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“The authors take full responsibility for the contents of this report. The opinions expressed do not necessarily reflect the view of the European Investment Bank”.

FIR Advisors (FIR)
Mobile financial services in Mediterranean Partner Countries

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Final Report

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EXECUTIVE SUMMARY

1. Analysis of the country context and environment for mobile financial services in Mediterranean Partner Countries (MPCs)

    1.1. Access to Finance and to Telecommunications services in in Mediterranean Partner Countries: Market potential for Mobile Financial Services

In the Mediterranean Partner Countries (MPCs) analyzed only 35.83% of the population older than 15 have an account at a formal financial institution. Excluding Israel, whose access to finance ratio is much higher than the other countries studied (90.47%), the average of the remaining seven MPCs studied is 28.03%, lower than the average for the upper middle income group of countries where (Algeria, Tunisia, Jordan and Lebanon belong) and approximately the same as the average for the low middle income group of countries where Morocco, West Bank/Gaza and Egypt belong. Thus, MPCs studied face an important challenge in terms of access to finance that jeopardizes their economic development and equality.

In macroeconomic terms MPCs have better ratios in terms of deposits as a percentage of GDP than New Member States (NMS), and BRICs (Brazil, Russia, India and China) both in terms of deposits and loans as a percentage of GDP. However, MPCs ratios are much lower than the average for EU 15 countries both in terms of deposits and loans as a percentage of GDP.

Mobile Cellular Penetration Rates in the Mediterranean Partner countries studied are very high, almost 100% or above in some cases. Only in Lebanon, due to the more restrictive definition they use of active lines, mobile cellular penetration is only of 81% of the population. Thus the mobile penetration average rate for the countries studied is 105.63% while access to finance average for the countries studied is only of 35.83%.

Recent research in the region shows how mobile financial services should be offered first to young urban unbanked and then to banked customers less than 35 years old. In the Mediterranean Partner Countries analyzed, the population is very young and most of them live in urban areas. Very high literacy rates and openness to technology are also enabling factors.

The combination of high mobile penetration and low access to financial services means that there is an opportunity for transformational mobile financial services in all the countries of the region analyzed except Israel where there is no problem of access to finance. However, potential customers need to see the value proposition before using a new service. This suggests a need for extensive customer awareness campaigns for the uptake of mobile financial services. Potentially highly demanded “Killer” applications for the uptake of mobile financial services in the region could be:

- International remittances due not only to the importance they have for the economies of the region in terms of GDP, especially for lower income segments of their populations, but also because prices of remittances in the region are still high compared to other regions.
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- Remote and bill payments in the context of policies of most of the central banks of the region analyzed to develop national switches for retail payments.

- Mobile financial services offered by microfinance institutions in the current context of the needed strengthening of the sector’s technical and technological capacities of most MFI’s of the region. Indeed, mobile financial services offered by the microfinance industry could not only become the killer application for the development of mobile financial services but also a critical tool for their sustainability in terms of improved efficiency and lesser delinquency ratios.

1.2. Review of the regulatory framework of Mobile Financial Services in Mediterranean Partner Countries

The regulatory framework in the Mediterranean Partner Countries studied promotes the development of bank led business models. It can be considered enabling in Egypt and Jordan and evolving towards enabling in Morocco; Restrictive in Lebanon and Tunisia; In Israel it is also enabling, although there is no interest in launching transformational business models. In the West Bank/Gaza and Algeria it does not exist.

Regulation is one of the main challenges for the deployment of mobile financial services, in particular e-money and agent regulation. All financial regulators of the region are looking into these issues, in order to better understand how mobile financial services can be used to increase access to financial services while maintaining the stability of the financial system.

Definitions of electronic money vary by jurisdiction, but a common definition is — monetary value stored on an electronic device which is issued on receipt of funds and accepted as a means of payment by parties other than the issuer. Most banks store money in this way (on their computers) and they are regulated in every country simply as bank institutions. A key question is whether non-bank organizations are permitted to issue e-money as well, and if so, under what conditions and subject to what prudential and non-prudential regulation.

The use of retail agents introduces new or enhanced risks policy makers and regulators should consider seriously. For example, agents present a variety of operational risks to the provider (particularly reputational risk, given that the agent is the public face of the provider) and to the consumer (particularly in terms of agent liability). Moreover, the use of agents adds a special dimension to the challenge of satisfying AML/CFT norms and to consumer protection — two other topics critical to mobile financial services.

2. Review of providers of low cost financial products: prepaid electronic methods of payments in Mediterranean Partner Countries

Retail payments infrastructure is not yet widely developed throughout Mediterranean Partner Countries. Only Morocco, Algeria, Tunisia and Israel have fully operational retail payments and card switches. Egypt’s retail payments and card switch is not fully operational yet for all payment services. Lebanon is currently implementing its retail payments switch, through which card systems will be interconnected. Jordan and...
the West Bank/Gaza are also willing to implement retail payment switches after successfully implementing RTGS systems. The Postal Service through its financial services unit is a major provider of retail payments in all the countries studied.

The card switches and processors of Tunisia (SMT), Morocco (CMI) and Egypt (EBC) are willing to lead the development of mobile financial services. Postal Systems throughout the MPCs studied are also able and willing to launch mobile financial services. Besides, payments service providers are also developing a mobile financial service offering in partnership with financial institutions and mobile operators.

3. Review of low cost financial intermediation networks in Mediterranean Partner Countries

Physical access to financial services in the Mediterranean Partner Countries (MPCs) analyzed, measured as the number of bank branches per 100,000 adults (15 or older) was in 2011 of 16,08. This ratio for OECD countries was in 2009 of 33,4 branches, while some individual countries with high ratios of physical access to finance like Spain had 38,3 branches in 2009 and the USA 35,74 in 2010.

Although Israel is the only MPC analyzed that has no access to finance problem, the ratio of bank branches per 100,000 adults does not change dramatically without taking it into account. Without Israel the ratio of bank branches per 100,000 adults in the remaining seven MPCs studied is of 15 bank branches per 100,000 adults, while with Israel it is 16,08. Both ratios are higher than the one for the MENA region as a whole (14,3), almost equal to the ratio for Latin America and the Caribbean (15,8) and slightly lower than the high income countries non OCDE ratio (19,8) in 2009.

A very distinctive characteristic of the majority of MPCs studied is that the Postal service has a dominant position in the distribution of retail financial services and payments. As a result, if we include the network of postal branches in order to obtain the ratio of branches per 100,000 adults including Banks and Postal Services, the result is 23,56 for all MPCs analyzed (22 without Israel). Money Exchanges, Payment Service Providers and Microfinance Institutions have also important networks in MPCs. However, the density of Mobile Network Operator networks franchises is by far the highest in the region, although the potential of these networks for cash in/cash out purposes remains to be exploited in the region.
4. **Review of providers of alternative risk analysis methodologies in Mediterranean Partner Countries**

4.1. **Review of the microfinance industry**

Although Microfinance in most Mediterranean Partner Countries is young compared to other areas of the world such as Asia or Latin America, it has developed extensively over the past years in some countries like Morocco, Egypt or Jordan. As a result the government institutions of Morocco, Tunisia, Egypt, West Bank and Gaza and Jordan are leading the development of new regulatory frameworks for microfinance that they expect to have ready by the end of 2012 or early 2013.

Most institutions interviewed consider that new technologies and capabilities such as mobile financial services could greatly favor the development of the microfinance sector. Also, in the future context of transformation of Microfinance Institutions (MFIs) in the region their performance and profitability ratios are likely to worsen due to the required operational investments and additional equity. As a result, the use of mobile financial services by MFIs can not only be useful in order to keep delinquency ratios at bay by improving microcredit payments mechanisms, but also by improving the efficiency of their operations and as a result their profitability and sustainability.

However, serving the microfinance industry will be successful when MFIs are allowed to offer not only microcredit payments through the electronic wallet but also the disbursement of the microcredit. Similar experiences in other countries probe that the receiver will keep approximately 15 to 20% of the microcredit balance in the e-wallet if they are offered useful payment services and trust in the system. The most important obstacle to widespread adoption of mobile financial services for microfinance is however MFIs’ lack of understanding of mobile payments. As a result, assistance in training MFIs on how to use and offer mobile financial services to their customers is needed.

4.2. **Credit information infrastructure in Mediterranean Partner Countries**

In the Mediterranean Partner Countries studied, while the quality of credit reporting has improved in recent years especially in Morocco, Egypt and the West Bank and Gaza due largely to the introduction of new credit bureaus, much remains to be done, both in terms of design and coverage. Six of the countries studied have Public Credit Registries (PCR) while only three have Private Credit Bureaus (PCB).

PCRs are administered by central banks or bank supervisors and basically collect information from supervised institutions. PCBs constantly seek to expand the scope of their information and thus develop a more complete picture of a borrower’s financial dealings. Because participation in PCRs is mandatory, they can build a picture of the regulated financial system relatively quickly, and support the oversight functions of the regulators. As a result, if PCR’s coverage was large enough, they could help nonbank mobile financial services operators enter the mobile financial services market.

5. **Review of providers of remittances**
International remittances could be one of the mobile financial services more demanded in Mediterranean Partner Countries due not only to the importance they have for the economies of the region in terms of GDP, especially for the lower income segments of the populations of MPCs, but also because prices of remittances in the region are still high compared to other regions. The uptake of mobile financial services in countries like the Philippines or Kenya is mostly explained by the success of operators such as M–Pesa, G-Cash, or Smart in providing remittances services, whether international (the Philippines) or domestic (Kenya).

In the Mediterranean Partner Countries studied, remittances inflows are important in terms of GDP in Morocco (7.04%), in Tunisia (4.45%), in Egypt (3.53%), in the West Bank and Gaza (15.39%), in Jordan (13.78%) and in Lebanon (19.38%). In Algeria and Israel remittances inflows are not relevant. In terms of prices, sending remittances to MPCs cost approximately the same as sending remittances to the other corridors followed by the World Bank’s remittances database. The average cost of sending 500 USD to MPCs was in the first quarter of 2012 of 5.56%, while the worldwide average for all corridors was 5.57%. As a result there is room for incoming players such as in the case of the Philippines, using mobile financial services to offer international remittances at a lower price.

6. Existing or potential mobile financial services operators (institutional, financial, or mobile phone players) that could fit into follow-up projects in Mediterranean Partner Countries

The involvement of banks and telecom operators in the delivery of financial services by mobile phones creates four different mobile financial services ecosystems, where we can identify four critical roles played in each scenario by the bank or the telecom operator. The first role to consider is who is legally responsible for the deposits; the second role, is who bears the reputational risk which implies whose brand is more exposed to the public; third, whether deposits can be accessed through agents or only trough bank branches or ATM’s; and the fourth and final role considered is who carries the payment instruction.

In the Mediterranean Partner Countries analyzed most of the existing mobile financial services regulatory frameworks encourage the development of bank-centric models. Collaborative business models, where the mobile operator is the dominant brand, and where can cash be accessed in networks other than the bank’s network are also emerging. Independent service providers such as cards associations are also launching mobile financial services in many MPCs studied.

Finally, we have only found one MPC, Jordan, where mobile operators have been able to launch operator centric models, although many others in the region are willing but unable due to the existing or lack of regulatory framework. Indeed, although the regulation is currently being amended, as of now the mobile operator holds the accounts/deposits (the bank only provides the settlement account but does not have individual information of the customers). Besides, the business model of Orange and Zain also meet the other three conditions defined previously for being considered an operator centric model such as: the dominant brand, where can cash be accessed and who carries the payment instruction.

7. EIB suggested support for follow-up projects
The lack of an adapted regulatory framework has been mentioned by all the players during the field visit as one of the main problems for launching mobile financial services initiatives. However, we have also been able to identify other obstacles for the uptake of financial services in MPCs such as the lack of understanding of mobile financial business models by most of the stakeholders at large. As a result, many institutions including all Central Banks/Financial Supervisors have asked about potential EIB funded Technical Assistance for training and workshops dedicated to mobile financial services, and focused in particular on prepaid platforms and agent networks. The Central Bank of Tunisia and the Palestinian Monetary Authority emphasized their interest in receiving such support.

This training program could be followed by assisting one institution/partnership per country, identified in this project as developing or willing and able to implement a pilot of mobile financial services. Although the services to be offered at the initial stage would be limited, the experience will allow the financial and telecom regulator to understand better the benefits and risks of a mobile financial solution. Finally, once the results were properly analyzed and the potential risks and benefits understood, both the financial and telecom regulator would be better equipped to adapt the regulatory framework as required.

The pilots suggested per country are:

1. Morocco: Al Barid Bank/ M2M
2. Algeria: Algérie Poste
3. Tunisia: Mdinar-Via Mobile/ ENDA/ BIAT- Expression of interest letter attached in the country report
4. Egypt: EBC/NBE/Mastercard/Fawry
5. West Bank and Gaza: Jawal
6. Jordan: Orange Money
7. Lebanon: Pinpay/Al Majmoua/Bank Audi. Expression of interest letter of Al Majmoua attached in the country report
8. Israel: The country does not have an access to finance problem although the Postal Bank aims at launching an initiative for the underbanked/unbanked.