

# The Goldfinch Report

## Payments for the Banked

Published by *Paycre8*, March 2009

Written By Peter Goldfinch

### About the Author:



Peter is one of the founders of Paycre8 and has been writing the Goldfinch Report for approximately 3 years.

He has been working in the payments industry for over 20 years and as a consultant completed assignments for clients in 20 or more developed and emerging markets.

Many would consider Peter to be a technology oriented professional but he also has a strong business background.

There is this focus on banking the unbanked in the emerging markets using mobile as the delivery channel to reach out to those ignored by the existing payment channels. The intentions are well meaning but will we see true success? New technology driven payment services in developed markets often experience rapid take up by the early adopters followed by a drawn out death. Early symptoms of success do not guarantee long-term sustainability. Will this same experience be seen in the emerging markets?

The questions being posed are:

- Should the effort not be directed towards building out the banking infrastructure for those that are considered banked and then supporting organic market development from a sound base?
- Should payment systems developed over three or more decades for and by completely different markets be imposed on emerging economies as an instant fix solution?

A survey<sup>i</sup> completed on the banking habits of Bangladesh mobile subscribers early in 2008 showed of the 28 million subscribers, (after adjustment for those subscribers who have two phones), there was 11.2 million (40%) with bank accounts.

The results of the survey clearly indicated that although 11.2 million have bank accounts they are unable to be considered truly active payment system users because the payments infrastructure is underdeveloped.

A summary of the results:

- 80% deposited funds monthly and a little more than 50% withdraw monthly.
- Less than 4% used bill payment services.
- More than 60% of domestic remittances were sent by hand

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This report is an opinion piece and is not intended to do more than reflect Peter's views at the time of writing. The subject matter often relates to current experiences resulting from his consulting experience.

The purpose is to generate debate through examination of current industry developments and directions. The author hopes you enjoy reading these reports.

- Little more than 5% have ATM cards but more than 25% of these are inactive. The inactive cardholders are dominated by the higher social economic categories of subscribers.

What does this really tell us? There are possibly two reasons for a bank account.

- A small sector of the population is depositing savings into accounts, indicated by the fact there are more individuals depositing than withdrawing.
- Funds are transferred or deposited into bank accounts and then either totally or partially withdrawn to enable payments to be made in cash.

The banking system in this emerging market and probably many others is not providing payment services. Consumer based banking services are providing a savings facility and a depository for receiving funds from overseas or for salary payments. But for consumers to access their funds for payments they must first withdraw cash. There is no viable alternative domestic payment system other than cash. Bangladesh has 10,600 points of acceptance for cards at the point of sale, (probably to support foreign cardholders). Considering the size of the population this number is insignificant. As an example Singapore has one POS device for every 64 residence.

How can this be addressed?

Payment systems advisors and architects generally come from the developed world. Their experience is based on the successes and failures of their own countries. The solutions they promote are developed country solutions that have evolved over the last 30 years or more. There are significant differences even between these developed countries. A simple comparison between the UK, Australia, Canada and the USA will clearly demonstrate this fact. So can you take a developed market payment solution and drop it into an emerging market such as Bangladesh? I suspect not.

# The Goldfinch Report - *Payments for the Banked*

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## About *Paycre8*:

The three founders of Paycre8 have been working in the payments industry for collectively over four decades. Most of this time they have worked as consultants, designers, integrators, developers and project managers on various projects internationally. They have experience in a wide range of payment channels, instruments and networks, normally working at the leading edge. The demand and referrals from old clients plus a passion for the creative aspects of the industry motivated the three founders to build what they believe is a unique and niche consultancy practice.

The simple and possibly best solution is to let these countries develop their own payment systems in pace with the development of their economies and in line with the social revolution that will accompany that development. To allow the payment system to become a product of economic success and not a cause. However well meaning donor organizations and economic development funds see that a developed payment system is the prerequisite to economic and social development. You must have a payment system like ours to have a society like ours.

The buying behavior of the middle classes in an emerging market is different to those of a developed market simply because the cost of labor is cheap and time is not a scarce resource. Middle class families in emerging markets have domestic staff. Partially driven by need but also there is a social responsibility to provide employment to the less fortunate. Goods are often purchased daily and this is a function performed by the domestic staff. So is queuing up to pay utility and other bills. In simple terms the family income earner(s) are not purchasing or making everyday payments. This is delegated to the staff and the simplest way for them to do this is by providing cash on an as need basis.

Compare this to a developed country where the labour pool is not sufficient plus the labour laws and minimum wage requirements, makes it impractical for the middle classes to employ domestic staff. The payment services have developed around the needs of time pressured individuals and families who must do their own shopping and pay their own bills directly. Supported by retailers, service providers and financial institutions who are all trying to manage the cost of doing business. Often through minimizing staff employed and encouraging customers to do more for themselves.

For a country such as Bangladesh the development of the payment system should not be concentrated on the development of the point of sale end of the payment chain. It should perhaps concentrate on the distribution of funds, the domestic remittances supported by an extended network of ATM and encashment agents.

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## *Paycre8*

### **Creators of Payment Solutions**

*Purpose* – to provide payment system advisory services to an international client base. Clients who currently operate payment systems or who are investigating starting up electronic payment services.

*Vision* - By providing fast responsive, informed expertise, and consistently high quality service. *Paycre8* aims to build an international reputation for excellence.

*Mission* – To be recognized as the foremost group of experts in payments.

The potential for deployment of ATMs in any country can be gauged by comparison of the “number of ATMs per million populations” with a range of other countries. The table below illustrates where Bangladesh stands compared to other countries at various levels of development.

Country	ATMS per Million
Canada	532
Singapore	530
Australia	500
Hong Kong	402
Thailand	86
China	66
Philippines	40
Bangladesh	2

The number of ATMs per million-mobile/banked population in Bangladesh sits at just under 50. There is a drive to increase the number of ATM devices so the level of penetration can be expected to improve over the next few years significantly. But ATMs are not a low cost payment channel, even though the cost of devices has declined significantly. The real cost comes in servicing an ATM network, particularly the cash management aspects.

A network of encashment agents provides a lower cost alternative. The Kenya experience provides an insight into how this can be achieved and the associated issues. One of the issues again relates to cash management. Managing the distribution of cash to ensure its availability has been one of those behind the scenes challenges for all payment systems regardless of development status. Understanding community spending habits is important. It is not always the case that individuals will spend their cash in the same geographical area from where it was withdrawn. Some areas will always have a cash shortage and

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## *Paycrest* - delivers a range of payment advisory services:

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- Market Surveys and Analysis
- Requirements Definitions
- Solution Development
- Business Planning
- Business Modeling
- Process Planning
- System Design
- Solution Evaluation and Selection
- Project Directorship
- Project Management
- Specialist Project Resourcing
- Business Training
- On-Going Business Reviews and Audits

others a cash surplus leading to a requirement to redistribute.

Emerging markets also seem to be afflicted by an excessive number of financial institutions, with few if any being of a sufficient size to lead or drive infrastructural development. There are also examples of there being one dominant player who is unmotivated to introduce new services. Leadership is often not coming from the central authority.

One lesson from the developed markets such as Australia, Singapore, Malaysia, Canada and others has been the development of payment services supporting the acceptance of payment instruments issued by all financial institutions.

Although generally individual banks take the initiative to start these services to gain a market advantage, they eventually realize the value of forming national networks. Individual banks or even small consortiums of banks find that the investment and operating costs can only be offset through interchange arrangements with their competitors. Payments are a business of economies of scales. Transaction volume matters.

What many emerging economies often do not have, or have but are not effectively utilizing are interbank clearing and settlement houses. The ability to transfer funds or make a payment from an account at one bank to another person's account at another bank either in real-time or overnight is not possible. It is not uncommon in some countries that when you change your job you need to change your bank. This enables your new employer to pay your salary via a direct credit in a timely manner. This results in many people having bank accounts with multiple institutions, which mirrors their employment history. It is critical for this situation to be addressed before any real progress can be made.

Implementing a clearinghouse is less about implementing technology and more about implementing processing rules, standards and controls. The first challenge often relates to motivating the banks to work together under the direction of the central authority. Interbank politics can hold up progress and often the larger banks see cooperation on infrastructural development as a

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[info@paycre8.com](mailto:info@paycre8.com)

threat to their market position. They do not understand it is about growing the market.

It is important to ensuring all financial institutions are participants/users even if it is through a tier structure.

Then the services relating to the various delivery channels can be the space where banks can compete. They can develop their services to meet the requirements of their target market segments etc. The payment system will evolve based on domestic need. Services such as cross border MMT will only need to connect to one in-country partner to gain access to all mobile subscribers and will therefore have a chance of being successful. In-country mobile payment services will also have a higher chance of gaining mass acceptance and therefore commercial success.

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<sup>1</sup>The survey was conducted by Org-Quest Research Ltd, jointly funded by AB Bank of Bangladesh and Catalyst Capital Limited of New Zealand.