2020

Report on the Second Enablers Network Discussion

Policy Research Institute of Bangladesh

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On the 23rd of February, 2020, the Policy Research Institute of Bangladesh (PRI) held the second Enablers Network Discussion on Bangladesh Digital Financial Services (DFS) under the aegis of a project “Policy Advocacy Initiative (PAI)”. The session was moderated by Dr. Zaidi Sattar, Chairman, Policy Research Institute of Bangladesh followed by keynote presentations by Dr. Bazlul Haque Khondker, Director, PRI and Dr. M.A. Razzaque, Research Director, PRI. The event was organized as a closed-door deliberation and by invitation only. It brought together some of the distinguished researchers, private sector business leaders, representatives and policy makers of the country who have been directly and indirectly involved in work related to digital financial services.

Dr. Bazlul Haque Khondker commenced the event with a comprehensive analysis of the importance of DFS in the study of economic issues. He presented a detailed review of the preceding quarter of the project, and briefly outlined the contents of the second study and the goals set for the following quarter.

In his detailed presentation, Dr. Razzaque carefully explained the development contents and findings of the first study of the PAI on ‘*improving efficiency in the G2P delivery process through mainstreaming and updating identity infrastructure*’. The presentation shed light on three frontiers of the DFS infrastructures that need to be addressed for higher efficiency: (i) identification and disbursement, (ii) interoperability of financial platforms and services, and (iii) payments and communications.

"Beneficiaries should have the freedom to choose between MFS providers, as well as the mode of G2P delivery process (branch banking, post-office, MFS accounts, etc.)."

Dr. M.A. Razzaque

An extensive analysis of the implementation of Government-to-Person (G2P) Payment System in Social Security Programmes (SSPs) and its resulting efficiency gains were highlighted during the presentation.

The discussion followed with an emphasis on different stages of interoperability, and the components required for a fully interoperable state in Bangladesh. The issue of high transaction costs of Mobile Financial Services (MFS) providers was also carefully deliberated by Dr. Razzque.

A key issue discussed during the session was how to enhance the payment infrastructure of Bangladesh by employing QR code based payment system. The QR system is easy to implement and proper development of it can improve the growth of formal/informal e-commerce in Bangladesh. The following segment of the presentation endorsed policy recommendations focusing primarily on regulatory sandboxing, recipient choice, gender gap, and fair competition.

Dr. Bazlul followed with a comprehensive analysis of the second study on "Enabling regulations to build an open and competitive DFS ecosystem (for e.g. by deregulating non-bank providers)". The presentation focused on three primary facets: key regulations for DFS, duality of regulators and question of uneven competition, and absence of guidelines for fintech regulatory sandboxing. During the discussion, research questions on operational infrastructure of Nagad, separate regulatory entity requirement, and the current payment infrastructure of Bangladesh Bank (BB) were presented to the network members.

With years of experience in the MFS sector and a leading market practitioner, Mr. Kamal Quadir, CEO, BKasH Limited, highly appreciated the creation of this forum. He highlighted the need to acknowledge the complexities that exist separately in both the financial industry and the telephone industry and discussed how these complexities can accelerate when these two industries are merged to provide digital financial services. While Dr. Razzaque applauded the progress made in Kenyan mobile financial service industry in his presentation, Mr. Quadir accentuated on two major aspects of the Kenyan digital market: i) the transaction limit per day is 140,000 Kenyan Shillings: a limit that is extremely high compared to the limit set for Bangladesh and ii) an individual can hold a maximum of five accounts in contrast to one account limit set for Bangladesh. While it is commendable that Bangladesh is seeing major progress in the DFS front, Mr. Kamal questioned the viability of comparing the Kenyan and Bangladesh DFS markets provided that the degree of liberty given to the service providers in both the countries is not comparable.

One facet of the Bangladeshi economy highly appreciated by Mr. Quadir is the smooth interoperability between existing telephone operators. While many countries witnessed delays in this respect, Bangladesh has always been ahead in allowing full interoperability between all mobile network operators since their inception. Bangladesh Bank in fact has already started a testing phase to extend the degree of interoperability between banks and MFS providers. Bkash and BRAC bank are currently going through the testing phase and showing good progress.

"Every market player needs to participate in testing phases and other arenas when and if required by Bangladesh Bank"

Mr. Kamal Quadir

In line with the topic of the second paper, Mr. Quadir questioned the current state of competition in the MFS market and the urgent need to regulate unfair activities. While Bkash is abiding by the laws set for achieving interoperability, there are players who are waiting for the interoperability system to be in place before participating in the testing phase. This compromises the concept of level playing field in the MFS market which was highly criticized by Mr. Quadir during the network meeting. He strongly emphasized on the need of every market player to participate in testing phases and other arenas when and if required by Bangladesh Bank.

A key issue debated during the session was the cost borne by the customers for undertaking mobile transactions. While many consider the cost to be relatively high, Mr. Quadir carefully outlined the cost structure to portray that a whopping 77 percent of the transaction cost goes to the agents and distributors, 8.5 percent to the telephone operators, and the remaining 14.5 percent is used for research, operating and overhead costs. Given the cost structure, the profit bracket of service providers remain narrow and vulnerable and only worsens with unfair market competition. He therefore strongly advocated for the need of level playing field in the DFS/MFS market and for all players to participate equally and ethically as required by BB.

"The bank-led model may create obstacles for MFS providers, Fintech companies, and start-ups to initiate practices in different sectors of the financial market"

Ms. Maliha Quadir

Maliha Quadir, Founder, Shohoz, highlighted that the current regulatory framework acts as a barrier to practicing creative work in the market. Investors often compare the regulatory framework of Bangladesh with other countries, and though each economy has its own home-grown model, sometimes such comparisons of regulatory frameworks can discourage investors from moving forward. Ms. Maliha emphasized on how the existing regulatory framework, particularly the bank-led model, may create obstacles for many MFS providers, Fintech companies, and start-ups to initiate practices in different sectors of the financial market.

In this respect, Ms. Maliha strongly advised further investigation on the efficiency of a bank-led model and the degree of its contribution to the development of the digital financial ecosystem. She questioned the viability of allowing a bank to own 51 percent of an MFS company and requested to investigate if it limits industry growth or contributes to it.

Referring to Dr. Razzaque's presentation, Ms. Maliha highly appreciated the concept of sandboxing and strongly emphasized on its importance for the growth of the industry.

The operational model of Nagad received spotlight during the discussion. Nagad has gained its popularity as a money transfer provider due to its low transaction cost. While it has received its fair share of criticism for not being under the purview of Bangladesh Bank's regulations, it is important to acknowledge that Postal Office, 51 percent shareholder of Nagad, has always transferred money across the country without being subjected to regulations of Bangladesh Bank. In this respect, Dr. Ashikur Rahman, Senior Economist, PRI, highlighted that the revamped services, including fintech solution, by the Post Office should come under the same regulations followed by all the existing MFS players. This will ensure a level playing field in the market.

The issue of Nagad was further discussed by Mr. Khondoker Shakhawat Ali, Honorary Fellow, Unnayan Shamannay. He very rightly pointed out that because Nagad is not under the purview of Bangladesh Bank, any financial transaction undertaken by Nagad will not be shown in BB's quarterly monetary reports. Given that Nagad's transaction value is relatively high, it is important to bring Nagad under BB's regulations to account for its financial transactions in the monetary reports.

In light of the performance of market players, Mr. Ali applauded the tremendous progress made by Bkash as an MFS provider. He outlined Bkash's good investment, good technology, and efficient distribution and management systems as the primary factors leading to its success story. Although Mr. Ali encouraged learning from other countries, he specifically emphasized on the importance of constructing home grown models that will complement the financial ecosystem of Bangladesh.

The meeting portrayed a common consensus on the liberty of customer choice. As highlighted by Ms. Afsana Islam, DFID Bangladesh: even privileged individuals in Bangladesh often lack the right to voice their choices as customers, the case can only be expected to be worse for the underprivileged groups. Ms. Afsana suggested further investigation in this field.

In light of Dr. Rzzaque's presentation, she also mentioned that gender gaps cannot be mitigated through better financial services only. It is a social issue that requires the support of various social programmes in addition to the programmes of financial inclusion.

Md. Ashraful Alam, Country Project Coordinator, SHIFT, UNCDF, stressed on the question of allowing MFS providers to operate credit facilities. While this is seen as a possible upgrade of the MFS market that definitely holds potential, Mr. Alam believes that the market will have to witness changes in regulations if operation of credit facilities is allowed. Initially MFS was thought as only a money transfer platform and the rules were accordingly set. If credit facilities are allowed, MFS institutions may have to transform into another form of entity supervised under a completely different set of regulations by Bangladesh Bank. One such entity could be a digital bank which in turn will give rise to the issues of capital requirement, financial stability etc. According to Mr. Alam, this is one area that needs to be further researched on.

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Mr. Ashraful Alam

In light of the comments received on interoperability during the session, Mr. Debdulal Roy, Executive Director, Programming, Bangladesh Bank, highlighted that two different bodies, Bangladesh Bank and A2i are currently working on separate interoperability infrastructures for Bangladesh.

"The current infrastructure is strong enough to process 10 million transactions per day"

Mr. Debdulal Roy

The initial plan was to create an interoperable platform by 2017 but due to certain issues the progress was delayed. However, BB is currently in the process of creating a universal payment infrastructure.

Mr. Roy also mentioned that BB has already introduced QR codes for all the QR code oriented financial transactions. QR code guidelines have also been made available; any institution interested in processing payment via apps using QR codes will have to abide by the QR code format to do the transactions.

Reflecting on the comments of Nagad's regulatory infrastructure, Mr. Roy confirmed that Nagad has recently reapplied for MFS license and BB is currently in the process of bringing Nagad within its regulatory umbrella.

In response to the query on BB's infrastructure, Mr. Roy assured that the current infrastructure is strong enough to process 10 million transactions per day. If it is processed through Electronic Fund Transfer (EFT), number of clearings will increase from twice a day to four times a day, a plan that is expected to be implemented by December 2020.

The session raised questions on the need of multiple regulatory bodies and the necessity of a bank-led model. Mr. Roy discouraged the idea of outsourcing as BB's experience with non-bank financial institutions (NBFIs) was subpar due to their lack of proper management and handling. According to him, if management of financial solutions is taken outside the regulations of BB and bank-led models, additional problems may arise. This is exactly why till date, BB is rigidly handling DFS/MFS activities, as the consequence of outsourcing regulatory authorities is already quite evident from NBFI's performance.

Mr. Roy followed his discussion by pinning language barrier as a primary technological limitation in Bangladesh today. He believes user experience and language barriers are two important aspects that are still not receiving adequate attention from the MFS providers.

The discussion was concluded by positive comments from the members of the enablers network. The participants commended Policy Research Institute of Bangladesh for a very timely discussion on an important subject and expect to contribute in building a high quality, comprehensive and constructive PRI research on the three primary studies.