innovations and develop appropriate regulations.
- recognise that the innovations can make payments and settlement solutions more efficient. However, security, certainty and stability must be maintained.

Taking Courage: Ultimately expanding financial inclusion through innovative solutions takes courage of governments, regulators, private sector and all other players.

4. Immediate next step

To support peer-to-peer learning and regulatory advancements among African regulators and policymakers striving to enable MFS, we are looking forward to once again partnering with the Alliance for Financial Inclusion to facilitate a follow up workshop to map progress to date on discussions held in the previous workshop. This workshop will create a launch pad to propel mobile financial services to the next level of growth and development in Africa.

About Central Bank of Kenya/ Policy Reflections

In this Policy Reflections piece, the Central Bank of Kenya provides insights from a policy maker's perspective into the role of mobile financial services in the expansion of financial inclusion. The Bank captures the key insights gained during the forum 'Mobile Phone Technology: Spurring Financial Inclusion and Growth' held at the Brookings Institution in May 2011, as well as examining the outlook for changes in the financial sector and the implications of those changes to the wider financial inclusion agenda.

The AFI Policy Reflections series is an outlet for AFI members to provide unique perspectives on financial inclusion related topics, in their own voice. This series serves as a channel for policymakers in developing countries to share and learn from the experience of other policymakers.