

**Inaugural Address by Mr. Yaseen Anwar, Governor SBP
Future of Branchless Banking, Payment Systems and
Financial Inclusion
(DECEMBER 19, 2012: AVARI HOTEL – KARACHI)**

Distinguished Guests,

Ladies and Gentlemen – Very Good Morning!

- 1. I am indeed delighted to be here at the workshop on “Future of Branchless Banking, Payment Systems and Financial Inclusion”. At the outset, I would like to express my gratitude to the CGAP team for leading this initiative which will help stakeholders to interact, develop common understanding of issues, and advance towards a unified vision for the market development in branchless banking. I believe that today’s event will greatly help to shape the future of branchless banking in the country.**

2. Today, I would like to talk about SBP’s vision on ‘Payment System and Financial Inclusion’. Both these areas have started becoming increasingly mutually-reinforcing, and their linkages are expected to deepen further in future. As both of these areas are very broad, I will focus on the aspects and issues that are more relevant to the developments in branchless banking.

First, I would like to share SBP’s perspective on “Payment system”, and then move on to the subject of branchless banking for promoting financial inclusion.

3. The Payment and Settlement System is a fast growing area, witnessing rapid innovations, spurred by market forces as well as new technologies. A safe and efficient payment system has always been a critical goal for us as it ensures the effective functioning of the financial system and smooth transmission of monetary policy. In this context, SBP became one of the few

Central Banks in the developing world that initiated work in early 2000 on laying foundations for a modernized payment system infrastructure. We started work on important projects like RTGS, and automated clearing of cheques. Some of the major achievements that we have accomplished so far are:

- Establishment of “1-LINK Switch” in 2001 by a consortium of 11 banks, to facilitate inter-bank electronic transactions. 1-LINK was subsequently extended to total 30 banks. Another switch MNET was also established around this time. Both switches were interconnected under SBP directive. Both switches are currently facilitating interoperability of almost 6,000 ATMs in the country.**
- 1-Link infrastructure also led to the evolution of *Inter-bank fund transfer* (IBFT) offering real time clearing between customers’ accounts of member banks.**
- Establishment of clearing house, NIFT (National Institution Facilitation Technologies) which is on its way towards**

automation of retail transactions and adoption of cheques truncation.

- **Real Time Gross Settlement System (RTGS), a high value payment system, went live in July 2008 which settled securities and cash transaction on real time basis with finality and irrevocability. Its primary objective is to facilitate money market and interbank transactions. RTGS' scope has been further extended to 'third party customer transfer' to facilitate banks' customers as well. Our vision is to make further dynamic expansion in the application of RTGS.**
- **A POS infrastructure was built which currently holds around 35,000 machines to facilitate payments via debit/credit cards.**
- **90% of total bank branches are currently processing real time online banking services across the country.**

- **One million internet banking users, 1.8 million mobile phone banking users, and more than 10 million call centers users are enjoying virtual banking**
4. **Despite these achievements, we feel that we could have done more to build on the initial successes. Unfortunately Pakistan lags behind many developing and regional countries in the area of Payment Systems. There is an urgent need to modernize and expand the payment system infrastructure both in large and retail value payment segments. Presently, we are contemplating such proactive measures that would minimize our current reliance on paper-based payment transactions through innovative approaches and new technologies. In this regard, a proposal is under consideration for the preparation of Payment Systems Strategic Road Map for the next Five Years.**

5. Global trends in Payment Systems indicate that traditional banks no longer have a monopoly on payments and settlement systems. Many new entrants like PayPal, Google Wallet, Square and Faster Payment have gained massive success in payment systems in a very short span. They are making dynamic changes in their business models, aligning their core businesses with advanced payment systems. Today, real innovations in payments are being stimulated by these new entrants in response to changing customer requirements. The payments landscape continues to shift away from paper based payment methods (cash and cheques) and conventional payment channels like bank branches to innovative and sophisticated modes like internet, smart cards, smart phones etc. In Pakistan, the last five years average shows that 36% of the transactions were routed through electronic channels and they evidenced a 23% average yearly growth compared to 2% average growth in paper based transactions. Although, these statistics show an increasing trend, these are still insignificant

for a country of 180 million inhabitants with a high currency in circulation to the tune of Rs. 1.9 trillion. This high currency in circulation is attributable to the fact that majority of our population is disconnected from banking system, and is heavily reliant on cash-based transactions.

- 6. In Pakistan, mobile phone subscribers are almost 120 million, and the number of adults with verifiable computerized Identity cards were up to almost 85 million in January 2011. In contrast, banking accounts are only 32 million whereas number of borrowers is as low as 5.7 million. These statistics indicate that there exist a large “financially-excluded” market, facing difficulties in buying goods and services, paying utility bills, borrowing and saving, or investing in their future. Bringing this un-served market into the formal financial system is our key objective as we believe that this would enrich the socio-economic development of our country.**

7. SBP has taken several policy and developmental initiatives to promote financial inclusion in the country. Today, our regulatory environment for microfinance and branchless banking is considered one of the best globally. As a result of SBP regulations on “Branchless Banking”, we have seen emergence of four mobile banking deployments which are not only advancing new frontiers for financial inclusion but also pushing the expansion in the payment ecosystem of the country. These providers are investing heavily in hiring, training, and branding their agents, thus contributing to the development of a new layer of distribution network for serving largely the unbanked market. For comparison, let me highlight that the brick and mortar retail network of the entire financial industry stands at around 11,000 outlets after 65 years whereas within a short span of 3 years, branchless banking retails agents’ network has grown beyond 32,000 agents. At these agent outlets, customers can deposit, withdraw or transfer funds besides making utility bills’ payment. With almost 1.8

million mobile banking accounts, branchless banking customers conducted almost 32 million transactions worth Rs. 140 billion during the quarter ending September 2012. The number and value of transactions per quarter are growing rapidly. The average size of each transaction is Rs 4,065 which shows that technology is helping ‘financial access’ of the unbanked.

- 8. To strengthen the growth trajectory, SBP has also been supporting innovative branchless banking initiatives through the Financial Innovation Challenge Fund (FICF). The FICF is a £10 million grant facility to provide grants to foster innovation and test new markets, lower the cost of delivery, enable systems and procedures to be more efficient, and provide new ways of meeting the larger demand for financial services. The first round of the Fund was held to promote the “Government to Person (G2P) Payments”, and has now been**

successfully completed by deciding to award Rs. 505 Million to six projects being undertaken by the applicant institutions.

9. Despite these initial successes, branchless banking is confronted with many early-development challenges. It is important for us to recognize these problems early on, and to develop an effective response to overcome such challenges, and move towards achieving our end-objectives. Accordingly, State Bank of Pakistan (SBP) has taken two key initiatives:

- Firstly, SBP has established a Consultative Group on Branchless Banking. The Group draws members from key stakeholders such as Pakistan Telecommunication Authority, NADRA, commercial and microfinance banks, mobile network operators and Technology Solution Providers. The group is currently working on developing proposals to respond to identified issues.**

- **Secondly, since September 2011 SBP has issued a quarterly “Branchless Banking Newsletter” to disseminate the key growth indicators/data, and various developments taking place in the area of branchless banking. We believe that these data disclosures and analytics will facilitate evidence-based policymaking and actionable decision-making, thus contributing to market development.**

10. Despite the initial developments of mobile phone banking, innovative delivery channels and products, cash still dominates our economy. Based on industry consultation and our own analysis, we keep identifying new challenges. At present, some key challenges are:

***First*, currently there is heavy reliance on over-the-counter (OTC) transactions which are pre-dominantly person-to-person (P2P) money transfers followed by complete cash-out. Instead of contributing to savings/deposit mobilization, this P2P service indicates that customers prefer to ‘store cash’ than**

to ‘store value’ on their mobile phone account. To bring a change in customer behavior, it is extremely important for the industry to develop appropriate saving products/m-wallets, and expand cash-handling infrastructure (such as ATMS, PoS, Agents etc.).

Second, the agent network is still “underutilized” as is evident by the average number of transactions by agent per quarter which currently stands at 1000. We all know that the development of these agents has started from scratch, and developing a business case for agents is complex and time-taking. The providers need to strengthen the process for hiring, training, monitoring, and incentivizing the agents.

The *Third* challenge relates to the mobile banking target market which has never been accustomed to ‘banking’. For these customers, opening and using an electronic/mobile account is a new and complex experience. The operators need to come up with creative marketing strategies, and financial

literacy schemes that provide basic learning and educative experience to their customers.

Conclusion

11. **A robust payment infrastructure is critical for the long-term development of mobile phone banking. It has been established that the advancement in both these areas needs contribution from a diverse set of players. Importantly, banks and mobile network operators (MNOs) have to develop partnerships to expand the agent network, leverage communication bearer channels, develop client acquisition strategies, and build a robust risk management framework. While there are enormous opportunities, there are also many ‘unknowns’ relating to competitors, partners, customers, and business rules. Among many uncertainties, one thing stands certain, that is, if the banks and operators want to succeed, they have to assign a strategic priority to branchless banking. In**

particular, we expect that instead of replicating the existing models, new players would bring in new and creative approaches to challenge the established players in the market. Let me emphasize that the board/CEO of banks and operators must have ownership of branchless banking. This will help to bring commitment, attention, and support from every level of the organization to this innovative, exciting and challenging service.

- 12. Finally, I hope that speakers and participants in this workshop will deliberate on the core issues, and develop some important recommendations to facilitate both the industry and regulator.**

Thank you!
