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Digital Financial Service Delivery to Poor Communities in South Africa: A Preliminary Assessment

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The integration of Information Communication Technology (ICT) into financial service delivery in South Africa has gained momentum. The rapid growth of ICT use in banking has brought a major focus on how it can be used to extend financial services to previously excluded poor communities. The paper highlights key developments in the banking industry in South Africa which include new mergers and acquisitions, ICT-driven service innovations, implementation of the Financial Services Charter Black Economic Empowerment (BEE) and a proliferation of new financial regulations. How these changes will collectively enhance access to banking services by previously neglected majority poor remains unknown. The paper describes emerging digital financial services such as Supermarket Banking, Mzansi Account and Portable Branch networks in the development of a more socially inclusive financial service sector in South Africa. The ultimate success of South Africa's financial service sector depends on how banks will adapt the new digital products to penetrate previously untapped markets in poor communities and reduce the digital divide in financial service delivery.

Field of Research: ICT for Development in Africa

1. Introduction

In South Africa, the black population has historically had limited access to financial services (PricewaterhouseCoopers, 2005). It is estimated that about 18 million South Africans have no access to banking services and majority of these individuals reside in townships and rural areas (Kitten, 2005). A decade after Independence in 1994, questions are still being asked about how to improve access to banking by marginalized communities. Without paying serious attention to these concerns, most of the black population will continue to face difficulties accessing financial capital, and their participation in the mainstream economy will remain peripheral.

The South African banking industry is facing several strategic changes with significant consequences for untapped markets. The industry stands at the cross roads of rapid economic growth estimated at 4.0% per annum in 2004, structural changes arising from new acquisitions and mergers, electronic communication technology (ICT) innovations, and a proliferation of new regulations. These changes will alter the strategic direction of the industry and unleash new opportunities to serve disadvantaged communities that have not received such services before.

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The emerging "information society" offers hope to poor communities to access financial capital required to help alleviate poverty and enable them to participate in the mainstream economy. The advent of ICT revolution presents a new challenge to banking institutions; to identify innovative financial service delivery to low income earners and penetrate new market segments. Therefore, banks need to become sensitive to the benefits of a more inclusive financial sector. Broad-based access to financial services enables the poor to participate meaningfully in economic development and help uplift their livelihoods. The use of ICT in financial service delivery has illuminated the debate on closing the "financial divide" in underserved communities.

The exclusion of poor communities in financing arrangements is a common phenomenon throughout Africa (Lwiza and Nwankwo, 2002). Instead, the urban elite or the more affluent, and large businesses have tended to dominate most of the share of financial resources from commercial banks. Exclusive financial service delivery has been justified on the grounds that it is costly to service the poor communities. While economically justified, continued "financial divide" is socially and politically unacceptable. For marginalized communities, ICT offers a source of hope to improve their access to finance at the lowest possible cost. Improved flow of financial capital to the poor has both a political and equity appeal particularly as it helps in building a more inclusive and socially cohesive economy.

Although digital financial service (i.e. used interchangeably with electronic banking) delivery has started to attract some interest from researchers in South Africa (Singh, 2004; Cracknell, 2004). Few research studies focus specifically on the complex issues surrounding extending the technologies to historically disadvantaged poor communities. An earlier study confirmed that ICTs are powerful instruments for empowerment, income generation and poverty alleviation (Kenny, 2002). In this vein, the growing importance of remittances in fighting poverty has introduced a new dimension on the role that ICT could play in facilitating financial transfers to poor communities in South Africa. The full potential of ICT as a catalyst for extending financial services to the poor in South Africa remains unknown. Therefore, given the foregoing, and the fact that the previously excluded poor communities constitute an untapped growth market, understanding the potential uses of ICT-based financial services and their diffusion especially among the relatively poor communities in South Africa is important.

The objective of the paper are to (i) highlight key changes taking place in the South African banking industry, (ii) describe digital services (and products) that are being made available to the poor communities and (iii) suggest ways to enhance access to digital financial services by disadvantaged poor communities. This paper is organized as follows; the next section provides an overview of the changes shaping the South African financial services sector. This is followed by a description of the methodology and literature review. After that, the paper describes emerging digital financial services for poor communities followed by a conclusion with remarks on future research areas.

1.1 Overview of Developments in the Banking Sector in South Africa

South Africa has one of the leading banking infrastructures compared to the rest of Africa (i.e. four major banks namely Standard Bank, Amalgamated Banks of South Africa (ABSA), First National Bank (FNB) and Nedbank; 31 million retail accounts, 2, 500 branches and 12, 500 Automated Teller Machines (ATM) (PricewaterhouseCoopers, 2005). The banking service market share is highly concentrated as the top four banks occupy approximately 98 percent of the sector assets while the remaining 2 percent is attributed to 11 other small banks (PricewaterhouseCoopers, 2005).

A number of key changes are taking place as banks position themselves to enter new markets and serve previously excluded poor communities. Firstly, the industry has experienced a wave of acquisitions the latest one being Barclays Bank's take-over of ABSA. Also, South African banks have made inroads into regional African markets. How the wave of bank consolidation will

transform the financial service delivery and assume a pro-poor community orientation remains to be seen.

Secondly, South African banks face a plethora of new regulations aimed at promoting financial business ethics and preventing financial fraud. These include the Consumer Credit Bill, amendments to the Competition Act, and the Financial Intelligence Bill (FICA). The National Consumer Credit Bill is aimed at improving credit accessibility, regulate credit bureaus and determine a ceiling on interest rates charged on micro-loans (Business Times, 2005). The Competition Act aims to promote a competitive banking environment while FICA is expected to minimize the negative effects of global financial crimes.

Thirdly, the financial sector has adopted a Financial Services Charter to drive transformation, promote employment equity and ensure that banks reach out to the "unbanked" and "under-banked". However, the jury is still out on industry-wide perceptions on whether the Black Economic Empowerment strategy is a threat or an opportunity (PricewaterhouseCoopers, 2005). An extensive assessment of the macroeconomic policies in the banking sector is beyond the scope of this paper, but it suffices to highlight that technology utilization by the poor will not occur in a policy vacuum given past disparities.

Fourthly, South African banks are actively involved in the provision of digital financial services to their clients (Singh, 2004). But the extent to which the digital services will afford banking opportunities for the poor remains unclear. For instance, Internet banking is a low cost form of service delivery that is growing in South Africa, yet its efficacy in reaching the poor is doubtful. The direct and indirect benefits digital innovations bring to the poor require scrutiny; and also whether or not the new forms of financial service delivery are sustainable. This paper argues that pro-poor digital financial services help to eliminate social exclusion, enhance accessibility, and uplift living standards for the majority poor.

2. Literature review

For most banks throughout the world, ICT have become the back bone of financial service delivery and finance networks have shifted from paper-based to the digital mode (Grace, 2004). However, digital financial service delivery confronts a number of challenges regarding its efficacy in closing the "financial divide" affecting the poor. Although e-banking is considered an inexpensive way to reach clients, its accessibility is hindered by a number of factors including poor Internet penetration, lack of e-banking awareness and customer inflexibility to new technology (Sohail and Shanmugham, 2002).

In developing countries most of which are characterized by extreme poverty and poor infrastructure, universal Internet-based service provision remains elusive (Kenny, 2002). Further, the author argues that developing nations need to improve educational standards and computer literacy prior to broad-based adoption and constructive use of Internet services. As result, the poor and unemployed remain disadvantaged in terms of access to rural Internet based services (IDRC, 2003). Real access to "well-functioning" and "efficient financial services" has the potential to empower poor communities (Imboden, 2005).

Financial service innovations have been classified into five key areas: (1) financial system innovation, (2) financial institution innovation, (3) processing innovations, as well as (4) product and (5) service innovations (Zeller et al, 1997). Moreover, demand oriented financial service innovations enhance accessibility by the poor thus playing a critical role in poverty alleviation (Zeller et. al., 1997). As banks expand their e-commerce activities, additional services can be integrated to enhance community development and engagement with ICT. However, a monumental effort in human capital development is required prior to the realization of the full potential benefits from ICT utilization by the poor (IDRC, 2003).

A host of critical questions arise regarding digital financing. How can the financial service sector take advantage of the growth in ICT use in Africa to end the financial divide? How much attention is devoted to lowering the entry barriers of new clients from previously excluded poor communities? To what extent are the different views of the rural poor clients integrated in providing digital financial products. These and other questions are fundamental to crafting viable policies to ensure socially inclusive digital financial services in South Africa. Understanding these questions is critical given that the South African environment is reported to be "favourable" for digital financial service provision (Cracknell, 2004).

3. Research methodology

Data collection for this preliminary study started in 2005. The study focused on the four major banks in South Africa namely ABSA, Standard Bank, FNB, and Nedbank. The study sought available information on banking products focusing on digital financing or e-banking solutions. The study uses mainly secondary data sources in the form of bank publications, websites, insights gained from interacting with industry experts, personal observations and experiences as a bank client. The data is used to describe the emerging pro-poor digital financial services in South Africa. Understanding factors affecting access to digital banking services by poor communities who constitute the "second economy" is a critical aspect of this research.

4. Results and discussion

4.1 The Rise in Supermarket Point of Sale (POS) Banking in South Africa

South African banks are striving to extend cheaper forms of banking to the public. For example, Pick'n Pay Supermarkets have established a strategic partnership with NedBank to provide digital retail banking services through the "Go Account" which enables clients to bank in the supermarket on their routine shopping visit. Direct benefits of the "Go Account" includes saving time on frequent ATM cash withdrawals, lower bank charges and conduct of transactions even on Sundays (Mail and Guardian, 2006). Such a "one stop" POS service is available at all Pick 'n Pay hypermarkets in South Africa. The "Go Account" targets "poor to middle income" earners (i.e. average monthly income of R5, 000) and it allows clients to conduct banking at the check-out counters. Similarly, ShopRite and Checkers in partnership with TEBA Bank offer POS services to their customers (Cracknell, 2004). The trend towards "supermarket banking" is driven by the rising tide in consumerism in South Africa, but broad-based involvement of the poor people remains unclear.

4.2 Standard Bank's Pure Save Account

Direct response to the South African Savings Institute's desire to see more household savings in the economy, Standard Bank introduced a card-based savings account termed the "Pure Save" facility with no monthly management fees. The account aims to discourage large transactional activities that tend to erode the propensity to save among most bank clients. Its characteristics include: inter-account transfers, debt orders, stop order payments, and minimum balance of R50 that allows participation by low income earners (Business Times, May, 2005). Additional digital financial products are a travel wallet, internet banking, cell-phone banking and the provision of value-added services (e.g. account transfers, air-time top-up, deposit facility, balance enquiry, stop payment if one loses their card etc.) designed to enhance the satisfaction level of clients.

4.3 The Mzansi Account

The desire by the South African government to promote equitable access to banking services is demonstrated by among others, the recent launch of the Mzansi Account. The card-based account is designed for low income South Africans with a valid identification book. As most of the commercial banks are expected to provide this product/service, a huge increase in new accounts has been witnessed across the major banks since the launch of this product. With new accounts being opened at a rate of about 6,000 a day, the total number of Mzansi accounts in operation could easily surpass 2 million. Not only does the new account provide a platform for poor South Africans to access digital banking services across eight banks including the Post Office, it also aims to cultivate a culture of savings among the poor. In addition to the traditional savings and withdrawal functions, the account (e.g. Standard Bank Mzansi Blue Account) offers additional service features such as salary deposits, money transfers, recharging of a client's cell-phone, and POS electronic transactions. The extension of diverse digital banking features helps to close the digital financial divide for the poor.

4.4. Automated Teller Machines (ATM), Cell Phone Banking and Internet Banking: Growing Digital Financial Service Options in South Africa

Like trends elsewhere, most South African banks offer other standard digital channels such as ATMs, mobile banking, Internet banking, and electronic funds transfer. The diffusion of ATMs, Internet and mobile banking services throughout South Africa especially in big cities and shopping malls offer customers greater satisfaction and convenience as they are able to save time and money travelling to their branches to conduct transactions. Moreover, the decline in the cost of ATMs and POS devices allows for scale economies in digital financial service provision (Cracknell, 2004).

In order to expand market share, and to keep in line with world wide trends, most of the banks in South Africa have also embraced telephone banking. The target market includes customers without mobile phones and those who have no access to a personal computer (i.e. for Internet banking) at home or at the office. It seems there is a fairly high level of consciousness regarding e-banking use by urban dwellers (Singh, 2004) but clearly this is not the case for rural people. A logical question is: How can the relatively rapid uptake of digital banking by urban dwellers spread to the poor in townships and isolated rural areas in South Africa? The switch to digital technologies is expected to improve customer satisfaction and loyalty by adding value to the banking experience. However, it is important to understand clearly, the factors that drive the demand (and supply) for these digital services/products before consumers can fully reap the benefits brought about by the ICT revolution. To minimize the problem of low uptake, digital service provision should articulate the needs of the community and in particular their views about the technology options. More appropriate technologies are needed as the cost of providing (and maintaining) networked services to customers in remote rural locations is higher compared to urban areas (Kenny, 2002).

4.5 Additional Measures for Expanding Digital Financing to Poor Communities in South Africa

4.5.1. Portable Branches

The establishment of portable branches in previously neglected communities by South African banks indicates a commitment to minimize the inequalities in financial service provision. For instance, Standard Bank, FNB and ABSA have opened up a portable branch networks in under-served regions. Standard Bank has erected 100 "portable banks" using broadband technology. Between 2003 and 2006, FNB opened 11 branches to service the poor with a target of 30 across the nation. These branches are located in Eastern Cape (i.e. Lady Frere and Cala),

Gauteng (i.e. Tembisa), KwaZulu Nata (Ekurhuleni, and Kosi Bay), and North West (i.e. Mogwase). ABSA has similar "portable bank" network that operates on generators and satellite equipment. Portable branches offer most of the service features including digital options such as "mini ATMs". Withdrawal transactions are "cashless" and clients can submit their receipt in exchange for cash inside the participating stores (Kitten, 2006). The growth in portable branch networks is expected to help stimulate socio-economic development of under-privileged communities.

4.6 Overview of Challenges in Extending Digital Financial Services to Poor Communities in South Africa

Firstly, despite the benefits arising from diversified access to, and enhanced utility from digital banking services, some clients still prefer face to face interactions and the personal touch characteristic of traditional banking. Besides, the near absence of computer literacy in rural areas in Africa coupled with low Internet penetration raises the fear that digital services will be appropriated by urban elite thereby widening rural-urban income disparities (Bhatnagar, 1999; Kenny, 2002). Of concern is the risk that ICT use in banking could perpetuate social exclusion, and thus threaten social cohesion.

Secondly, digital banking revolution brings security, technological, economic, legal, and "reputation" risks. Generally, digital financial services are subject to the whims of hackers. Security codes and/or passwords can be abused by unauthorized users. Similarly, personal identity numbers are easily stolen resulting in "legal and economic risks" from the manipulation of client accounts. Innovative banks keen to provide digital solutions to their customers need to think seriously about how to stem out security breaches of client accounts and preserve their image. Also, the problem of trust poses significant challenges, and has direct implications on the successful uptake of Internet banking (Suh and Han, 2002).

Thirdly, as banks adopt ICT to improve and diversify their services, one must bear in mind that not everyone in South Africa is technologically literate. For South Africa, a country with a relatively high illiteracy rate on the continent, there is an inherent risk that majority of its poor people might be sidelined from accessing these innovative services as they are not conversant with the new banking methods. Incidences of strangers pretending to help illiterate clients at ATMs are fairly common in South Africa especially during weekends and holidays. During such encounters, unsuspecting clients end up loosing large sums of money to thieves through illegal transactions. The anticipated, significant uptake of digital financial services by the poor could be severely threatened unless problems of rural infrastructure, trust, attitudes, security risks, and computer/financial illiteracy problems are confronted head-on. How banks responds to these challenges will define success or failure of digital financial service provision in South Africa.

5. Conclusion and Recommendations

In the past, access to financial services was dominated by a few affluent members of the society in South Africa. But the poor require dependable financial services to boost their economic potential, escape the poverty trap, and sustain decent livelihoods. The rise in digital banking is perceived as key to providing new solutions to improve access to financial services by the poor. The South African banking industry has reached a crossroad and can no longer provide flimsy excuses for not reaching out to marginalized communities. Digital technologies can be harnessed as powerful "instruments for social change" and the elimination of the "financial divide."

Central to the provision of digital financial services is the need for equitable access by the majority poor in South Africa. The effort to modernize financial services through digital banking will add convenience to the banking experience, lower costs and enhance access by poor communities. However, digital solutions face some e-challenges that require dedicated security investments. With ICT driving service innovation, banks are being forced to adapt them for use

by underprivileged communities and to not push forward sophisticated products as an excuse to perpetuate the financial divide.

There is need to clearly understand how the growing availability of digital financial products (ATMs, mobile, Internet, POS, and telephone banking etc.) should be extended to townships, rural areas, and other marginalized communities. To acquaint the poor with the new ways of banking, and improve their computer/financial literacy, educational campaigns will be required. Also, banks need to recognize the value of inclusive financial services. In this regard, research is needed to (1) identify factors affecting the adoption of digital financial services by the poor in South Africa (2) provide insights on diffusion of digital financial services to a broad base of urban (i.e. including townships) and rural-based clients, and (3) investigate e-risk management strategies to enhance access and the utility derived from digital financial service delivery to poor communities.

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