MAP TOOLKIT SERIES

6

Performing the MAP Diagnostic: Analysing the supply side

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TOOLKIT 6: Performing the MAP Diagnostic: Analysing the supply side

6

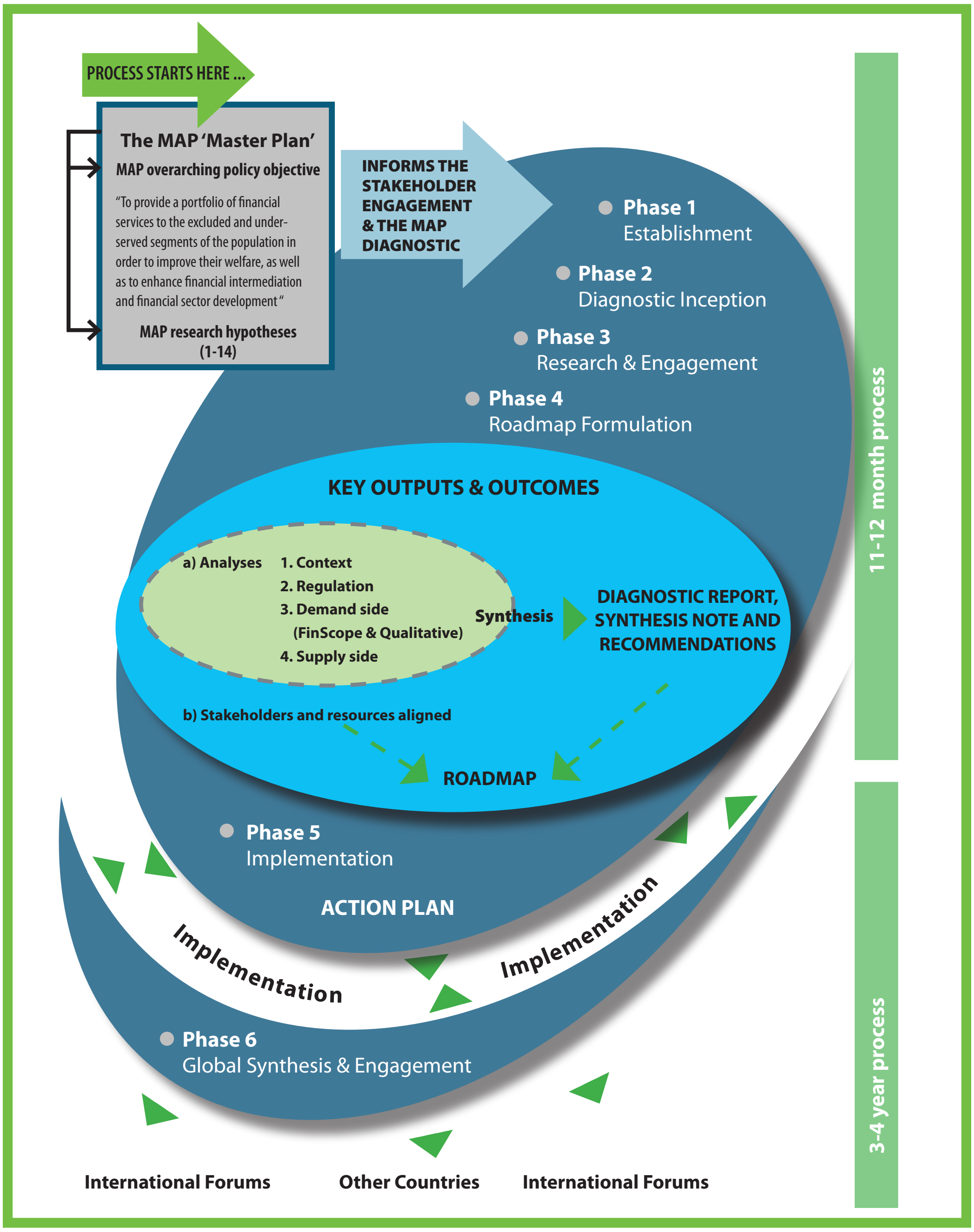
In this Toolkit:

THE MAP PROCESS

CONCEPTUAL OVERVIEW OF THE MAP PROCESS

1. Conceptual overview of the MAP process: supply-side research and analysis

The diagram below provides an overview of the MAP process. The focus of **Toolkit 6** is on conducting the supply-side aspect of the diagnostic.



2. Introduction

Toolkit 6 sets out the components of the MAP supply-side diagnostic, with a focus on providers, products and distribution channels.

As set out in **Toolkit I**, the overarching policy objective pursued through financial inclusion policies or strategies is:

> To provide a portfolio of financial services to the excluded and underserved segments of the population in order to improve their welfare, as well as to enhance financial intermediation and financial sector development.

The supply-side diagnostic deals with the first component of the overarching policy objective: the portfolio of financial services.

For the purposes of MAP, the portfolio of financial services is understood to comprise: savings/store of value; payments; credit; and insurance. MAP covers all four of these product markets, considering them not as discrete but as interrelated markets, where the development of one market may be dependent upon the development of another. Understanding and advising upon these interrelationships is a core element of the MAP diagnostic.

For the other three focus areas of the MAP diagnostic research and analysis, see **Toolkits 3** (context), **4** (regulation) and **5** (demand side). See **Toolkit 7** for information on pulling the analyses together into a diagnostic report with recommendations.

Note: For completing the analysis, the research is divided up into the four main focus areas (viz. context, regulation, demand side and supply side). However, there is considerable overlap between the focus areas. For example, both context (see Toolkit 3) and regulation (see Toolkit 4) feature very strongly in the supply-side research, and thus there will be large overlaps with the supply-side data-gathering exercise covered in this toolkit. Nevertheless, for purposes of both conceptual clarity and division of labour with regard to undertaking the research, it remains helpful to separate out the focus areas, while remaining alert to the considerable intersection between them.

3. What are the aims of Toolkit 6?

Working through this toolkit should enable you to:

- Understand what is entailed in researching the supply side of a MAP diagnostic;
- Gain an overview of aspects to cover related to the providers, products and distribution channels for each of the four product markets covered by MAP: savings, payments, credit and insurance;

- Confidently undertake the MAP diagnostic exercise in relation to researching the supply side and analysing the findings; and

- Pull together the insights gained into the supply side from undertaking the supply-side research and diagnostic, to reach relevant conclusions.

Something to think about

Mapping the total financial sector landscape in this way can be a daunting task, as it requires multi-faceted data gathering and analysis. However, there is 'method in the madness'. All information gathered should be relevant to the *core organising principle* for the analysis as represented by the MAP overarching policy objective.

4. Scope and structure of Toolkit 6

The supply-side analysis has three separate yet interrelated components:

1. Provider landscape;
2. Product markets; and
3. Distribution.

Provider landscape: This component focuses on the institutions rather than their products.

Product markets: This component focuses on the suite of products available within each defined product market segment, their features and the access barriers posed. The supply-side analysis covers four product markets: savings, payments, credit and insurance:

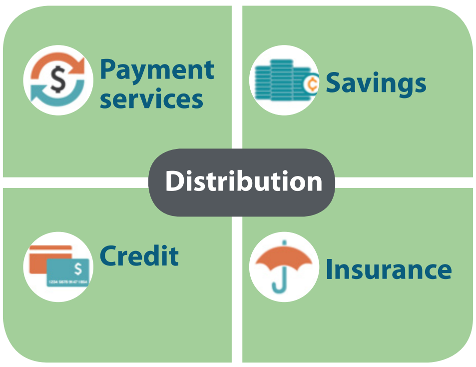


Figure 1. MAP product categories

Distribution: As indicated in Figure 1 (above), distribution cuts across the four product markets. This component of the supply-side analysis takes a cross-cutting view of financial services distribution.

Something to think about

Due to the complexity of financial services markets, it will not be feasible to cover each and every product for each product market in all countries. As part of the initial phases of a MAP project – during which the preparation and the desktop research work of the diagnostic take place – the product scope should be defined in the light of the objectives of that specific in-country MAP study.
For example: At this stage, you would need to consider whether to include a detailed review of health financing and pensions in the scope of the exercise.

At this point, it makes sense to take a look at Diagnostic Resource E: Applying issue tree logic. That resource explains the analytical logic applied in conducting the MAP diagnostic. Applying the issue tree logic will assist in setting the parameters or key areas of analysis for the MAP supply-side diagnostic exercise.

5. How do you go about gathering the supply-side data?

There are two primary research methods for gathering the supply-side data and information:

- Stakeholder interviews; and
- Desktop research.

The toolkits recommend a range of players to consult, topics to cover and information to gather. This supplementary information is to be found in Diagnostic Resources A, B and C (part of **Toolkit 8**), which provide checklists and example interview questions to guide the actual supply-side research process. The resources explain how to go about gathering data, in the following way:

- ***Diagnostic Resource A*** considers whom to meet with (an indicative meeting list) in order to gather the information during in-country consultations. It sets out categories of institutions and the rationale for meeting with different parties.

- ***Diagnostic Resource B*** lists a number of questions to cover for each institutional category – i.e. it discusses what to ask during interviews. It explains the steps in preparing for meetings, and the rationale and method for determining which questions to prioritise. It then outlines indicative questions to cover.

- ***Diagnostic Resource C*** provides data matrices/templates to populate from desktop research as input to the analysis – i.e. it stipulates data points to gather for desktop research purposes. These templates should be completed before or in parallel with the in-country diagnostic exercise. They will render the detailed data points for the analysis, allowing the interviews (Diagnostic Resource B) to focus on unpacking key issues and trends.

See Toolkit 8 for these support resources.

Something to think about

Toolkit 6 is intended as a guide to and framework for data gathering and analysis, giving guidance on what to cover in the analysis – it is not intended for use as a template document to be filled out. Thus, the toolkit does not outline the structure of the actual supply-side report. However, it can be very useful, while undertaking the research, to remain mindful of the possible shape and form of the data as it will be presented in the diagnostic report – and thus it is sensible to look ahead to **Toolkit 7**, in which an example template structure for a diagnostic report is provided.

Hypothesis 5

Financial services that improve welfare and deliver value to low-income households can be provided by public, private and community-based providers.

Hypothesis 6

Financial services must be provided by entities or business units that are financially sustainable, whether on a purely commercial basis or through ongoing national fiscal provision.

Hypothesis 7

Private commercial financial service providers will naturally expand their target market according to the level of profitability of each target market, progressing from the most to the least profitable.

6. The provider landscape

Financial products are delivered by financial services providers. This section focuses on these providers as institutions, whereas the next section looks more closely at the products that are delivered by the institutions. This section aims to answer the following questions:

- Which entities are currently providing services to the excluded and underserved population?
- How do these entities relate to one another in discrete product markets (primarily for the four product/service categories)?
- Are these entities prepared and able to continue or expand their provision of services to the underserved market? and
- What inhibits or incentivises their provision of financial services to the underserved market?

6.1. What do we want to achieve?

We want to identify the relevant financial services providers and then analyse their respective positions, in order to test the following of the MAP research hypotheses:

In identifying and analysing the various providers in the financial services landscape, we want to do the following:

- Get an understanding of the providers and their respective market positions.

Note: This aspect draws on regulatory terminology (see also Toolkit 4) in terms of the types of entities or institutions operating in the market, as well as the de facto market structure and the target market they serve. It should include formal and informal players. It is expected that this exercise will also require close consideration of the products offered by each player (Section 7 of this toolkit outlines the exercise of investigating the product terrain).

- Identify key innovators and instances of innovation in the market.
- Explore the ability to and incentive/s for different categories of providers to serve lower-income markets.

Note: This is likely to be a combination of various factors: profitability, efficiency, competitive dynamics in the market, ownership structure, and the mandate of the provider organisation in each case.

- Explore the ability to and incentive/s for different categories of providers to offer value to clients.

For example:

- o A funeral service provider will have an incentive to offer a good-value insurance product if they benefit from the claim (in that it guarantees that the person will be able to buy the funeral service from them); and
- o An agricultural value chain player such as a processor that wants to buy produce will have the incentive to offer credit to farmers to prevent them from delaying selling their crops to get a higher price.

- Explore the impact of regulation (see **Toolkit 4**) at the provider level.

Note: By setting barriers to entry and imposing direct and indirect compliance costs, regulation can either serve as an absolute access barrier for providers, or it can discourage entry or expansion into the unserved market. In other instances, regulation can facilitate entry or create incentives for expanded provision.

'Financial capability' is a term often used in this toolkit. **See Diagnostic Resource G** (in Toolkit 8) for detail on financial capability.

Related link

Collins, D., Morduch, J., Rutherford, S. & Ruthven, O. (2009). Portfolios of the Poor: How the world's poor live on $2 a day. Princeton: Princeton University Press. Available online from: http://press.princeton.edu/titles/8884.html

Related link

Porteous, D. (2004). Making Financial Markets Work for the Poor. Paper commissioned by FinMark Trust. Available online from: http://ndp.treasury.gov.za/Courses%20Library/2007,%2029%20Oct-2%20Nov%20-%20TTRI%20Overview%20Course,%20Midrand/Day%203%20-%2031%20Oct%202007/Reading%20-%20MMW4P%20Porteous.pdf

6.2. Getting going on researching providers

To build up the required information, the task of researching providers will cover the following parameters:

- Market structure and trends;
- Innovation;
- Business models/priorities;
- Ownership;
- Capacity and infrastructure;
- Efficiency;
- Financial strength (stability/solvency);
- Profitability; and
- The informal market.

TOOLKIT 6

THE MAP RESEARCH HYPOTHESES

Diagnostic do's and don'ts: where and how to find the necessary provider information

- The aspects to cover indicated below are not the 'entire universe' of indicators to track; neither will information on all aspects necessarily be available in the particular country. Work with what you have.
- Be informed by the rationale for each parameter and let that shape the information gathered and questions asked during in-country interviews. Always work towards the master plan (i.e. the MAP overarching policy objective and the resulting research hypotheses).
- Use the interview as an 'entry point' to request more detailed information afterwards. Start by requesting current and past annual reports – these are often the single best source of information.
- As it will not be possible within the time available to meet all the players, use market-level data from aggregated industry/supervisor reports. Request supervisory data upfront and prioritise interviewees and interview questions on this basis.

Each of these parameters is discussed further in the following sub-sections, which follow a similar structure: each starts by unpacking the rationale for understanding the specific parameter as part of a financial inclusion diagnostic, then considers aspects to be covered in researching the specific parameter.

Note: This section has both a market and an individual provider dimension: some of the parameters are focused on the market (e.g. the size and growth of the overall market) while others also consider individual providers.

6.3. Market structure and trends

A key objective of MAP is to develop a framework within which the various providers in a particular market can be located in terms of the products they offer and the clients they serve. The first parameter to consider is the market structure, in terms of both current structure and trends over time. Market structure includes the number and categories of players active in the financial sector, and the total size of the market and growth patterns in this regard, as well as the market shares of various institutions, and trends in entry, exit and consolidation in recent years that will impact on the level of competition in the market.

The table below highlights the rationale for the market structure analysis, as well as the various aspects to cover, subject to data availability.

Remember: The list provided here is not necessarily exhaustive, but indicative only.

A note on business growth and expansion

The nature of growth and expansion is not smooth or linear. Business volumes may grow linearly or exponentially, but the operational and infrastructure side often grows in discrete steps.

With regard to business growth and expansion: in the first stage of market development, business can be done from centralised headquarters, with limited distribution infrastructure, and can focus on a few large clients. This scenario requires limited staff, and the use of higher-skilled staff can be optimised from headquarters. This model may be able to deal with the first stage of branch expansion via a centralised management structure. The second stage of development may require decentralisation of management and processes. This will require adding more management staff at branch level, which increases the numbers required and implies the need for stronger business process systems. It may also require the development of more advanced management information systems (MIS) with branch-level connectivity. Indeed, at the nexus of the two stages of development, providers sometimes move from a paper-based to an electronic system.

RATIONALE	This section of the supply-side diagnostic seeks to answer the following questions: • Who is currently providing services? What is their relative size, strength and distribution footprint? • What are the different component markets within the savings, payments, credit and insurance markets, and who are the providers in each of these component markets? • What is the overall size of the different markets in terms of turnover? What are the growth trends? • How mature are the different markets: i.e. at what stage of development are they, and how competitive is each market? • How competitive is the overall market? Are there dominant/large players? If so, could their infrastructure be leveraged to accelerate market growth, or does it undermine competitiveness? • What are the trends in entry, exit and consolidation in the market in recent years? In what way do these trends serve as indicators of the health of and opportunities in the market? For example: o If a number of new players have entered, it indicates that players think there are untapped opportunities or that the regulatory framework makes it favourable for them to enter. The resultant increase in competition may create the need for incumbents to find new market segments, including in the low-income market; o Conversely, exit or failures may indicate a struggling market; and o Consolidation trends are an indication of competitive dynamics, changing market conditions or tightening regulatory requirements.
Aspects to cover	• The total number and different types of entities operating in specific markets (e.g. banks, MFIs and government players operating in the credit market; third-party payments providers vs banks operating in payments; different types of insurers etc.). Consider the following: o Size of various players in terms of total turnover, assets and client base, as well as percentage share, in each, of individual providers, and categories of players relative to the total market or to a subset (such as banks, credit providers, payments providers, deposit-taking institutions, and insurers); o Overall market concentration levels; o Institutional categories of players: e.g. cooperatives, mutual institutions and/or corporations, and the relative shares of each in terms of total numbers of players, as well as total assets, turnover and client numbers; and o The specific product category being focused on (e.g. unsecured loans within the larger credit market) and the nature of the product suite. • The aggregate size of the financial sector and of different categories of financial services providers relative to the economy (GDP) – to show whether the specific product sector is growing in line with the economy or more slowly/faster – as well as relative to other players; • The stage of development in terms of business volumes as well as systems and operational infrastructure; • The number of players that have entered over the past year, past five years and past decade, respectively; • The number of players that have exited over the past year, past five years and past decade, respectively, and the reason for exit (noting failures, as well as strategic decisions to withdraw from the market by multinationals); and • The number of mergers and acquisitions in the sector over the past year, past five years and past decade, respectively.

Tracking these elements should enable the diagnostic to build up a fairly complete picture of the provider landscape, market structure and trends in the specific country.

6.4. Innovation

The extent and nature of innovation in each specific product segment, as well as in the financial sector as a whole, is especially relevant to uncover, as it speaks to one of the core MAP hypotheses, namely: 'Significant advances in financial inclusion in a particular market require business model innovation, whether in product or distribution' (Hypothesis 9). Innovation may be an indicator of the level of competitiveness in the market, which creates an incentive to reduce costs and enter new market segments (including the previously unserved market). The absence of innovation, in turn, may indicate complacence and limited incentives for breaking open new market segments.

The table below highlights the rationale for the innovation analysis as well as aspects to cover.

RATIONALE	This aspect of the supply-side diagnostic seeks to answer the following questions: • Who are the key innovators in the financial sector? and • Do they tend to be particular types of providers (e.g. small new entrants), or does innovation tend to be concentrated among certain types of product providers (such as in the payments space)?
Aspects to cover	• The major innovators; • Examples of innovation; • Key aspects of innovation; • Main barriers to innovation; and • Any regulatory requirements that inhibit or promote innovation.

TIP: **Consider these aspects in brief only as part of the provider analysis – actual product and distribution innovation are covered under those respective parts of this diagnostic toolkit.**

TIP: Many of the aspects discussed here will also be covered under other provider parameters or as part of the exercise to research distribution. Here, the purpose is to show some of the elements that could be explored in interviews, but there is no complete list of questions. Neither are interviewees likely to have explicitly formulated their business models or strategy. Ultimately, you will need to read between the lines to infer the answers. In each case, ascertain the firm's stated strategy and then match that up with the structure and capacity of its business.

6.5. Business models and priorities

This parameter speaks to the business models and priorities – the underlying philosophy, so to speak – of providers. It considers the interest in and priority placed by providers in the retail market versus corporate business, as well as in mass market expansion and financial inclusion.

RATIONALE	This aspect of the supply-side diagnostic seeks to answer the following questions: • Are there certain types of providers (e.g. by size, product focus or ownership structure) that are more likely to pursue financial inclusion than others? and • In what way do providers' underlying business model priorities or outlook shape institutional strategy? How can this help you to understand financial inclusion trends and challenges?
Aspects to cover	• Mandate: Does the provider have an explicit mandate from shareholders that dictates its strategy? Examples can include: serving rural areas, expanding into niche markets, or pursuing product and distribution innovation in order to gain market share. It is more typical for state providers to have such a specific mandate, but it may also be applicable to private companies. • Current target market: It is relevant to ascertain whether a provider has a defined target market or not. The absence of such a target market is evidence of limited strategic focus and results in particular market dynamics. Among those who do define their target market, it is important to know whether they target the low-income/unserved/mass retail market or not. This may be a function of their stated mandate, or an implicit business strategy. If companies are explicitly not targeting low-income or previously unserved segments, it presents a different challenge to where they are interested in pursuing this market or already touching it. • Distribution strategy: Whether the distribution strategy is branch based, relies on partnering with third parties, leverages mobile phones, or whatever the case may be, can be an indication of business model priorities. Note: Detailed investigation into distribution is covered in Section 8 of this toolkit. Here, the focus is just on ascertaining strategic priorities. • Product strategy: This refers to the spread of products being offered or in the pipeline, and the relative importance of different types of products in terms of current revenue and future strategy. This aspect can cut across product categories or relate to only one, depending on the type of provider. Product strategy links to target market. For example: If the target market is small businesses, this will dictate a focus on certain credit products (leasing, factoring etc.)..

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THREE LEVELS OF ENGAGEMENT

Aspects to cover	• Overall business strategy and approach: Other business pressures such as competition may lead to interest in the unserved market. Conversely, macro trends such as a recession or rising labour costs may act as a disincentive to expansion in new, untested markets. To inform likely changes for the future, it would be important to understand the factors that shape a provider's view of its target market. This aspect is linked to ownership (see 6.6, below). For subsidiaries of multinational or regional companies, the overall strategy or approach in one country may be impacted on by the strategy at group level.

Diagnostic do's and don'ts: is everybody on the same page?

Terms such as 'low-income market' or 'unserved market' may be understood differently by different people. In conversation with providers, be sure to unpack the meaning of such terms.

For example:

When discussing their strategy, the provider may understand the low-income market to refer to the ultra-poor and may respond to say that they do not prioritise this market segment and do not have any products branded for the low-income market. However, their entry-level ('vanilla') product offering – e.g. basic bank accounts, remittance products, microloans or insurance – may be relevant for the lower-income market, more broadly defined as first-time customers of a particular financial service.

This shows that the diagnostic exercise requires you to apply your judgment, read between the lines and probe specific aspects in order to answer the questions necessary to test the MAP research hypotheses. Simply asking a number of structured, predefined questions to each interviewee will not render the required insights for a meaningful set of findings.

TIP: **As with the distribution strategy (above), the intention here is not to conduct a full investigation into products, but to understand strategic priorities. Sometimes insights can be gained from the disjuncture between the stated strategy and the actual business model pursued.**

6.6. Ownership

Ownership structure is another key parameter to be understood in the provider landscape, as ownership structure plays a major role in shaping strategy.

RATIONALE	Analysing ownership structure helps the diagnostic team to understand dynamics in the market on a number of fronts: • Is ownership shareholder-based or mutual, and how does this impact on organisational strategy? • Is foreign ownership high? If so, how does it impact on incentives to serve the low-income market? Something to think about...In markets with constrained local capacity in terms of human resources and systems, foreign players may offer some quick opportunities by importing the necessary skills and systems. It is also not uncommon for local (typically protected) players to have limited energy and incentive to enter more challenging low-income markets. In these cases, foreign players may trigger development. There may be some regional players specialising in particular financial inclusion-relevant market segments. Conversely, foreign players may target the high-income market, thereby prompting domestic players to extend into lower-income segments to gain a competitive advantage. >>

RATIONALE	(CONTINUED) . • What is the balance between public and private ownership? In many countries publicly owned players still play a major role in the financial services market. Government players may react differently to regulatory changes and market dynamics and may have different mandates than private players. For example: In some cases, a state-owned financial services provider may have an explicit mandate to offer credit to a particular market even if it is not commercially viable. Given that state-owned players may serve certain markets with other motives than profit, it will impact on the incentive of private players to enter that same market. For instance, what is in effect a subsidy by the state to provide services at prices that would not otherwise be viable, may render it unviable for private players to enter, as they do not have the incentive to subsidise a particular segment on an ongoing basis. In more problematic cases, credit may be used to build support for election purposes. In these cases, loan recovery is often not a priority and it risks creating a bad credit culture. Public ownership or part-ownership may also be a positive force for financial inclusion, notably where government has a particular social goal or mandate to serve a market that would not otherwise be reached by private players. • Is privatisation a relevant issue? Irrespective of whether it may be the appropriate route, the changes occurring as part of privatisation will have a major impact on the market (more so where the state-owned financial services provider is a dominant player).
Aspects to cover	• Institutional categories (e.g. cooperatives, mutuals or corporations): Map the types present in the market and the number of players in each type. Note how institutional composition differs across product markets (e.g. there may be more mutual savings organisations, but more corporate banks). • Foreign vs domestic ownership: Note the number of players that are majority foreign-owned. Note any regional ownership trends or dominance in foreign ownership from a particular country. Explore reasons for multinationals investing in the particular market. Where institutions are foreign-owned, probe whether they respond differently than local players to market and regulatory conditions. • Public vs private ownership: Note the number of organisations across product segments that are majority publicly owned, as well as the number of fully state-owned enterprises or parastatals. • Privatisation: Note the number of organisations that have been privatised in the past decade, and the privatisation mode followed, as well as any privatisation plans that are in the pipeline.

6.7. Capacity and infrastructure

The fifth provider parameter to explore is capacity and infrastructure. Many of the aspects covered here will also be relevant to the exercise of researching and analysing distribution, but the emphasis here is on understanding these aspects from a provider perspective and on gathering such information from provider data and interviews. Three sub-parameters together inform the capacity and infrastructure landscape:

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- Systems and IT;
- Staff numbers (distinguishing between professional and sales staff); and
- Distribution/value chain infrastructure.

Below, we consider the rationale for considering each sub-parameter, as well as the aspects to cover in unpacking it.

RATIONALE	The analysis seeks to establish the following: • What is the current state of systems and IT in different parts of the financial sector? • To what extent does professional and managerial staff capacity constrain market development? • In what ways do the number and quality of sales staff impact on the capacity of the provider to sell and service the product? and • Does the current branch infrastructure/value chain distribution capacity have implications for reaching low-income consumers in a cost-effective manner? Note: Distribution channels are covered in detail in Section 8 of this toolkit. Here, the focus is on understanding the impact of distribution capacity and strategies from a provider perspective and at a high level.
Aspects to cover	• Systems and IT: Ascertain whether providers use paper-based or electronic systems and, in the case of electronic systems, whether large legacy systems dominate, or if certain players have more nimble, innovative systems. Where the latter is the case, identify who these players are and if systems innovation tends to cluster in certain institutional or product market types of providers. Also track: o The ability to process high volumes of low-value transactions; o The ability to add on services (e.g. some MIS systems focus only on credit and cannot add payments); o The ability of management to understand and monitor their current performance (e.g. paper-based systems will not be able to allow real-time monitoring of product performance); o IT costs in-country, policy and regulatory support for subsidies, assistance provided with innovation; and o Any relevant support institutions: e.g. whether there are credit bureaus and training institutions, and how effective they are. • Staff numbers: Track the professional, managerial and frontline sales staff contingent, respectively, across different providers. Also ascertain how many vacant posts there are and whether skills and human resources are a constraint for many or some providers. As hiring of foreign staff members may be an indicator of professional or management staff constraints, the diagnostic should investigate what proportion of management and professional staff is foreign. Also be on the lookout for regulatory restrictions on foreign hiring; and • Branch and other distribution/value chain infrastructure: Describe the nature/categories of distribution infrastructure employed and how it differs for different types of providers. Where such information is available, note the geographical spread and urban/rural split of such infrastructure for different institutions and categories, as well as the overall geographical footprint of the financial sector.

6.8. Efficiency

Efficiency is another important provider parameter to cover. It refers to how cost-effectively the provider operates.

RATIONALE	Efficiency impacts on the ability and incentive of providers to serve low-income consumers. This section seeks to uncover: • Is the level of operational and systems efficiency sufficient to profitably serve the financial inclusion target market? Low-income consumers would most likely use small loans and/or payments, make small deposits or investments, and buy small-premium insurance. • Do cost structures/inefficiencies undermine the ability to offer value? For example: If distribution costs are particularly high, it will trickle down to transaction costs (in the case of banking or payment products), may mean lower effective returns (in the case of savings and investments), or may mean lower claims ratios (in the case of insurance). In each instance, the value for money provided to the customer is eroded.
Aspects to cover	• Track cost structures such as sales expenses, management expenses and overheads, where available, from annual reports or other statistics; and • During interviews, probe related factors to get an overall sense of levels of efficiency.

6.9. Financial strength

The seventh parameter considers the financial strength of providers, which in turn determines stability – one of the pillars of regulation and a prerequisite for financial inclusion and, indeed, any kind of operation.

RATIONALE	This section of the supply-side diagnostic seeks to uncover the following: • In what way does financial soundness impact on financial inclusion in the particular country, and how does this differ across institutional types? Financial strength will impact on financial inclusion by shaping what is on the mind of senior management of financial service providers, and their strategic agenda. Financial strength is also an indicator of the ability of providers to take on additional, and potentially more challenging, developments and of the risk of failures, which will impact adversely on financial inclusion.
Aspects to cover	• Relevant indicators regarding solvency, capital adequacy and liquidity (see Toolkit 8, Diagnostic Resource C: Data templates – Table 2: Data points to be collected on financial products for an overview of financial statement information to be covered).

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6.10. Profitability

It is also important to track how profitable various financial institutions are.

RATIONALE	This section of the supply-side diagnostic seeks to uncover the following: • How do levels of and trends in profitability impact on companies' strategy and incentives for mass market expansion? For example: If there is limited competition and a bank is making high returns by serving a small, high-income market, that institution is less likely to try to extend into lower-yielding and riskier lower-income markets. On the other hand, struggling firms may prioritise branching into new markets in an effort to achieve economies of scale and enhance profitability. Something to think about...However, lower levels of profitability will not necessarily lead to a move downmarket. Profits can also be curtailed by, for example, high distribution costs or internal cost structures, lack of appropriate investment opportunities or regulatory compliance costs. In these instances, an organisation may find it difficult to expand even if ideally they would wish to move downmarket.
Aspects to cover	• Document overall profitability for various players, as gleaned from income statements, as well as sources of profitability (interest rate spread, transaction charges, or investment income); • Highlight any noteworthy trends in profitability over time and potential drivers thereof; • Note how profitability and sources thereof vary across institutional categories and product markets; and • Include a more specific investigation into whether various types of providers are making money out of the low-income or mass market.

6.11. The informal market

The last provider parameter stands apart from the other parameters as it deals with a different type of provider landscape, namely informal providers. The informal market is a critical component of the supply-side analysis. In many of the MAP participating countries there will be substantial informal financial markets.

For the purpose of a MAP diagnostic, 'informality' is defined as any product or service rendered without the provider thereof being regulated or supervised to do so.

Note: Informality can be institutional (the entity itself is not registered or licensed, e.g. for tax or employment purposes) and/or functional (the entity is not licensed to provide the particular product or service).

The MAP diagnostic is primarily interested in functional informality. That is to say, a product or service, and the provision thereof, will be seen as informal if the provider is not licensed, by the relevant authority responsible

INFORMAL VS ILLEGAL: It is important to note that informality is not always illegal: sometimes legislation simply does not exist, or particular categories of providers are exempted from legislation; for example, if their turnover falls below a certain threshold, or if they are member based. The services they render may also not meet the exact definition of the relevant regulated financial service, thereby implicitly placing them outside the scope of the regulatory framework.

for regulating that product or service, to provide the product or service, even if the provider may be institutionally registered.

While many of the parameters discussed in Sections 6.3 to 6.10 above will also be relevant for informal players, it is worthwhile dedicating a separate discussion to the informal market.

The quantitative demand-side data from the FinScope Consumer Survey and the qualitative demand-side research (see **Toolkit 5**) will be instrumental in helping you to understand this sector. In particular, interviews with informal providers as well as their clients may provide key insights. Note that exact numbers or data will not be available for informal players as, by definition, they are not monitored. Interviews must be used to get a sense of orders of magnitude, on which a meaningful discussion can be based.

RATIONALE	Ideally, the analysis should pose and answer the following questions: • What are the competitive dynamics relating to informality? The balance of providers operating in the formal vs informal market may be an indicator of the level of development and sophistication of the market and may impact on competitive dynamics (as informal players are not subject to compliance costs). • Does informality signal untapped formal financial inclusion opportunities? The presence of informal markets reflects: i) the need for a particular service; and ii) willingness to pay to obtain it. Thus the presence of informal providers is an indicator of pent-up demand for financial services that is either not served by the formal market, or is served by formal providers in an inadequate way (e.g. inappropriate features, not affordable, not physically accessible, or not trusted by those opting for informal services). Something to think about...Even if the existence of an informal market signals pent-up demand, it does not necessarily present an easy opportunity for formal financial services. In some cases the driver of informal product use cannot be replicated by the provider (e.g. burial societies offering community and comfort to bereaved families). In other cases the model cannot be replicated by the formal sector due to the structure of the informal offering (e.g. informal risk management mechanisms can ignore insurable interest as a policy condition, as they can control it through relationships – formal providers do not have that option) or cost/viability (informal credit providers can leverage time of members as volunteers and do not comply with regulations, which will add costs). • What are the consumer protection implications of informality? As informal financial services are not subject to any prudential or market conduct regulation, consumers do not have a legal guarantee that providers will deliver on their promises or safeguard customers' money. There are also no formal recourse options should something go wrong; nor are consumers guaranteed a certain level of disclosure. In some instances, for example in member-based lending schemes or self-help groups, these risks may be mitigated by the discipline enforced by community bonds.

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Something to think about

Where informal mechanisms do not pose particular consumer protection risks, the regulator may choose not to focus on them. If, however, there is evidence of widespread consumer abuse, the regulator may choose to intervene – be it by imposing penalties to informality, or by setting favourable regulatory requirements for formalisation.

RATIONALE	• What can formal providers learn from the value informal services offer to clients? Despite the consumer protection concerns inherent in informality, informal financial services are often valued and trusted by customers and play an important role in the absence of formal delivery.
Aspects to cover	• List the types/categories and number of informal players; • Describe the size of the informal market in terms of client base and turnover (relative to the formal market); • Provide an overview of informal activities and show orders of magnitude in terms of the number of informal players and their share of the estimated total client base (because even if the figures are not exact this is an important issue in terms of determining policy priority); • Consider the risks to consumers (notably market conduct and prudential risk) and to the market at large (in terms of potential stability impacts) stemming from unregulated financial services provision; • List typical eligibility requirements for client acceptance by informal versus formal institutions, and highlight any pertinent aspects of client value in the informal service offering vs the formal sector; and • Investigate opportunities for formalisation by: o Considering the barriers to entry set by regulation relative to the risk inherent in a particular market segment: is there scope for encouraging formalisation by lowering regulatory requirements in a proportionate way? and o Documenting any existing regulatory attempts at formalisation and evaluating how feasible such formalisation attempts are, given the size and nature of the informal market and the level of supervisory capacity.

Something to think about

The fact that the sector is informal is often because the regulator does not have the capacity to supervise all entities active in the market. Changing regulation will not change the ability of the supervisor to enforce formalisation.

Hypothesis 1

The personal financial services that are most likely to improve the welfare of low-income households are savings, electronic payments, credit and insurance.

Hypothesis 3

Low-income households will use formal financial services on an ongoing basis only if they are affordable, accessible and appropriate to their needs.

Hypothesis 2

The demand (as opposed to need) for the different types of formal financial services (savings, electronic payments, credit and insurance) does not develop simultaneously or independently. The demand for certain types of service develops before the demand for other types of service. Significant gains in access to certain services also depend on other services being available (e.g. the availability of low-cost electronic payments will facilitate the growth of savings, credit and insurance).

Hypothesis 8

To be successful in low-income markets, financial products must be specifically designed to fit the characteristics of that market, rather than being miniature versions of products for higher income markets.

Hypothesis 9

Significant advances in financial inclusion in a particular market require business model innovation, whether in product or distribution.

7. Product markets

The second separate yet interrelated component of the supply-side research and analysis is product markets.

Consumers choose between different products that meet a particular need. Although the choices are made based on multiple motivations, they can only be made between the products that are actually available to that consumer. The purpose of this component of the diagnostic is to demarcate the different product markets (savings, payments, credit and insurance, but also relevant sub-markets within each of these, e.g. an agricultural credit market, if that is applicable in a country) and analyse the products available in each, with a view to identifying gaps and opportunities for increasing financial inclusion.

7.1. What do we want to achieve?

We want to research and analyse the various product markets in the financial services landscape, each done separately because they operate separately and consumers treat them as discrete markets. This will contribute to testing the following of the MAP research hypotheses:

7.2. Getting going on researching the product markets

In terms of the product markets, it is useful to consider the following questions:

- What are the current needs of the excluded and underserved population for formal financial products in each of the four service categories?
- Compared to the needs, what services or products are they currently using and who provides these services?
- Are the products affordable, accessible and appropriate? and
- If not, what are the opportunities offered by and constraints on the provision of improved services that can meet the gaps in service provision?

Note: In order to understand which products and institutions are most relevant from a financial inclusion point of view, and where the bottlenecks and opportunities for greater financial inclusion lie, the diagnostic will initially consider the full payments, savings, credit and insurance landscape. Thereafter, the focus of the analysis will be only on those products relevant to the particular target market – namely, the excluded and underserved population (as defined in Toolkit I and in the MAP overarching policy objective).

Mapping the various product markets will require the following to be done in respect of each of the four financial services markets:

- Identify most prominent drivers of use (also referred to as 'use cases');
- Map current usage;
- Identify the providers that serve the market, and the market-wide dynamics that affect them;
- Compile a product list and describe the features of the products;
- Use the access framework (explained later in this toolkit) to evaluate the products that are offered in the market in terms of their appropriateness, accessibility, eligibility and affordability;
- Identify regulatory constraints or issues;
- Identify other obstacles to increased usage of products; and
- Identify gaps and opportunities.

Each of these activities is discussed in further detail below.

Identify the most prominent drivers of use: A driver of use is an identified need or use for a particular service among the target market.

For example:

o A driver of use for payments could be to make remittances from urban to rural areas, or for migrants to remit funds cross-border; and

o Credit for agricultural production is usually an important driver of use for credit in societies with large rural populations.

The examples provided of drivers of use are meant to be illustrative rather than exhaustive, and are intended to focus the discussion on the actual or potential needs expressed in the market and the potential roles that a particular product could fulfil.

Note: The qualitative and quantitative demand-side research (see Toolkit 5) will inform an understanding of the drivers of use, as will an overview of products on the market and insights from provider interviews.

TIP: Use FinScope data (see Toolkit 5), overlaid with data on registered users or client numbers requested from providers, to estimate the total likely user numbers overall, as well as for each product market in the country. Where possible, indicate both formal and informal usage, and distinguish between number of accounts and number of users, as one user may have more than one account. The FinScope Consumer Survey is likely to be the most reliable source, with a comparative discussion on the insights rendered by supply-side information.

Map current usage: How many people currently use each of the products available in the market – formal and informal?

Where detailed usage information is not available by product category, or where usage of informal options is not documented, an indication can be given of orders of magnitude as gauged from consultations or triangulated from provider estimates of number of clients.

Identify the providers that serve the market, and the market-wide dynamics that affect them: This can be done at a collective level.

For example:

- List the variety and nature of payment services offered by banks, mobile network operators and third-party bill payment networks, respectively, the savings and credit products provided respectively by MFIs, SACCOs and banks, or the number and types of insurance products provided by informal community-based schemes versus licensed insurers.

Note: This element differs from the provider analysis outlined in Section 6: the provider landscape pertains to overall market structure, competitive dynamics and provider performance. Here, the focus is on provision within a particular product market.

Compile a product list and describe the features of the products: List all products that are relevant from a financial inclusion point of view and their key features. (As already discussed, there is no single 'formula' for defining the target market or filtering products that would be relevant to the target market; this topic is considered in further detail in **Diagnostic Resource C**, in **Toolkit 8**). If relevant, the products should be grouped according to their drivers of use or any recognised product segment within the overall product market:

For example:

- There may be a defined consumer credit market, an SME credit market, an agricultural production credit market, and/or a leasing market within the overall credit market.

Use the access framework to evaluate the products offered in the market: Apply the access framework (see more detail, below) to assess the appropriateness, accessibility, eligibility and affordability of the products offered. At the same time assess the value offered to clients by the different products.

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Access framework

The methodology used to assess products' implications for financial inclusion typically focuses on factors that may exclude individuals from being able to use a particular product. This is referred to as the 'access framework'. Five drivers of access have been identified (Porteous 2004):

- Proximity: This considers how far a person must travel to access the service concerned and is usually defined in terms of the time required and/or the cost of travel.
- Affordability: The measure of affordability will differ across financial products, but the basic premise is that people are likely to be excluded from a particular financial service if the cost of using the service exceeds a critical threshold relative to their monthly income and/or the value of the transaction. The only financial service for which an affordability benchmark or rule of thumb is available is transaction banking. The benchmark typically used for deposit accounts is that bank charges should not exceed 2% of household income. No equivalent benchmark is available for other financial services.
- Appropriate product features: The features of the service should be appropriate to the user and be able to meet the user's particular needs for the financial service.

For example: Some workers and smallholder farmers will have seasonal income, which may imply that their transaction profile is also seasonal. Thus a bank account that is classified as 'dormant' if it does not have a set frequency of transactions will not fit the needs of this particular target market.

- Appropriate terms or eligibility requirements: These are defined as eligibility requirements imposed by financial service providers beyond what is dictated by regulation. Contractual terms imposed by financial service providers may inappropriately exclude specific categories of users from making use of the service.

For example: Some deposit accounts may require minimum balances, levels of income or formal employment, which may exclude the poor and/or unemployed.

- Regulation: Regulation may inadvertently exclude specific groups of people (e.g. if regulation requires migrants to provide proof of legality of stay, thereby excluding undocumented migrants), or increase the cost of serving particular client groups (e.g. requiring banks to open physical files for clients even if account balances are low and transactions limited).

The access framework as applied to each product market will focus on the first four access criteria; a separate discussion is dedicated to investigating regulatory barriers and issues for each product market (see below).

Related link

Porteous, D. (2004). Making Financial Markets Work for the Poor. Paper commissioned by FinMark Trust. Available online from: **http://ndp.treasury.gov.za/Courses%20Library/2007,%2029%20Oct-2%20Nov%20-%20TTRI%20Overview%20Course,%20Midrand/Day%203%20-%2031%20Oct%202007/Reading%20-%20MMW4P%20Porteous.pdf**

Note: There is a difference between access and usage. A person may technically have access to a product, but may choose not to take up or use such a product. In addition to these access barriers there will therefore be usage factors that discourage people from taking up the product even if they have access. These include the availability of informal alternatives, social security or state-provided alternatives, fear of 'officialdom' and the paperwork required by formal players, perceptions that formal financial products are 'for the rich', and/or distrust of the formal sector.

See also Toolkit 5 (demand-side analysis), which considers drivers of use.

Identify regulatory constraints or issues: Identify any relevant regulatory provisions or implications (sometimes the lack of a regulatory provision can also be a constraint) that impact on the inclusiveness of the particular product market and the ability of providers to deliver services in the particular market.

Identify other obstacles to increased usage of products: Identify any other obstacles that inhibit the use of financial services in the particular market.

For example:

o In addition to access barriers there will be usage factors that discourage people from taking up the product even if they have access. These factors are the subject of Toolkit 5 (focusing on the demand-side analysis) and will therefore not explicitly be discussed for each product market below. However, it will be important to incorporate them into the diagnostic report.

Identify gaps and opportunities: Reach conclusions with regard to gaps between the current product offering and the types and features of products needed by the low-income market – as gauged through the demand-side research (see **Toolkit 5**) and captured in the examples provided of drivers of use. Identify the first- and second-order opportunities to fill these gaps.

See Diagnostic Resource B: Illustrative interview questions for more detail on questions to ask as part of the analysis.

The sub-sections to follow provide an in-depth overview of how to cover each of the elements outlined above in each of the four product markets.

7.3. The market for Savings

7.3.1. Rationale

Savings can be defined simply as putting money aside for future use; that is: forgoing current consumption for future consumption.

The need to store value and save securely is a core financial service need alongside the need to transact. It is arguably even stronger for the low-income market than for the wealthy, as the poor spend the bulk of their money on day-to-day needs such as food and will simply not have money at hand for even modest expenditures such as clothing or household goods. Thus, to meet the expenditure they either need to go without, sell an asset, or find some way to tap into past or future income – the former via savings, the latter through credit (which can be defined as an advance against savings that you plan to make in future). Savings services thus help people to manage money by storing past income for future access.

The purpose of saving through an institution, be it formal or informal, rather than at home, can be three-fold: to ensure a secure store of value, to instil savings discipline and to generate a return on savings.

In an inclusive savings market, there will be a diversity of players offering a variety of savings products to the low-income market and there are paths for formal institutions towards accepting deposits other than becoming a fully fledged bank. Furthermore, providers will see a business case or have another imperative for providing savings to further-downmarket/lower-income clients, and there will be sufficient competition between institutions to ensure appropriate, value-for-money products. Consumers will trust providers, who will be prudentially sound and will use consumer research to inform product decisions and understand client perceptions. The reality is, however, often different. A limited formal infrastructure or footprint, coupled with low returns/high costs and/or negative perceptions and a lack of trust in the formal sector may mean that many people save at home or in-kind (e.g. by investing in livestock). It will be the task of the supply-side diagnostic to sketch the savings landscape, in order to build an understanding of the lie of the land and the dynamics relating to how it shifts and develops.

Related link

See Rutherford, S. (n.d.). The Economics of Poverty: How poor people manage their money. Available online from: **http://media.microfinancelessons.com/resources/Economics_poverty_rutherford.pdf**

7.3.2. Aspects to cover

7.3.2.1 Drivers of use for the market for savings

The drivers of use for savings are determined largely by the savings goal. At the heart of the savings landscape is the need to store value. Such a store of value can either be for everyday use or for emergencies and unexpected eventualities. Alternatively, or in addition, the need can be for an accumulation of a targeted lump sum towards the purchase of an asset or service – ranging from household consumables or capital for a business, to saving for a trip. Savings needs can also relate to long-term asset formation such as housing, savings for old age, or saving for a wedding or for the long-term education of a child.

The savings goal will determine what type of product a person uses (see discussion below: 7.3.2.4) and, within each category, what type of instrument is prevalent.

As part of the supply-side diagnostic exercise, use the demand-side research findings (see **Toolkit 5**) to determine what the main savings goals and corresponding drivers of use are for the underserved population in the particular country in question. As an example, a recent in-country diagnostic identified the following main drivers of use with regard to savings in the country:

- Short-term savings for consumption smoothing and unplanned eventualities;
- Compulsory savings for loans;
- Savings for education; and
- Longer-term saving for investment.

TIP: Examples of drivers of use can include formal and informal savings mechanisms. Keep these drivers of use in mind as a reality check when evaluating the products offered to the target market and the appropriateness of their features.

7.3.2.2 The market for savings: Current usage

The FinScope Consumer Survey (see Toolkit 5 for more) has a section aimed at uncovering savings behaviour. Use the findings to ascertain the proportion of adults that save in some way (be it 'under the mattress' or through informal mechanisms), as well as how many people save through the formal system. Do this for the total adult population, as well as across target market segments as introduced in Toolkit 5. Where possible, distinguish savings usage according to drivers of use.

7.3.2.3. The market for savings: Providers

People save with a variety of formal and informal institutions.

In the formal sector, deposit-taking is usually strictly regulated, as people entrust their money to the institution and there thus need to be safeguards in place. A retailer or service provider (such as a hospital service or funeral service provider) may also sell savings stamps towards the goods or service sold. In the formal sector, savings services can be rendered by traditional banks, deposit-taking microfinance institutions, insurers, cooperatives, investment houses or government (e.g. where it provides savings bonds). Increasingly, payment service providers are implicitly acting as savings institutions as people keep a float in their electronic wallets or wait to cash out money transfers at, for example, a retailer.

Informally, people save in savings clubs or with a community member that collects and keeps savings on a regular basis. They can also save at home,

Something to think about

M-Pesa is a system used most prominently in Kenya and Tanzania for money transfer. It derives from the Swahili word 'pesa', meaning 'money', and 'M' for 'mobile'. M-Pesa is currently the most developed mobile payment system in the world.

or in kind (e.g. by buying gold or livestock), but this is not intermediated through a third party.

Whereas the purpose of the provider analysis (see **Section 6** of this toolkit) is to analyse the market structure and performance across institutions, the purpose here, in terms of researching the market for savings providers, is to list those providers active in the savings sphere and to highlight any issues or trends relating specifically to deposit-takers.

7.3.2.4. The market for savings: Products and features

In addition to 'under the mattress' saving, there are a multitude of formal and informal savings instruments. They can roughly be grouped into three categories:

- Store of value: Store of value is for an indefinite term, typically for short-term transaction needs and on an ad hoc basis. Some value may be stored as a float for payments, or it can be kept in an account to draw upon for everyday needs. Store of value accounts are typically low cost, with low or no return on the deposit. Examples include the float in a bank account, a money transfer wallet or account such as M-Pesa, a money guard service, prepayment of goods in the form of savings stamps/coupons or lay-byes, or even overpayment of bills to have a positive balance to draw on.

- Savings: The next 'step up' in the savings evolution from a pure store of value is to save for a specific purpose. Typically, savings products offer some return and relate to short- to medium-term accumulation goals. Capital is not at risk and the saving can be ad hoc or contractual.

For example:

o Bank accounts;

o Building societies;

o MFI deposit accounts; and

o Rotating savings associations.

- Investmen: Investments are usually made with longer-term accumulation goals in mind and offer higher potential returns – but in turn the capital may not be guaranteed. Investments can be contractual or ad hoc.

For example:

- o Retail bonds;
- o Collective investments/unit trusts; and
- o Pension/provident fund products.

After establishing the drivers of use, the diagnostic should explore the savings product landscape according to the various store of value, savings and investment instruments available on the market. Where possible, distinguish between formal and informal options. The purpose of the exercise is to take stock of what products are on offer that are relevant to the target market and what their features are, before the rest of the analysis then evaluates the product suite against the access framework.

In listing the key features of a product, consider:

- Who provides it?
- What is the main target market?
- What driver of use is addressed?
- What instrument is used? and
- What are the main product features, what fees are charged and what interest is provided?

TIP: The best source is the FinScope Consumer Survey (see Toolkit 5), as it will ask respondents to list how close they are to various outlets, how long it takes them to reach such outlets and how much it costs to do so.

7.3.2.5. Accessibility of the market for savings

The crux of the savings analysis is to evaluate the suite of products against the four criteria in the access framework.

Proximity: Gauge the proximity of clients to various outlets for depositing or withdrawing savings – most notably bank branches or savings and credit cooperatives, but also retail stores, ATMs or mobile money agents in the case of stored value.

The survey data should be superimposed on and checked against data gathered from service providers on the number of service outlets and their geographical reach. You should draw on qualitative demand-side research findings for further insights into perceived physical accessibility and whether the existing footprint speaks to client needs and preferences.

See Toolkit 5 for more on conducting the demand-side research and analysis.

Affordability: It is difficult to assess affordability of savings instruments, as the act of saving implies that a person has surplus money to set aside and the choice of instrument is a matter of relative value for money, rather than absolute affordability. There is no rule of thumb for acceptable charges on savings products. Indeed, a person would reasonably expect to make a return on savings or investment, not to 'pay to save'. However, in practice this is often not the case, as interest earned is typically low to negligible on all but long-term fixed investments, and transaction charges will erode any returns. People may also be willing to pay for a savings mechanism in return for the savings discipline that it instils (e.g. where a person in the community acts as money guard) and the security that it provides.

It is therefore important to assess the value for money that different savings options present.

- Are financial savings vehicles capable of delivering value on small-value savings?
- In what way do delivery costs reduce yield? and
- Does new technology offer efficient channels for collecting and managing savings, thereby improving value for money?

It is likely that perceptions and experiences regarding affordability and value for money as gauged through the qualitative demand-side research (see **Toolkit 5**) will render the richest insights. In addition, relevant questions in the FinScope Consumer Survey can be explored, and the interest rates offered and fees and charges should be compared on different savings options, as gauged through supply-side data or product brochures.

Appropriate product features: Understanding whether the product suite on offer speaks to the target market's savings behaviour and preferences requires an integrated view of non-financial (e.g. physical assets) and informal ways of saving, to be gauged from the demand-side research (as outlined in **Toolkit 5**). For this part of the analysis, overlay the main 'client-facing' product features (including minimum balance requirements, any investment term stipulations or transaction limits, whether the account becomes dormant after a period of inactivity and so on) with FinScope (quantitative) and especially qualitative demand-side research findings on client needs, savings behaviour and realities. Reach conclusions on whether the types of savings instruments on offer and the features of such products are appropriate to the needs of clients for each driver of use. Also consider whether and why certain products on the market are more appropriate than others.

Appropriate terms or eligibility requirements: Map account-opening requirements and any other terms or requirements that dictate which prospective customers are eligible to access the service – and under what conditions. Reach conclusions on whether there are any aspects related to product terms or conditions that pose a barrier to access and, if so, how severe such barriers are likely to be.

7.3.2.6. Market for savings: related regulatory issues

Savings are likely to be covered alongside transaction banking under banking regulation. Savings-relevant regulation will be covered in the diagnostic as part of the regulatory framework (see Toolkit 4). Here, the focus is on highlighting regulatory constraints and issues related specifically to the savings environment.

Of relevance would be whether non-bank deposit-taking is allowed, by whom, and under what conditions, in order to assess whether the regulatory framework poses barriers to entry that skew the playing field in favour of banks, or facilitates entry by new and community-based players.

It will also be important to assess which entities may act as distribution channels for savings products (e.g. retailers or post office outlets selling savings bonds) and what the agency requirements are.

Consider whether there are any specific consumer protection concerns in the savings environment and what the regulatory challenges in this regard are.

Use the stakeholder interviews to ascertain whether there are any particular regulatory constraints or challenges relating to the savings market. Also assess whether there are jurisdictional overlaps or grey areas between regulators (e.g. between the central bank as bank regulator and the cooperatives authority/non-bank financial institution regulator as regulators of non-bank deposit-takers) that impact on the functioning of the market.

7.3.2.6. Market for savings: gaps and opportunities

Based on the various aspects of the analysis, reach conclusions on what the main access gaps are in the savings arena. This requires the following:

- An estimation of the potential formal savings client base, compared to the current client base, with particular attention to priority savings needs across target markets;

- An analysis of the features of the product landscape and regulatory framework that challenge uptake by a broader client base or specific target markets; and

- A discussion of the opportunities for reaching the unserved market in general and priority target markets in particular and potential touch points in this regard (to be gauged from the distribution analysis in Section 8 of this toolkit).

Consider the extent of informal savings, be it through family/friends, at home, or through an informal institution and what the scope for and challenges to formal intermediation of such savings are.

In reaching conclusions on the scope for inclusive savings markets, take into account the linkages between product markets – for example: the fact that the development of the savings market may be driven in part by the development of the credit and capital markets, or that store of value options can develop on payments models.

7.4. The market for Payments

7.4.1. Rationale

All people need to transact. Thus payments are the most basic financial service need and often the first formal financial service used by a household. The MAP approach seeks to uncover how people pay (or would want to pay). The process of answering this seemingly simple question will not only expose the types of instruments used by customers, but will also identify patterns and payment profiles.

The MAP diagnostic research assumes that the current retail payment environment is largely dominated by cash transactions. One of the related objectives of the research is to determine where innovations in electronic payment transactions are occurring – with 'electronic transactions' defined as any transaction that converts cash into electronic funds or vice versa (e.g. a cash deposit or withdrawal) or that transfers funds electronically (e.g. a card payment at a point-of-sale device, or an electronic funds transfer between accounts or electronic wallets, or a money transfer). The rationale for increasing the penetration of electronic transactions is to reduce the cost of managing cash, and to allow customers and businesses to benefit from greater security and efficiency in their respective retail payment activities.

7.4.2. Aspects to cover

7.4.2.1. Drivers of use for payments

The drivers of use for payments are determined by two categories of distinguishing characteristics:

- Why used?
- Who is making the payment, and to whom?

Why used? Which needs are being met, and what typical uses are the products being put to?

For example:

o The need for payments can relate to paying bills, purchasing goods and services, sending and receiving remittances, or receiving money from an institution (e.g. a social transfer such as a grant or an insurance payout).

Who is making the payment, and to whom? Who the counterparts to the transaction are is a core factor defining different payments solutions. Generally, five categories can be defined:

- Person to person (P2P): a transfer or payment from one natural person to another, be it a payment for goods or services rendered, or a remittance. A natural person refers to individual consumers transacting as part of day-to-day activity, based on consumption of goods and services.
- Person to business (P2B): a transfer or payment from a person to a business, e.g. to procure a good or service. Where the business is informal, it can be denoted 'P2b' (with 'b' in lower case not caps).
- Business to person (B2P): a transfer or payment from a business to a person, e.g. to pay a wage. Where the business is informal, it can be denoted 'b2P' (with 'b' in lower case not caps).
- Government to person (G2P): a payment from government to an individual, e.g. a social grant or other type of transfer, or through the government payroll. As used here, the term 'government' refers to institutions that have a mandate to disburse funds as part of specific programmes designed to subsidise the economic activity of a specified domestic population.
- Donor to person (D2P): the same as a G2P payment, except that the source of the funds is a donor rather than government.

The following likely drivers of use exist for payments, to be tested and adapted for each country:

- Bill payments (including utilities, insurance premiums);
- Purchase payments (for products and services, including airtime);
- Converting electronic money into cash, and vice versa;
- Receipt of salary or wages;
- Remittances (domestic and cross-border);
- Pension payments; and
- Debt receipts and payments.

7.4.2.2. Payments: current usage

FinScope data (see **Toolkit 5**) can be used to gauge total payment usage, most likely tracked according to transaction banking and remittances. Indicate how usage differs across target market segments. It is unlikely that ready data will be available on number of users for each example of drivers of use. Where possible, use FinScope data and insights from interviews to estimate orders of magnitude of usage across the various drivers of use. That means that impressions and available data points would need to be triangulated to arrive at an informed opinion on the relative ranking of drivers of use in terms of uptake in the particular country and where the most growth potential or, conversely, the bottlenecks lie.

7.4.2.3. Payment providers

Payment providers include the traditional providers, namely banks and remittance service providers (the likes of Western Union and MoneyGram), as well as more recent entrants to the financial services sphere such as mobile network operators and retailers. In most instances, there is an important role for technology providers, and some partnership will be struck between the various parties.

The profile of providers of payment services can vary greatly, depending on the spectrum of institutions authorised to participate in the payment system.

Dynamics of a 'healthy market'

For the purposes of this assessment a 'healthy' market will exhibit the following provider dynamics:

The market will include a broad range of institutions, including banks and non-banks, which operate in an environment where each institution type fulfils a particular role in a dynamic and evolving payment service environment.

In aggregate, the providers offer a variety of services to meet the needs of the customers, providing a choice of service as well as institution for users of the payment system. This in turn facilitates a competitive market that is encouraged to innovate by using new technologies to deliver affordable and reliable service. Providers see a business case in offering payment services to low-income customers.

As part of the process of navigating the evolving nature of the payment service environment, a robust industry association plays a critical role in aligning incentives and brokering business rules among the competing needs of providers in the market. This is particularly relevant to ongoing communication with the payments regulator to develop an appropriately balanced regulatory environment that encourages innovation while providing sufficient legal certainty.

Underpinning the business arrangements of the various providers is the need for a robust electronic payment infrastructure. The infrastructure must not only function as an efficient interbank payment system but must also provide clearing and settlement processes for high- and low-value payments. The systems standards for such infrastructure must also be accessible for all payment institutions, to encourage the necessary interoperability of the payment backbone to facilitate interconnection of products and services. The infrastructure must be sufficiently robust to handle high volumes of electronic payments.

7.4.2.4. Payment products and features

This part of the analysis takes stock at a high level of what products are relevant to the target market and what their features are, before the rest of the analysis then evaluates the product suite against the access framework. Two main aspects should be covered:

- What are the various payments service options on the market? For each driver of use, list the various product offerings; and
- For each option, what are the main features? Who provides it, how does it work, what are the fees, who is the customer, what transaction

functionality is provided, and what instrument is used?

The variety and features of formal or electronic payment products on the market will be determined by two key parameters: i) the transaction path followed and ii) the instrument used.

The transaction path followed: Every transaction occurs on a path that has an originating source and a final destination.

For example:

o A customer makes a cash payment at a retail agent outlet, which facilitates the transfer to another individual's stored value account. The payer originates the transaction with a cash deposit and the payee receives the funds in electronic form.

Transaction paths can be classified according to whether customers use cash, stored value accounts or bank deposit accounts. This will allow the research to address formal/traditional channels (banks), informal means of payment (cash) and innovative product models (e-money). While there may be other models in each respective market, we can assume that an understanding of these three will allow us to sufficiently identify both how informal and formal transactions occur, and the emergence of innovative payment models.

Payments can be:

- Cash to cash (C2C): as for any normal cash transaction;
- Account to cash (A2C): e.g. a remittance sent from an account and redeemed in cash;
- Cash to account (C2A): e.g. making a deposit into a bank account or store account facility; or
- Account to account (A2A): as would be the case for any electronic fund transfer.

Note: In each instance, the 'account' option can also be e-money or a money transfer solution (e.g. a mobile money wallet or a money transfer account that's not linked to a bank account); i.e. not a traditional account necessarily provided by a deposit-taking institution, but some innovative electronic store of value such as an electronic wallet.

The instrument used: Various instruments can be used to make payments. This refers to the mechanisms or instruments that facilitate payment transactions.

Generally, the payment instruments to be considered are:

- Cash;
- Cards;
- Credit transfer;
- Debit transfers; and
- Remittances.

Other core features: Other features distinguishing different payments products from one another include:

- Whether it is a domestic or international service;
- Whether it is purely a payment product, or also entails a store of value (e.g. an electronic wallet from which remittances can be made and into which they can be received);
- Whether it is linked to another financial service (e.g. payment functionality on the back of a bank account, versus a stand-alone remittance product);
- Whether the transaction is one-off or recurring (with a person signing up for the service); and
- Whether it is conducted through the formal sector or informally (e.g. formal remittance service providers vs informal hawaladar or hundi – which are different names, internationally, for informal money-transfer systems).

The supply-side diagnostic should explore the payments product landscape according to the transaction path, instrument and other core feature parameters in order to start to form a typology of different models on the market.

Payments infrastructure: The payments system is the backbone of the financial system. It is an important element of distribution, as distribution channels need to facilitate transactions between clients and financial services providers. In an ideal set-up, customers will be able to pay anyone, any amount, from anywhere. At a minimum, system interconnection should allow customers to perform basic cash-in/cash-out services across networks and providers, to engender trust in the system and drive uptake. In the real world, however, proprietary interests often overrule interconnection.

The diagnostic should describe the payments system as well as the level of interconnection, and identify any pertinent issues in this regard.

7.4.2.5. Payment accessibility

Accessibility should be evaluated against the following four key components of the access framework outlined earlier: proximity, affordability, appropriate product features, and appropriate terms or eligibility requirements.

Proximity: The first part of the access framework is to measure the physical accessibility of the various payment service options. This is done by gauging the proximity of clients to various outlets for cash-in/cash-out transactions or transfers.

The survey data should be superimposed on and checked against data gathered from service providers on the number of service outlets and their geographical reach. Qualitative demand-side research findings should be drawn on for further insights on perceived physical accessibility and whether the existing footprint suits client needs and preferences.

TIP: As with the accessibility of the market for savings, the best source is the FinScope Consumer Survey (see Toolkit 5), as it will ask respondents to list how close they are to various outlets, how long it takes them to reach such outlets and how much it costs to do so. Where there are mobile money options available, use FinScope to gauge the percentage of adults who own or have access to a mobile phone.

Affordability: Secondly, a meaningful way must be found to gauge the affordability of the different payment product options. Once again, relevant questions in the FinScope Consumer Survey should be the first port of call. Perceptions and experiences regarding affordability will also be gauged through the qualitative demand-side research.

From the supply-side perspective, the analysis should cover the service fees charged on different payment options. In particular, the comparative costs for different options to serve the same drivers of use must be determined.

Appropriate product features: For this part of the analysis, overlay the main 'client-facing' product features (including minimum or maximum transaction size, daily or monthly transaction limits, whether the account becomes dormant after a period of inactivity, functionality in terms of whom you can pay or send and receive money from and so on) with FinScope and especially qualitative demand-side research findings on client needs and realities. Reach conclusions on whether the types of services on offer, as well as the features of such products, are appropriate to the needs of clients for each driver of use. Also consider whether and why certain products on the market are more appropriate than others.

Appropriate terms or eligibility requirements: Map registration requirements and any other terms or requirements that dictate which prospective customers are eligible to access the service, and under what conditions.

Something to think about

In assessing issues of affordability and appropriateness (see more, below), it is important also to consider the counterfactual: what would be the cost – or benefits – of transacting in cash rather than electronically? This can be tangible (e.g. withdrawal or deposit fees), but also implicit, such as enhanced security related to electronic transactions, or convenience.

For example:

o Is an e-money service available to all mobile network subscribers – or only to bank account holders?

Reach conclusions on whether there are any aspects related to product terms or eligibility requirements that pose a barrier to access and, if so, how severe such barriers are likely to be.

7.4.2.6. Payment-related regulatory issues

Diagnostic Resource B (in **Toolkit 8**) includes various regulation-related questions to cover in the payments analysis. While Toolkit 4 deals in more detail with the regulatory environment, here the focus is on highlighting regulatory constraints and issues related to the payment system and payment services.

In order to ascertain whether the payments regulatory framework is enabling of market development and innovation, the supply-side diagnostic should answer the following questions:

- Who is the lead regulator for the national payment system and how does payment system regulation relate to banking supervision?
- Who can access the national payment system? What is the definition of deposit-taking and the business of a bank in the specific jurisdiction? Can non-banks be payment providers?
- Is there a centralised national payment system strategy, endorsed by the industry and directed by the lead regulator?
- What are the main compliance costs related to the payment system?
- Are so-called 'know your customer' (KYC) requirements that are imposed under anti-money laundering/combating the financing of terrorism regulation challenging low-cost payment products? If so, in what way/s?
- Do regulations take into account the use of new technologies, and have they been adapted to the increased usage of electronic payments?
- Are there specific regulations in place to address the use of stored value services, particularly those offering basic cash services via agent networks?

- Are various distribution channels (including non-bank agents) accounted for in the regulatory framework, taking into account various operational risks and institutional management requirements?
- Are there any pertinent consumer protection issues in the payments sphere? And how does regulation address this, or what are the gaps? and
- What investment restrictions apply, and how do these drive cost/s?

TIP: In so doing, investigate the capacity of the supervisor, and whether there are any jurisdiction issues between different regulators or departments of the central bank that are likely to shape payment system regulatory outcomes.

In evaluating the above questions, it will be important to answer the following:

- What is the current situation?
- How does the current situation differ from the desired state? and
- What are the challenges in moving from the former to the latter?

7.4.2.7. Payment gaps and opportunities

From all of the aspects of the analysis above, and especially by comparing the drivers of use with actual product delivery and the appropriateness of such delivery, reach conclusions on what the main access gaps are. This requires:

- An estimate of the potential target audience for payments services, compared to the current client base and a conclusion on priority payment needs across target market segments;
- An analysis of the features of the product landscape and regulatory framework that challenge uptake by a broader client base; and
- A discussion of the opportunities and potential touch points for reaching the unserved market in general and priority target markets in particular, and potential touch points to do so (to be gauged from the distribution and infrastructure analysis in Section 8 of this toolkit).

7.5. The market for Credit

7.5.1.Rationale

For many people, the need for credit is a fact of life, as income and savings are insufficient to meet lumpy expenditure needs, or to respond to the financial implications of a risk event. Market research may show that people are averse to incurring debt; yet emergencies, productive and consumption needs mean that many people do borrow – some more regularly than others. They may save at home and transact in cash, but once they need money beyond what they can borrow in the family or community structures, they approach a formal or informal lender.

Access to credit may depend on a person's level and regularity of income or whether he or she has some form of collateral. These requirements will differ between the formal and informal sectors and will impact on a person's choice of credit provider and instrument.

Due to the fact that credit is subject to interest and people often borrow at a time when they are in dire need of cash and may not rationally compare their options, credit gives rise to special consumer protection and disclosure/ transparency considerations. It is the task of the supply-side diagnostic to sketch and unpack the dynamics in the credit landscape in order to reach conclusions on the scope for inclusive, non-abusive credit markets in the particular country in question.

7.5.2 .Aspects to cover

7.5.2.1. Drivers of use for the market for credit

The drivers of use for credit are determined largely by the purpose of the loan. Consumers borrow either for consumption or productive purposes, or to accumulate assets:

- Borrowing for consumption purposes entails borrowing for emergency expenses such as medical or funeral expenses or to recover losses in, for example, agriculture or due to a risk event such as a fire, or for expected lump-sum expenses – such as a wedding, a holiday, buying clothing, a vehicle or household goods – for which cash flow is insufficient;

- Borrowing for productive purposes entails investment in a business, borrowing to purchase working capital or manage the business's cash flow, or borrowing to finance education or other expenses that can help build productive capacity; and

- Credit can also be in the interest of asset formation: e.g. a mortgage on a house.

Another determinant of the drivers of use is who the borrower borrows from: a bank, building society, non-bank credit provider, microfinance institution, informal moneylender, a state financial institution or from a community vehicle (e.g. savings and credit cooperatives, village loan associations, self-

TIP: Keep these drivers of use in mind as a reality check when evaluating the products offered to the target market and the appropriateness of their features.

help groups or family members). Drivers of use can include formal and informal lending mechanisms.

As for savings, the demand-side research findings and supply-side interviews should be used to determine what the main drivers of use for credit are for the underserved population in the particular country.

For example:

o The following drivers of use emerged in a recent in-country diagnostic:

- The use of credit for agricultural production;
- The use of loans for health or education expenses;
- The use of credit to service existing debt;
- The use of credit for small-scale enterprises;
- The use of loans for consumption smoothing; and
- The use of credit for on-lending.

7.5.2.2. The market for credit: current usage

FinScope Consumer Survey findings will indicate the percentage of adults that borrow in some way, as well as those that have formal credit. Explore the survey findings for any insights related to usage by specific drivers of use and unpack usage of credit across target market segments.

7.5.2.3. The market for credit: providers

Credit can be provided by a variety of regulated institutions, depending on the regulatory framework in the particular country, including banks, non-bank financial institutions, microfinance institutions, asset or household goods vendors, supply-chain input providers or cooperatives. In most countries there will also be a variety of informal moneylenders, and people will often resort to social networks such as their employer, family members or community members for loans.

The MAP diagnostic will identify the various credit providers and their relative importance in the identified drivers of use. The overarching provider analysis (see Section 6 of this toolkit) identifies institutional trends and features of relevance to the product market analysis.

7.5.2.4. The market for credit: products and features

After establishing the drivers of use, describe the main loan products available to the target market and compare the products in terms of their key features. The various payment products to be on the lookout for as part of the diagnostic include personal loans, trade credit, revolving loans, store credit, factoring, leasing, payroll lending or asset-based/collateralised credit.

Key features to cover in terms of loans include:

- Group vs individual lending;
- Formal vs informal credit;
- The maturity of the loan;
- The interest charged;
- The frequency and method of repayment: payroll, direct debit or cash; and
- Whether it is collateralised/secured lending or not.

TIP: It will be important to ascertain the difference between individual and small business loans, and secured versus unsecured lending, as well as the term of the loan, whether it is for productive or consumption purposes and whether it is provided by a formal institution or informally.

As with the savings and payments analyses, the purpose of the exercise is to take stock of what products are on offer that are relevant to the target market and what their features are, before the rest of the analysis then evaluates the product suite against the access framework.

In listing the key features, consider the following:

- Who provides the credit?
- Who is the main target market?
- What driver of use is addressed? and
- What instrument is used?

It is also important to understand the nature of the provider and the funding structure (equity, venture capital, investments by hedge funds, pension funds or donors). Currently, the business model of many non-bank credit providers in developing countries relies on donor funding, which will impact on product features and mode of operation. Pricing models may also differ between different types of lenders.

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WHO ARE THE MAP STAKEHOLDERS?

TIP: In gauging proximity, investigate what granularity is provided by the FinScope Consumer Survey in terms of access-point mapping – then add insights from qualitative demand-side research on the physical accessibility of credit, and overlay that with data requested from providers in terms of their geographical footprint.

7.5.2.5. Accessibility of the market for credit

As with savings and payments, the exercise to research and analyse credit is followed by an accessibility assessment against the following four key components of the access framework outlined earlier: proximity, affordability, appropriate product features, and appropriate terms or eligibility requirements.

Proximity: The first step in the accessibility analysis is to investigate the physical accessibility of credit access points to the target market. Credit can be accessed through a variety of channels, including bank branches, savings and credit cooperatives, retailers, credit unions, village- or community-level lending associations or groups, microfinance institutions, moneylenders etc. The credit footprint is therefore likely to be relatively pervasive, depending on what type of credit is considered.

Affordability: Of all the product markets, credit is the one with the most direct consumer protection concerns. Many of the consumer protection concerns relate to the levels and transparency of interest rates charged and the total cost of credit once fees and 'fine print' are included. Hence, the affordability assessment is of prime importance. However, the task of measuring affordability is challenged on a number of fronts. There is no rule of thumb for acceptable interest rates, and a strong need for credit (e.g. due to an emergency) will increase a person's willingness to pay even to the point where they sacrifice other budget essentials for it, thereby making it difficult to assess actual affordability. It is furthermore difficult to assess the relative value for money of different types of credit, as each has a unique pricing structure based on the term of the loan, the level of default risk posed, and whether there is collateral or not. It is therefore best to assess affordability per driver of use. In doing so, average interest rates in the particular country can be compared with those of other countries. FinScope Consumer Survey and qualitative demand-side research insights can also be drawn upon to unpack perceived affordability and customer satisfaction.

Appropriate product features: The appropriateness of the credit offering to the target market's realities and needs is an equally important consumer protection consideration. People that are desperate for credit may not pay sufficient attention to the features of the product, including the maturity and repayment terms. It may also be, for example, that a person does not have access to a productive loan and therefore takes out a personal loan instead, which is not appropriate to the purpose for which the loan is needed. The situation is exacerbated where consumer financial capability is low.

To assess appropriateness, diagnostic researchers should compare the client-facing product features (including type of loan, size of loan, and maturity and repayment terms) to the features of the target market as gauged from FinScope and qualitative demand-side research findings, posing and answering the following questions:

- What are the average income bands, and are typical loan sizes appropriate to persons of this income profile?
- What are the main drivers of use/needs for credit, and are the products on offer appropriate to those needs in terms of the types of loans, maturity and repayment terms? and
- Are certain types of credit offerings (by certain types of providers) more appropriate than others?

Appropriate terms or eligibility requirements: Eligibility is likewise very important in the credit sphere. Many people are denied access based on their income or employment profile, credit history or lack of collateral. The upshot may be that a person takes out a type of loan that is accessible to them (such as a personal loan) but not necessarily appropriate to their specific borrowing need. Or it may be that the person resorts to an informal moneylender, at a higher interest rate than charged in the formal market, as they are denied access to the formal system. It will be important for the diagnostic to unpack the particular dynamics in the country in question, as well as the interplay between eligibility, appropriateness and affordability.

Eligibility requirements for loans should be assessed for different types of credit/drivers of use and compared to the profile of the target market as gauged from qualitative demand-side research and FinScope. Reach conclusions on the extent to which eligibility barriers shape credit market dynamics and consumer protection outcomes.

7.5.2.6. The market for credit: related regulatory issues

Credit is likely to be covered under banking and non-bank financial institution regulation, but there may also be a dedicated regulatory framework for credit and a dedicated regulatory authority for credit. Some countries set limits to interest rates charged, which may differ by institution or type of loan, and some have usury exemptions for small loans. Some countries have specific consumer protection regimes or codes of conduct that will be relevant to credit.

As credit regulation can be quite complex and is interwoven with consumer protection issues, it is important to unpack the credit policy, and the regulatory and supervisory landscape, and to understand the specific regulatory and supervisory challenges as well as the access issues or consumer protection concerns that the regulatory framework needs to respond to. This allows you to take stock of the adequacy of the framework in achieving consumer protection objectives within the inclusion sphere, and what the challenges or imperatives are for the future.

For example:

Sound governance structures are key for both donor-funded and for-profit entities. What governance regulation is in place and what are the gaps?

Also consider how microcredit can be integrated into the overall credit and financial sector through tiering and graduation, and what the regulatory challenges are in this regard: is there potential to progress credit providers to providers of a wider set of financial services – and, if so, how would regulatory frameworks need to adapt to facilitate this?

7.5.2.7. The market for credit: gaps and opportunities

Reach conclusions on any specific gaps in the provision of credit across target market segments, as well as other challenges faced by the target markets in accessing credit. Importantly, also consider the appropriateness of the credit offering, levels of indebtedness and the sustainability of the credit situation of the target markets. Highlight any unscrupulous practices identified or any noteworthy consumer protection concerns.

In concluding on the scope for an inclusive credit market that provides value and does not exploit customers, explore the following emerging credit market themes and issues:

- Is there evidence of gaps in product provision (e.g. loans are available to certain market segments, but others have no formal options)?
- How can the credit market be extended without risking over-indebtedness? Specifically relevant here is the scope for productive credit;
- Is it possible to leverage off the extension of payroll credit while protecting consumers?
- How can the transition from donor-financed to sustainable self-financed entities be assured? What alternative sources of funds can be used?
- What complexities arise around funding structures, and how do these impact on the evolution of the market?

- What evidence is there of consumer abuse, and how best can it be addressed? and
- What linkages between markets impact on access to credit (e.g. the development of the deposit and capital markets)?

7.6. The market for insurance

The global Access to Insurance Initiative (A2ii) has published a dedicated toolkit for conducting an in-country insurance diagnostic. It provides a comprehensive analytical framework for an insurance diagnostic, as well as indicators to cover and process considerations. For the purpose of a MAP analysis, the A2ii toolkit is the primary source document and the details thereof will not be repeated here. However, it is important to note that, by its nature, the MAP diagnostic cannot be as detailed on the insurance component as a dedicated insurance diagnostic would be. In deciding what level of detail to cover, the 'master plan' (i.e. the MAP overarching policy objective and the research hypotheses that flow from it) should be the point of departure or disciplining factor.

Remember: In deciding which information to collect and analyse, the test for relevance should time and again be: Is this piece of evidence necessary to prove or disprove the MAP research hypotheses and realise the MAP overarching policy objective? This is the only way to ensure that the scope of the diagnostic remains manageable. So: only gather information relevant to the master plan!

Related links

A2ii (Access to Insurance Initiative). (2010). Access to Insurance Initiative – Toolkit No. 1 Microinsurance Country Diagnostic Studies: Analytical framework and methodology. Available online from: **www.a2ii.org/knowledge-centre/tools-and-guidance/a2ii-toolkits.html**

7.6.1 .Rationale

All people are exposed to risks that will impact on them financially. This prompts them to find ways to manage the impact of such risks – be it through savings, credit, community support, adapting of spending and work patterns, selling of assets, or through insurance. How people manage or respond to risks will differ between individuals (based on their risk appetite, financial resources, available risk mitigation mechanisms and understanding and perceptions of insurance) and across countries (based on culture and other factors, as set out in the demand-side toolkit – see **Toolkit 5**).

Insurance can be defined as an arrangement or contract whereby one party (a company, community-based structure or government agency) provides another party (an individual or a business) with a guarantee of compensation for a specified loss, damage, illness, or death in future, in return for the payment of a premium.

Traditionally, retail insurance markets in developing countries are relatively underdeveloped and serve only the upper end of the market. This means that those in the low-income or mass market have few formal options and often 'reinvent' insurance by pooling risks informally among themselves. However, various innovative models are coming to the fore that recognise the traditionally underserved market as a potential client base – in the process creating lessons on what it takes for such models to be viable, as well as regarding client value. Insurance targeted at the low-income market, broadly defined, is often referred to as microinsurance.

The purpose of the insurance part of the MAP supply-side diagnostic is to:

- Map the insurance landscape in the particular country in terms of the providers, product suite and distribution models;
- Understand the extent to which the landscape accommodates the mass retail/low-income target market; and
- Understand what it is that drives the development of the insurance market.

It will thus be important to understand market players' incentives and priorities, as well as the features of the current and pipeline product suite and the interaction thereof with the regulatory framework.

As discussed in Section 8 of this toolkit, distribution is core to more inclusive insurance markets.

7.6.2 .Aspects to cover

7.6.2.1. The market for insurance: drivers of use

As with the other product markets, drivers of use for insurance largely relate to the reasons for taking out insurance. Insurance responds to a number of consumer needs, including the following:

1. Individuals need to manage significant risks that will lead to unexpected costs or impact on their ability to earn an income.

For example:

o Should a breadwinner die, or should a person be in an accident or become seriously ill, it will impair the ability to generate an income and

Related links

Related links A whole literature has been developed, internationally, on the emerging models and unique challenges relating to microinsurance – broadly defined as insurance targeted at the low-income or underserved market. For an overview, see Churchill, C. & Matul, M. (2012). Protecting the Poor: A microinsurance compendium, Vol. II. Available online from: **www.munichre-foundation.org/home/Microinsurance/MicroinsuranceCompendium.html** lead to costs that the household budget will be unlikely to absorb; and

- The same holds for adverse weather impacting on crop yields or diseases affecting livestock.

2. Insurance can ensure the delivery of a service that a person finds critical and would not otherwise be able to afford.

For example:

- Many people in Southern Africa and Latin America value a dignified funeral and know that, by saving alone, they would not be able to afford it, should a family member die. They may also not want to incur debt in the eventuality of the funeral. Taking out a funeral insurance policy therefore guarantees them the appropriate service at the appropriate time, in exchange for a regular monthly premium;

- The same holds for health insurance where it enables access to healthcare; and

- Likewise, credit life insurance is necessary in order to obtain access to certain types of credit, including agricultural credit, small business loans, personal loans or home loans.

3. Insurance allows people to protect key assets.

For example:

- If you are a taxi driver, vehicle insurance will ensure that you do not lose your source of income in the event of an accident;

- Likewise, smallholder farmers may want insurance for their livestock or crops, or a household may want to insure its house against fire or flood.

There is often a cultural element to the reason for insurance demand. Thus there are also regional trends in terms of the dominant driver/s of use. In Latin America, for example, funeral assistance and extended warranties on appliances, are particularly strong drivers of use. In West Africa and India, health insurance through community-based risk pooling plays a dominant role.

Other typical drivers of use can include insurance taken out to comply with regulation (such as third-party liability vehicle insurance, workers' compensation, or unemployment insurance).

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See also Toolkit 5 the demand-side findings will inform the specific drivers of use identified alongside an assessment of the products on offer in the market.

7.6.2.2 The market for insurance: current usage

As with the other product markets, the FinScope Consumer Survey findings can be used to establish the number of people who have insurance in total and will also generally break usage down into life and general/non-life insurance. Mostly, the survey results will furthermore indicate the percentage of adults that belong to a community-based risk pooling group or otherwise insure informally. This analysis should be done for the total adult population, as well as across target market segments.

7.6.2.3. The market for insurance: providers

The supply-side diagnostic should identify and research the various types of insurance providers in the country in question and their relative importance or popularity in terms of serving the various drivers of use.

In the formal market, insurance can be provided by commercial insurers (which can be local or foreign, private or state owned, or a combination), cooperative or mutual insurers or, in some instances, directly by government. In the latter case, insurance is distinguished from social assistance in that government manages the risk pool according to insurance principles, rather than just as a social transfer scheme. Insurance can also be provided by third parties whose core business is supported by insurance, such as credit providers, health service providers or funeral service providers.

Where such entities conduct insurance in-house without an insurance licence (rather than just serving as a distribution channel for registered insurers), this would be an instance of informal insurance. Other examples of informal insurance would be risk pooling by community groups.

For example:

- o Community-based health schemes;
- o Agricultural or credit cooperatives; and
- o Burial societies.

7.6.2.4. The market for insurance: products and features

The diagnostic will cover the full landscape of insurance products in the particular country, but will focus specifically on those relevant to the previously unserved, low-income or informally employed market. This is typically referred to as microinsurance. Insurance products can be grouped according to the type of risk that they cover: life event-related products (often classified as life or sometimes as long-term insurance), asset-related policies (mostly classified as general insurance, sometimes called non-life) and health-related policies. In some countries, there is a regulated demarcation between insurance (life or general) as provided by insurers, and health insurance or medical aid as provided by medical schemes.

The following types of insurance products will be covered in the research and analysis exercise, and are discussed in more detail below:

- Life event-related policies;
- Asset-related policies; and
- Health policies.

Life event-related policies include:

- Life insurance;
- Credit life insurance;
- Funeral insurance;
- Unemployment insurance;
- Income replacement insurance;
- Education insurance;
- Critical illness insurance; and
- Personal accident insurance.

Typically, long-term contractual savings products, including pensions, would be excluded from the scope of the insurance side of a diagnostic, which deals primarily with risk products, but may be relevant for the savings analysis.

Asset-related policies include:

- Household structure and contents;
- Vehicle insurance;
- Extended warranties;
- Mobile phone insurance;
- Business insurance (e.g. for SMMEs); and
- Agricultural insurance.

Note: In many countries some policies classified here under life event-related policies – most notably personal accident insurance – would be grouped with asset insurance into the general insurance category for regulatory purposes.

Health policies include:

- Medical aid or medical schemes;
- Hospital cash plans;
- Dental plans; and
- Primary care plans.

When researching and analysing the insurance landscape, it is important to take note of the incidence and variety of products aimed at the financial inclusion target market.

Also track whether various types of insurance are provided on a compulsory basis (e.g. credit life insurance, which is a condition for a loan being taken out; or personal accident or other cover that is embedded in a bank account or mobile network subscription) or on a voluntary basis (with the consumer consciously deciding to buy the product).

Furthermore, ascertain whether the insurance offering is bundled with another financial service (e.g. credit), or is stand-alone, as well as whether the insurance product itself bundles cover for various types of risks, or covers a single risk event.

7.6.2.5. Accessibility of the market for insurance

As with savings, payments, and credit, the exercise to research and analyse insurance is followed by an accessibility assessment against the following four key components of the access framework outlined earlier: proximity, affordability, appropriate product features, and appropriate terms or eligibility requirements.

Proximity: As the discussion on distribution (Section 8 of this toolkit) shows, much of the emphasis in microinsurance innovation is on alternative distribution channels. The heart of the drive for alternative distribution is to i) place insurance within the reach of the target market, as well as ii) tap into existing groupings of people (be they clients of a retailer chain or bank, or members of a cooperative or association) in order to bring down distribution costs. Both speak to proximity issues.

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In many developing countries insurance branches are few and far between and only the minority of people are reached through a traditional one-on-one broker or agent sales model. The diagnostic should use both demand-side research insights and supply-side interviews to gauge how 'reachable' people perceive insurance outlets to be to them, as well as what the footprint of the insurance sector is – both directly through branches and agencies, and indirectly by leveraging the infrastructure of third-party client aggregators for alternative distribution purposes. The role of technology (e.g. mobile phone-based distribution) in breaking down proximity barriers should also be investigated.

Note: The term 'aggregators' is used to refer to third parties, including retailers, utilities, cooperatives or any other entity with an existing client or member base, that could be accessed for insurance distribution purposes.

Affordability: As with credit and savings, there is no affordability rule of thumb or threshold for insurance. Depending on the type of insurance, willingness to pay is likely to vary widely. For example:

- A person may be willing to pay a significant proportion of the monthly household budget towards health insurance (or funeral insurance in the case of some cultures), but will not prioritise scarce budget resources to pay an asset insurance premium.

Affordability should be assessed relative to the value offered by the insurance to the individual. Value, in turn, has a relative dimension: how affordable is the insurance relative to that of alternative risk management methods (such as taking out a loan in the event of an adverse risk event happening)?

Affordability should therefore be gauged in a qualitative way: by probing perceived affordability and willingness to pay in the qualitative demand-side research, and by understanding what alternative coping strategies people have and what the cost of these would be. In addition to the qualitative findings, typical policy premium levels could be collected for various classes of policies and then compared to the benefit level, to calculate the premium-per-benefit unit price as an indicator of value (which can then be compared across classes of policies and, where relevant, across countries). Typical or average premium levels for microinsurance-relevant products can also be compared to average or different scenarios of income levels for the target markets. This will allow for an informed discussion on likely affordability, if not an absolute assessment as to whether the product suite is affordable or not.

Appropriate product features: Appropriateness is an access criterion in insurance. Insurance can be quite complex, with detailed fine print, and it may be that the terms of the policy, as well as the types and levels of risks covered, are not appropriate to the actual needs or realities of the target market. Product features to consider include the following: whether the benefit is paid in cash or in kind (e.g. a funeral service or medical expenses); whether the product is stand-alone or embedded in another service (as described above); whether the sale of insurance is bundled with the sale of another product; and whether the decision to purchase insurance is voluntary or compulsory.

Appropriateness can be assessed by analysing the terms of typical microinsurance-relevant policies relative to the nature and realities of the target market (e.g. whether extended family members or foster children can be included on a policy). The demand-side research will also be an important source of perceived appropriateness.

Another important element of appropriateness is the value offered to the client by the insurance product. Often, insurance targeted at the low-income market has very low claims ratios (net claims paid over net premium income). That means that only a small proportion of the claim is paid back to clients in the form of claims paid, with the rest being consumed by distribution and other costs. Value can be assessed by tracking the claims ratio for various product lines.

Eligibility: Eligibility relates to whether a person is allowed to buy an insurance product or not. It will vary according to the type of product. Generally, asset insurance can only be bought by the owner of the asset, and for life insurance the person buying the insurance must have an insurable interest on the insured life. It may also be that certain persons are excluded from insurance based on their risk profile or, for example, due to prior medical conditions. The supply-side diagnostic should assess what eligibility requirements apply in microinsurance-relevant products, and to what extent these could pose access barriers. Supply-side interviews, analysis of product brochures and the findings from the demand-side research should be combined to render the necessary insights.

7.6.2.6. Market for insurance: related regulatory constraints and isues

See Diagnostic Resource B: Illustrative interview questions for a number of regulation-related questions to cover in the analysis; here, the focus is on highlighting regulatory constraints and issues related specifically to the insurance environment.

Insurance regulation is typically included in dedicated legislation, and in some jurisdictions there is a regulated demarcation between life, general and health insurance. Where jurisdictions strive to adhere to international

Something to think about

Importantly, in insurance it is perceptions that drive uptake decisions. Customer perceptions regarding the appropriateness of the insurance offering should therefore be taken as seriously as the actual state of affairs – even if the perceptions are thought to be ill-founded.

Related links

See the microinsurance key performance indicators as developed by the Microinsurance Network for more detail: Wipf, J. & Garand, D. (2010). Performance Indicators for Microinsurance. A handbook for microinsurance practitioners (2nd edition). Luxembourg: ADA microfinance expertise. Available online from: **www.microinsurancenetwork.org/publication/fichier/KPI_MI_Handbook_v2_EN.pdf**

See also: **www.microfact.org**

best practice without applying a proportionate response, it can lead to a regulatory framework that is not attuned to the realities of the domestic context.

Related links

www.gpfi.org/sites/default/files/documents/G20%20Principles%20for%20Innovative%20Financial%20Inclusion%20-%20AFI%20brochure.pdf

Note: International best practice is embodied in the Insurance Core Principles (ICPs) – the international standards and guidance for insurance regulation and supervision, issued by the International Association of Insurance Supervisors. The ICPs provide for proportionality in regulation and supervision. Proportionality is one of the nine principles for innovative financial inclusion adopted by the G20 Global Partnership for Financial Inclusion (ATISG 2010). Principle 8: Proportionality reads: 'Build a policy and regulatory framework that is proportionate with the risks involved in such innovative products and services, and is based on an understanding of the gaps and barriers in existing regulation'.

Potential regulatory issues include the following:

- Barriers to entry, in the form of prudential requirements and institutional limitations (i.e. not allowing cooperatives or mutuals to obtain an insurance licence) disincentivise formalisation;
- Intermediation regulation does not explicitly allow for alternative distribution channels, and agent or agency requirements are not in tune with the realities of the multitude of new salespersons entailed by alternative distribution. Microinsurance is said to be controlled by the distribution channel, which often controls access to the client and leads the initiative to offer insurance products. Such intermediaries often offer microinsurance as an additional product and service. It is therefore relevant to understand what the regulatory requirements are that the channel must meet – from the insurance regulatory authority as the intermediary, but also from the regulator of the underlying product or service;
- Regulation does not yet allow for electronic contracting or the risks of electronic commerce;
- A high compliance burden challenges cost-effective insurance provision and renders an unlevel playing field between regulated and unregulated players;
- A lack of supervisory capacity challenges formalisation and consumer protection. It also means that many supervisors do not actively monitor indicators of client value and hence do not respond to emerging market trends that erode client value;
- The absence of health regulation in the insurance legislation creates grey areas for unregulated medical aid schemes to operate;

Related links

IAIS (International Association of Insurance Supervisor). (2013). Insurance Core Principles, Standards, Guidance and Assessment Methodology, October 2011 (revised October 2013). Available online from: **www.iaisweb.org/Insurance-Core-Principles-material-adopted-in-2011-795**

- A lack of clarity in definitions and inconsistencies in regulatory requirements lead to ad hoc regulation and an unlevel playing field; and

- Insurance, by its nature, requires policyholders to trust insurers to deliver on a future promise. Insurance products are complex to understand and microinsurance products are often embedded in another service. All of these create potential consumer protection concerns: how can regulators ensure consumer protection without adding unnecessary costs?

The supply-side diagnostic should explore the extent to which these and other pertinent issues are relevant in the country in question.

Insurance is the one product market where international regulatory and supervisory guidance has been developed on inclusive markets, as contained in the 2012 IAIS Application Paper on Regulation and Supervision Supporting Inclusive Insurance Markets.

7.6.2.7. The market for insurance: gaps and opportunities

Reach conclusions on any specific gaps in the provision of insurance to meet needs for particular target market segments, as well as challenges faced by various target markets in accessing insurance. Such challenges may relate to the accessibility framework, to demand-side usage barriers, or to context aspects such as inadequate health services or underdeveloped agricultural sector infrastructure. Importantly, also consider the appropriateness of the insurance offering and whether it offers sufficient value to the client base, and highlight any noteworthy consumer protection concerns or trends.

Then reach conclusions on the main opportunities in terms of the size of the potential untapped target market, priority target markets and potential touch points for reaching them, and types of products and features that would appeal to the target market. Ask and answer:

- What are the challenges to unlocking this potential relating to the market, regulatory framework and context, respectively?

One of the key challenges remains efficient, low-cost delivery of appropriate products through distribution channels that are able to achieve take-up and ensure informed decisions. Ask and answer:

- How best can this be achieved in the particular context?

There are also important linkages between the insurance market and other product markets. Premium collection is one of the most important

Related links

Please refer to the application paper for a more in-depth discussion of regulatory issues and what a proportionate response would entail: IAIS (International Association of Insurance Supervisors). (2012). Application Paper on Regulation and Supervision Supporting Inclusive Insurance Markets. Available online from: **www.iaisweb.org/Application-papers-763** challenges to low-cost distribution, meaning that the payments market analysis can have important implications for the insurance analysis. Likewise, insurance is often offered on the back of credit, or savings and credit are used to mitigate insurable risks. Therefore also conclude, where relevant, on cross-product implications.

8. Distribution

Distribution or intermediation of financial services can be defined as the delivery of a product or service to the consumer (moving the product from providers to customers), as well as any interaction with the consumers. Distribution covers all steps in the financial services value chain between the financial services provider and the end client, including marketing, sales, product administration, cash-in/cash-out transactions, and disbursement or servicing by third parties.

Related links

See the Access to Insurance Initiative insurance diagnostic toolkit for a full discussion of the synthesis process: A2ii. (2010). Access to Insurance Initiative – Toolkit No. 1 Microinsurance Country Diagnostic Studies: Analytical framework and methodology. Available online from: **www.a2ii.org/knowledge-centre/tools-and-guidance/a2ii-toolkits.html**

Traditional vs alternative channels: In considering distribution channels, the supply-side diagnostic needs to look at all current and potential distribution channels, as well as the underlying infrastructure (including the payments system, technology platforms and physical infrastructure) required to bring products to market.

Distribution channels can be grouped into traditional channels and alternative channels (the latter defined as any emerging channel outside of the formal financial sector infrastructure that is traditionally used for financial services distribution).

Example channels to be researched and analysed include the following, shown in Table 1.

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Table 1: Examples of traditional and alternative distribution channels

Traditional distribution channels	**Alternative distribution channels**
Bank branches	Mobile network operators and their vendor networks
ATMs	Retail stores (including petrol stations, supermarkets, pharmacies and asset or white-goods vendors)
Point of sales networks	Informal traders or home-shops
Microfinance institutions	Agricultural distributors, input suppliers or processors
Savings and credit cooperatives	Service providers e.g. hospital service or funeral service providers
Brokers and agents	Utilities e.g. electricity suppliers
Credit unions	Informal societies or networks
Post offices	Labour unions or market associations

Channel convergence: The same distribution channel is increasingly used for the distribution of multiple financial services – a phenomenon that can be described as channel convergence. It is therefore no longer useful to consider distribution only by type of financial product/service (savings, payments, credit or insurance); rather, it becomes necessary to deconstruct distribution into its constituent elements or functions, and then to assess the nature of a country's existing and potential financial services distribution channels in terms of these constituent elements. The critical elements are the following:

1. Client acquisition: This entails any actions to register a client. Client acquisition (or sales in the case of loans or insurance) can be active (personal sales effort to sign up customers) or passive (relying on customers to respond to general marketing techniques, with no salesperson involved).

2. In-person client servicing: This refers to the situation where the client needs to conduct certain transactions or account maintenance duties face to face or over a telephone, but in each case a live person is required to interact with.

3. Distance communication: This refers to situations where a financial services provider communicates with a client without in-person contact e.g. through a call centre, by sending SMS or email updates to clients,

or by mailing product-related documents, or where the client is able to access the financial institution over a distance to make a transaction.

4. Collections: Collections might be of deposits, payments, loan instalments or premiums, collected in cash or electronically.

5. Payments: Payments can be in the form of withdrawals, cash-out of transfers, loan disbursement or insurance claim payments, in cash or electronic.

6. Technology platform: This refers to the information technology and management information systems that facilitate the various other distribution functions.

8.1. What do we want to achieve

Distribution plays a leading role in financial inclusion, as it represents the gateway to and interface with clients. Which distribution channel is employed therefore has a fundamental impact on clients' interaction with, trust in and understanding of financial services. Distribution is also often a significant cost component in financial services delivery. Innovations to bring down distribution costs – be it through the use of technology or through new distribution channels – are therefore at the forefront of financial inclusion developments internationally.

8.2. Getting going on the distribution channels

In terms of distribution, it is useful to consider the following questions:

- What channels are currently used to distribute financial services?
- What is their footprint and efficiency?
- Is it possible to increase the footprint with existing channels not yet used for the distribution of financial services?
- What are the incentives for and obstacles to using these channels? and
- Are there distribution opportunities between different financial services?

In analysing and listing the various distribution channels in the financial services landscape, we want to do the following:

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Hypothesis 9

Significant advances in financial inclusion in a particular market require business model innovation, whether in product or distribution.

Hypothesis 10

Convergence between the distribution channels used for different financial services can reduce the cost of rendering services and increase the value of financial services for low-income households.

Hypothesis 13

The pace at which financial inclusion can grow depends also on the level of physical, telecommunication, governance/institutional and social infrastructure of a country.

- Create an overview of existing distribution channels and their key features and footprint;
- Identify potential distribution channels;
- Describe the role of financial services distribution across different products and product providers;
- Explore the ability of and incentive/s to channels to offer financial services (including business model priorities) and to serve lower-income markets – particularly for potential channels;
- Explore the ability of and incentive/s to different channels to offer value to consumers;
- Identify instances of distribution innovation in the market; and
- Explore the impact of regulation on the ability of channels to intermediate financial services.

Why do we want to do this? By building an understanding of the distribution landscape across these elements, the MAP supply-side diagnostic will inform the following of the MAP research hypotheses that, in turn, speak to the overarching policy objective of improving welfare through a portfolio of financial services: innovation, whether in product or distribution.

8.3. Traditional distribution channels

Traditional channels used for financial services distribution are the starting point for the exercise to research and analyse distribution.

RATIONALE	As distribution is about reaching the market, it is important to understand the landscape and reach of financial services distribution outlets. The discussion of traditional distribution channels seeks to understand the following: • What is the reach of the traditional channel footprint? and • What are the challenges or limitations to distribution at scale through traditional channels?
Aspects to cover	• Number, geographical spread and level of connectedness (real-time electronic connection or not) of the branches of financial institutions and post offices; • Number and geographical spread of ATM and POS devices; • Current rates of expansion or contraction of branch networks, ATM and POS networks; • Categories, numbers and geographical concentration of MFIs, cooperatives providing financial services and other registered or informal community-based financial services providers, and the distribution/intermediation capacity of each category; and • Numbers of insurance brokers and agents, as well as non-bank agents permitted by law.

8.4. Alternative distribution channels

In addition to traditional channels used for financial services distribution, it is important to research and analyse alternative channels.

RATIONALE	This section of the supply-side diagnostic seeks to answer the following questions: • **To what extent are non-financial institutions being leveraged for the distribution of financial services?** Distribution partners may also enter as intermediaries, but then graduate to product providers in their own right. For example: Where a mobile network operator obtains a banking or insurance licence. • **Does distribution innovation decrease cost?** A key justification for the use of new channels and technologies (such as mobile) is the lower operating cost when compared to traditional means. Is this the case in the country in question? • **Why are alternative channels interested in financial service distribution?** Incentives drive behaviour. For example: A retailer that wants to increase profits by intermediating financial services will behave differently from one that provides financial services to facilitate cash management, enhance customer loyalty or increase in-store spending. • **Is there channel convergence?** For example: Are retail stores or mobile network operators distributing payment services as well as savings, credit and/or insurance? • **To what extent do the distribution channels control access to the client?** Some of the most interesting channels are not under the direct control of traditional financial service providers. • **What is the relationship with the client?** The nature of the relationship will determine the level of information that the channel has on the client, the degree of control over the client, and the ability to communicate with the client. The relationship between the channel and the client can range from a less structured client footfall (e.g. a retail store where a certain number of clients will pass through on a regular basis), to loyalty programmes or account-based relationships where there is a more direct communication channel to clients. • **Is the brand of the channel more important than that of the financial services provider in the eyes of consumers?** The brand of the intermediary is important in instilling trust and gaining customers for the financial service where the client associates the financial service primarily with the distribution channel. • **What is the main target market for different distribution channels?** Understanding who the channels' target market is will inform providers on whom they can reach through the respective channels.

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Aspects to cover	• Number, type and reach of alternative channels (in terms of number of outlets/agents and geographical footprint). In particular, note the following: o Which networks exist (e.g. retail stores or mobile network operator agent networks), and the size of such networks. This holds for current as well as potential distribution channels; and o The number of agents for different types of distribution channels, their skills or level of education, and the incentive structures that apply. • Emerging and established innovative distribution models in the country in question, and how they have evolved over time. • The variety of financial services distributed through various distribution channels; • The motivation for various distribution channels in distributing financial services; • The main distribution cost elements, noting differences between channels; • The management information and information technology systems that the various channels employ, and whether there are any connectivity or other system-related challenges; • The nature of the relationship between the distribution channel and the client, including the following: o Is it an employee relationship or not? Employee-based entities normally create opportunities for payments through existing salary payment mechanisms; o Is the organisation membership-based or not? Do members take collective decisions or not? o Is there a contractual client relationship or is it a casual relationship? and o How do clients make payments for goods and services purchased? • The brand value of the various channels, and whether financial services distributed through such channels are white-labelled under the channel's brand or not; and • The size of the respective channels' client base and which market segments they target.

Something to think about

Suppliers, products and distribution channels combine into particular models for extending financial inclusion. Often, the defining characteristics of a particular model relate to the distribution channel.

Diagnostic Resources B and C contain details on interview questions and data points to cover in order to build up the requisite distribution market picture.

8.5. Regulatory constraints and issues

Many of the regulatory issues relevant for distribution will be covered in the product market analysis. Here, the emphasis is on extracting information on distribution-specific issues.

RATIONALE	This section of the supply-side diagnostic seeks to understand the extent to which regulatory requirements constrain distribution, as well as any particular regulatory issues arising in the distribution sphere.
Aspects to cover	The focus is on highlighting regulatory constraints and issues relating to the distribution environment, most notably the following: • The playing field: This is about whether non-branch distribution/agent-based distribution is allowed and, if so, by whom and under what conditions. It is important to ascertain whether distribution regulation – across the various product markets – facilitates a broad playing field also for non-financial service providers to serve as distribution channels. If the playing field is restricted, what are the implications for the development of alternative distribution channels? • Regulatory challenges: Even if various players may distribute the product, there may be regulatory challenges to entry or expansion. For example: o Intermediation regulation regarding who can sell/intermediate and what requirements they must meet (qualification, competence or experience-related) could affect costs and incentives; and o Other regulatory requirements such as reporting requirements may serve as indirect barriers by impacting on compliance costs. • Convergence: Non-bank networks offering payment services are evolving from payments providers to agents of a wider set of services (financial and non-financial). Taking a bank-centric approach to regulating these networks may result in over-regulation of the agency function. The diagnostic should therefore assess whether a single channel is allowed to distribute more than one type of financial service. If so, under what conditions? If not, how does this impact on the scope for alternative distribution? • Electronic commerce: Is there provision for electronic contracting via mobile and internet-based channels? In what way does the presence or absence of such regulation shape distribution methods? • In-person client acquisition: To what extent do requirements for in-person client acquisition as well as KYC requirements under anti-money-laundering regulation and/or regulation combating the financing of terrorism impact on the accessibility of financial services and the reach of distribution channels? What are the main barriers in this regard? • Client ownership: Where non-traditional payments players are starting to assert client ownership as they are the gate-keepers to clients, what are the implications for consumer protection? Are regulators aware of such issues and, if so, how are they responding?

As we saw earlier with regard to payment-related regulatory issues, in evaluating the above questions, it will be important to ask and answer the following:

- What is the current situation?

TIP: In so doing, investigate the capacity of various supervisory authorities, and whether there are any jurisdiction issues between supervisory authorities or departments that are likely to shape distribution regulatory outcomes

- How does the current situation differ from the desired state? and
- What are the challenges in moving from the former to the latter?

Note: Furthermore, as payments are one of the core elements of distribution of other financial services, most of the regulatory constraints and issues discussed in terms of the market for payments (see Section 7.4.2.6: Payment-related regulatory issues in this toolkit) will also be relevant from a distribution point of view.

8.6. Gaps and opportunities

Given that distribution is a fundamental component of each financial service, and that different financial services increasingly converge on the same distribution channels, it is likely that conclusions on gaps and opportunities in distribution will already be reached as part of reaching conclusions on each of the product markets discussed above.

In concluding the distribution section, the focus should fall on the relative feasibility of various potential channels as financial services conduits – e.g. by looking at number and capability of agents/representatives, level of infrastructure, connectivity, link to core business, why interested in financial services distribution, and so on – as well as the overall reach and appropriateness of the distribution network in the particular country across the various product markets, what the main cost drivers or bottlenecks are with regard to distribution at scale, and how distribution relates to and brings together the respective product markets.

9. Conclusion

Toolkit 6 has focused on the challenging task of undertaking the supply-side diagnostic, which is a crucial source of information for broadening financial inclusion in-country. The three main focus areas for the supply-side research have been covered in detail: the provider landscape, products, and distribution or financial intermediation. The use of Diagnostic Resources A, B and C (in **Toolkit 8**) were emphasised as invaluable in conducting the stakeholder interviews and desktop research.

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