# Toward the Cashless Economy in Africa

*By Garikai Matambo and Simon Schaefer (November 2013)*

This thought-leadership piece was compiled from content discussed at the recent *Africa Frontiers Forum* hosted by Frontier Advisory. Panel speakers included *Mark Carolus* (Division Lead South Africa, MasterCard South Africa), *Prof. John Board* (Dean, Henley Business School), *Yolande Van Wyk* (CEO: e-Wallet Solutions, First National Bank), *Riaan Eksteen* (Partner: Deloitte Consulting-Strategy and Innovation), *Zanele Mgidi* (Head of Mobile Money, MTN SA). The panel was chaired by *Dr Martyn Davies* (Chief Executive Officer, Frontier Advisory).

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*Financial innovation has gone hand in hand with ICT leapfrogging*

Over the last decade innovation in the financial services sector in Africa has seen the introduction of internet banking, multi-currency cards and mobile money amongst other things. The adoption of technology in financial services is allowing the sector to leapfrog traditional infrastructure. Between 2011 and 2013, Africa recorded a compounded annual growth rate of 36% in mobile subscriptions and a 52% penetration rate in 2012. It is also the fastest growing region in terms of mobile penetration and mobile broadband penetration.In Kenya for instance, 31% of the country's GDP is transferred through phones as MPesa has become the dominant method of sending remittances from workers in the city to relatives in rural areas.

*Nigeria and South Africa are transitioning to 'cash-light' economies*

In light of the evolution in the ICT industry, Africa is on a steady growth path with a more progressive approach in terms of financial services adopting technology. The Nigerian and South African economies are good examples in this regard with the former recorded as being in the inception stage and South Africa in a transition phase towards a "cash-light" society. 90% of retail payments in Africa are in cash with10% conducted through electronic payment systems. In South Africa, however, around 30-35% of retail payments are electronic and 60-65% are cash payments. This transition could be a welcome move given that on average reserve banks estimate the cost to society of using cash to be about 1.5% of GDP. Electronic payments, however have proven to boost economic growth.

*Innovation should address local needs*

Due to varying backgrounds in Africa's different regional economies, innovation and the implementation of such innovation should not be generalised, but rather customised to suit regional and local needs. Growing demand from the populace has driven mobile operators, banks and other players in the finance sector to innovate in line with different needs and requirements of economies. This demand and the subsequent response by financial services providers has resulted in increased levels of financial inclusion.

*Financial inclusion is a key driver of economic growth*

The increase in financial inclusion in Africa provides the "unbanked" with access to the formal financial system and services such as savings, payments, transfers, credit and insurance.Some of the key success factors of financial inclusion include the ability of banks and mobile service providers to innovate and broad-based government commitment to financial inclusion through the backing of central banks and regulators. Building on success and the breakthrough point of financial inclusion is also a key development factor. This has a direct positive impact on individual countries' GDP and the African economy at large.The financial services ecosystem has thus evolved, to not only include traditional players such as banks, but also new competitors outside the traditional sector such as mobile service providers.

*Regulation can be a tool for creating an enabling ecosystem*

The evolution of the financial services ecosystem in Africa should also be accompanied by flexible regulation. Regulation should not be complex, but conducive to the creation of a favourable environment for private investors as innovation stems mainly from the private sector. This does not imply that regulation has to be lax, but for regulators to 'walk' with market evolution agents (banks, mobile service providers) to create a more enabling

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environment in the development of a less cash-dependent economy. In addition, government actions speed up the trajectory for growth in the use of technology in financial services. This is through the implementation of policies that are enabling for the mobile service providers to render financial services as well as for banks to integrate their financial services with technology.

*Collaborative action essential in the evolution to a 'cash-light' economy*

Competition to becoming the leader in innovation and facilitating "cash light" transactions, however, still exists amongst the financial and mobile service providers.A more collaborative approach is required to achieve atipping point in the evolution to a less cash-dependent economy. In light of this, adoption of technology in the financial sector to date has seen some early signs of inter-connectivity amongst innovation players. For instance, the use ofUnstructured Supplementary Service Data (USSD) in transactions in the mobile space hasenabled users to transfer funds across networks and platforms regardless of the device used.In addition, service providers and merchants have developed methods to make withdrawals and deposits more convenient by establishing pay points in various merchant outlets.

*Trust is difficult to gain, but easy to lose*

The value placed on money in its physical form has been indoctrinated in most African societies. For decades, individuals have derived a high utility value from using cash while on the other hand utility in the digital economy is yet to stand the test of time. The introduction of technology in the financial services sector was initially met with suspicion but as the use of virtual money and trading without the exchange of 'money' in its physical form develops, so is its legitimacy as a way of transacting. The big question however is whether the system can be trusted. Trust is built on the efficiency and reliability factor of the technological infrastructure that is used in the system. Technological advancement in the finance sector has to be coupled with system reliability. Basic support infrastructure that is well regulated and well maintained is essential in winning the trust of the masses. A rapid response rate to issues such as online scams and system overloads will boost confidence that is required in building the trust of the end-user. Despite the recent increase in the number of users outside of the banking system, banks still remain the symbol of trust in the financial sector. Part of this is attributed to the test of time and the size banks have grown into.

*Track record guarantees legitimacy and trust*

Most financial institutions such as banks have the economies of scale and a track record that guarantees legitimacy and ultimately being trusted financial services providers. An interesting observation, however, is the presence of MTN in East Africa in providing mobile financial solutions. In Uganda, MTN's mobile banking solution is close to surpassing the total banking industry in the economy. While the company has witnessed a boom in the number of mobile money subscribers in a short space of time, there still is a heavy reliance on the banking system to facilitate deposits. Furthermore, regulation has also slowed down the growth process and the diversification of product range from mobile operators for instance.

*iTunes, Amazon; all could be financial service providers of tomorrow*

Consumer platforms that have easy access to a large subscription base such as Amazon, iTunes and mobile network operators have a comparative advantage in terms of market penetration and great potential in scaling up operations to cater for financial services. One of

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the reasons why companies like MTN for instance have difficulty in winning trust, gaining traction and scaling up their service offering has to do with country specific regulations around rendering financial services and the complexity of changing people's perceptions on using one device or platform for leisure and banking at the same time. Financial literacy or the lack thereof has also been an obstacle in financial institutions and mobile operators in scaling up service offerings.

*Is the pseudo-cashless society the way forward?*

It may be difficult to abandon cash completely in Africa, but the use of cash may be minimised resulting in a less cash-dependent society.Different regions in Africa will require different strategies to facilitate financial inclusion and this will further require collaborative action from traditional financial institutions and technology service providers. In essence what is developing is a convergence of payments which are being initiated by different players in the financial services and the ICT space.

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