The Digital Remittance Revolution in South Africa

CHALLENGES AND NEXT STEPS FOR AFRICA'S LARGEST CROSS-BORDER PAYMENTS MARKET

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Executive Summary

Cross-border remittances originating from South Africa are of particular importance on the international stage. Nearly $2 billon is sent every year from South Africa to Southern African Development Community (SADC) countries, making it the largest inter-Africa remittances market. There are 3.2 million migrants from SADC countries in South Africa – of which 2 million are from Zimbabwe – working across service, agriculture, construction and other sectors. Many of these workers send over $60 per month to their families and friends in neighboring countries, representing a significant portion of their monthly earnings. On the recipient end, whole communities depend on this money to support their daily living expenses.

Sending remittances from South Africa is traditionally expensive, with an average cost per transmission (or "send") of 18 percent of the total remittance along formal channels, compared with a global average of approximately 10 percent. Sending along unsecured, informal channels can incur even higher costs – especially when adjusted to reflect the risk of loss – as these channels are not secured or regulated. However, a number of new formal remittances-services providers have recently entered the market with disruptive products that use modern payments technology. Using a cost-effective model, these providers have great potential to reduce the fees for digital remittances, with providers charging between 5 and 10 percent of the value of remittances sent. They are also more accessible than traditional formal services, offering senders the option to initiate remittance payments by phone, online, or in stores. On the receiver end, remittances can be collected straight to account (leveraging the expansion of lightweight and mobile accounts in the region) or at partner stores.

Despite this digital revolution, 60 percent of remittances sent from South Africa travel on informal channels due to a number of barriers to adopting formal remittances services. The first is cost. Not all service providers have dropped their fees significantly enough to attract users away from known channels. The second is documentation. While some new players are taking advantage of lower documentation requirements, others have not invested to update their systems. The third is financial inclusion. Limits to inclusion levels, particularly on the recipient end, prevent users from being able to access digital remittances services that are designed to interact with formal accounts. Financial literacy is, relatedly, still very low in countries like Mozambique. Finally, access to technology, such as ATM and POS terminals, inhibits broad expansion of these services by creating a dependency on cash.

By acting in a coordinated way, the multiple actors in this market have the potential to capitalise on over $1 billion in uncaptured send value. Continued product development can refine the offering, including the development of interoperable remittance platforms that foster economies of scale and greater competition. Providers and regulators working together on educational materials could increase take-up. Finally, a clearer road-map for future regulation in this space should help to facilitate investment by all providers. By working together, stakeholders can move towards a more open market that allows all remittances users the option of a formal, secured and low-cost service – ensuring more money ends up in the hands of those who need it most.

Introduction

Cross-border remittances originating from South Africa are of particular importance on the international stage. Totaling nearly $2 billion per year, they comprise the largest intra-African remittance corridor. However, this corridor is also one of the most expensive in the world, with an average cost per transmission (or "send") of 18 percent of the total remittance along formal channels, compared with a global average of approximately 10 percent.[1] Sending along unsecured, informal channels – still the most common method – can incur even higher costs, especially when adjusted to reflect the risk of loss.

The huge potential to improve the effectiveness of the South African remittance corridor lies both on the supply side, through the emergence of new market players offering competitive offerings, and on the demand side, through the adoption of digital channels that offer lower costs and greater security for senders and recipients.

Since many recipients of remittances are dependent upon this income to meet their daily living costs, improving access to affordable, secured, digital channels would directly improve the lives of the communities supported. This report – a collaboration between the global payments technology company Visa and the nonprofit organization TechnoServe – recommends steps to increase the efficiency of the market for the benefit of migrants, their families and surrounding communities.

Research for this report was conducted between October 2015 and February 2016.

Glossary

Digital remittances: mechanisms for sending money using electronic systems for the "settle" and "exchange" part of the channel

Exchange: the process of crediting the recipient's account by the sender's account

Formal channels: regulated mechanisms for sending money, almost always digital

Informal channels: unregulated mechanisms for sending money, typically cash transfer

MTOs: Money Transfer Operators – entities focused on providing remittances services

Payment-in or cash-in: the mechanism by which the sender credits the remittance transaction

Payment-out or cash-out: the mechanism by which the recipient collects the remittance

Pure digital remittances: digital payments that also incorporate cashless "payment in" and "payment out" into the remittance chain

RSPs: Remittance Service Providers – all entities offering remittance services

SADC: The Southern African Development Cooperation, representing 15 countries in the region

SARB: South African Reserve Bank, the regulator for remittances in South Africa

SIRESS: The System for Real-Time Electronic Settlements

Settlement: A daily netting of "exchange" value between corresponding banks

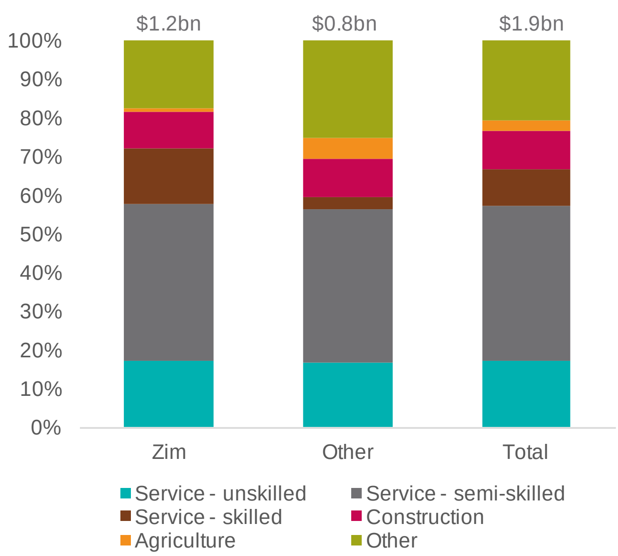
[1] Remittances Prices Worldwide; TechnoServe analysis

Millions of Remittances; Billions in Value

The market for remittances from South Africa to other countries in the Southern Africa Development Community region is estimated at around $1.9 billion per annum, based on a total migrant population of 3.2 million.

The main senders of remittances from South Africa are the 3.2 million migrant workers from neighboring countries, 2 million of whom come from Zimbabwe. Based on field research with 86 migrant workers, TechnoServe segmented migrant workers into different types, and apportioned average send values and frequencies. Combining this information, TechnoServe was able to estimate the overall value of the remittance market, according to worker segment. Across all migrants from the SADC region, the average send value is around 63 per month, or 20 percent of a sender's average earnings.

Figure 1: Remittance value by migrant worker type and remittance destination country



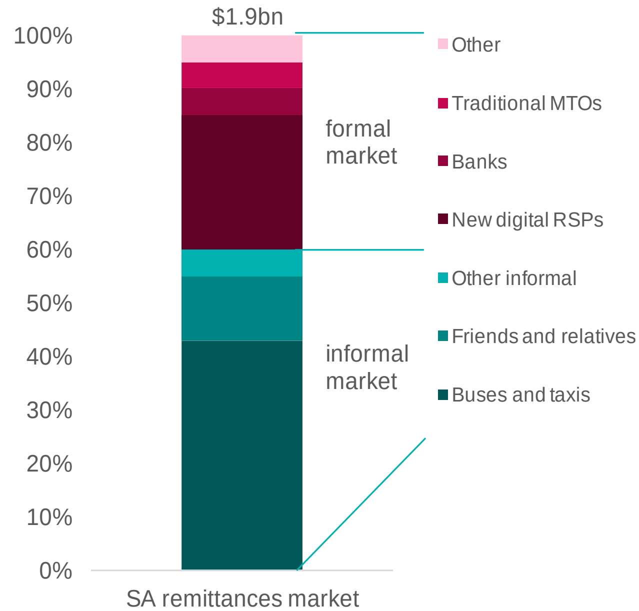
The service sector is the largest contributor to the remittance market, accounting for approximately $1.3 billion of value sent. Two other significant sectors are agriculture and construction. While historically important, the mining sector no longer attracts large numbers of foreign migrants, and is therefore not a major factor in the cross-border remittance market.

Remittance senders in the low-to-mid-income segments account for 90 percent of the overall market. This is not because these segments account for the vast majority of migrant workers but, importantly, because they send much more in proportional terms than their high-income counterparts. Our research shows that remittance send amounts are determined more often by the recipient's needs and dependency levels than by the sender's income. This is not surprising considering remittances are a lifeline for those who receive them, and are to be spent on items such as food, school fees and healthcare.

A Digital Remittance Revolution

While informal channels still account for 60 percent of the market for remittances from South Africa, new Remittance Service Providers (RSPs) are rapidly gaining share.

Figure 2: Market breakdown by channel

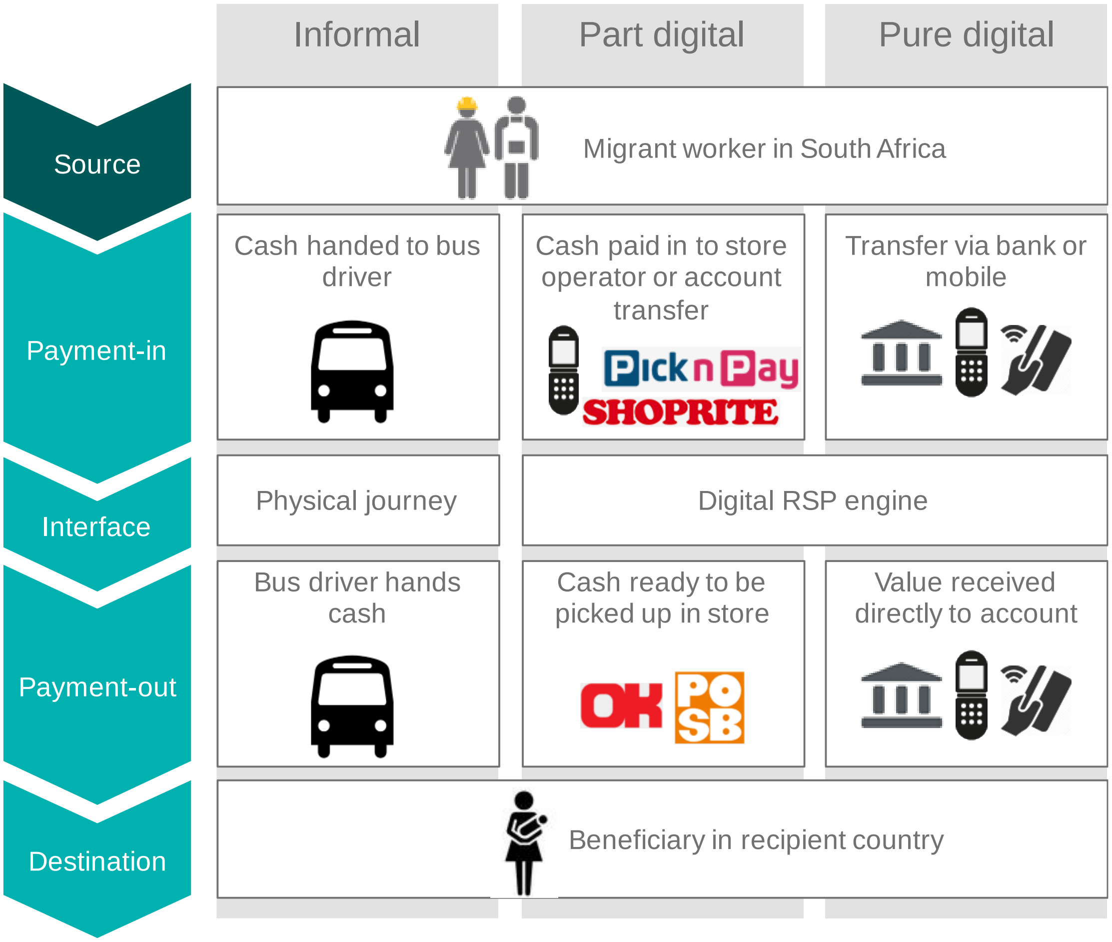


Informal channels are generally unsecured and expensive, costing up to 20 percent of the value sent. Entrepreneurial bus and taxi drivers offering delivery of cash and goods make up the majority of the informal market. However, these channels offer no security to the user; moreover, they may take several buses and/or require the recipient to travel a long distance to collect the remittance at a designated stop.

The traditional formal players include banks and traditional Money Transfer Operators (MTOs), such as Western Union and MoneyGram. Their services are also relatively expensive in South Africa, typically costing between 15 and 20 percent of the value sent, and often involving onerous procedures, making them difficult to access. Banks in particular tend to market their remittances services to existing customers, which can limit these services to senders and recipients who have bank accounts (although some exceptions do exist, such as First National Bank South Africa’s “Send Money” service).

New, dedicated RSPs have been emerging over the past five years and have rapidly gained traction, accounting for 25 percent of the overall market. These RSPs provide specific remittances services along digital rails, and usually operate using partnerships that can provide cash-in and cash-out mechanisms. These partners are typically stores, banks or mobile wallet providers, and have great potential to reduce the cost of secured remittances, with providers offering between 5 and 10 percent of the value of remittances sent. In South Africa, the largest single RSP by market share is Mukuru, which alone accounts for 20 percent of money transfers to Zimbabwe, and covers six other geographies through a series of partnerships with operators handling payment-out for recipients. Other new providers attracting attention include Mama Money and Hello Paisa, both of which focus on pure digital mechanisms, using mobile phones to initiate and/or collect payment.

Figure 3: Illustrated remittance examples



Barriers to Adopting Digital Remittances

A number of barriers remain to accessing digital channels. Until these are addressed, many migrant workers will still entrust their hard-earned cash to informal channels, and risk losing it in the process.

The barriers to adopting more formal sending methods include cost, documentation, access to technology and supporting infrastructure, and financial literacy.

COST

The lower price advantage of formal remittance channels may not be as compelling as it first seems. Although some RSPs have lowered fees to 5 percent of the value sent, these are mainly niche-service providers operating along purely digital rails. Mukuru, the largest player by market share, sets its fees at 10 percent of the value sent. While a big improvement compared with most informal providers, this may not be enough to attract some customers to switch, given the other barriers we explore below.

Moreover, some formal remittances contain hidden costs. For instance, remittance channels that tie transfers to vouchers or involve the purchase of goods from one side of the border to another can be more expensive than purchasing goods in South Africa and sending them on informally organized transport.

Overall, RSPs' margins are still protected by the limited number of players in the field who partner with the main cash-in and cash-out providers. We expect that greater competition will drive these margins down in the future.

DOCUMENTATION

Documentation requirements continue to represent a barrier to the adoption of formal services. There have been significant advances within the regulatory space to reduce these requirements, including the introduction of "FICA light" registration, which allows for small sums to be sent with just a simple ID. However, not all RSPs have adopted light registration. Banks and traditional MTOs in particular have not considered it an investment worth making – in part a risk-averse decision in case the trend toward reduced requirements is reversed – and this means that their products do not meaningfully compete for the low-income worker.

Figure 4: The "FICA light" remittance exemption

	Before June 2015	**After June 2015**	
Applies to: Documents required:	All customers	Small, single transactions	FICA "business relationships"
ID	✓	✓	✓
Proof of residency	✓	✗	✓
Source of income	✓	✗	✓
Source of funds	✓	✗	✓
Reason for sending	✓	✗	✓
Restrictions		Person-to-person Limit of <R3,000/day and R10,000/month (cross border) or <R5,000/day and R25,000/month (domestic)	

Perceived issues around documentation can be as dangerous as real ones. There is a generally-held view among migrants that forms to access financial services are near-impossible to complete. Banks and traditional MTOs in particular should not only try to make the process easier, but should also work hard to win the trust of senders, and demonstrate that the registration process is not as painful as they might fear. This includes communicating to migrants that the financial services industry is separate from border authorities – a key concern given that many migrants lack work documentation.

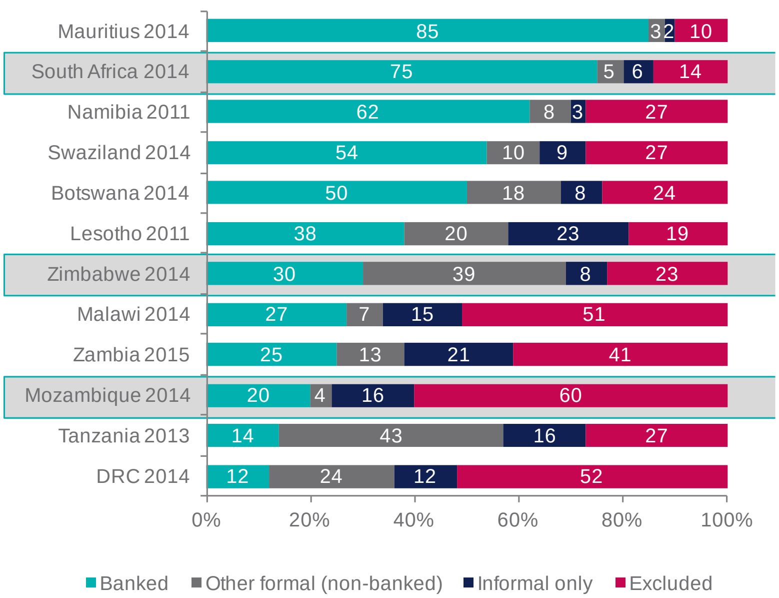
The SARB and the SA government have a clear role to play in providing clear assurances to providers that regulation requirements will continue to become less, rather than more, onerous. This will encourage RSPs to make the required investments to simplify their customer-on-boarding processes and systems.

FINANCIAL INCLUSION

The financial inclusion levels of the sender *and* the recipient are important in remittance selection, as both must be connected to the chosen channel. Key factors include:

- The ability of the sender to access, and discern between, different channels for cost, reliability, security etc.
- The recipient's ability to understand and access financial products that can be used as a vehicle to receive money (bank accounts, m-wallets, etc.).

Figure 5: Financial inclusion levels of SADC countries



Source: FinScope Consumer Survey Zimbabwe 2014

There are important differences in financial inclusion between Zimbabwe and Mozambique. For instance, 60 percent of the population of Mozambique is completely excluded from any kind of financial service (bank, non-bank or informal), whereas this is only true for 23 percent of the population in Zimbabwe, due to an established and competitive market for mobile wallets and easy-access accounts. These lightweight accounts can serve as reception points for straight-through digital payments via some of the emerging RSPs – including Mukuru, Mama Money and Hello Paisa – negating the need for the remittance recipient to travel to a collection point (although if they need to access cash later, they will need to use the agent or bank network of their account provider). Senders are acutely aware of any additional costs to the recipient who is dependent on the remittance. For rural recipients without a formal account or m-wallet, using a formal channel implies a journey to the nearest town or city to pick up cash, which can be costly in terms of transport and lost time that could be spent generating income.

Financial literacy is an important counterpart to financial inclusion. To some extent, a more accessible supply of formal products can itself drive financial literacy as sender and recipient communities find it easier to take up services and, in turn, educate one another. However, the lack of financial literacy is also often a barrier to adopting formal services, particularly in the case of remittances. For one, remittances include layers of cost, such as a transfer fee, an exchange rate margin, and sometimes an ongoing account cost, which can be difficult for the remittance user to unravel. Secondly, documentation and access are still in many cases more complex for remittances than other financial services products, although this is changing with the advent of FICA light, as outlined above.

ACCESS TO TECHNOLOGY AND SUPPORTING INFRASTRUCTURE

Access to technology and infrastructure is an important driver of financial inclusion. Low levels of mobile phone ownership and underlying telecommunications connectivity, particularly in countries like Mozambique, has limited the uptake of domestic digital payments, including m-wallets. However, linking digital sends to mobile wallets has huge potential in terms of reducing recipient costs (both real and opportunity) to collect remittances, as well as offering a secure store of value for recipients to keep remittances. Improving digital infrastructure is therefore a pre-cursor to increasing financial inclusion levels, which in turn will help to drive take-up of digital remittances.

The Road Forward: Maximizing Digital Potential through Collective Action

The informal remittance market from South Africa offers a prize of over $1 billion in total send value for formal providers. Assuming an average fee structure of between 5 and 10 percent, this represents between $50 million and $100 million of uncaptured fee value for RSPs. Unlocking this value will require coordinated action between providers, regulators and other industry stakeholders.

REFINE AND CUSTOMIZE PRODUCTS TAILORED FOR THE LOW-INCOME MIGRANT WORKER

Migrant workers and their families have specific needs that, in many cases, are still being better served by informal services, despite the higher cost and risk involved.

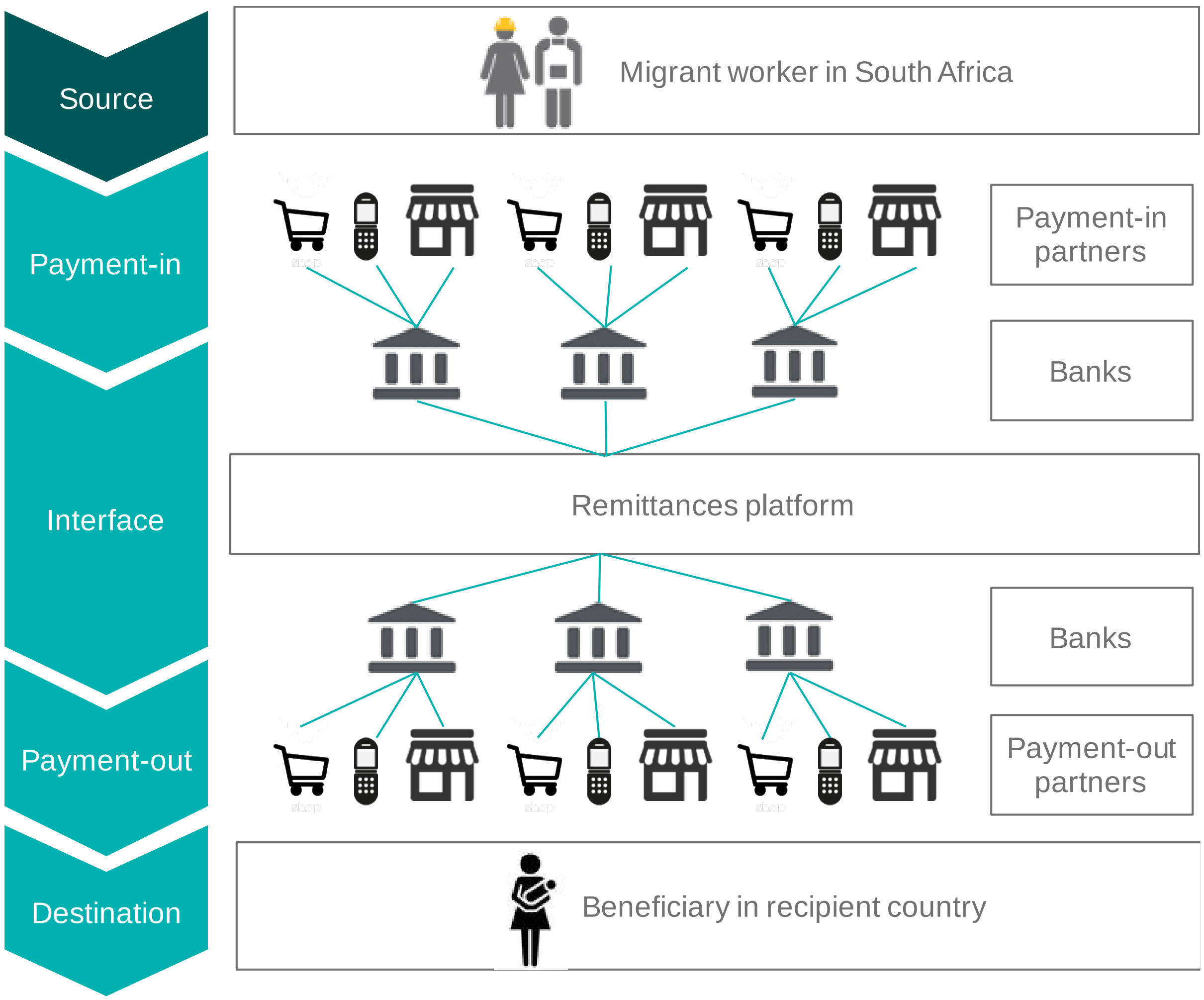
First, RSPs should work to **widen the cost advantage of their products** over the alternatives.

Second, they should improve access as broadly as possible by taking advantage of **reduced documentation for registration**, and by **bringing the payment-in and payment-out to the doorstep of both sender and recipient**, by including agents, stores and m-wallets in their distribution partnerships. RSPs working in urban hubs in South Africa have been successful in expanding their sender base; however much less has been done to bring payment services to rural locations.

CO-CREATE INTEROPERABLE REMITTANCE PLATFORMS

The most successful new RSPs **offer a variety of mechanisms** to maximize the number of payment-in and payment-out options for each unique sender-recipient pair. Rather than see these mechanisms as a series of negotiated partnerships, the future lies in **interoperable remittance platforms** which can provide the “switch” to exchange and transfer money between the bank accounts of distributors at the payment-in and payment-out end of the remittance chain **using standardized messaging and processes**. Rather than requiring each partner to invest in integration costs, such platforms would achieve greater economies of scale. Furthermore, the expansion of partnerships will invite greater competition on both the send and receive end.

Figure 6: An interoperable remittance platform approach.



Industry standardization across all parts of the payment process will help to facilitate the development of interoperable platforms, driving competition between them and lowering costs. SIRESS, the system for real time electronic settlements in the SADC region, is expected to expand its settlement infrastructure to include non-bank providers in the future, meaning that these providers can also benefit from more efficient daily netting of owed balances between institutions. Similar standardization of messaging and clearing processes will enable more efficient cross-border payments between multitudes of different actors. Regulators and the banking associations can help to set standards for secure messaging and payment systems.

WORK TOWARDS A CLEARER ROAD MAP ON REGULATION

Moves by the South African Reserve Bank (SARB) to ease documentation requirements for those sending smaller remittances are welcome. However, many financial services companies have not yet invested in updating these requirements within their systems, because legacy systems can be complex and expensive to update. Increased clarity from regulators about the **future road map for regulation, including documentation requirements**, will help to drive those investments without fear of regulation reversal. Furthermore, **banks should invest upfront to make their systems more agile** in order to reduce the expense of updating processes. Cooperation between regulators across the SADC region is also advised to ensure that requirements are consistent for all geographies, regardless of the direction of the payment.

WORKING TOGETHER ON AWARENESS AND FINANCIAL LITERACY

Financial literacy can accelerate the uptake of new digital remittances channels by improving customer understanding of how to choose between and access different channels. Through door-to-door marketing efforts, some RSPs have increased awareness and understanding of digital channels, but this activity has been focused within certain urban hubs due to commercial viability. Moreover, a social agenda to increase financial literacy for the benefit of both migrants and the broader industry would go beyond single product marketing. Industry players, public bodies and other stakeholders – for example church groups, migrant societies and savings groups – would be advised to come together to invest in awareness-raising programs to help migrants understand the benefits of digital channels and how to access them.

Awareness-raising on remittances could take many forms, from **targeted education programs** delivered by local organizations, to **mass media campaigns**. Leaflets and SMS learning platforms could be used to deliver clear instructions to migrants on how to access different channels. Another idea that merits particular mention is a **single-point database** that outlines remittances options by corridor, including latest pricing data and information on how to access each option. This would build on the information available through Remittances Prices Worldwide, a website developed and maintained by the World Bank.

Lastly, all service providers have a responsibility to deliver **responsible marketing including financial literacy education** if required, alongside **transparent communication of pricing and terms** to customers.

Bringing the Strands Together: What Next?

With new players reaching the mass market with formal products for remittances for the first time in South Africa, we are now at the advent of a digital revolution for remittances. The current transition has been achieved by a handful of disruptive players and a regulator willing to open up the market. The next phase of the digital revolution in remittances from South Africa will need to ramp up innovation and coordination in order to reach those last remittance users still reliant on informal channels.

Each stakeholder has an important role to play. RSPs should drive the continued refinement and customization of their services for the low-income migrant. They should also support payments systems operators, who will lead the co-creation of interoperable remittances platforms to foster economies of scale and greater competition. Banks should become more involved in this important market by adopting more convenient and accessible means of cross-border payments, and by underwriting other service providers. Government and regulatory authorities will also be critical in setting the roadmap for future regulation, encouraging all-important investment in new offerings and supporting systems by RSPs and supporting actors. We outline the incentives, capabilities and priorities for action of each of the stakeholders in *Appendix 1*.

Greater use of formal remittances services has benefits to everyone. New and traditional RSPs benefit from a greater “pie” to capture market share. Banks and financial services providers benefit from increased trust in formal services, which has a knock-on effect for other services, from domestic payments to savings and loans. The government and regulator will be able to more readily meet their mandate for financial inclusion, as well as having increased visibility of an important cross-border flow. Finally, by lowering the cost and raising the accessibility of formal services, more money can arrive safely and securely in the pockets of dependent remittance recipients. Only by adopting a joint sense of ownership will stakeholders be able to generate much needed improvements in the industry, so that all can reap the rewards.

Appendix 1: Incentives, Capacities and Priorities for Remittance Stakeholders

Stakeholder	Incentive	Capacities	Priorities for action
Banks	Use remittances as lead product to widen customer base Increased trust and use of formal financial services generally	• Bank infrastructure (branches / ATMs) can be used for payment-in and payment-out (including for non-bank customers) • Connecting bank accounts for payment-in and payment-out (bank customers only) • Membership of international banking systems (e.g. SWIFT) facilitates payments • Membership of SIRESS facilitating settlement of intra-bank balances • Role as sponsoring banks of non-bank FS entities, providing comfort for regulators	• Implement straight-through processing and relax documentation requirements to make services more convenient • Joint platforms to offer cash-in and cash-out services for remittances channels, outside of existing bank customer base • Invest in more agile systems to be able to absorb changing regulation

Government and regulators	Mandate to facilitate financial inclusion nationally (with Treasury support)
	
	Desire to increase visibility of cross-border payments
	
	Attract diaspora remittances to bolster economy
		• Authority to set framework for:
		  • sender documentation requirements
		  • pricing fairness and transparency
		  • regulating competition
		• Expertise on financial literacy
		• National-level coordination
			• Set clear roadmap for documentation, incentivise investment by banks and RSPs to integrate new requirements into systems
			• Encourage expansion of partnerships between RSPs and distributors; facilitate development of broader payment platforms; lower the barriers of entry for non-banks
			• Oversee national awareness and education programmes
			• Oversee standardised messaging and payments systems for the industry
			• Develop and maintain a remittances-information and cost-comparison database
			• Consider opening up cross-border payments to mobile-money operators

<table>
<tr><th>Stakeholder</th><th>Incentive</th><th>Capacities</th><th>Priorities for action</th></tr>
<tr><td>New digital RSPs/ MTOs</td><td>Increase customer base</td><td>• Existing customer base of remittance senders and recipients
• Remittances systems and infrastructure
• networks of marketing agents in migrant-dense areas (in some cases)</td><td>• More tailored products with lower price points and improved accessibility
• Develop common remittance platforms; utilise standard messaging and payments processes; increase interoperability to maximise payment-in and payment-out options
• Use of marketing agents to facilitate broader education/awareness of digital remittances
• Transparent pricing and access information; collaboration with national database</td></tr>
<tr><td>Payments system operators (e.g. VISA)</td><td>Use remittances as lead product to widen customer base</td><td>• Existing cross border payments system
• Relationships with all major banks</td><td>• Provide payments switch for remittance platform between banks, new RSPs, MTOs etc.
• Bring in existing (bank) and new relationships to broaden payment-in and payment-out options</td></tr>
<tr><td>SADC Banking Association</td><td>Reduce costs to banks associated with offering remittances</td><td>• Existing infrastructure for common regional electronic settlement (SIRESS)
• Can bring together capacities of regional banks including recipient countries</td><td>• Facilitate and manage SIRESS including widening to non-banks
• Represent regional banks in development of common remittances platforms</td></tr>
<tr><td>Large retailers</td><td rowspan="2">Offer remittance payment-in or payment-out service to increase footfall and sales</td><td>• Existing retail infrastructure which can be used for payment-in and payment-out
• Trusted service providers holding existing relationship with potential remittance users</td><td rowspan="2">• Participate as distributors on common remittance platforms
• Offer basic pricing and access information to remittance users</td></tr>
<tr><td>Individual small businesses</td><td>As above, plus:
• Physical accessibility especially in remote and poorly serviced geographical areas</td></tr>
<tr><td>Mobile phone service providers</td><td>Increase customer base through offering value-add services</td><td>• Network infrastructure providing access to e-bank and m-bank tools
• Operating mobile money services</td><td>• Participate as distributors on common remittance platforms
• Potential to expand mobile money systems to operate cross-border, if regulator allows</td></tr>
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