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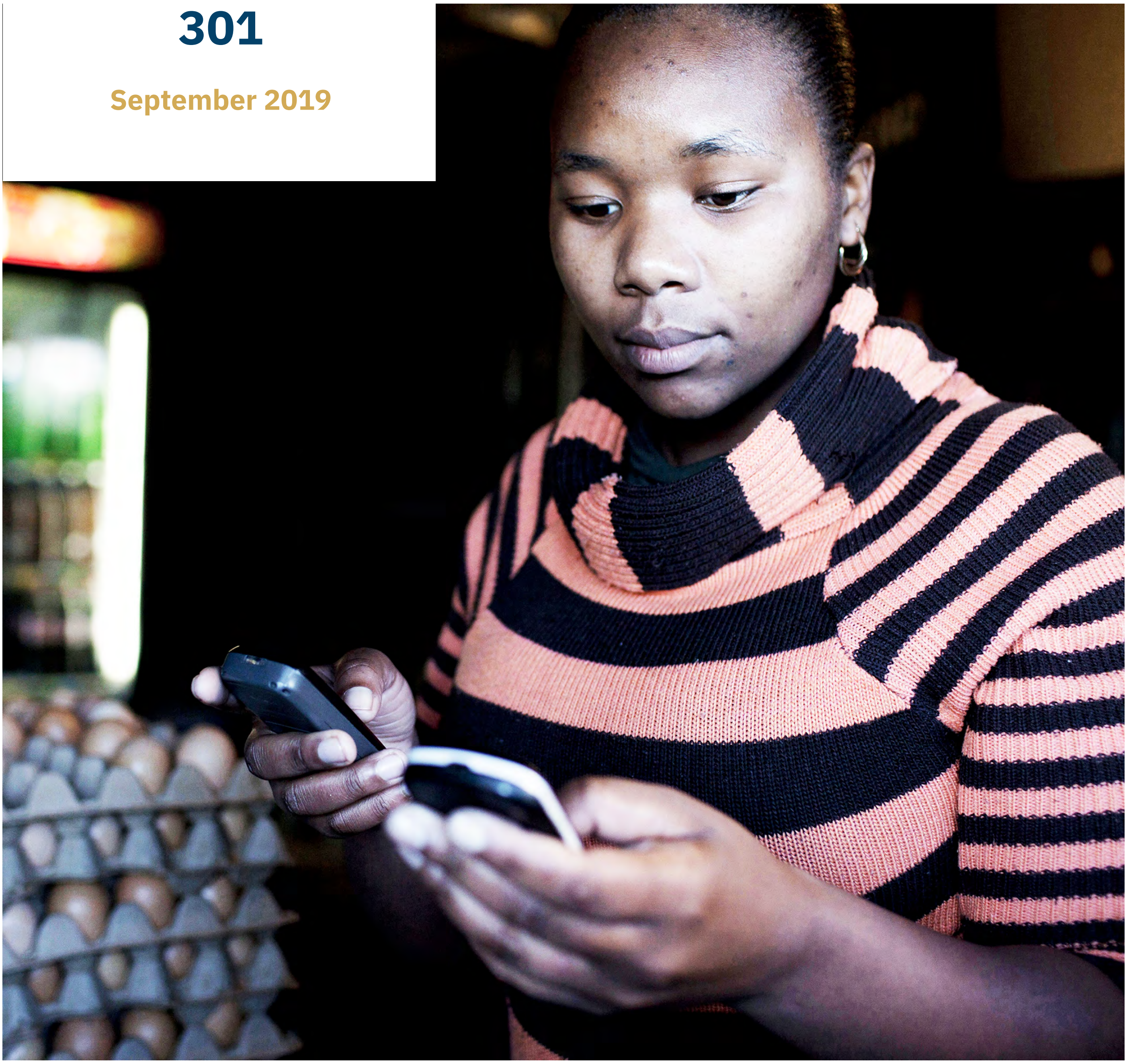

Digitising Financial Services: A Tool for Financial Inclusion in South Africa?'

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African perspectives
Global insights

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Abstract

Financial inclusion offers incremental and complementary solutions to tackle poverty, promote inclusive development and address the Sustainable Development Goals. This paper examines financial inclusion and provides a macro view of the overall benefits and risks associated with digital financial services insofar as they are used to promote financial inclusion. It highlights some of the progress that financial inclusion has brought globally and unpacks the key issues raised regarding financial inclusion in a digital era.

The second part of the paper is an examination of South Africa's efforts at financial inclusion. South Africa is an ideal case study for examining financial inclusion in driving access to the financial sector. In particular, the South African case study provides a snapshot of current progress in achieving financial inclusion, existing challenges in deepening financial inclusion and developments towards further reforms to achieve enhanced inclusion. The third part of the paper examines the opportunities that could be leveraged to improve digital financial inclusion in Africa.

The paper concludes by making recommendations for the potential strengthening of the South African financial inclusion strategy as applicable takeaways for the broader African continent pursuing financial inclusion.

Introduction

Financial inclusion refers to the access and usage of financial services with the aim of providing appropriate and beneficial[1] financial services and products to the un- and underserved segments of the population. Financial inclusion is being promoted globally as a development building block. Its principles include accessibility, affordability, appropriateness, usage, quality, consumer financial education, innovation and diversification, and simplicity. Financial inclusion enables increased access to economic well-being for users, but does not automatically lead to such an outcome. It is a necessary but not sufficient condition for financial well-being.

According to the World Bank, in developing countries there are more households that own a mobile phone than have access to electricity or clean water.[2] Nearly 70% of the lowest income population own a mobile phone. The number of Internet users has more than tripled in the last decade in developing countries, from 1 billion in 2005 to an estimated 3.2 billion at the end of 2015. In tandem with this development is the increase in access to financial services. There is no doubt that financial inclusion is on the rise, with an additional

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1 Appropriate and beneficial imply that the products and services will be sustainable for both users and providers, meet the needs of users and improve the quality of life of users.

2 World Bank, Digital Dividends, World Development Report 2016, 2016, http://www.worldbank.org/en/publication/wdr2016, accessed 2 April 2019.

515 million adults (62–69% of the adult population) around the world having opened an account at a financial institution or through a mobile money service between 2014 and 2017.[3] Nonetheless, there are still 1.7 billion adults who remain unbanked and inequality persists globally. Mobile money is one of the major drivers of increased financial inclusion in most regions, with Africa emerging as a world leader in mobile money.[4] There are twice as many mobile money accounts than bank accounts per 1 000 adults in low-income economies.[5]

The rapid proliferation of digital financial services over the past decade has affected how transactions are done today. Digital transactions offer consumers, businesses and governments convenience, efficiency and security when accessing their funds. Digital financial services also promote greater financial inclusion by enabling those without other access to the formal banking system a means of entry into formal financial services. Mobile phones became the primary device to access financial services in 2014, making it a landmark year for the financial services industry in many developing and developed countries. Mobile banking is widespread. For example, in the UK it has surpassed the use of branches, and the Internet is the most used channel among bank clients. In 2014 unprecedented levels of investment in fintech companies (12 000 start-ups investing $12 billion) were recorded as well, helping the industry cross over to the 'Mobile First' financial services world.[6] For many, digital is a survival tool, not a disruption. The financial services industry, especially banks and insurance companies, is generally viewed as less innovative than digital pure plays. Some analysts predict that traditional banking will lose about 35% market share to digital pure plays by 2020, while others estimate that digital laggards may lose up to 35% of their net profit.[7] Banks are yet to be shaken to their core by the digital disruption – when that time comes, the survivors will be those that are able to effectively adapt their business models to the realities of the digital financial services world.

This paper unpacks financial inclusion as a concept as well as its potential global significance and impact, especially for developing countries. It also looks at continental opportunities to enhance financial inclusion, providing a broad picture of the progress made thus far, and outlines important roles for policymakers in creating an enabling environment for improved and beneficial financial inclusion. An in-depth country case study is made of South Africa, one of the top performers in financial inclusion in Africa. The case study and analysis were completed through a desktop policy review, as well as interviews with institutions responsible for financial inclusion in the country and industry

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3 GPFI (Global Partnership for Financial Inclusion), *G20 Financial Inclusion Indicators Database*, http://datatopics.worldbank.org/g20fidata/, accessed 2 April 2019.

4 Osafo-Kwaako P *et al.*, 'Mobile Money in Emerging Markets: The Business Case for Financial Inclusion', McKinsey & Company, March 2018, https://www.mckinsey.com/industries/financial-services/our-insights/mobile-money-in-emerging-markets-the-business-case-for-financial-inclusion, accessed 2 April 2019.

5 GPFI, *op. cit.*

6 *The Fintech Times*, 'Organic growth of a fintech venture', 1 June 2016, https://thefintechtimes.com/organic-growth-of-a-fintech-venture-is-this-possible/, accessed 2 April 2019.

7 Oliver Wyman, *The Challenges Ahead: The State of the Financial Services Industry 2014*, https://www.oliverwyman.com/content/dam/oliver-wyman/global/en/files/insights/financial-services/2014/Jan/Oliver%20Wyman_State%20of%20Financial%20Services%20Industry%202014.pdf, accessed 2 April 2019.

experts. The resulting analysis seeks to provide a view of South Africa's overall progress in achieving effective financial inclusion, identifying both policy strengths and weaknesses. The paper concludes with recommendations on ways of strengthening South Africa's financial inclusion strategy, which could serve as possible guidelines for the broader African continent pursuing financial inclusion.

Understanding the importance of financial inclusion

Tackling poverty by addressing the needs of those without access to finance was pioneered over 30 years ago by Mohammed Yunus, the 2006 Nobel Laureate who founded the Grameen Bank using a social banking model.[8] Financial inclusion already dominated debates about poverty eradication before the global financial crisis of 2008, but has gained significant impetus since then, as shown by the series of international declarations and key publications[9] that have served to cement its emergence. There was a realisation fairly early on that financial inclusion per se would not reduce poverty and that additional developmental initiatives (education, appropriate physical and digital infrastructure, etc.) were equally if not more important. Financial inclusion is an enabler of economic well-being, not a necessary and sufficient condition for such a state.

Former World Bank president Jim Yong Kim said in 2014 that[10]

> [f]inancial inclusion has moved up the global reform agenda and become a topic of great interest … For the World Bank Group, financial inclusion represents a core topic, given its implications for reducing poverty and boosting shared prosperity. The increased emphasis on financial inclusion reflects a growing realisation of its potentially transformative power to accelerate development gains.

There was a realisation fairly early on that financial inclusion per se would not reduce poverty and that additional developmental initiatives (education, appropriate physical and digital infrastructure, etc.) were equally if not more important

8 Chibba M, 'Financial inclusion, poverty reduction and the Millennium Development Goals', *European Journal of Development Research*, 21, 2, April 2009, pp. 213–230.

9 UN DESA (Department of Economic and Social Affairs Poverty), *Financial Inclusion*, https://www.un.org/development/desa/socialperspectiveondevelopment/issues/financial-inclusion.html, 22 March 2019; AFI (Alliance for Financial Inclusion), https://www.afi-global.org/, accessed 22 March 2019; GPFI (Global Partnership for Financial Inclusion), https://www.gpfi.org/, accessed 22 March 2019; World Bank, 'Financial inclusion', http://www.worldbank.org/en/topic/financialinclusion, accessed 22 March 2019.

10 World Bank, *2014 Global Financial Development Report: Financial Inclusion*. Washington DC: World Bank, 2014, p. xi.

Financial inclusion is about delivering appropriate, responsible and beneficial formal financial products and services to all segments of a population. Four dimensions underpin it, namely usage, access and quality, as well as choice (an essential part of the latter two).[11] Emerging as another dimension is impact/economic health/benefit. There are five basic financial service needs, namely remitting money; transacting (making payments and receiving money); saving money for future needs; borrowing to improve circumstances or increase productive capacity; and insuring against loss, damage, illness or death, all serving in a sustainable and beneficial way to positively affect economic development.[12] Financial inclusion means that individuals and enterprises can access and use a range of appropriate and responsibly provided financial services offered in a well-regulated environment. The population with a bank account is often used as the most appropriate indicator of financial inclusion, but there are a number of financial inclusion indicators[13] that provide a more nuanced and informative view of the financial inclusion landscape. The financially excluded comprise both the unbanked and the underbanked. It is clear that including people in the informal economy has become imperative in fighting poverty, tackling inequality, and fostering inclusive growth.

One of the key enablers in reducing poverty and achieving inclusive economic growth is financial inclusion. Despite this, nearly 2 billion adults remained unbanked (ie, do not have access to a bank account, credit, insurance, a safe place to keep savings or a secure and efficient means to receive social benefit payments) in 2014, with the majority of the unbanked in emerging and developing countries.[14] Thus, the size of the financially excluded population in the world is enormous.[15] While a growing number of people have adequate access to financial institutions or mobile money accounts, some stark disparities persist in financial inclusion. In 2014 account penetration rates in financial institutions were at 14% in the Middle East, 33% in sub-Saharan Africa and 45% in South Asia. Today, more than half of adults in the poorest 40% of households in developing countries still do not have an account, while the gender gap is not narrowing in any significant way – only 58% of women have an account, compared to 65% of men globally. In Latin America and the Caribbean, mobile subscriber rates continue to increase, and it is estimated that the number will reach 60% of the population by 2020. Active mobile money accounts in that region grew from less than 1 million in December 2011 to more than 10 million by the end of 2016.[16] The 2017 Global Findex states that sub-Saharan Africa persuasively demonstrates the power of financial technology to expand access to and the use of accounts, with 21% of adults now having a mobile money account. This is nearly twice the share in 2014 and

11 FinMark Trust, FinScope South Africa 2015, 2015, http://www.finmark.org.za/wp-content/uploads/2016/03/Broch_FinScopeSA2015_Consumersurvey_FNL.pdf, accessed 22 March 2019.

12 World Bank, *Achieving Effective Financial Inclusion in South Africa: A Payment Perspective*, http://www.treasury.gov.za/publications/other/Achieving%20Effective%20Financial%20Inclusion%20in%20South%20Africa.pdf, accessed 13 April 2019.

13 The GPFI has one that is updated from time to time, the AFI has one that is ever expanding and the OECD has one that is more focussed on developed economies.

14 World Bank, *The Global Findex 2017*, https://globalfindex.worldbank.org/, accessed 10 January 2019.

15 UNCDF (UN Capital Development Fund), '*Financial inclusion*', https://www.uncdf.org/financial-inclusion, accessed 8 January 2019.

16 Almazan M & J Frydrych, *Mobile Financial Services In Latin America & The Caribbean: State Of Play, Commercial Models, And Regulatory Approaches*. London: GSMA, 2015.

easily the highest of any region in the world. However, around 300 million people globally are digitally excluded and therefore unable to enjoy the socio-economic benefits that come with mobile connectivity and Internet access. A lack of digital skills and financial literacy exacerbates exclusion even where there is digital access.[17]

Although the use of formal financial services continues to improve, widespread access and use remain a challenge. Between 2011 and 2014 bank account ownership worldwide increased from 51% to 62%, a clear indication of significant progress in extending access to formal financial services despite substantial imbalances across geographic boundaries and between genders. In addition, the depth of engagement varies with different financial products: only 18% of adults use a bank account to receive wages or pay utility bills, and only 11% borrow from formal sources.[18] Significant imbalances in financial inclusion exist within markets. There are also differences between regions, between urban and rural areas, and between men and women. At the same time many countries have adequate levels of infrastructural capacity, as well as sufficiently developed financial systems to enable the growth of digital financial services (DFS).

Financial inclusion has been identified as an enabler for 7 of the 17 Sustainable Development Goals[19] (SDGs) and contributes to the fulfilment of SDGs 8 and 9. SDG 8 seeks to 'promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all'. Subcategory 8.3 of this SDG promotes productive economic activities, especially from small, medium and micro enterprises (SMMEs), where digitisation of payment systems can offer enormous improvements in inclusivity. SDG 9, in its first subcategory, emphasises increasing small-scale industrial and other enterprises in developing countries' access to financial services, including affordable credit, and their integration into value chains and markets. This directly addresses the digitisation of financial services as an opportunity to improve accessibility of affordable financial services. Financial inclusion is a target in 8 of the 17 developmental goals in the SDGs, including SDG 1, eradicating poverty; SDG 2, achieving food security; SDG 3, profiting health; SDG 5, achieving gender equality; SDG 8, promoting economic growth; SDG 9, supporting innovation and infrastructure; SDG 10, reducing inequality; and SDG 17, strengthening the means of implementation where there is an implicit role for greater financial inclusion through greater savings mobilisation for investment and consumption that can spur growth.

Evidence – theoretical, empirical and anecdotal – suggests that financial inclusion, in conjunction with other developmental initiatives, can reduce poverty, promote pro-poor growth and address the SDGs.[20] Financial inclusion, an integral part of inclusive

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17 *Ibid*.

18 Asian Development Bank, Accelerating Financial Inclusion in South-East Asia with Digital Finance, Oliver Wyman, 2017, https://www.adb.org/sites/default/files/publication/222061/financial-inclusion-se-asia.pdf, accessed 22 November 2018.

19 World Bank, 'Financial inclusion: Overview', http://www.worldbank.org/en/topic/financialinclusion/overview, accessed 22 March 2019.

20 Chibba M, *op. cit.*; Agyemang-Badu AA, Agyei K & EK Duah, 'Financial inclusion, poverty and income inequality: Evidence from Africa', *Spiritan International Journal of Poverty Studies*, 2, 2, 2018.

development and one of several approaches to poverty reduction, can allow the poor and low-income earners in developing countries to lead better lives. It provides enhanced money management, access to finance at reasonable cost reflecting the cost of credit, a safe place to keep savings and more protection and options than those available in the informal sector. Similarly, SMMEs and entrepreneurs can benefit from financial inclusion.

It is important, however, to distinguish between financial inclusion in richer and poorer countries. In the former, financial inclusion typically targets a generally small group of people who, for whatever reason, are unable to obtain a basic formal financial service that is otherwise the norm in their society. In the latter countries, financial inclusion is a much more extensive agenda, because using formal financial services is the exception rather than the norm. In these countries, financial inclusion is more far-reaching – access to financial services is a critical enabler in reducing poverty, boosting shared prosperity, and supporting inclusive and sustainable development.

There is growing evidence that financial inclusion can help to support overall economic growth and the achievement of broader development goals; and create more stable financial systems and economies, mobilising domestic resources through national savings and helping to boost government revenue. Evidence also shows that increased levels of financial inclusion through the extension of savings, credit, insurance and payment services contribute significantly to sustainable economic growth. One study concludes that digital finance can spur inclusive growth that adds $3.7 trillion to the gross domestic product (GDP) of emerging economies within a decade, thus benefiting billions of people.[21]

Various benefits and risks are associated with digital financial services in the context of broadening financial inclusion.

The 'holy grail' of digital financial services and associated risks

The G20 and the Organisation for Economic Co-operation and Development (OECD) have adopted a working definition of DFS: 'Financial operations using digital technology, including electronic money, mobile financial services, online financial services, i-teller and branchless banking, whether through bank or non-bank institutions.'[22] DFS encompass various monetary transactions, including depositing, withdrawing, sending and receiving money; payment; credit; saving; pensions; and insurance, as well as non-transactional services such as viewing personal financial information through digital devices. Digital technologies have been integrated into the global economy and as such have a significant impact on the financial industry by introducing new products, services and providers.

21 Osafo-Kwaako P *et al.*, *op. cit.*

22 *Ibid*.

Different market players all interested in 'going digital' form an ever-widening ecosystem of financial service providers. Industry players are advocating the use of digital capabilities to ensure more efficient benefit transfers in government–to–person (G2P) schemes such as pensions, social welfare benefits and salaries.[23] Digitisation affects everyone – from individuals to businesses – globally, with digital connectivity enabling various types of digital payments and mobile money services in 64% of developing countries. It is estimated that their spread is likely to increase with the growing penetration rate of mobile connections (estimated to exceed 100% globally by 2020).[24]

It is owing to these changes that the G20 and OECD are advocating for more effective financial education, financial consumer protection and financial inclusion policies that adapt rapidly to this changing environment and that address the unique and additional risks being introduced by digital financial service provisioning. Digital innovation has the potential to fundamentally change the provision of financial services to the underserved through new technologies, including:[25]

- alternative platforms, such as mobile phones and digital platforms, to reach the financially excluded and people in rural areas without the need for physical bank branches;
- digital information, such as biometrics data, to verify customer identity for account opening and payment authorisation where a working national identity system is not available;
- analysis of transactional and digital footprint data to generate insights to improve customer targeting and credit risk assessment; and
- mobile wallets developed by non-banks, such as mobile network operators (MNOs) and other regulated mobile money operators, to improve customer experience in savings and payments.

Digital advocates are drawn towards digital financial inclusion[26] because of the following three 'holy grails'.

Transaction costs: Proponents of digital financial inclusion emphasise how expensive cash is compared to digital money (whose transactional costs are lower and thus hold the promise of efficiency gains). Governments can save up to 75% on administrative costs by going digital, as handling, securing and distributing cash and administering cash

23 Mader P, 'Card crusaders, cash infidels and the holy grails of digital financial inclusion', *BEHEMOTH A Journal on Civilisation*, 9, 2, 2016.

24 OECD (Organisation for Economic Co-operation and Development), *G20/OECD INFE Report On Adult Financial Literacy In G20 Countries*. Paris: OECD, 2017.

25 Asian Development Bank, *op. cit.*

26 The G20 Global Partnership for Financial Inclusion (GPFI) defines 'digital financial inclusion' as the use of digital financial services to advance financial inclusion. It involves the deployment of digital means to reach financially excluded and underserved populations with a range of formal financial services suited to their needs, delivered responsibly at a cost affordable to customers and sustainable for providers.

programmes are expensive.[27] Some digital payment solutions also have low transaction fees. There is a need for a properly constructed market protection mechanism to enable fair service provisioning for all (eg, privacy protection and the sale of personal data).

Micro big data: The digitisation of money brings with it vast amounts of accessible data, because digital transactions leave behind a digital footprint of users. Big data allows for the detection of consumers' spending patterns and gives them a credit history, which means they can borrow money more easily and at a reasonable cost. It also allows for tailored offers of financial products to those customers who most need it. Cash only leaves minimal traces of the transaction values and destinations or recipients.

Governmental efficiency: Digitising G2P services has the potential to expand the reach of government through more efficient and targeted social benefit payments while also helping governments battle corruption, leakage and crime. The real impact is that financial tools help the poor to be more disciplined and make better financial decisions, allowing people to graduate out of poverty over time.[28]

The use of digital technologies for personal finance management provides new tools to support consumers and entrepreneurs in improving their lives and financial well-being. Examples include:

- more secure, faster and timely transactions of financial capital flows (for both advanced and emerging economies);
- an increasing number of fruitful and customised interactions between consumers and financial service providers, potentially increasing consumers' confidence in financial services; and
- more players in the market, which increases market access and competition, leading to greater innovation and efficiency potential.[29]

While the financial inclusion agenda builds on many established features of microfinance, the underlying theory of how finance should benefit the poor has changed with the advent of financial inclusion. Microfinance institutions (MFIs) were largely perceived as pro-poor alternatives to other formal financial actors and informal lenders when they pioneered the credit technologies that made it possible to channel loans to scores of poor people in the Global South. Today their survival is threatened by the digitising of financial inclusion by large banks, mobile network operators and other major financial service providers such as credit card companies, which have far greater resources at their disposal.

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27 World Bank, 'Governments can save up to seventy-five percent with electronic payment programs', Press Release, 2 August 2012, http://www.worldbank.org/en/news/press-release/2012/08/02/governments-can-save-up-seventy-five-percent-with-electronic-payment-programs, accessed 1 April 2019.

28 Mader P, *op. cit.*, p. 74.

29 OECD, 2017, *op. cit.*

The shift to financial inclusion evokes ideals of equality, even though much of what is called 'financial inclusion' implies the provision and use of a range of products that MFIs have not been able to provide.[30] For the OECD, digital payments represent a more cost-effective, efficient, transparent and safer means of disbursing and collecting payments. Plastic money – not cash – is now king. Over the last few years, mobile transactions[31] have been embraced in many parts of the world in different ways. Instead of paying with cash, cheque or card, people can use a mobile phone to pay for goods and services. The key to achieving financial inclusion therefore is digital access to funds through cards and mobile phones.[32] Digital payments are not just convenient but also play a crucial role in stimulating economic growth. One study estimates that greater use of digital payments added $983 billion to global economic growth, which is the equivalent of creating 1.9 million jobs.[33]

Plastic money – not cash – is now king

Low population density, poverty, poor physical infrastructure and the high costs of delivery associated with traditional 'brick and mortar' models make banking difficult in many parts of the world. These factors also contribute to the present digital financial inclusion hype or the idea of going cashless. In Africa, many of the poor live in rural areas where they do not have access to basic financial services such as ATMs and branches. However, with technological innovation, access to basic financial services has become economically viable for financial service providers wishing to provide poor and marginalised people with a wider range of products and services.[34]

Notwithstanding the benefits of digitising financial inclusion, DFS carry new risks for consumers which, if not properly addressed, may pose serious threats to the financial well-being of individuals and entrepreneurs.

- If DFS are market driven, providers can make use of new methods to unethically take advantage of uninformed consumers and new technologies to maximise their profits and exploit consumers' biases.
- If DFS are regulation and supervision driven, restrictive regulatory frameworks may deter investment in the industry. This could inhibit market participation and competition, including limiting cross-border DFS with companies making use of more favourable

30 Mader P, *op. cit.*

31 Mobile money, mobile payments, mobile money transfer and mobile wallet refer to payments made from a mobile device such as a smartphone.

32 Romon E & S Sidhu, '*Philanthropy, digital payments and financial inclusion*', *OECD Observer*, 19 December 2019.

33 Moody's Analytics, *The Impact of Electronic Payments on Economic Growth*. Philadelphia: Moody's Analytics, 2016.

34 Mader P, *op. cit.*

conditions in other markets. It would also limit companies' potential to expand across borders.

- In a consumer-driven scenario without adequate user capability campaigns, a rise in DFS could create increased risks for uninformed consumers.
- In a technology-driven scenario, access to DFS could still be limited since the service design will not be user-centric and could incorporate inflexible algorithms that might be difficult to interpret.[35]

These risks can have a negative impact on both consumers and entrepreneurs, and can result in a range of negative outcomes, such as:

- lack of trust in DFS, the financial system and technological innovation;
- new forms of exclusion for certain groups such as the elderly and low-income users who might not be able to afford devices such as smartphones and computers to access DFS, or owing to the increasing use of data and digital profiling for credit and insurance decisions (if used inappropriately in a regulated environment);
- increased self-exclusion owing to low levels of financial and digital literacy, as well as a lack of familiarity with new product providers;
- over-indebtedness among consumers who may be vulnerable when digital credit is being provided without any human interface; and
- increased customer vulnerability to possible mis-selling, phishing schemes, account hacking and data theft.[36]

In some African countries, regulators are already emphasising to donor agencies the need to recognise payments as public goods, thereby resisting the urge to privatise them with digital money schemes. A payment system is a public good that may be provided by the private sector if there is a properly constructed and regulated payment system in which multiple players can participate. The digitisation of financial service provisioning could also be a threat to existing 'brick-and-mortar' microfinance operations premised on group lending and face-to-face interactions designed to include the poor.

Case study: South Africa

The South African financial sector presents an ideal case study in financial sector development: before 1994 financial sector policies resulted in gross financial sector

35 *Ibid*.
36 *Ibid*.

inefficiencies such as the financial exclusion of over 60% of the adult population in 1994.[37] Since then the democratic government and the financial sector have worked hard to promote financial inclusion and provide a wide range of financial products and services to all South Africans.

Relevant sector developments

The financial services landscape in South Africa is fairly diverse. This industry is one of the largest, most innovative and profitable in the country. South African banks are trying to expand their reach and pushing to increase their customer base by leveraging the power of new digital avenues such as mobile channels. The use of the latter gives banks the opportunity to bring on board new clients who may never have had access to financial services before. Thus, with digital technologies banks can reach previously underserved areas and 'bank the unbanked'.

Financial services companies are leveraging technology to advance their own growth, development and sustainability. In order to remain relevant in a rapidly digitalising society, banks are using new channels primarily to drive down the cost of service provisioning to existing clients. Incidentally, this also offers opportunities for new, lower-income customers. Nonetheless, the latter is not their primary driver. At issue remains the design of a comprehensive operational market engagement model where all the service elements are available, market needs are met and the bank is in a position to reach out to unserved clients and reduce costs. The use of mobile devices for bank transactions has increased significantly in the past few years.[38] The role of branches is changing as customers move over to digital channels that offer fast and convenient banking, which has become the new industry standard. Branches and ATMs are expected to significantly decrease as primary banking channels in the medium term,[39] with their role in user services changing. Most branch traffic is driven by the least profitable mass-market customers, while there is increasingly limited usage by younger, more affluent customers. There is also the reality that some customers in the South African environment still value and require a human interface.

The rapid adoption of digital services has become a driver for change, as increased accessibility to connected devices creates a more empowered and digitally savvy society. In South Africa, this explosive proliferation of smart devices is fuelling the adoption of mobile banking and other digital financial services. Mobile device growth has increased rapidly in the past few years with these devices becoming ever more sophisticated. By 2015, 51% (or 18.9 million) of the adult population had smartphones. Of this, 40% were using

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37 Kirsten M, '*Policy Initiatives to Expand Financial Outreach in South Africa*', Paper presented at World Bank/Brookings Institute Conference, Washington DC, 30–31 May 2006.

38 Telkom, *Technology in Financial Services: Considerations and Trends for the Banking and Insurance Sector*, http://www.telkom.co.za/today/media/downloads/Technology_in_Financial_Services.pdf, accessed 15 April 2019.

39 *BusinessDay*, 'Standard Bank to cut 1 200 jobs and close 91 branches', 14 March 2019, https://www.businesslive.co.za/bd/companies/financial-services/2019-03-14-standard-bank-to-cut-1200-jobs-and-close-91-branches/, accessed 25 September 2019.

smartphone apps and 31% cell phone banking/money to manage their finances, mainly to buy airtime. Internet banking penetration increased from 11% in 2013 to 13% in 2015, while cell phone banking increased from 28% to 31% in the same period.[40] The development of smartphone-based payments and e-commerce payment platforms such as digital wallets and mobile banking apps becomes increasingly disruptive, as their adoption has been gradual but marked. These services allow customers, for example, to store card details digitally and conduct transactions with their phones without merchant authentication of their cards or through electronic fund transfer payments. These developments are supported by next generation security measures such as location-based identification and biometrics, which protect customers and increase confidence in digital channels. Mobile money has not gained traction locally,[41] with most domestic start-ups and international brands closing operations. The use of crypto-currency remains niche even though the country has access to international cryptocurrency platforms as well as domestically developed cryptocurrencies and exchanges.[42]

In addition to the proliferation of smart devices, other key digital trends are emerging. Software development and distribution are constantly getting more efficient with software platforms and app stores making it easier to create and sell mobile services. This reduces barriers to entry for enterprising entrepreneurs. Fibre connectivity is more accessible and the advent of long-term evolution has improved connectivity speeds, both of which are driving increased demand for online services.[43] Enhanced security levels and continual technological advancements also support the rising adoption of mobile financial services. Overall this digital migration results in reduced operational costs and improved efficiency. However, it is also creating a digital divide in the country. Improved digital services are not available everywhere and the low-income segment of the population cannot afford these services, leaving them digitally and financially excluded.

Laying the foundation for financial inclusion

South Africa's National Development Plan (NDP), which has been criticised for its lack of understanding of the developmental role that financial inclusion can and should play in the country, is one of the main pillars guiding the country's financial inclusion objectives, with a financial inclusion target of 90% by 2030. In line with the requirements of the Broad-based Black Economic Empowerment (BBBEE) Act of 2003, the financial services industry undertook to implement the Financial Sector Charter from 2004 as a voluntary transformation policy agreed to at the National Economic Development and Labour Council (NEDLAC) to promote social and economic integration and access to the

40 FinMark Trust, *op. cit*.

41 There is no mobile money regulatory framework in South Africa, so all such implementations had to use existing bank account structures in some form or another.

42 CoEFS (Centre of Excellence in Financial Services), *The Impact of the 4th Industrial Revolution on the South African Financial Services Market*, https://www.coefs.org.za/research-reports/impact-4th-industrial-revolution-south-african-financial-services-market-report/, accessed 15 April 2019.

43 Telkom, *op. cit*.

financial services sector. One of the key objectives of the charter was the effective provision of accessible financial services to black people.[44] The government sought to align the industry's transformation objectives with the generic Codes of Good Practice and gazetted the Financial Sector Code (FSC) in 2012, replacing the charter that had expired in 2008. The Financial Sector Transformation Council (FSTC) oversees the implementation of the FSC, a regulation governing the transformation of the financial services sector that has obvious touchpoints with the country's financial inclusion policy objectives. The FSTC has set various industry standards for compliance under the scorecard for access to financial services in order to achieve the financial inclusion targets. These standards refer to qualifying criteria for products to be considered for inclusion in terms of the requirements of the FSC. There are three scorecards with targets for the different formal financial service providers: banks, and short- and long-term insurers. The FSC was amended in 2017 and is currently being reviewed by the FSTC and other stakeholders.

Strong commitment from the private sector has also proved invaluable in efforts to further the reach of transaction accounts that meet the needs of the unserved or underserved. The banking sector implemented the Mzansi Initiative, a low-fee bank account, in 2004. The aim was to significantly improve access to and take-up of transactional banking. The Mzansi Initiative was a success – by 2008, 6 million new accounts had been opened by people who had not previously banked at the same bank at which the account was opened, two-thirds of whom had never before had a bank account. The Mzansi Initiative reached the FSC's target of 2 173 930 active accounts by December 2008. Most of these accounts were opened by the targeted LSM 3-5 range.[45] However, 42% of accounts opened became 'inactive or dormant' or were closed. Dormancy was substantially reduced through appropriate communication and education measures. This inactivity explains the difference between the 6 million opened accounts and the 3.5 million users recorded in 2009. The banking sector also made progress in other areas – by 2010 the industry had provided up to 74.5% access for LSM[46] 1-5 to bank branches within a 15km radius; ZAR[47] 16 billion ($ 2.113 billion) in SME finance; and up to 79.2% access to branches and ATMs within a 10km radius (against a target of 80%).[48]

The FSC currently requires banks to offer basic affordable accounts that meet the minimum requirements set by the FTSC, such as non-discrimination (ie, based on income), accessibility, affordability and simplicity. Yet banks are no longer offering Mzansi accounts – instead they are promoting their own basic bank account offerings and new products and services such as mobile services. Some of the reasons put forward for this approach are:

44 Financial Sector Transformation Council, *Transformation of the South African Financial Sector, 2016 Annual Report Summary*, https://fstc.org.za/pdf/reports-and-reviews/2016-Annual-Report-Summary.pdf, accessed 17 September 2019.

45 FinMark Trust, *The Mzansi Bank Account Initiative in South Africa*. Johannesburg: FinMark Trust, 2009.

46 LSM 1-5 refers to the bottom five segments within the 'Living Standard Measures' of the All Media Product Survey (AMPS) categories, a consumer marketing tool commonly used in South Africa as a wealth proxy by marketing agencies to describe the nature of the market and its various sub-sectors. It mostly measures what material things and services one's household has, and ranges from 1 (very low use of these defined goods and services) to 10 (high use). In general, although technically not an income measure, LSMs 1-5 are correlated with the broader international poverty line of $2 per head per day.

47 Currency code for the South African rand.

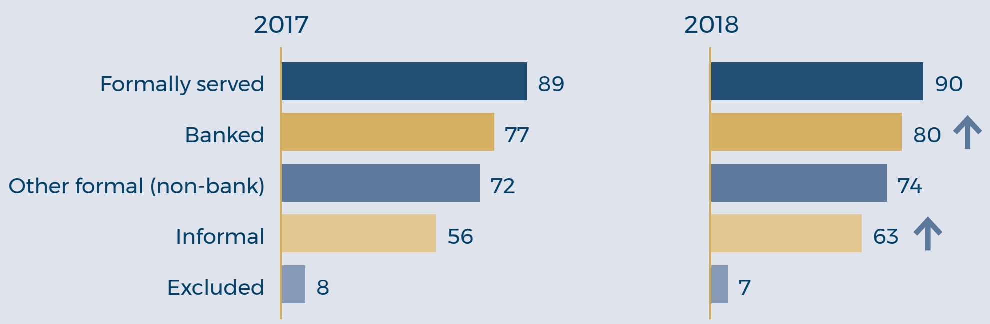
48 Banking Association South Africa, https://www.banking.org.za/what-we-do/overview, accessed 2 April 2019.

the perception that the Mzansi account was a 'poor man's account'; the establishment of a brand other than that of the bank (including the Postbank); and the 'common approach' to service provisioning, which inhabited service innovation. It is thanks to the efforts of the banks (and Postbank) that South Africa achieved its current position where every financially active adult has (or has access to) an account and many economically inactive people have accounts. There are currently 11 million Mzansi accountholders, but some have graduated out of the target market (now earning beyond the targeted income bracket or preferring to use a different transactional account owing to the limited services offered by the Mzansi account).[49] Under the current FSC, these accounts are now being measured under the 'access qualifying product' target.[50]

State of financial inclusion

In an interview with FinMark Trust it was confirmed that, according to the latest FinScope 2018,[51] South Africa has 90% formally served adults, thereby meeting the NDP target. Adults who are banked are now at 80% and those using other non-banking services increased to 74%. The number of adults completely excluded from the formal sector dropped from 8% in 2017 to 7% in 2018 (Figure 1). According to FinScope 2015, levels of financial inclusion are highest among adult women (90% compared to men at 84%), those living in urban areas (90% compared to 81% in rural areas), and white people (97% compared to black people at 86%). There are overlaps with consumers using a combination of formal and informal financial services and products – for example, almost 36% use a combination of banked, other formal (non-bank) and informal mechanisms to manage their finances. Of course, a consumer can use multiple service providers as well, for example

Figure 1 Overview of financial services/products uptake



Source: FinMark Trust, interview conducted on 30 April 2019

49 Personal interview, FSTC official, Johannesburg, 7 May 2019.

50 FSTC (Financial Sector Transformation Council), 'Amended FSC Series FS700: The Measurement of the Access to Financial Services Element of Broad-based Black Economic Empowerment', Government Gazette, 1 December 2017, https://fstc.org.za/pdf/amended-code-series/Amended-FSC-Series-FS700.pdf, accessed 2 April 2019.

51 Unpublished.

having a bank account and an insurance policy. A total of 3.4% of adults rely exclusively on informal mechanisms to manage their money.[52] This is as a result of consumers' needs not being fully met by the formal sector alone, or a preference or trust issue.

Transactional banking (100%) is the main use of banking services, while credit (74%) and insurance (58%) are the key drivers of other formal (non-bank) products. Burial societies (53%) are the most popular form of informal product usage. The savings culture in South Africa is dismal – 64% of adults do not save. Remittances are on the increase, with 11.6 million adults (36% of the population) involved in remittance transactions in 2015. Over 85% of these adults remit through formal means: 36% used banks, 50% used supermarkets and 27% used cell phones. The success of retail payment services depends heavily on the availability, physical proximity and reliability of customer service and access points.[53]

Account ownership is significantly higher in South Africa than in sub-Saharan Africa and on par with ownership levels in other upper-middle-income countries (MICs). According to the 2014 Global Findex, 70.3% of adults in South Africa have access to a transaction account (including mobile money accounts), compared to 34.5% in sub-Saharan Africa and 70.5% in other upper-MICs. When compared to its BRICS peers in terms of bank account ownership, South Africa is ahead of India by a wide margin, on par with Brazil and Russia and lagging behind China. When focusing only on mobile banking, South Africa is ahead on all fronts with 14.4% of adults owning a mobile account, compared to 11.5% in sub-Saharan Africa, less than 3% in India, and less than 1% in other upper-MICs and Brazil.[54]

Quality financial inclusion

There is no doubt that South Africa has experienced a tremendous improvement in the level of financial inclusion. This journey has been a success as a result of the efforts of both the public and private sector. Its resilience is demonstrated by the increased uptake of financial services and products, despite tough economic conditions, including a technical recession in 2017, rising income inequality and 27% unemployment. The need for cheaper, faster, accessible and convenient financial products and services transcends economic means (ie, all income groups equally need them). Digitising the social grants system in the country contributed about 30% of the adult banked population.

The need for cheaper, faster, accessible and convenient financial products and services transcends economic means (ie, all income groups equally need them)

52 FinMark Trust, *op. cit.*

53 FinMark Trust, *op. cit.*

54 World Bank, 'Achieving Effective Financial Inclusion in South Africa', *op. cit.*

Broadening the scope of financial inclusion

The growth in financial inclusion in South Africa shows that it may be reaching its saturation point. As such, focus should turn to quality financial inclusion to address pressing issues such as the productive use of financial services, small enterprise financial service provisioning, the relatively low level of digital payments and risk cover, the low level of savings and over-indebtedness. The starting point is broadening the definition of financial inclusion (ie, not looking at it from only a banking perspective) and enhancing efforts to deepen financial inclusion. Over and above this, there is the issue of transforming financial service providers (FSPs) – more BEE-owned FSPs would be a good addition to the landscape. The FinScope 2015 report stated that it would be introducing a new quality indicator for financial inclusion to understand financial products/services usage and optimisation. This is based on the recognition that, first, high levels of inclusion do not necessarily mean that people's quality of life has improved or that they are benefitting from the financial products that they have. Second, the definition of 'fully served' will have to examine the depth and appropriateness of each product (savings, insurance, credit and payments) component.[55] This coincides with the FSTC's advocacy for a broader definition of financial inclusion, since current efforts are focusing heavily on banking. It is also in line with the Financial Sector Regulations Act (FSRA), which requires regulators to promote financial inclusion across all regulated financial service providers. According to the FSTC, effective access to financial services is defined in terms of the availability and proximity of a sufficiently wide range of first-order financial products and services. In addition, there should be affordable and sustainable access to banks, ATMs and other origination points within 20km of all LSM 1-5 individuals. Accessibility in this regard means dispensing appropriate and affordably priced products and services in a non-discriminatory way by structuring and describing financial products and services in a simple and easily understood manner.[56]

> Focus should turn to quality financial inclusion to address pressing issues such as the productive use of financial services, the low level of savings and over-indebtedness

The FSTC is in discussions with Micro-Finance South Africa (MFSA) to get micro-finance lenders to participate in the FCA by developing their own scorecard and offering 'access qualifying products'. The MSFA is keen to participate in the FSC in 2019 but will report separately on its scorecard, which it will jointly develop with the FSTC. The MFSA initially refused to participate in the FSC – the change of heart is attributed to a new BEE board

55 FinMark Trust, *op. cit.*

56 FSTC, *op. cit.*

member's pushing for transformation. Borrowing behaviour and financial inclusion cannot be understood in isolation,[57] which is one reason why the government enacted the National Credit Act to regulate the creation of a more efficient market to access credit at affordable rates. Access to micro-credit is an important element in improving one's quality of life and should therefore also be used to measure financial inclusion. For example, low-income households access this type of credit to pay for education, transport to work, etc. The 2015 FinScope does include borrowing and credit, and the National Credit Regulator provides quarterly updates on the take-up of various forms of credit from all regulated credit providers, including MFSA members. Nonetheless, there should be a consolidated financial inclusion measure for the country in order to provide a complete picture. The key drivers of credit are unsecured lending and the fact that 64% of adults do not save. Overall, including micro-finance lenders will broaden participation in the FSC and increase the relevance of financial inclusion targets.

The FSTC now also emphasises risk cover by both short- and long-term insurers and medical aid cover. In broadening the definition of financial inclusion, insurance such as hospital cover (which is currently excluded from the FinScope Survey) would also be considered. The FTSC also hopes to get medical schemes on board (to participate in the FSC), given that medical aid is regarded as insurance.[58] According to the 2015 FinScope, 50% of South African adults are uninsured, 27% are members of informal burial societies, 11% are insured through banks and 34% through formal non-banks (eg, funeral cover from an undertaker or insurance company). The concern is that people find themselves over-insured in one area (ie, funeral cover), thereby paying more than they can gain, but left uncovered in other areas such as life cover, physical impairment, etc. The FSTC will review the entire code to remove over-saturated products and will consider setting a limit on the number of funeral policies one person can have. This practice is not new – the previous review led to the exclusion of cell phone insurance cover from the scorecard as a target for financial inclusion.

Productive use of transactional accounts

Focus should turn to productive usage, where banks promote the full use of transactional accounts because they are an essential financial service that can serve as a gateway to other financial services such as savings, credit and insurance. Thirty per cent of the banked are beneficiaries of the South African Social Security Agency (SASSA) who mostly use their transactional accounts once-off (to withdraw money received from SASSA) even though the card allows other uses. Changing this behaviour requires interaction with the Department of Social Development to view grants not only as poverty relief but also as development aid. Accessibility is not an issue, with the exception of rural areas, as the country has a reasonably well-developed network of access points and also makes use of extensive technology in both enabling and extending the service reach. In addition, there is a need

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57 NCR (National Credit Regulator) & FinMark Trust, *Credit and Borrowing in South Africa: FinScope Consumer Survey South Africa 2012*, http://www.ncr.org.za/documents/pages/research-reports/jun13/NCR_14.03.2013.pdf, accessed 4 April 2019.

58 Personal interview, FSTC, *op. cit*.

to promote other financial services such as savings/investment and insurance (against dread diseases, death, disability, etc.), as well as digital channels. According to the unpublished 2018 FinScope, 75% of the adult population have transactional bank accounts; 43% are insured; 40% have funeral insurance cover; 65% are credit-active consumers; 23% save in formal institutions and 15% save informally; and 42% use cell phones to access financial services and products.[59]

It is also possible that the country has reached saturation point for transactional banking

It is also possible that the country has reached saturation point for transactional banking, because some people do not have the financial means to open bank accounts or may just prefer using informal sector channels. The informal sector is made up of large, underdeveloped communities where 38% of working-age citizens are desperate for economic opportunities. These communities are also home to nearly 60% of the country's unemployed.[60] The mass-market population targeted for financial inclusion is largely found in the informal sector, which is mostly cash-driven. Improving usage of transactional accounts, promoting other formal banking and non-banking products and services, and using mobile and other digital channels will only be possible if there is a concerted effort by both the public and private sector to educate people, especially the low-income consumer market and informal sector, about the benefits of formal financial products and services. More so, there is a need to establish digital payment eco-systems in informal areas and/or the township economy. Quality financial inclusion is about productive usage, including product/service optimisation. Through awareness and financial literacy efforts, consumers could learn about the benefits of transaction accounts, how to use those accounts effectively for payment and store-of-value purposes, and how to access other financial services.

As the percentage of the formally served increases, there should be a corresponding – whether proportional or not – decrease in the excluded and those relying on the informal sector. But that has not been the case. FinScope 2018 shows that the number of adults relying on the informal sector has increased from 56% to 63%. This could be attributed to the convenience, accessibility and proximity of the cash-based informal financial services sector. Here, cash is still king. To reduce the risks and expenses of handling cash, policy intervention is required. The industry can assist by ensuring that the FSC review

59 Personal interview, SARB official, Pretoria, 16 May 2019.

60 Sandeep M, *The Economics of South African Townships: A Special Focus on Diepsloot*, Study 89917. Washington DC: World Bank Group, 2014.

includes initiatives that will lessen dependence on cash-based services and shift physical transactions into online and mobile channels in the formal financial sector. Banks can also reduce the costs of servicing customers by moving day-to-day transactions out of branches to alternative channels such as online and mobile banking. It is for this reason that the Banking Association of South Africa (BASA) is keen on increasing its electronic access target to promote the use of digital financial services in the revised FSC. BASA has been finding it difficult to meet its banking densification target under the current FSC and would therefore prefer not to increase the target during the FSC review.[61] Electronic payment services will address the limitations of cash as a payment instrument and provide new opportunities for greater speed, safety, convenience and other relevant features in a rapidly changing world.[62]

In the absence of appropriate policy interventions by the National Treasury, the review of the FSC could consider both the current challenges the industry faces in meeting some of its targets and those targets that have been exceeded by the industry. For example (although this is a regulatory issue), the development of appropriate products for financial inclusion by insurers has been an issue. At the same time the sector contributes through the over-investment in funeral insurance mentioned earlier, with approximately 5.7 million active policies.[63] There is a need to understand both the key drivers of informal sector product usage and its mechanisms, as a significant number of people rely on it daily. For example, burial societies are the most popular usage of informal sector products, even though they are not regulated by the Financial Sector Conduct Authority (FSCA). This means there is no legal recourse in the event of non-compliance with consumer protection regulations.

Hindrances to greater financial inclusion

A closer assessment of the remaining financially excluded may also shed some light on why financial inclusion, which is generally linked to socio-economic development, is not yet universal in South Africa. Some of the key reasons [64] why some South Africans are not keen on banks are provided by the Boston Consulting Group's recent research on the state of financial inclusion in the country. (As illustrated in Figure 2.)

- South African bank fees are four times higher than those in countries such as Germany, Australia and India. This is partly owing to the high operating costs of banks and the proliferation of cybercrime. Of the 80% of adults with transaction accounts, only 24% conduct more than three monthly transactions such as withdrawals, deposits or card swipes, resulting in more than 60% of all purchases being paid for in cash. Addressing the lack of an enabling and inclusive digital payment eco-system is critical.

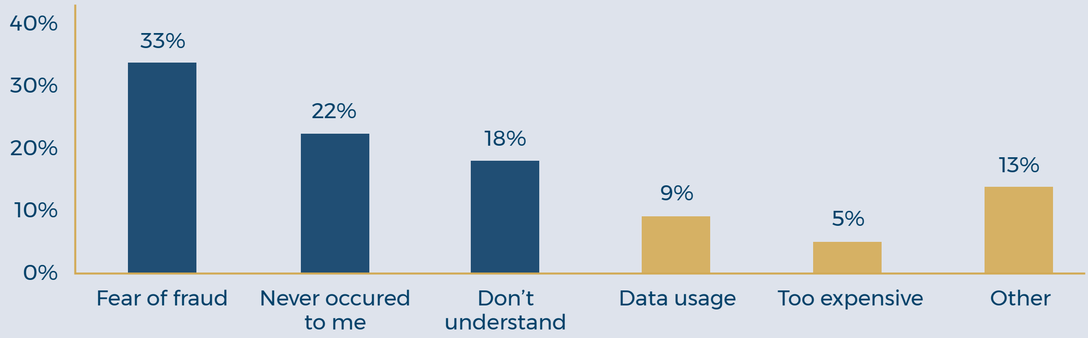
61 Personal interview, FSTC, *op. cit.*

62 Bank of International Settlements & World Bank Group, Payment Aspects of Financial Inclusion, April 2016, https://www.bis.org/cpmi/publ/d144.pdf, accessed 2 April 2019.

63 Personal interview, FSTC, *op. cit.*

64 WEF (World Economic Forum), '*6 challenges to financial inclusion in South Africa*', 27 April 2017, https://www.weforum.org/agenda/2017/04/financial-inclusion-south-africa/, accessed 2 April 2019.

Figure 2 Key reasons why some South Africans do not use mobile banking



Source: WEF (World Economic Forum), '6 challenges to financial inclusion in South Africa', 27 April 2017, https://www.weforum.org/agenda/2017/04/financial-inclusion-south-africa/, accessed 3 April 2019

- As a result of past financial sector market misconduct/abuse such as inappropriate marketing and selling of financial products, people in low-income brackets generally do not trust the sector. They fear being exploited.
- Some low-income earners prefer using cash instead of digital channels simply because of a lack of familiarity or illiteracy, and a fear of ATM and mobile/Internet banking fraud. Traditional banking approaches such as branch transactions come with the comfort of possible human intervention if an issue arises. Fear of fraud is the number one reason for not utilising digital channels.
- More than 40% of South African households use *stokvels*[65] (trust-based models used to save money that provide a safety net for emergencies and offer social interaction for the purpose of entertainment or advice). These community-based models are mostly prevalent in lower-income populations and provide the flexibility and support structure that is perceived as lacking in the banking industry. It is estimated that there are over 800 000 *stokvels* in South Africa with a combined membership of 11.5 million people, handling over ZAR 44 billion ($ 3.679 billion) per year.[66]
- Bank requirements such as payslips and bank statements to access formal financial sector services such as loans are seen as onerous, if not a barrier. In addition, banks also have lengthy processing timelines that low-income earners may view as restrictive, especially when they have personal or family emergencies such as needing money to travel to work or to buy food. It is this rigidity that prevents some South Africans from

65 A stokvel is a savings or investment society in which members regularly contribute an agreed amount that is then divided among them, according to a method agreed on by the members.

66 National Stokvel Association of South Africa, 'Three Decades of Stokvel Banking', May 2018, http://nasasa.co.za/site/wp-content/uploads/2018/05/Three-Decades-of-Stokvel-Banking-Andrew-Lukhele-NASASA-2018.pdf, accessed 2 April 2019.

using formal channels, resulting in many turning to *mashonisas* (community loan sharks) or friends and family.

- A significant amount of business is conducted informally, making it difficult for such enterprises to access the formal banking sector, which requires proper registration in order to open business banking accounts and loans. The 2013 Survey of Employers and Self-Employed[67] found that more than 1.5 million people (mostly Africans with lower levels of education) were running small, informal businesses. Small businesses also find bank fees prohibitively expensive, thereby further limiting their use of such services.

When SASSA made it compulsory for social grants to be paid directly into bank accounts, financial institutions and some non-financial providers (such as associates of the grant distribution service provider and airtime sellers) decided to take this opportunity to target grant recipients with products such as funeral cover and micro-loans, automatically deducting their fees from recipients' accounts. There was a public outcry when many grant recipients were left with little money for necessities, which led to an investigation into the legality of the practice. The way in which the scheme was implemented and administered (ie, single service provider) was equally to blame for this situation. Currently, only deductions for funeral insurance not exceeding more than 10% of the value of the social grant by an accredited financial service provider are allowed.[68] South Africa has established an Ombudsman for banking services to address complaints and also has a consumer protection framework. However, there are still no specific provisions for non-bank financial services (including payment services) whose innovations help to deepen financial inclusion.

South Africa benefits from digitising government-to-person services

The country has benefited from the use of digital solutions in its social grant system. South Africa has a well-established social welfare system and is currently disbursing over 17 million social grants monthly.[69] In 2018 one-third of the banked population owned a SASSA MasterCard (launched in 2012), which was replaced in 2018 with the new gold SASSA-SAPO (South African Post Office) card. Grant recipients are allocated a biometric smart card that has multiple benefits, including the ability to receive grants anywhere in the country. The cards can be used as a debit card and to make other purchases and payments, including airtime and electricity. It can also be used to check balances, withdraw cash at certain till points without incurring any transaction costs or at ATMs at a cost, cash pay-points, etc. Recipients are allowed to use alternative payment methods such as banks, including Postbank.[70] SASSA is engaging commercial banks on the provision of low-cost accounts for

67 SSA (Statistics South Africa), *Survey of Employers and the Self-employed 2013*. Pretoria: SSA, August 2014.

68 SASSA (South African Social Security Agency), 'You and Your Grants 2019/20', https://www.sassa.gov.za/publications/Documents/English%20You%20and%20Your%20Grants%202019-20.pdf, accessed 11 March 2019.

69 SASSA, 'Statistical Summary of Social Grants in South Africa', June 2018, https://www.sassa.gov.za/statistical-reports/Documents/Fact%20Sheet%20-%20June%202018.pdf, accessed 11 March 2019.

70 Department of Planning, Monitoring & Evaluation, 'An update on the new SASSA card', 16 August 2018, https://www.dpme.gov.za/news/Pages/SASSA--Update-on-the-new-payment-system.aspx and https://www.dpme.gov.za/news/Newsletters/E-Newsletter%20July%20-%20Update%20from%20SASSA%20on%20the%20New%20Payment%20System.pdf, accessed 11 March 2019.

social grant beneficiaries, but its long-term plan is to use accredited financial institutions to pay social grants in future.[71] However, SASSA re-assesses beneficiaries' eligibility if they keep a balance on their SASSA account and do not withdraw/use their funds, which means they are seldom used as transaction accounts. In addition, the account-issuing bank has a limited footprint in the country,[72] and regulation 26 (A) of the Social Assistance Act of 2004 allows only one direct debit from the account for funeral insurance, in an effort to stop undue direct debits. There is thus untapped potential for the new SASSA-SAPO to improve usage and broaden financial inclusion.

Although not without controversy and fraught with corruption, South Africa began rolling out biometric cards to social grant beneficiaries in 2012 in order to curb fraud in the grants system, improve on the delivery of grants, and reduce the costs involved in making payouts.[73] Before the Special Investigation Unit (SIU) began its investigations in 2006, it is estimated that the government was losing about ZAR 1.5 billion ($ 180.399 million) a year through the maladministration of social grants and corruption.[74] The SIU prosecuted 20 554 people for fraud and corruption relating to grants, which resulted in 17 880 convictions between 2006 and 2012. The government was able to recoup ZAR 304.9 million ($ 36.669 million) from 46 237 individuals who were incorrectly receiving social grants and cancel fraudulent grants paid to 7 133 beneficiaries. The SIU's investigation helped the government recover over ZAR 104.6 million ($ 12.579 million) and recommended the removal of all improperly received grants. As a result, the government saved over ZAR 1 billion ($ 120.266 million) and prevented future losses of over ZAR 11.8 billion ($ 1.419 billion). The implementation of the then bespoke biometric payment system, which required the re-registration of grant beneficiaries, helped the government save ZAR 800 million ($ 96.212 million) per year.[75]

There are other examples of how the South African government has leveraged large-scale programmes to benefit from digital solutions. Although these examples are not G2P services, they are e-government services that help to educate the population about digital channels and promote their usage. The modernisation of the South African Revenue Service (SARS), which began in 2007, changed the landscape for revenue collection and returns in the country, and marked the start of SARS's transition from paper to digital with a view to speed up the rate of tax processing. The modernisation project was scaled up in 2013 when SARS implemented an automated and centralised customs management system[76] for all commercial trade across South Africa's borders, replacing a variety of older legacy systems and paper-based manual administrative processes. The popular use

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71 SASSA, file:///C:/Users/A0056768/Downloads/sassa.sapo%20statement.pdf, accessed 10 June 2019.

72 Bank of International Settlements & World Bank Group, *op. cit*.

73 SASSA, *2012/13 Annual Report*, https://www.sassa.gov.za/annual%20reports/Documents/Annual%20Report%20-%20January%20 2013.pdf, accessed 12 March 2019.

74 *South African Government News Agency*, 'New biometric card to boot out social grant fraud', 8 June 2012, https://www.sanews.gov.za/south-africa/new-biometric-card-boot-out-social-grant-fraud-0, accessed 11 March 2019.

75 *Ibid*.

76 National Treasury, 'Implementation of the new Customs Systems Modernisation Programme', Media Statement, 22 August 2013, http://www.treasury.gov.za/comm_media/press/2013/2013082201%20-%20Implementation%20of%20the%20new%20 Customs%20Systems%20Modernisation%20Programme.pdf, accessed 11 March 2019.

of electronic channels has resulted in an efficient tax administration system, enhanced compliance and a significant drop in tax-related fraud. The Department of Labour's U-Filing system is also linked to the SARS system, providing employers and the labour force with a secure and convenient way of contributing and applying to the Unemployment Insurance Fund.[77] There are various other e-government services, such as the eNaTIS online system to allow motorists to make online pre-bookings for the renewal of their driver's licences and learner licences;[78] and the National Student Financial Aid Scheme online bursary application for higher education and training for students from poor and working-class families.[79] By encouraging a culture of using digital channels, online services can promote more efficient service delivery and combat corruption.

The role of government in digital financial inclusion

Digitisation is a key element of economic development policies everywhere, and should be at the heart of all innovative initiatives. Given that over 60% of the world's population now has access to mobile/digital financial services, and that DFS offer disadvantaged groups opportunities for financial inclusion, it is important for policymakers to focus on digitalisation. More so, new products, interfaces, providers and delivery mechanisms present specific risks and challenges, and policymakers have to come up with a comprehensive package to tackle market challenges and reduce consumer risk.

Digital technologies have spread rapidly in much of the world even though the digital dividends – the broader development benefits arising from these technologies – have lagged behind.[80] Digital technologies have boosted growth, expanded opportunities, and improved service delivery. Yet their aggregate developmental impact has fallen short and is unevenly distributed. Indeed, the digital revolution has brought immediate private benefits such as easier communication and information, greater convenience, free digital products and new forms of leisure. There is now a profound sense of social connectedness and global community. However, massive investments in digitisation have yet to generate real digital dividends such as faster growth, more jobs and better services. Closing the remaining digital divide by increasing access to the Internet is one means of ensuring that digital technologies benefit everyone, everywhere. However, greater digital adoption will not be enough.

In order to enhance financial inclusion, governments should focus on four issues.

Firstly, regulators should encourage traditional and digital financial literacy by supporting the inclusion of financial education for DFS elements within existing national strategies

77 South Africa, Department of Labour, 'Ufiling', https://www.ufiling.co.za/uif/follow-me, accessed 29 May 2019.

78 Arrive Alive, 'National Traffic Information System', https://www.arrivealive.co.za/National-Traffic-Information-System, accessed 29 May 2019.

79 NSFAS (National Student Financial Aid Scheme), 'Mission', http://nsfas.org.za/content/mission.html, accessed 29 May 2019.

80 World Bank Group, *2016 World Development Report*, 'Digital dividends', http://www.worldbank.org/en/publication/wdr2016, accessed 2 April 2019.

to reach consumers and entrepreneurs. The process of transferring knowledge of the management of financial resources and the usage of financial products and services is known as financial literacy or financial education.[81] The OECD International Network on Financial Education (OECD/INFE) has developed policy guidelines for policymakers responsible for the implementation of the G20 Principles for Innovative Financial Inclusion and the G20 High-level Principles on Digital Financial Inclusion. The aim is to promote the responsible and beneficial development of digitalisation by building trust and confidence in the acquisition and use of digital financial services by the financially excluded.[82] There is an urgent need for such initiatives in countries such as South Africa, where systemic education issues have resulted in a poor and financially illiterate population that mistrusts the formal financial sector. Particularly, financial education plays a crucial role in the broader consumer protection environment and can help engender trust in the formal financial system by the low-income market. Although there have been efforts through the FSC to have FSPs advance non-product financial literacy since 2004, the results are not encouraging. Notwithstanding the rising adoption of smartphones and millennials' high usage of digital technology, South Africa's digital ecosystem and relatively low levels of financial literacy have constrained the use of sophisticated financial services. Income also plays a role, since more than 80% of the population does not save, invest or insure against risk.[83] Digital and fintech innovations also largely cater to a niche, relatively affluent and financially savvy consumer market. Strengthening digital financial literacy or any type of financial education is important, owing to the digitisation of financial products and services that have unique characteristics, advantages and risks and have become an important component of the global policy-making agenda. As part of its commitment to financial literacy, BASA started the StarSaver programme in 2008 to foster a culture of saving among children. A lesson plan was developed in conjunction with the Department of Basic Education and has been integrated into the Economic Management Science curriculum in South Africa. The Banking Sector Education and Training Authority has developed consumer credit education material that can be used by the industry in consumer engagement and education strategies. The aim is to improve consumer credit education in South Africa and assist in educating consumers about responsible borrowing behaviour. Treasury released a policy statement ('A safer financial sector to serve South Africa better') in February 2011 that led to the launch of a national consumer financial education strategy in 2013.[84] Treasury, together with the FSCA and the National Consumer Financial Education Committee, in 2019 plans to pilot MoneySmartWeek, an education and awareness platform involving financial institutions, companies, schools and communities. It is envisaged that the project will help consumers manage their personal finances better, which is why it is being offered to all consumer segments, demographics and income levels. The South African Reserve Bank (SARB), the Association for Savings and Investment and the South African Insurance

81 *Ibid*.

82 OECD, 2017, *op. cit*.

83 CoEFS, *op. cit*.

84 National Treasury, *National Consumer Financial Education Strategy*, July 2013, https://www.fscaconsumered.co.za/Documents/National%20consumer%20financial%20education%20strategy%20(23%20Aug%202013).pdf#search=financial%20education, accessed 4 April 2019.

Association have also been actively promoting financial literacy. The impact of the various initiatives has not been fully assessed yet, but the Human Sciences Research Council (HSRC) has made an effort to measure their impact through two monitoring surveys. The HSRC research shows that the country's overall financial literacy score declined marginally from 52% in 2011 to 54% in 2013.[85] In 2016 South Africa was last out of 30 countries participating in an OECD survey measuring financial knowledge.[86] Efforts need to be stepped up to increase financial literacy. A comprehensive and nationally coordinated public–private partnership approach is needed if progress is to be made in curbing the overreliance on informal sector services and cash, and promoting the use of formal financial products and services and digital channels.

Secondly, regulations must take into account the specific DFS opportunities and challenges faced by consumers and entrepreneurs. Government, in partnership with the private sector, should coordinate the collection of data to better understand the developmental implications of DFS for consumers and entrepreneurs. Digital innovation can provide a significant boost to financial inclusion, but digital finance also presents new challenges for regulators that are charged with protecting consumers in a rapidly changing and increasingly complex global ecosystem. Regulators also have to deal with the growing risks related to data governance stemming from data generated by individuals' digital footprints. Coordination between regulators is needed to deal with data governance issues relating to how data is accessed, used, stored and shared.

Thirdly, regulators must enhance regulation, supervision and market conduct while ensuring an enabling framework for digitisation. Regulatory aspects and competition/market conduct are the most important policy concerns in terms of DFS, given the importance of regulation in creating an open and level playing field for digital finance providers, ensuring effective market conduct and competition, and establishing adequate rules of the game for bank and non-bank market participants, mobile network operators and other relevant actors. The introduction of new models and actors poses a risk to the financial stability of the overall system. This is what regulation must address – while being flexible enough to accommodate rapid changes in markets, technologies and business models and ensuring sufficient regulatory confidence for companies to take risks and spearhead innovation. Additionally, regulation needs to be implemented by institutions with the jurisdiction and expertise to consider all the alternatives, and should be designed to protect consumers from potential harm associated with a particular service [87] – which is what the newly established FSCA is trying to achieve in South Africa.

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85 HSRC (Human Sciences Research Council), *Financial Literacy in South Africa: Tabulation Report Based on the 2013 South African Social Attitudes Survey Round*, 2014, http://www.hsrc.ac.za/en/research-data/view/6893, accessed 12 March 2019.

86 OECD/INFE (International Network on Financial Education), *International Survey of Adult Financial Literacy Competencies*, 2016, http://www.oecd.org/daf/fin/financial-education/OECD-INFE-International-Survey-of-Adult-Financial-Literacy-Competencies.pdf, accessed 4 April 2019.

87 European Commission, 'National Initiatives for Digitising Industry across the EU', 21 November 2017, https://ec.europa.eu/futurium/en/system/files/ged/national_initiatives_for_digitising_industry_across_the_eu.pdf, accessed 12 February 2019.

Finally, regulators, public policymaking institutions and the private sector, especially supply-side participants, need to work together to address structural issues impeding financial services growth in segments such as SMMEs, women and the youth. Resource and investment mobilisation continue to be held up by the unattractive economics of serving these segments. In addition, the solutions offered by the formal financial services sector often do not appear attractive enough as alternatives to existing informal solutions (partly because of the low level of financial literacy and overall awareness among this user group).

South Africa's policy responses

The government plays a central role in creating an adequate enabling environment for financial inclusion in South Africa. It is making strides in transforming the financial sector and contributing towards greater inclusion since parliamentary hearings were held in 2017 that noted the slow progress in meeting the Financial Sector Charter objectives. Treasury is responsible for financial sector development, which includes financial inclusion. However, transformation and financial inclusion are two separate issues and should be addressed separately from a policy perspective, with clear objectives for each initiative. Naturally, the formulation of a financial inclusion policy should take transformation objectives into account, but the objectives of financial inclusion (the provisioning and productive use of appropriate, beneficial and sustainable products and services) are not limited to transformation objectives. Financial inclusion objectives are aimed at society as a whole – as is the case globally.

Treasury indicated that the FSC review would take into account proposed measures for effective financial inclusion, including ensuring improved data collection, monitoring and reporting; strengthening sanctions for non-FSC compliant firms; aligning licensing conditions to FSC requirements; and raising transformation targets, as well as the country's historically low savings and investment rates.[88] Treasury, as a policymaker for the financial sector, implemented the new twin peak financial regulation model[89] in 2018 by introducing the FSRA to protect customers and the domestic financial system more effectively. The newly established FSCA is responsible for significantly improving customer protection in the financial sector and driving better customer outcomes, including providing financial education and promoting financial literacy. The FSRA requires the FSCA to be the driving force behind financial inclusion, which will ensure that South Africans get access to financial services and products, and that products are developed and distributed in a manner that adheres to Treating Customers Fairly principles.[90] The same act also requires the Prudential Authority to support financial inclusion. This will ultimately strengthen transformation initiatives in the sector and other initiatives aimed at BBBEE.

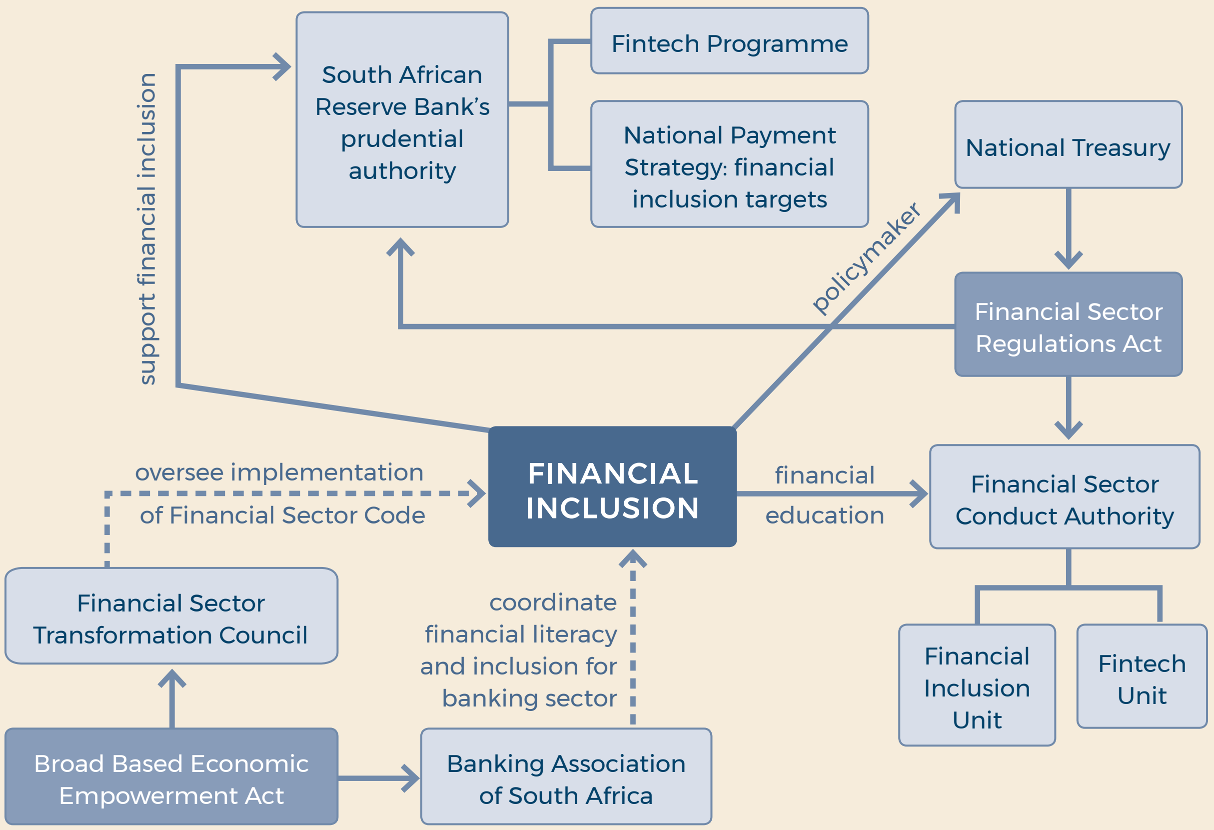
88 National Treasury, 'Budget Review 2018', 21 February 2018, http://www.treasury.gov.za/documents/national%20budget/2018/review/FullBR.pdf, accessed 17 May 2019.

89 National Treasury, 'New Twin Peaks regulators established', 29 March 2018, http://www.treasury.gov.za/twinpeaks/Press%20release%20Twin%20Peaks%20implementation%20March2018_FINAL.pdf, accessed 14 May 2019.

90 Financial Sector Conduct Authority, *Regulatory Strategy of the Financial Sector Conduct Authority: October 2018 to September 2021*, https://www.fsca.co.za/Documents/FSCA_Strategy_2018.pdf, accessed 14 May 2019.

The FSCA has two new units, one for financial inclusion and the other for fintech. The former unit deals with financial inclusion from a customer outcome or conduct perspective. Figure 3 gives an overview of the key role players in South Africa. According to the 2018 Budget Review, Treasury was supposed to publish a policy document outlining South Africa's approach to achieving financial inclusion in 2018. All the interviewed stakeholders indicated that they were not engaged by Treasury in the drafting of this policy document but are awaiting its release in order to understand their roles and responsibilities in advancing and supporting financial inclusion. The release of a national Financial Inclusion Policy would be supported by a South African Financial Inclusion Monitor (measuring and interpreting a variety of indicators of financial services use). This would in turn be followed by the establishment of a financial inclusion forum, with state actors (including the policymaker and the regulators) and representative organisations of the industry. The mandate of this body would be agreeing on the strategy and how it is implemented, coordinating efforts in terms of meeting the agreement, monitoring the effect of initiatives and suggesting adjustments where necessary. Of necessity, the plan of action must liaise closely with the objectives of the FSC, and thus the FSTC needs to be a part of this forum. The key issues here are coordination and measurement/monitoring.

Figure 3 Institutions playing a role in financial inclusion in South Africa



Source: Author's depiction

The World Bank (under the South African Financial Sector Development and Reform Program) published a policy document in 2018 outlining South Africa's approach to achieving effective financial inclusion from a payment perspective. Currently, the South African Banks Act of 1990 limits deposit-taking and the provision of payment services to banks because of the current definitions requiring only banks to hold intermediate deposits.[91] Financial inclusion efforts benefit not only those who will become financially included but also the national payments infrastructure and, ultimately, the economy. As such, efforts are underway to modernise the country's payment system legislation, the National Payment System (NPS) of 1998. The aim is to allow new players, such as retailers, to participate in the payment system and support more affordable account technologies such as mobile money and e-wallet.[92] The policy paper on the review of the NPS calls for enabling non-banks to provide payment services that involve pooling funds, such as e-money, remittances and transactional accounts, independently – thus, without the need to partner with banks, as currently required by legislation. Financial inclusion requires a well-functioning retail payments ecosystem that encourages innovation without compromising the safety and soundness of the national payments system. Although non-bank payment service providers and innovative business and technological approaches have helped to expand access to payment services, the associated risks need to be managed without stifling competition and innovation.

One of the keys to greater financial inclusion is an open and accessible payment system. Thus, there is a need for the interoperability of payment systems across the various payment options offered

Furthermore, one of the keys to greater financial inclusion is an open and accessible payment system. Thus, there is a need for the interoperability of payment systems across the various payment options offered. If this were achieved, consumers would have far more options without having to consider the point-of-origin or point-of-destination of a payment and the system as a whole would be more cost effective, which could eventually translate into lower costs for users. In South Africa, the majority of payment types are interoperable by design, but this is not the case with domestic and cross-border remittances, or for mobile-to-mobile payments. The SARB is currently engaging the industry to agree on and implement a scheme to make domestic remittance services interoperable. Quality financial inclusion, inter alia choice, also means diversifying financial products, such as having non-banks offering transactional accounts.[93] Interoperable domestic remittances will establish

91 The World Bank, 'Achieving Effective Financial Inclusion in South Africa: A Payments Perspective', http://www.treasury.gov.za/publications/other/Achieving%20Effective%20Financial%20Inclusion%20in%20South%20Africa.pdf, accessed 14 May 2019.

92 National Treasury, 21 February 2018, *op. cit.*

93 Interview with SARB, *op. cit.*

a level playing field for both banks and non-banks offering money transfer services and/or transactional services, while also establishing a regulatory framework that addresses the pooling of funds by non-banks when they provide such payment services.

Other options for effective financial inclusion that can be considered by the industry are having 'brandless or white' branches and ATMs in a non-competitive environment, representing a pooling mechanism. This could be done by banks and insurance companies as part of their FSC commitments with the view of deepening financial inclusion for the 'bottom of the pyramid' population that is currently under-served and unbanked. These 'brandless or white' branches and ATMs would be placed in poor communities (ie, rural and peri-urban areas) where BASA members find it challenging to meet their set targets for 'banking access via densification and geographic access' under the financial sector charter. This would be in line with BASA's current push to lower these targets in favour of upping the electronic customer infrastructure access target. The 'brandless or white' branches and ATMs would offer full banking and non-banking products and services, including selling short- and long-term insurance and encouraging and helping customers to switch to digital channels (eg, using mobile financial services such as bank apps and e-money to remit). Funding to establish such branches and ATMs could be sourced from companies' social investment budgets. In other instances, banks could make a few of their branches currently located in remote areas available for this initiative. For this to work, the industry would have to put aside commercial interests and prioritise the transformation agenda. Alternatively, this idea could be implemented using existing structures that are well equipped to increase banks' reach, such as post offices and Lotto agencies.

South Africa's financial regulation is not seen as creating an enabling environment for fintech development. The challenge is to design a legal and regulatory framework that is fair and balanced and that promotes innovation. A lack of clarity and guidance on how fintech fits into existing regulations means South Africa's regulatory environment deters fintech start-ups and generates significant compliance risk.[94] Government is dealing with this from an intergovernmental point of view. In 2016 it established an Intergovernmental Working Group on Financial Technology and Innovation (IFWG) made up of Treasury, the SARB, the FSCA and the Financial Intelligence Centre.[95]

Fostering change requires the ability to bring together diverse interests. The IFWG has been engaging the Department of Home Affairs and the Department of Science and Technology to draft a financial innovation framework that introduces regulatory, financial and human capital incentives, and innovation zones. This is seen as a proactive approach to understanding fintech, including considering the appropriateness of innovation facilitators such as innovation hubs and regulatory sandboxes. The SARB recently launched a new fintech programme with the objective of assessing the appropriateness of policies and regulatory regimes in light of fintech innovation. This is an effort to embrace fintech

94 CoEFS, *op. cit.*

95 National Treasury 21 February 2018, *op. cit.*

and new ways of providing services while continuing to focus on consumer and investor protection and keeping a watchful eye on risks, including money laundering and terrorism financing, growing cybersecurity risks, contagion and systemic risks. The FSRA requires the SARB to support financial inclusion, and it has therefore started developing indicators to monitor it from a payment perspective. It also currently chairs the IFWG and has added financial inclusion targets to its National Payment Strategy (Vision 2025).[96] Furthermore, there have been positive developments in South Africa that will contribute to increased competition in the financial services sector, thereby driving costs down and deepening financial inclusion. The SARB granted three bank licences in 2017 to companies planning to use their significant digital capabilities in the banking sector. Introducing competition in the financial services sector has the potential to reduce costs to consumers.

Digital financial services in Africa – what are the opportunities?

Africa is positioned advantageously for a digital transition. It is the world's second largest continent and is experiencing an unprecedented and dynamic period of population growth, with the UN Department of Economic and Social Affairs: Population Division estimating that its population will reach 2.5 billion by 2050.[97] Africa has the youngest population globally with a median age of 18 years, which is in stark contrast with the global median age of 31.[98] This makes Africa a true demographic outlier and the youngest continent, with a unique chance to undergo radical digital transition. Young people are exponentially more inclined to accept digital solutions. Corporations see markets with dynamic demographics as an incentive to be innovative, as their existing client base may be shrinking. There is thus an opportunity to attain new-to-market prospective clients by adapting core value propositions, among others. Africa also increasingly offers the necessary economies of scale sought by corporations. In sub-Saharan Africa the youth literacy rate increased from 65% in 1990 to 75% in 2016[99] while the number of tertiary students increased from 400 000 in 1970 to an approximate 7.2 million in 2013.[100] As literacy rises, the digital literacy provided by governments, donors and the private sector is also rising. Digital transition, being location-independent, will help Africa bridge its unconnected geographic location.[101]

96 Interview with SARB, *op. cit*.

97 UN Population Division, 'World population prospects 2019', https://esa.un.org/unpd/wpp/Publications/Files/WPP2017_KeyFindings.pdf, accessed 29 April 2019.

98 WEF (World Economic Forum), 'Mapped: The median age of the population on every continent', February 2019, https://www.weforum.org/agenda/2019/02/mapped-the-median-age-of-the-population-on-every-continent/, accessed 29 April 2019.

99 UNESCO, 'Literacy Rates Continue to Rise from One Generation to the Next', Fact Sheet 45, September 2017, http://uis.unesco.org/sites/default/files/documents/fs45-literacy-rates-continue-rise-generation-to-next-en-2017_0.pdf, accessed 29 April 2019.

100 Darvas P *et al*., *Sharing Higher Education's Promise beyond the Few in Sub-Saharan Africa*, World Bank Group, 2017, http://documents.worldbank.org/curated/en/862691509089826066/pdf/120693-PUB-PUBLIC-PUBDATE-10-25-17.pdf, accessed 29 April 2019.

101 Gyori D, 'Africa's ten key advantages in digital transition', The Asian Banker, 23 February 2018, http://www.theasianbanker.com/updates-and-articles/africas-ten-key-advantages-in-digital-transition, accessed 29 April 2019.

Africa's middle class has grown considerably, which is a key enabler of private sector growth on the continent, accounting for much of the effective demand for goods and services.[102] The continent has a burgeoning commerce sector, especially e-commerce, which is linked to the rising rate of urbanisation. E-commerce was one of the key drivers of the digital transition in Western countries and is expected to continue in Africa, enabling the middle class to buy cutting-edge consumer hardware and software solutions and allowing users to directly participate in all digital markets. With about 30% of Africans having access to the Internet, satellite is said to be the best technology to spread the Internet to areas with inadequate infrastructure. The number of active satellites can easily be doubled in the coming five years, as new launching technology will cut fixed costs by 80% to 90% and satellites themselves are getting smaller.[103] As the production cost of satellite technology decreases, Internet coverage will increase in Africa (with some estimating that Internet penetration will reach 65% by 2022, translating into half a billion new-to-Internet consumers). This an unprecedented Internet boom that will boost digital transition immensely. China has become Africa's largest trade partner and is ahead of the West in its digital transition, especially in financial services. This digital advantage can be exported to Africa, helping it leapfrog its development.[104]

Only 35% of the population in sub-Saharan Africa has access to electricity, and the region has the lowest road and railroad densities among developing countries.[105] A digital transition will help Africa bridge its infrastructure gap, since digital consumer electronic solutions such as smart phones do not require that much energy or a different approach to providing such access (ie, solar, etc.). Compared to Western corporations such as banks that are struggling with long-outdated 'legacy IT systems' and complex intertwined 'spaghetti software', corporations in Africa have more up-to-date, agile and less complex IT infrastructure, giving them an advantage in terms of fulfilling digital customer needs and ultimately easing a digital transition.[106] In addition, fully developed and mature MNOs in the West have not diversified from their core competence of providing telecommunication services, whereas in high-growth emerging markets such as Africa there is a 'digital convergence' whereby MNOs are highly active in financial services. This has been driving digital transition in many industries in Africa, as shown by the continent's leading position in mobile money.

The best-known mobile money service in Africa is M-Pesa. The pioneering mobile payment system, created in 2002 when Kenyans started using airtime as a substitute for money transfers, led other developing countries to introduce mobile payment solutions to extend

102 AfDB (African Development Bank), 'The Middle of the Pyramid: Dynamics of the Middle Class in Africa', Market Brief, 20 April 2011, https://www.afdb.org/fileadmin/uploads/afdb/Documents/Publications/The%20Middle%20of%20the%20Pyramid_The%20Middle%20of%20the%20Pyramid.pdf, accessed 29 April 2019.

103 Gyori D, *op. cit*.

104 *Ibid*.

105 World Bank Group, 'Why we need to close the infrastructure gap in sub-Saharan Africa', *Africa's Pulse*, April 2017, http://www.worldbank.org/en/region/afr/publication/why-we-need-to-close-the-infrastructure-gap-in-sub-saharan-africa, accessed 29 April 2019.

106 Gyori D, *op. cit*.

financial services to an unbanked or underbanked community, with mixed success.[107] With M-Pesa's rise to fame, mobile payment systems have emerged as game changers and a grand new frontier in the financial inclusion arena.[108] There are over 10 countries in Africa where more people hold mobile money accounts than traditional bank accounts.[109]

Mobile financial services/money promises a cheaper and more scalable alternative to traditional banking in sub-Saharan Africa, where financial inclusion is low. Yet there has not been much progress, with the exception of M-Pesa, partly because of uncertainty whether markets other than Kenya are sufficiently robust. A large part of the continent still pays with cash and, according to McKinsey, Gallup's survey of 11 countries in sub-Saharan Africa shows that more than 80% of adults uses cash to pay bills. Significant cash-payment volumes through informal channels are also prevalent. These transactions represent a large untapped market for mobile financial services. The lack of digital payment penetration means that there is a high cost to cash payments, including record keeping, counting, storage, security and transportation. It is easier and less costly to make those payments electronically. The major obstacle to increasing mobile money penetration is not the lack of mobile technology, since two-thirds of adults in sub-Saharan Africa currently use mobile phones. Many regulators are laying the foundations for e-money and electronic remittances and also allow the entrance of non-bank operators to provide digital financial services.[110] Together, these factors will allow digital payments to leapfrog.

By leveraging the power of mobile networks to accelerate the digitising of financial inclusion, mobile technology already plays a role in addressing a range of social challenges, including the digital divide and financial inclusion

Africa is at the forefront of mobile financial innovation, even though the value of fintech investment is comparatively low. The high uptake of mobile phones and the relatively underdeveloped banking infrastructure have fostered an explosion of mobile financial services.[111] By leveraging the power of mobile networks to accelerate the digitising of financial inclusion, mobile technology already plays a role in addressing a range of social challenges, including the digital divide and financial inclusion. Mobile technologies

107 Lal R & I Sachdev, 'Mobile Money Services: Design and Development for Financial Inclusion', Harvard Business School Working Paper, 15-083, July 2015, http://www.hbs.edu/faculty/Publication%20Files/15-083_e7db671b-12b2-47e7-9692-31808ee92bf1.pdf, accessed 19 September 2019.

108 Mader P, *op. cit.*

109 Paycorp, 'How Africa is leading the adoption of mobile money', 8 October 2015, https://paycorp.co.za/news-views/how-africa-is-leading-the-adoption-of-mobile-money/, accessed 29 April 2019.

110 Kendall J, Schiff R & E Smadja, 'Sub-Saharan Africa: A major potential revenue opportunity for digital payments', McKinsey, February 2014, https://www.mckinsey.com/industries/financial-services/our-insights/sub-saharan-africa-a-major-potential-revenue-opportunity-for-digital-payments, accessed 29 April 2019.

111 CoEFS, *op. cit.*

generated 6.7% of GDP in Africa, equivalent to $150 billion in economic value. It is estimated that this will increase to more than $210 billion (or 7.6% of GDP) in 2020 as countries benefit from the improved productivity and efficiency brought about by the take-up of mobile services. About 3.8 million jobs are supported by the mobile ecosystem, and this will increase to 4.5 million in 2020. The mobile services sector contributed $17 billion in taxes in 2015, which is estimated to increase to $20.5 billion by 2020.[112] The Global System Mobile Association is of the view that it is possible to expand financial inclusion in Africa if governments give mobile operators access to the low-frequency spectrum they need for mobile broadband coverage, as the spectrum has no intrinsic value but can be used to help Africa. However, for this to be effective the low-frequency spectrum would have to be maintained and the bandwidth either regulated or monitored for quality control. South Africa lags behind the rest of the world in terms of digitalisation of communications (ie, TV, etc.), which severely hampers the use of the bandwidth that can be used for mobile services. This, in part and in conjunction with corporate greed, is contributing to extraordinarily high data costs (orders of magnitude higher than comparable countries).[113] This is a major inhibitor for financial inclusion, underlining the urgency with which the Department of Communications needs to finish the transition to digital services.

There is no doubt that digital financial services such as mobile money continue to deepen financial inclusion in Africa as they expand, and the potential to change the landscape of financial inclusion for the unbanked or underserved is becoming greater. More regulators are recognising the importance of creating an open and level playing field for non-banks to participate in this space and to make the system interoperable. Digitisation will provide an important avenue for Africa to leapfrog the development of many sectors, particularly financial services.

There is no doubt that digital financial services such as mobile money continue to deepen financial inclusion in Africa as they expand, and the potential to change the landscape of financial inclusion for the unbanked or underserved is becoming greater

Conclusion and recommendations

Financial inclusion is the adoption, beneficial usage and sustainability of financial services, but it is not an end in itself – rather it is an enabler of development and a powerful tool to

112 GSMA, 'The Mobile Economy: Africa 2016', https://www.gsmaintelligence.com/research/?file=3bc21ea879a5b217b64d62fa24c55bdf&download, accessed 13 March 2019.

113 Personal interview, independent consultant, Johannesburg, 24 May 2019.

achieve economic development and the SDGs. Despite the rapid changes and financial opportunities in the DFS domain, 2 billion people around the world still do not have access to an account. The digitalisation of financial services will create new winners and losers, which is why it is important to develop solid digitalisation strategies to keep pace with digital migration. Governments must review their financial inclusion strategies to adapt to newer technologies, thereby being poised for significant growth opportunities in broadening financial inclusion. Digitisation has been an important avenue for creating market access in Africa and, in particular, has brought financial services within reach. Countries that have embraced digital financial services have seen an improvement in financial inclusion. With the proliferation of mobile devices, consumers around the world are embracing mobile as a vital channel that can be used to deepen financial inclusion, especially in Africa. With technological innovation taking place at an unprecedented speed, digital innovation has the potential to broaden financial inclusion but can also exclude consumer segments with low levels of digital and financial literacy. Countries that are underperforming in financial inclusion need to start providing financial education, which has assumed a new importance in the international development field.

South Africa's world-class and sophisticated financial sector exists within the confines of a developing economy subject to serious socio-economic challenges. The country's significant potential to achieve effective financial inclusion must be considered alongside concerns over whether this will be transformational and inclusive by helping to eradicate poverty and improve people's quality of life. Technology can be transformational if it is inclusive, efficient and innovative, thereby allowing digital technologies to promote development. However, there are limitations, as seen in the South African case study.

The uptake and usage of financial services and products, digital channels and fintech innovations are constrained by a low-income consumer market with many earning an income from the informal (and largely cash) economy. Digital products and services have to be relevant in this largely informal society that is highly dependent on cash. Moreover, notwithstanding the high rate of financial inclusion achieved thus far in South Africa, the bulk of financially included adults are less than adequately served (ie, through the non-productive use of acquired financial services). The uptake of financial products is severely constrained by inadequate knowledge of available financial products and services, and digital channels – or a complete lack thereof.

It is against this backdrop that this paper makes the following policy recommendations:

- Explicit, strong and sustained commitment from both the public and private sector to broaden financial inclusion is crucial if meaningful progress is to be made. As such, the development of a national financial inclusion strategy is an important tool to advance financial inclusion objectives in South Africa. Treasury should engage all relevant stakeholders before releasing the much-anticipated policy document outlining South Africa's approach to achieving financial inclusion with the aim of launching it, jointly with other relevant regulators, as a national financial inclusion strategy. Engaging the industry is useful to encourage the private sector to align initiatives with the policy.

- Treasury should be the 'glue' that brings all the financial inclusion players together and, as such, it bears the responsibility to establish a financial inclusion forum to coordinate and periodically adjust indicators and monitor progress using the South African Financial Inclusion Monitor.
- A comprehensive and nationally coordinated public–private partnership strategy for financial education is needed, instead of the current scattered approach. There are many financial education initiatives that need to be structured properly if both the private and public sectors are going to make a meaningful impact in improving the country's financial literacy score. This could be initiated by the FSCA in conjunction with Treasury.
- The financial inclusion agenda in Africa must focus on financial intermediation such as savings mobilisation, asset transformation and risk mitigation to be relevant to development and to lead financial deepening, hence improving people's quality of life.

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Cover image

A shop owner makes a banking transaction on her mobile phone in Khayelitsha, Cape Town, South Africa (Per-Anders Pettersson/Getty Images)

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