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How ecosystem issues fail rural FIs to promote digital financial services: Observations from MFIs in Tanzania

Justus Njeru and George Muruka, Agricultural Economists and Value Chains development specialists at *MicroSave*.

Digitisation of financial services is critical for Microfinance Institutions (MFIs[1]) to "go-rural, reach the unbanked" and achieve the financial inclusion goal. Studies show that MFIs stand to gain value if they digitise their finance services. MFIs get the opportunity to reach a higher scale, grow their loan assets, and earn additional non-interest revenues.

For example, in Bangladesh, SAJIDA Foundation, a microfinance NGO, realised positive value by offering digital finance services. In Kenya, Musoni, a leading MFI that offers only digital services, has consistently reported profitability. However, digital channels pose an important threat to the traditional group-lending process, an innovation credited "the microfinance revolution." At the core of the group lending are group norms, social cohesion, and co-guarantee mechanisms. And these create the pathway to provide the financial services to resource the poor people. Realising the importance of these functions, SAJIDA Foundation reverted to client group meetings, though limited to monthly meetings[2].

In his remarks at the 2016 European Microfinance Week conference, G. Wright noted that MFIs can and must adapt to the digital age for survival. MFIs are important and, perhaps, critical to providing financial services to rural-based adult populations in many developing countries. But, must they adopt digitisation? In some deep rural locations, the traditional Microfinance Model – a field office at the market centre and field officers addressing groups of women at the office or in a village further out – may be the only appropriate mechanism to ensure access to financial services to the growing rural populations. Such MFIs may not immediately give way to the on-going digital transformation of financial services in Africa.

Secondly, there are some ecosystems that have limited MFIs to provide financial services through digital channels. Our recent work in Tanzania identified mobile penetration, levels of literacy among clients, transaction fees, and liquidity issues as the leading factors impeding MFIs' digital transformation.

Mobile phone penetration

Mobile phone and mobile money services present a unique financial service delivery channel. While the use of smartphones in rural areas globally is on the increase, the pace is slower in Africa. According to a survey by Intermedia, only 54% of the rural population in Tanzania own a mobile phone and only 42% of those that own mobile phones in rural areas use advanced functions. Further, many households share mobile phones among family members.

MicroSave's work with a group of small-holder farmers in southern Tanzania showed that as many as 62% of the farmers owned basic feature mobile phones. And about one in five (18%) did not own a mobile phone at all – an indication that, access to and ownership of mobile phones is not universal yet and remains an impediment to accessing services by a large proportion of people in rural locations. Some of the farmers bought new sim cards, rather than renew their existing numbers every time they lost their mobile phones. This has led to the loss of valuable information, which the MFIs would have used to disburse loans, necessitating new registration.

Literacy levels

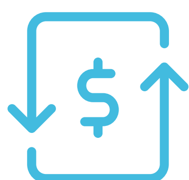
In many developing countries, people have low literacy levels. According to UNESCO, though the levels of adult literacy have been rising, globally, there are about 750 million people – three quarters being women – who are illiterate. Sub-Saharan Africa recorded the lowest levels compared to other regions – 65% of adults are literate MFI clients; especially those in rural areas have relatively low levels of literacy and numeracy.

As such, many of the financial services transactions by microfinance groups are undertaken by more literate group

[1] MFI represent Microfinance, SACCOs, Cooperatives, and For-Credit only institutions
[2] https://nextbillion.net/mobile-money-killing-off-group-microfinance-model-bad-thing/.

leaders. Low literacy and numeracy affect the extent to which these clients use digital financial services. For example, many farmers we met in Tanzania only used mobile phones for voice services, that is, receiving and making calls. Many of those who had used mobile money services "had been assisted to transact" and "could neither initiate nor complete a transaction on their own."

A study by Intermedia in Tanzania found that, across all demographic groups, financial literacy of the adult population was the lowest, that is, 16% and 18% in rural and urban areas, respectively. Literacy of mobile money services is equally low – about 17% of the adult population. *MicroSave's* work on oral population segments (see Digital wallet adoption for the oral segment) has shown that, with appropriate representations and symbols, institutions can still provide digital financial services to the oral clientele. However, there is a lot more work to be done on universally agreed on signages and symbols, to serve the oral market segment.



Cost of transactions

MFI groups task the group leaders to undertake the group banking services including banking savings, repayments, and withdrawal of loan disbursements. While the group members share travel costs and banking charges – translating to marginal cost to each member – this is not the case when each individual member transacts through digital channels, especially mobile banking services.

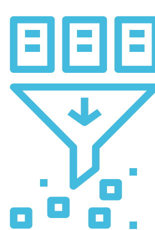
MFI clients in northern Tanzania were concerned about the transaction fee for mobile money services, including transfers of loan amounts from the MFI and subsequent cost of cashing out the funds. For example, a loan of TZS 500,000 costs the client TZS 2,000 on transport if the group leader transacts at a bank branch. However, when the member receives the same amount into his or her Vodacom MPesa e-wallet, they incur a transfer fee of TZS 2,200 and TZS 7,000 to cash out – 3.6 times the cost of the transaction through the group mechanism. MFI clients are more sensitive to transaction costs and tend to trade off values such as convenience and time-saving that come with digital services.

Chrissy Martin asks in his blog, "Do Farmers Really Want to be Paid in Mobile Money?" The debate begs the question, "Whether digital financial services are more supply-led or demand-led?" And that, perhaps, digital financial services per se are not the right solution for the unbanked, low literacy, and numeracy-rural populations.

Liquidity management

Clients in rural areas have relatively similar incomes and expense cycles due to a heavy reliance on seasonal agricultural production and small trades. Community cash flows mirror the production, weeding, and harvesting seasons – two to three months windows each – yet, many mobile money agents are not in tune with the seasonal cycles to match the demand and supply of money in these locations. The terse phrase "I have no float" turns away many clients – a disappointing experience. MFI groups meet at their homes, usually at some distance from the agents. It is discouraging to walk a long distance with cash in hand, only to be turned away due to lack of float. With a low footprint of agents in these communities, digital services continue to be costly to the MFI clientele.

Kiarie and Wright on Liquidity – Solving Agents Perennial Problem noted that liquidity management is the life-blood of a successful agent network. Agent network managers must monitor the float on a real-time basis across the network, as has been aptly captured by Ogwal on ebbs and flows of liquidity, especially in rural locations where one service misstep may mean that the customer never comes back to transact or, worse, spreads negative messages across the market.



Products and process suitability

Rural-based MFIs only have standard one-type-fits-all products that are not nuanced to meet the needs of the clientele. This is mainly due to the lack of staffing capacities and functional banking systems. For example, in our work, we meet MFIs and SACCOs that provide typical business working capital loans to farmers, with all the inflexibility there can be, such as single disbursement, flat interest rates, and limited information to the borrower. There is limited service and product diversification at the agent level. Agents, on the other hand, mainly provide cash-in and cash-out (CICO) services.

While the DFS promises to expand access to financial services to the unbanked clientele, it meets the headwinds of ecosystem-wide gaps especially in the rural areas, including sparse agent footprint, relatively low mobile phone ownership, unsuitable products, and liquidity management challenges. The ecosystem actors may consider promoting wider access to mobile phones for the rural population (there is progress on this with the prices of mobile phones being lowered to the range of USD 5 – USS 10), financial literacy for customers to embrace DFS, promote e-value transactions in the local markets, and affordable fees. An effective digital ecosystem should encourage payments relative to CICO services as we move towards cash-lite economies.