

Fighting Poverty, Profitably: Transforming the economics of payments to build sustainable, inclusive financial systems

Key Findings

1. Digital payment systems, including mobile money and direct electronic account deposits, offer the highest potential for financial inclusion. They are much cheaper and more efficient and can reduce transaction costs by up to 90 percent, and offer greater potential for generating adjacent revenues not tied to user balances.
2. To date, no payment system has reached its full economic performance – all countries have the potential to lower costs and broaden access.
3. There are great opportunities in the developing world to improve the economic performance of their payment systems – from optimizing the location of ATMs to streamlining operational processes.
4. A payment model where fees are based on a customer's activity has the best chance of sustainably reaching poor users.
5. Innovations offer increasing potential for improvements in payments systems as new technology, revenue sources and business models emerge.
6. In most developing countries, improvements to system design and operations – such as eliminating printed statements or increasing process automation – together can help lower costs by as much as 70 percent.
7. Evidence from across the globe suggests that access to cash will remain important even after digital payments take root. For payment platforms to adequately serve the poor, they need both a viable digital payment system, complemented with traditional solutions for both collecting and dispensing cash.
8. Only countries with relatively widespread access to digital transactions (through either a bank or a mobile money provider), achieve high levels of financial inclusion. In countries where more than 70 percent of people can pay digitally, financial inclusion is over 85 percent.

Report Highlights

The Bill & Melinda Gates Foundation commissioned a study with McKinsey & Company, *Fighting Poverty, Profitably: Transforming the economics of payments to build sustainable, inclusive financial systems*, to identify sustainable ways in which payment systems could be extended to serve poor people in developing countries. It presents the most comprehensive picture of the economics of payment systems to date and is the first of its kind to benchmark data from both developed and developing country markets. The study includes data from more than 30 countries with in-depth analysis of payment systems in six countries – China, India, Kenya, Nigeria, the Netherlands and the United States.

The report offers insights that apply across geographies and are relevant to all stakeholders involved in the payments sector, including regulators, policymakers, and the private sector. It emphasizes the need to understand the unique characteristics of each country's payment system to address the root causes of inefficiencies – and to help bring high-quality, affordable financial services to those people for whom they are currently out of reach.

Below are highlights from the report. The full report, annexes and other supporting documents provide an in-depth view of the analysis and can be found at:

<http://gates.ly/1eBbPE6> .

Understanding Payment Systems in a New Way

The report introduces a new framework (ACTA) to analyze the performance of the payment system as a whole, rather than just specific elements, to provide policymakers, regulators, and the private sector with a better understanding of the major payment activities and underlying market dynamics. The ACTA framework provides a foundation for understanding how to transform payment systems so they are sustainable, and inclusive of the poor.

The ACTA framework looks at system-wide revenues and costs to determine what drives profitability by considering activities that fall under the four core elements of all payment systems: **Accounts**, **Cash-in-cash-out**, **Transactions**, and **Adjacencies**.

Accounts

Account activities include opening new accounts and maintaining existing ones. Common examples include current accounts with banks and mobile money accounts with mobile money providers. All accounts need to provide customers with a secure but accessible store of value.

Key Findings

- Countries with lower account fees have higher levels of financial inclusion.
- Digital payments help lower costs overall (beyond just accounts), and increase the possibilities for adjacent revenues (activities that support revenue-earning products) thereby increasing the chances for sustainably reaching the poor.
- In most developing countries, improvements to system design and operations – such as eliminating printed statements or increasing process automation – together can help lower costs by as much as 70 percent.
- Costs for both accounts held by banks and mobile money accounts could be cut to as low as \$5 per year.

Cash-in-cash-out (CICO)

Cash-in-cash-out (CICO) activities support customers' abilities to move cash into or out of their personal accounts. This occurs at access points such as bank branches, ATMs or mobile money agents – and is supported by cash distribution. CICO must be convenient for customers, enabling them to quickly and safely convert cash to digital funds and back to cash.

Key Findings

- Using agents to provide CICO services is universally important to ensuring reach to poor customers at costs that can be as much as 90 percent lower than alternatives such as branches. In all developing markets evaluated, agents play an indispensable role for quickly expanding reach and building scale. It is vital for payment systems to scale up their agent networks by providing them sufficient incentives.
- Improving system design and operations, such as the optimization of CICO distribution outlets and cash centers and better cash forecasting can lower CICO costs in developing countries by as much as 40 to 60 percent.
- Evidence from across the globe suggests that access to cash will remain important even after digital payments take root. For payment platforms to adequately serve the poor, they need both a viable digital payment system, complemented with traditional solutions for both collecting and dispensing cash.

Transactions

Transaction activities support a customer's ability to transfer funds directly between accounts. Debit and credit card transactions, credit transfers, and direct debits, as well as mobile money transfers are all types of transactions. Both the payer and the person being paid need to be able to participate in the transaction, trust that funds will be transferred, and receive some benefit over using cash.

Key Findings

- Lower variance in costs is a major benefit from digital transactions. Therefore, payment providers are much more likely to realize the cost gains they hoped for when transitioning to digital payments. Only countries with relatively widespread access to digital transactions (through either a bank or a mobile money provider), achieve high levels of financial inclusion. In countries where more than 70 percent of people can pay digitally, financial inclusion is over 85 percent.
- However, high digital transaction access does not alone ensure financial access for poor people. Other efforts are needed to reduce costs and prices to levels that allow providers to serve poor consumers sustainably.
- To lower transaction costs in a meaningful way, it is necessary for systems to achieve minimum scale and improve operational efficiency. Together, these steps can lower costs by as much as 85 percent.

Adjacencies

Adjacencies are activities that support revenue-earning products that link to the basic payment system. There are three types of adjacencies. First, some adjacencies tie to direct use of the payment system. For example, banks earn interest on money that users deposit in current accounts. Second, adjacencies stem from use of financial services linked to payments. These can come from additional financial products (e.g., savings, insurance, lending). Third, non-financial adjacencies accrue from services unrelated to payments or financial services (e.g., the sale of transaction data to advertisers or rating agencies).

Key Findings:

- Adjacencies will play an important role in shaping the value chain of services to low income consumers and in attracting new players beyond banks and mobile operators.
- In the case of mobile money, mobile operators may benefit from a reduction in customer churn (i.e., mobile phone customers will forgo a tempting offer to switch providers so they can retain their mobile money account). Safaricom in Kenya, for example, generates an estimated \$3 profit per customer from churn reduction through its ownership of M-PESA.
- For non-financial adjacencies, data from digital footprints can help providers understand customer behavior better and design new products and services with revenues that can be 2 to 5 times larger than financial services revenues.

About Financial Services for the Poor

The Bill & Melinda Gates Foundation's Financial Services for the Poor program believes that effective financial services are key in the fight against poverty. Nonetheless, today about 80 percent of the world's poor adults do not have a bank account or use other formal financial services. Increasing their access to high quality, affordable financial services will accelerate the well-being of households, communities, and economies in the developing world. One of the most promising ways to deliver these financial services to the poor – profitably and at scale – is to connect them to digital payment platforms.

To learn more, visit: <http://www.gatesfoundation.org>.