Financial Access: Opportunities for Africa

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Abstract

This paper will focus on the financial access amongst the general public in various African countries *(Kenya, Uganda, Tanzania, Ghana and Zambia)*. Financial access categories covered in the paper include transaction banking, savings, credit and insurance. The paper will be based on a number of national surveys conducted in these markets and highlight the opportunities and gaps for current and potential investors in the financial services sector. The opportunities to be highlighted include product innovation attributes and delivery mechanisms.

Opportunities in Sub-Saharan Africa (SSA)

Leke et al. (2010) notes that Africa's economic pulse has quickened, infusing the continent with a new commercial vibrancy: real GDP rose by 4.9 percent a year from 2000 through 2008, more than twice its pace in the 1980s and '90s. It would be clearer to examine Africa's potential from the trends that have taken place in the last 10 years to possibly get an idea of the factors that contributed to this growth and project the financial opportunities available in Africa. Various things could have contributed to this growth and various scholars have claimed a stake at particular attributes. For instance, Dr. Ndii of Foresight Economics (2011) posits that this growth could be attributed to governance dividend, economic reform, demographic dividend and technology. In terms of governance dividend, he notes that there was a reduction in the number of leaders who left power through coups/violent overthrows while in the same period of time, there was a reduction in the prevalence of Anti-growth syndromes. McKinsey Global Institute (2010) on their part hold similar views that Africa's growth acceleration resulted from more than a resource boom but more importantly were government actions to end political conflict, improvement in the macroeconomic conditions and the creation of better business climates. The same is confirmed by Leke et al. (2010) who note that several African countries halted their deadly hostilities, creating the political stability necessary to restart economic growth. Various economic sectors were seen to grow as highlighted in this paper:

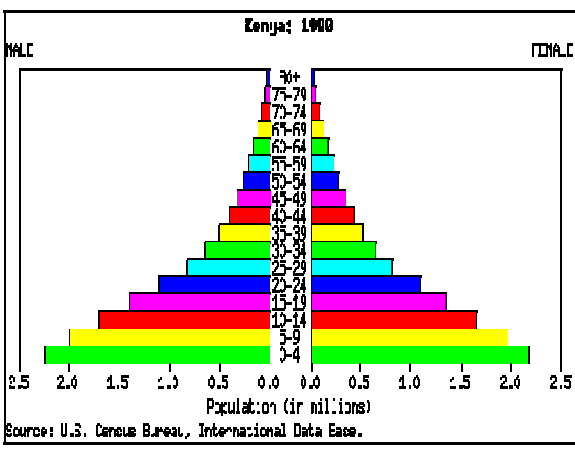
a. Market Liberalisation - there were increased trade activities in the region both from within and from other continents. Markets have become liberalised which in turn has increased competition at the benefit of the market. There are now players who have a wider geographical spread beyond the political boundaries. These include, Ecobank, Equity, United Bank of Africa, Bank of Africa, Guaranty Trust Bank, Zenith, KCB, among others.

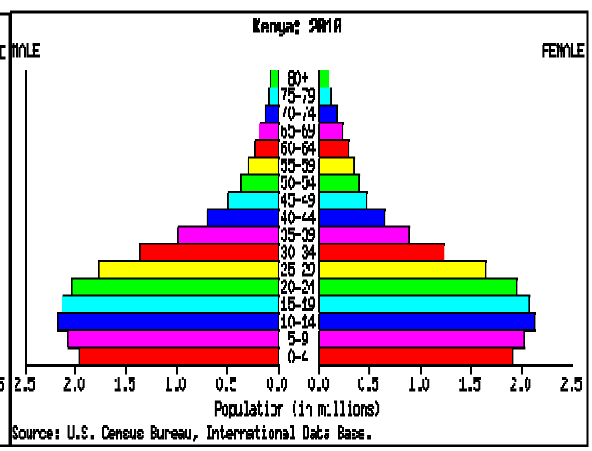
b. Expansion in the aviation industry - The aviation industry noted various foreign players enlist more African destinations. For example, Kenya Airways in its annual report in 2006 noted that all African regions experienced increased passenger growth; West & Central Africa 26%, Southern Africa 22%, North Africa 21% and East Africa 5%. The report adds that the Kenyan domestic network experienced 22% increased frequencies in response to increased passenger demand and realised a traffic growth of 25%. In addition to that, other African players such as Ethiopian Airlines and South African Airways expanded their market reach. International players were also witnessed in the market in the same period. Virgin Atlantic, Emirates, Turkish Airlines and Delta Airlines for instance started or expanded their operations in Africa within the same period. It can therefore be deduced that for such profit making entities to have entered the African market, potential was envisioned which can be related to growth in the industry.

c. **The tourism industry** - The tourism industry in Africa continues to enjoy growth both from domestic and foreign tourism and the increased domestic flights within countries and between countries in Africa confirm this.

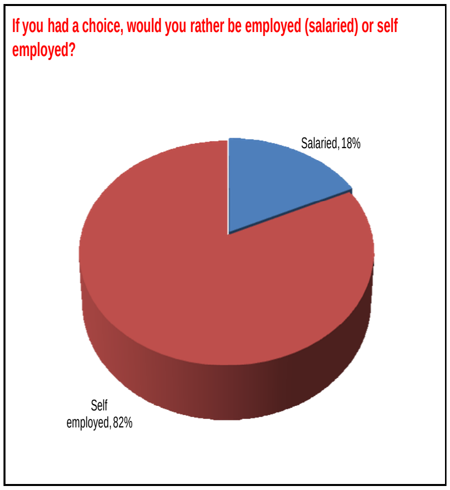
d. **Improved literacy levels** – The enrolment rates in schools in most countries has gone up in the recent past. There also positive development on access to tertiary education in Africa with the number of universities and colleges expanding year on year. Financial access studies in Africa show lower proportion of financially excluded among those with tertiary education. In Kenya for example, Finaccess (2009) show 70% and 20% of those with tertiary education are formally banked or informally banked respectively.

e. **More economically active than dependant populations** - Other changes in the market noted included an increased number of people within the economically active age category. Dr Ndii (2011) adds that in terms of the population distribution as drawn from Kenyan example below, there has been an increase in the number of persons within the economically active categories which is a departure from the situation in the '90s.





f. **Shift from formal employment to self employment/entrepreneurship** - However, a significant departure from the past was witnessed in various African countries where there was a shift from formal employment to self employment and entrepreneurship. For instance, as per an opinion poll released to the media in January 2011 by Synovate Pan Africa indicated, 82% of Kenyans interviewed preferred to be self employed than employed as shown below.



This finding is similar to the expert opinion of Dr Ndii (2011) of Foresight Economics, who notes that there was a shift from a formal economy to an informal economy in Africa during the last ten years. For policy makers and economists who have been warning that the large numbers of the unemployed- especially the youth were a political risk, this change in perception is welcome. The Managing Director of Synovate Pan Africa stated that he believed that this trend was a result of significant barriers to self-employment that were coming down in addition to more Kenyans having access to funds from initiatives like the Youth and Women Fund. This was part of the Kenyan government effort to target these two groups that have traditionally found it difficult to access funds from commercial banks. The latter have also become more aggressive as competition has increased and in the last few years have targeted small and medium enterprises (SMEs) that were the preserve of micro finance institutions for decades.

g. **Reduction of communication costs** – with the entry of various mobile services providers, there has been increased competition that has in turn caused a reduction of communication costs both within a country and between countries and in addition to that, this has significantly reduced the cost of doing business. The presence of various multi-country players such as MTN, Vodafone, Orange France and Airtel which have created competition as the scramble for the customer base and as a result have reduced call rates to achieve a competitive edge.

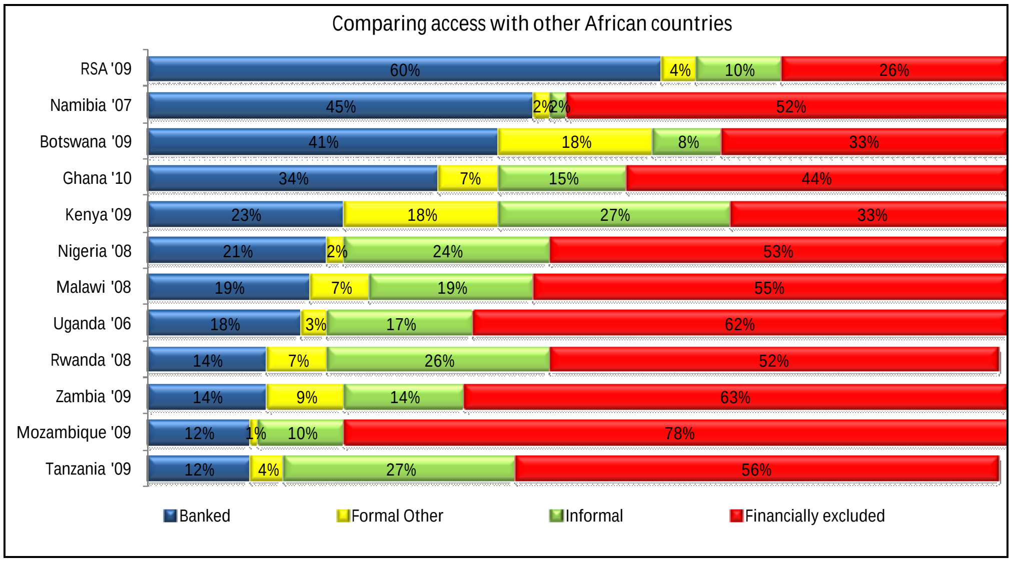
h. **Increased adoption of technology** - Dr. Ndii (2011) notes that there has been an increased adoption of technology: mobile and internet subscriptions have increased. For example, technological innovations have transformed the Kenyan financial sector landscape in the years since 2002, by helping to extend financial services to millions of poor people at relatively low cost (FSD Kenya, 2010). Automated teller machines (ATMs) have become common even in rural centres in Africa while mobile subscription has remarkably increased.

While Africa still faces some serious challenges, it has made remarkable strides in the last few years. Less is known of its potential as well as its staying power, but more importantly, as the World Bank puts it, an economy's financial markets are critical to its overall development. The financial markets in Pan Africa are thus the focus of this study and as Ajakaiye (2005) notes, as economic agents, (household, businesses and government) carry on their consumption and production activities, they need the facilities of credit (short and long-term credit) and equity (financial services) provided by the financial sector.

Financial Access in Africa

The primary role of the financial sector, especially in a developing, is that of mobilising financial resources from the savers and directing these resources into channels of desired development activities (Ajakaiye, 2005). Countries with better developed financial systems, i.e. financial markets and institutions that more effectively channel society's savings to its most productive use, experience faster economic growth (Beck et al (cited in World Bank, 2007). They continue that financial sector development helps economic growth through more efficient resource allocation and productivity growth rather than through the scale of investment or saving mobilization. However, while remarkable growth has taken place in the continent, Prof. Ndungu (2010) of the Central Bank of Kenya in a speech delivered at the Mobile Policy Forum in Africa noted that more than 80 percent of households in Africa do not have access to financial services. He added that expanding basic financial services has the potential to lift the majority of the population out of poverty and build better lives. As Landau (2009) notes: "The lack of accessible and effective banking and identity infrastructure coupled with predominantly cash based societies in much of the developing world has hampered the individual's ability to proactively and safely chart a path out of poverty into economic self-determination."

Access to finance refers to the availability of financial services – in the form of deposits, credit, payments, or insurance – to individuals or enterprises. The availability of such services can be constrained for instance by physical access, affordability or eligibility. According to the Finscope Ghana Report (2010), a significant majority of the population is unbanked: with a large proportion of the population being financially excluded.



Source: Finscope Ghana 2010 Report

Even where such services are available, low-income individuals and small and medium businesses may have difficulty in meeting eligibility criteria such as strict documentation requirements or the ability to provide collateral. Those able to meet such demands may find they are still excluded from formal financial services by cost barriers, in the form of high transaction fees or substantial minimum requirements for savings balances or loan amounts.

Lowering these barriers to access and offering suitable financial products can allow households and small businesses to maximize the leverage of their savings or earnings for increased productivity, contributing to higher incomes, job-creation and, ultimately, growth. Using these categories of the banked, formal other, informal providers and money transfer services, we will explore the financial trends that have taken place in Africa.

a. **The formal financial sector –** The formal financial sector is dominated by banks. The banking industry in Sub Saharan Africa (SSA) has both local and international players; however, very few formal banks have shown the willingness to provide financial services to the small-scale entrepreneur and the rural operators. Poor road, power and landline telephone infrastructure in Africa has in the past been a great challenge to retail financial services. The PwC Pan African Banking Survey (2007) confirms this situation and notes that in all markets there was concern about how best to service the unbanked market. For example in Tanzania, Uganda, Zambia, Nigeria and Kenya, banking penetration is extremely low and the banks are chronically under-represented outside the major urban centres. However, various banks have an inter-country presence and notable of these are multi-country banks such as United Bank of Africa, Fidelity Bank, Standard Chartered Bank, Barclays Bank, Ecobank, Equity Bank and KCB. Both local and international banks have been engaged in branch expansion network strategies in addition to having customer service agreements. Owing to low income levels, the costs charged for transaction and also access to services has kept many out of the system. In addition, the time and cost related to travel are barriers to financial inclusion as noted by about a quarter of the unbanked (Nigeria financial access survey, 2008). However, recently, interest rates have significantly reduced and so have the formalities in lending been simplified. There has also been a drive by banks to minimise the paper work when transacting. Some banks have equipped themselves with digital cameras and photocopies to ease the barriers of the paper requirement when customers are opening accounts.

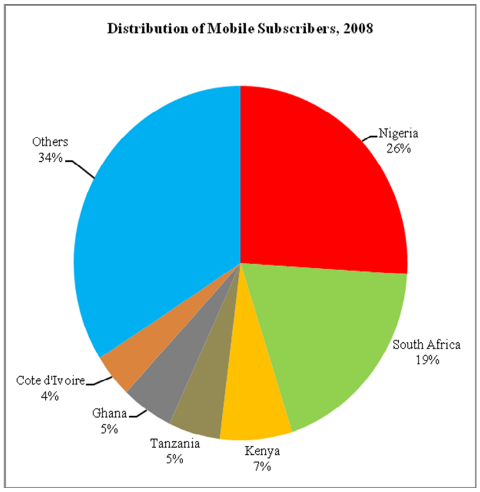
b. **The formal other financial industry** – this consists of MFIs and SACCOs and these could be said to be serving the rural and agricultural dependent populations, various changes have been taking place in the formal other financial industry. In some markets MFIs and SACCOs have transitioned to deposit taking institutions. For instance in Kenya, Muramati Sacco served farmers around the Central Province and farmers use the institution to sell farm produce. At the end of the month, farmers would initially queue at their SACCO branches to get paid but with the changes in law, such institutions have transitioned to deposit taking organisations that provide banks like services to its customers. It can now provide loan facilities and has put up automated teller machines to serve its customers. Legislation and regulations governing rural and micro finance institutions (RMFIs) in Ghana have evolved with the market, both opening up possibilities for new types of institutions and tightening up to restrain excessive entry and weak performance in the face of inadequate supervision capacity. As a result, there are about 135 rural and community banks in Ghana which as Steel and Andah (2003) put it, have partnered with various NGOs to increase the reach in rural financial service provision.

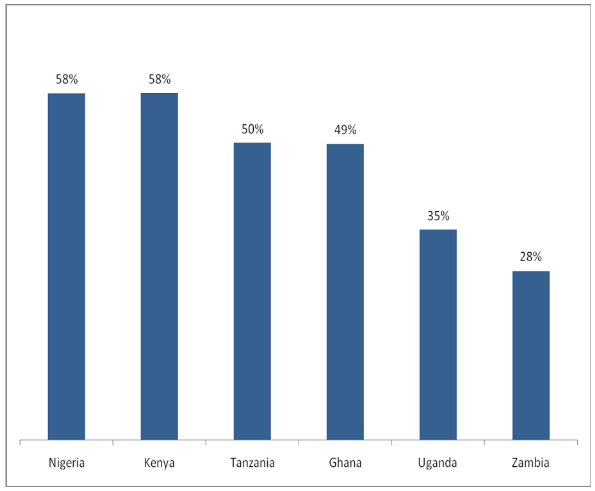
c. **The Informal Financial Industry -** By the mid-1960s, money lending had become more of a part-time activity by traders and others with liquid funds than a full-time profession (Offei, cited in Steel & Andah, 2003). Loans from money lenders have short repayment periods ranging from a day up to any agreed period but rarely above six months. They require security and sometimes, offer high interest rates than other financial services. Due to their accessibility and reduced formality requirements, they are the most preferred in a emergency when there is no other means available. Unlike commercial banks, moneylenders incur little transaction costs in enforcing pledges of such collateral made before family members or traditional authorities, as the moneylender can simply make use of the property until the debt is repaid. Verbal guarantees from family heads, friends and relatives have been reported as acceptable security (Steel & Andah, 2003). Many people have been reported by the media as having lost their goods/securities and regulation of this sector is not stringent in SSA.

The ROSCAs & ASCAs are common across various countries in SSA and are known by various names such as merry-go-rounds, *chamas* in Kenya,,*osusu* in Nigeria, *susu* in Ghana; but in essence operate in a similar manner. They are common in rural areas and their names (ROSCAs and ASCAs) are used interchangeably. In Ghana, the *susus* are somewhat sophisticated and have linkages to *susu* co-operative societies where they receive other financial services. Kenya has an almost similar manner of operation where banks and MFIs give savings and credit services to the *chamas*. Some lend to within the group to other members, while some are flexible enough to lend to non members while others are able to borrow on behalf of their members from banks. In such a borrowing arrangement, the loan amount is shared within the group, spreading the risk of non payment and increasing the level of monitoring.

d. **Money Transfer Services -** Money transfer services in the '90s were characterised by either slow affordable but unreliable postal service provision or the significantly expensive but fast services. As such, those within the lower income ranges were left with no alternative but to use the postal services or bus courier services. The formalised money transfer services generally excluded populations residing in rural areas.

However, recent development in Information Communication Technology (ICT) is gradually transforming the African market place. Africa's ICT has had a strong and sustained growth in the past decade with impressive rise in mobile telephony subscription. Mobile subscription in Africa has continued to grow at a higher rate than the global and other developing countries. In 2000, South Africa had three quarters of Africa mobile phone users. In the past ten years, the growth in subscription in Nigeria, Kenya, Tanzania, Ghana, and Cote d'Ivoire has however significantly changed the distribution in the region. According to the regulators data in respective countries the penetration in Kenya and Nigeria is estimated at 58%.





Sources: ITU World Telecommunication/ICT Indicators database-2008. ITU and various Telecommunication Regulators (-2010)

e. Mobile Money and E-commerce the African way - As Prof. Ndung'u (2011) notes, mobile phone technology has in a few years of its existence demonstrated how financial inclusion can be leapfrogged on a major scale and in a short time span using appropriate technological platforms. The mobile money service in Kenya was first piloted through mobile airtime vendors serving as points of repayment of loans owed to microfinance institutions. The service was later launched in March 2007. The increased usage of mobile phone banking services has increased the access of financial services even to the very remote areas. Prof. Ndung'u notes that in only four years of the existence of mobile phone money transfer services; four mobile phone operators have launched the services and have enrolled over 15.4 million customers and recruited over 39,449 agents. Total transactions have now reached Ksh.2.45 billion a day and Ksh.76 billion a month. This reflects the fact that when cost of transactions decline, transactions increase in volume.

On the foundation created by the growth in mobile phone and the mobile money services in Kenya, Nigeria, Ghana, Uganda, Tanzania and Zambia access to financial services has been greatly enhanced.

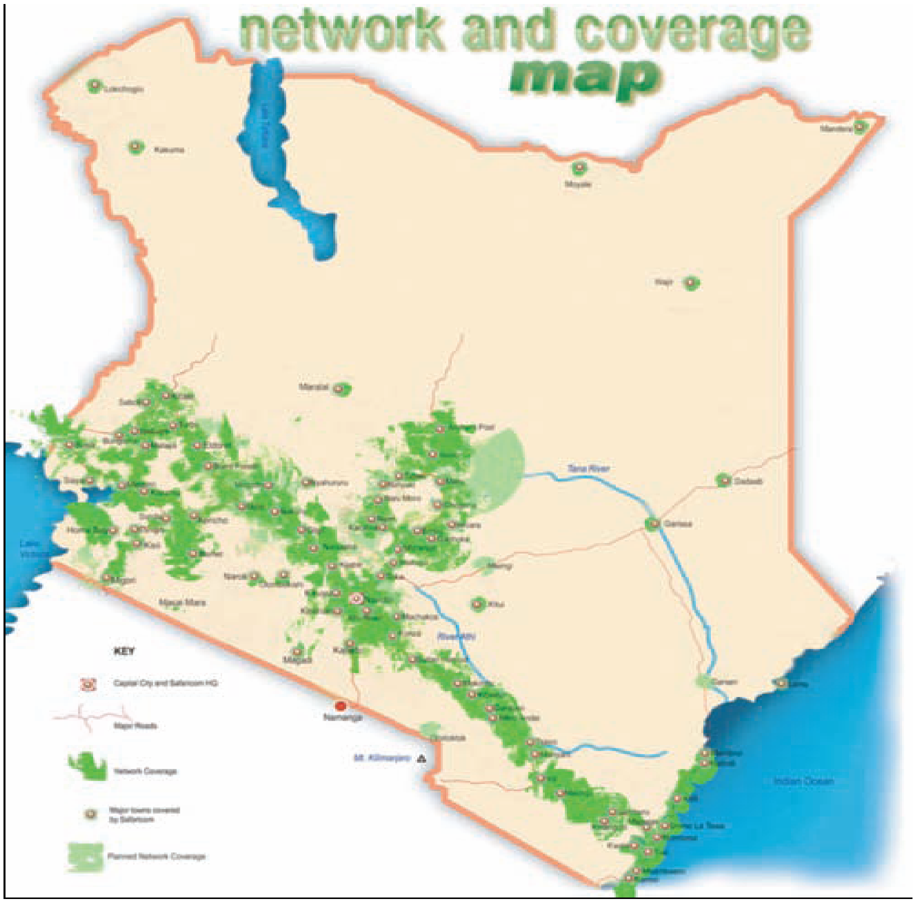
In the more developed markets, plastic money is a good alternative to cash. Big brands in the developed economies like Visa, Mastercard, American Express among others have proved good alternatives to cash transactions. These payment systems have low penetration in the market and are only used by a minority of the banked populations in Africa. In Kenya for instance, usage of ATM was at 13.4% according to the Finaccess Survey (2009) despite the technology being more than 20 years in the market. Other payment modes like Travellers cheques have never really picked in Africa. It therefore demonstrates that with the right technology and support Africa can support e-commerce.

In the past the African landscape has had low access to plastic money and even for those who had access utilisation was generally curtailed by   knowledge and limited card merchandising outlets. Mobile money is rapidly transforming this and creating alternatives to cash economy where there were none. The mobile money service has created opportunities for e-commerce in markets with minimum utilisation of cash alternatives. Currently mobile money transfer is being used shopping, utility bills payment (water, electricity, mobile phone airtime purchase), insurance premium remittance, over and above the being a means of saving.

The barrier of accessing money from banks located distances away from home is being overcome through this service. The user can now load money onto their mobile money account from their bank account. The mobile money dealer network in these markets has been built on a network of mobile phone handset and airtime outlets- access to depositing or withdrawing points is widely spread than formal or informal channels of finance. The cost barriers of starting such outlets are significantly lower when compared to alternative channels to cash access.

In markets where mobile money has taken off, the mobile money dealership network is wider than all main banks ATM and branch network combined. These dealerships have created job opportunities for the African youth therefore getting a significant number in the population into formal employment. All Financial Access studies in the six countries have identified a low rate of saving and access to credit from formal sources. The mobile money service has started attracting attention among players interested in creating a culture of saving in Africa. This innovation initially creates platform of mobile money account to access micro-credit. Some players have a design that links credit and saving.

In addition to being all that it is, mobile money is slowly evolving as a channel of rolling out insurance among the rural communities. The service has also linked people to formal source of information about finance. Mobile money users are using their mobile phone to improve their financial literacy.



M-Pesa Network in Kenya: Source FSD Kenya

f. The Stock Market - By the end of 1996, there were only 11 operating stock markets in sub-Saharan Africa, excluding South Africa. Today, Africa has about 20 active stock exchanges, including one of the only regional stock exchanges in the world, linking eight French-speaking countries in West Africa. This only shows the potential in the region and cross border policy establishment is needed to expand the stock market both across borders and even outside the capital cities.

Conclusion: Is Africa the last/next frontier? What do we need to take it there?

Sub-Sahara Africa is the next frontier and the headlines will soon read, “From hunger, war, disease to opportunity.” However, for Africa to realise efficiencies of services there are certain things that need to be done. Cross border trade barriers need to be lifted at a policy platform to enable financial service providers to enjoy the economies of scale. For instance, the mobile money transfer services could connect a farmer in rural Tanzania with another farmer in rural Senegal. Cross border policies will be needed to enable cross border transactions to enable Africa to operate under once economic block. As far as we know, various economic blocks such as EAC, ECOWAS, SADAC and COMESA have made great leaps in negotiating for an even operating ground but more needs to be done. In addition to that, countries in SSA need to invest in innovations and technology to enable wider and efficient distribution networks for financial services.

There is also need to increase volumes rather than margins when it comes to selling technology within SSA. For instance, Kenya’s Central Bank Governor Njuguna Ndung’u urged the country’s mobile money transfer (MMT) operators to reduce their transaction fees. According to the Governor, “There is no way one can send 50 Shilling at 35 Shillings”. This translates into a seemingly exorbitant 70 percent fee for a small transaction equivalent to less than $1. As Mohapatra (2011) notes, whether mobile money transfer costs are reasonable, transparent and affordable is important in the quest for increasing financial inclusion of the poor. He adds that increased competition and technological advancements will no doubt put downward pressure on mobile money transfer costs in a dynamic industry.

Regulatory reforms are also needed in order to harness the potential of SSA countries. In recent years, the legal and regulatory environment of several African countries has been undergoing a necessary process of modernisation and establishment of more effective enforcement mechanisms. Several countries are currently in the process of undertaking legal reforms, and efforts are underway in several regional organizations to harmonize legal and regulatory frameworks across member states. These reforms are among other things beneficial for the market in the following ways. Restructuring the banking sector to make banks viable and efficient; Nigeria reformed most of the banks that had low capital base and risked insolvency. Strengthening the regulatory environment; minimises possible risks the customers are likely to be exposed to and increasing trust among the unbanked. In addition to that, revitalizing the financial sector by creating new financial institutions as has happened in Kenya by the growth of SACCOs and agency banking would lead to increased penetration.

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