

**Research Study:**

**Financial Inclusion in Pakistan**

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## Executive Summary

Recently Pakistan has taken several steps towards financial inclusion for achieving faster inclusive growth. This study seeks to examine the past and current trends of financial inclusion in Pakistan. This study has mainly used the data published by the State Bank of Pakistan (SBP), Financial Inclusion Insight Program and Global Findex.

Financial Inclusion is considered to be the core objective of many developing nations since from last decade as many research findings correlate the direct link between the financial exclusion and the poverty prevailing in developing nations. According to World Bank report “Financial inclusion, or broad access to financial services, is defined as an absence of price or non price barriers in the use of financial services.” The term Financial Inclusion needs to be interpreted in a relative dimension. Depending on the stage of development, the degree of Financial Inclusion differs among countries. It’s been surprising fact that India ranks second in the world in terms of financially excluded households after china .For the inclusive growth process of economy the central bank has also provided high importance to the financial inclusion. Normally the weaker sections of the society are completely ignored by the formal financial institutions in the race of making chunks of profits or the complexities involved in providing finance to the weaker section. Financial inclusion or inclusive financing is the delivery of financial services, at affordable costs, to sections of disadvantaged and low income segments of society.

There have been many formidable challenges in financial inclusion area such as bringing the gap between the sections of society that are financially excluded within the ambit of the formal financial system, providing financial literacy and strengthening credit delivery mechanisms so as to improvised the financial economic growth. Unrestrained access to public goods and services is the sine qua non of an open and efficient society. Thus Financial Inclusion is the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as weaker sections and low income groups at an affordable cost.

Well-functioning financial systems serve a vital purpose, offering savings, payment, credit, and risk management products to people with a range of needs. More-inclusive financial systems those that allow broad access to appropriate financial services are likely to benefit poor people and other disadvantaged groups. For instance, access to formal savings and credit mechanisms may facilitate investment in productive activities such as education or entrepreneurship. Lacking such access, individuals rely on their own limited, informal savings to invest in their education or become entrepreneurs, and small enterprises on their limited earnings to take advantage of promising growth opportunities. This can contribute to persistent income inequality and slower economic growth.

Despite sustained efforts of SBP, the level of financial inclusion remained very low in Pakistan. In 2014, just 10.3% of Pakistani adults had an account with a formal financial institution, well below both the South Asian

average of 33% and the average for all lower-middle-income countries of 41.4%. National Financial Inclusion Strategy was developed in 2015 which guides efforts to promote financial inclusion over the five years (2015-2020). It includes targets and objectives that are being monitored, but it was intended to be a living document that can be adjusted as required. Pakistan achieved real gains in financial inclusion in 2017. Financial inclusion increased by 5 percentage points, from 9% of adults in 2016 to 14% in 2017. Pakistan lags behind India and the South Asia and East Asia and Pacific regional averages in individuals' usage of accounts with formal financial institutions. Income is also associated with the use of financial services. The gap between the access rates of the lowest and highest income quintiles in Pakistan is double than that of India.

## UNDERSTANDING FINANCIAL INCLUSION

**What is financial inclusion?** Financial inclusion means that individuals and businesses have access to useful and affordable financial products and services that meet their needs – transactions, payments, savings, credit and insurance – delivered in a responsible and sustainable way. Financially included individuals are those who have an account in their name with a full-service financial institution

**How is it measured?** Financial inclusion is measured as the percentage of adults (15+ years old) who report having at least one account in their name with an institution that offers a full suite of financial services, and comes under some form of government regulation.

**How is it created?** Financial inclusion is created through the uptake and use of individual accounts with institutions that offer a full suite of financial services – savings, credit, money transfers, insurance and investment. Full-service financial institutions include banks, mobile money service providers, and nonbank financial institutions, such as deposit-taking microfinance institutions (MFIs) and financial cooperatives.

**What institutions and services do not count?** Individuals who own accounts with institutions that are not full service, such as credit-only microfinance institutions (MFIs), are not considered financially included. Individuals who do not have their own full-service account or use someone else’s account are not considered financially included. Individuals who only use services such as money guards, savings collectors, and digital recharge cards that are not attached to a bank or MFI account are also considered financially excluded.



## INTRODUCTION

Over half of the world's adult population, or 2.5 billion people, lacks access to formal financial services, with the overwhelming majority of the unbanked (90%) living in developing countries. Greater financial inclusion can bring these people into the financial mainstream, with positive effects on economic growth, financial stability and social cohesion. Both theoretical and empirical studies<sup>1</sup> have shown that financial exclusion inhibits human and physical capital accumulation, contributing to persistent income inequality and poverty.

Given the positive welfare effects of increased access to finance, building inclusive financial systems has become an important objective for policymakers around the world. In 2010, the G-20<sup>2</sup> produced a set of recommendations known as “The Principles for Innovative Financial Inclusion”. The following year, the Alliance for Financial Inclusion (AFI), a global network of concerned policymakers and supervisors, developed the “Maya Declaration”, the first set of global and measurable commitments to financial inclusion. The declaration, which has been endorsed by over 80 countries—including Pakistan, commits to:

- Create an enabling environment that increases access and lowers costs of financial services, including through new technology;
- Implement a proportionate regulatory framework that balances financial inclusion, integrity and stability;
- Integrate consumer protection and empowerment as a pillar of financial inclusion; and
- Use data to inform policies and track results.

A number of recent developments have contributed to the timeliness of making a push for financial inclusion, including:

- technological innovation such as mobile financial services
- a more open regulatory approach to financial inclusion
- a greater understanding of some key ingredients of success
- a recognition that market forces alone will not solve the problem of persistent financial exclusion. Developing countries have been on the forefront of pursuing innovative solutions to tackle the problem of financial exclusion so global initiatives rely heavily on peer-to-peer learning and knowledge sharing among developing countries.

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<sup>1</sup> Inter-alia, Khandker, 2005, Karlan and Zinman, 2010, Banarjee et al, 2009, and Beck Levine and Levkov, 2010

<sup>2</sup> The Group of 20 (G-20) is a forum for the governments and central bank governors from 20 major economies, accounting for 85% of gross world product.

## **BRIEF BACKGROUND OF FINANCIAL INCLUSION IN PAKISTAN & STEPS Taken BY SBP**

Since the early 1990's, Pakistan's financial sector has undergone considerable reforms that have significantly strengthened its soundness, profitability, efficiency and diversity. Until that time, it had been dominated by a handful of nationalized banks that suffered from poor performance and weak asset quality. By December 2013, the sector comprised of 38 commercial banks; 10 regulated Microfinance Banks (MFBs); a number of unregulated microfinance institutions (MFIs); 46 nonbank finance corporations (NBFCs); 50 insurance companies, of which 40 non-life insurers, 9 life insurers and 1 non-life reinsurer and 3 stock exchanges.

Banks and MFBs have also been involved in branchless banking in partnership with Mobile Network Operators (MNOs). The banking sector, now 85% privately-owned, dominates financial services and represents approximately 90% of total financial sector assets.

Pakistan has been a pioneer in championing financial inclusion for over a decade under the regulatory control of State Bank of Pakistan (SBP). There have been a large number of significant following milestones achieved which includes<sup>3</sup>:

- Creation of a regulatory framework for MFBs (2001)
- Expansion and modernization of the online credit information bureau (e-CIB, 2005)
- A series of measures to strengthen the safety and efficiency of payments, including the establishment of the Pakistan Interbank Settlement System (PRISM) (2008)
- The development of inter-operable inter-bank card payments platforms; the adoption of Branchless Banking Regulations (2008, amended in 2011);
- Adoption of a tiered approach to know-your-customer (KYC) requirements;
- Establishment of a specialized microfinance credit information bureau (m-CIB, 2009-2012)
- Launch of a nationwide Financial Literacy Program (2012)
- Work on an Inclusion, Stability, Integrity and Protection (I-SIP) methodology (2014).

SBP and the Government of Pakistan (GoP) have also sponsored a number of guarantee facilities and subsidized lending schemes aimed at encouraging lending to the under served. Pakistan's efforts have been recognized internationally. In 2011 and 2012, its microfinance regulations were ranked best in the world by the

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<sup>3</sup> National Financial Inclusion Strategy Pakistan

Global Microscope report and Pakistan was ranked in the top-ten countries for its enabling environment for financial inclusion in the most recent Global Microscope 2014.

## **LIMITATIONS TOWARDS FINANCIAL INCLUSION IN PAKISTAN**

Despite sustained efforts of SBP, the level of financial inclusion remained very low in Pakistan. In 2014, just 10.3% of Pakistani adults had an account with a formal financial institution<sup>4</sup>, well below both the South Asian average of 33% and the average for all lower-middle-income countries of 41.4%<sup>5</sup>. Fifty-six percent of adults used neither formal nor informal products. 36% of adults were saving out of which only 4% was saved with the formal financial institutions<sup>6</sup>. Similarly, while one-third of adults borrowed money, only 3% borrowed from a formal financial institution.

After years of steady growth, credit to the private sector declined in real terms from 2009 to 2014. While the total assets and deposits of Pakistan's banking sector doubled since 2008, private sector credit to GDP declined from 22% in 2009 to just 14.7% in June 2014. The decline in credit provided to SMEs particularly pronounced, falling from 16% of bank lending in 2008 to just 7% in June 2014. The agriculture sector, which represents 21% of GDP, accounted for just 6% of total lending. The figures on housing finance were even starker. Of a total population of 180 million people in 2014, there were only 76,000<sup>7</sup> housing loans outstanding in the banking sector. Against a backdrop of slow economic growth and rising government borrowing, banks invested heavily in government securities, which amounted to 122% of total bank credit to the private sector. Private businesses received just 40% of bank credit, and this supply was skewed towards larger enterprises with around 0.4% of bank borrowers accounting for 65% of all bank loans<sup>8</sup>.

## **REASONS FOR LOW LEVEL FINANCIAL INCLUSION**

The low level of financial inclusion and the decline in credit to the private sector can be attributed in part to factors which go beyond the scope of financial sector policy and should be addressed in the broader economic, social and political context. These include the following:

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<sup>4</sup> Financial Inclusion Insights

<sup>5</sup> Findex, 2011. Pakistan is categorized by the World Bank Group as a lower-middle-income country, i.e. one whose per capita gross national income falls between USD 1045 and USD 4125.

<sup>6</sup> Financial Inclusion Insights, 2014. This excludes National Savings, which provides savings to approximately 7.7 million Pakistanis.

<sup>7</sup> SBP Quarterly Housing Finance Review, 1st Q 2014

<sup>8</sup> Pakistan 10-Year Strategy Paper for the Banking Sector



**The economic cycle:** The decline in credit to the private sector is due to cyclical factors. Credit, including to underserved segments such as SMEs and housing, had been growing rapidly prior to the economic downturn in 2008 which was followed by the lowest average five-year period of GDP growth (2.8%). The economic downturn resulted in a decline in demand for credit. However the economy started showing signs of improvement in 2014, with growth estimated at 4.3% for 2013/14, and private sector credit growth also showed signs of recovery in respective months.

**Business climate:** The challenging economic and business climate, including severe energy shortages and security concerns, has been highly disruptive for businesses, particularly MSMEs, negatively impacting their creditworthiness. There was a sharp deterioration in asset quality post-2008, particularly in the SME and housing sectors, where NPLs now stand at 34% and 29%, respectively. This has understandably dampened banks' risk appetite and resulted in a "flight to quality"<sup>9</sup>.

**Rapidly rising government debt:** Public sector debt rose rapidly, with the fiscal deficit rising from under 3% of GDP in 2005 to 8.5% of GDP in 2012/13. Over the same period, private credit declined as a share of banks' total lending from 75% to 45%. Banks' deposit base continued to grow during this period, but this growth deployed to a rapid expansion of holdings of government securities, which provided banks with a relatively attractive yield at low risk.

**Gender barriers:** Women are largely excluded from the formal financial system. Only 7% of adult females have an account with a formal institution, compared to 20% of males<sup>10</sup>. Mobility and social interaction limitations restrict women's access to financial services. These may be partially addressed by the rapid expansion of digital financial services. However, there is a 42% gender gap in mobile phone ownership and 30% of females do not even have access to somebody else's mobile phones. As women comprise half of the adult population, Pakistan will not be able to achieve an inclusive financial sector unless financial services become truly accessible to all. It will require a concerted and creative effort from both government and the private sector to address ingrained cultural and social barriers that prevent women from participating in the financial sector, and to investigate further the causes of, and potential solutions to, exclusion.

**Growing informality in the economy:** Research estimates<sup>11</sup> showed that the size of the informal economy is 75-91% of the size of the formal economy -much larger than previously estimated. The informal sector appears to be expanding while the formal economy is in retreat. Since banks and other formal financial institutions are reluctant to do business with informal firms, growing informality has contributed to financial exclusion.

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<sup>9</sup> A flight-to-quality is a financial market phenomenon occurring when investors sell what they perceive to be higher-risk investments and purchase safer investments, such as Treasuries or gold.

<sup>10</sup> Financial Inclusion Insights, 2017.

<sup>11</sup> Ali Kemel and Waqas Qasim, Pakistan Institute of Development Economics, 2012.

Other reasons for the low level of financial inclusion are varied, and differ from one market segment to another. However, there is a broad consensus among stakeholders on several cross-cutting financial sector issues, notably<sup>12</sup>:

- While SBP has been very proactive in promoting an inclusive financial sector, many of the issues that need to be addressed fall outside of its regulatory mandate. For example, a number of longstanding problems cannot be solved without legislative changes, but important draft bills, including those on secured transactions, deposit insurance, insolvency and credit bureaus, have been in an uncertain legislative process for years. Progress towards a more inclusive financial system has also been slowed because of limited commitment and weak coordination between several government and private sector stakeholders.
- Weaknesses in the basic financial sector infrastructure and the legal and judicial framework discourage lending, particularly to those perceived as riskier borrowers. The supply of credit to underserved markets is further depressed by: poor contract enforcement, serious deficiencies in land titling and registration, the absence of a secured transactions framework and electronic collateral registry for moveable collateral and the inability to enforce collateral outside of the slow and unpredictable judicial system.
- Lack of capacity in both financial institutions and clients is also a constraint to greater financial inclusion. Most financial institutions have focused on the upper end of the business and retail markets and have not developed the skills, techniques and products required to serve other market segments profitably. Microfinance providers have developed this knowledge for microfinance clients, but there is a large “missing middle” which is currently not being served. On the client side, a basic lack of financial literacy and awareness serves to limit demand for financial products and services.



<sup>12</sup> National Financial Inclusion Strategy Pakistan.

## DEVELOPMENT OF NATIONAL FINANCIAL INCLUSION STRATEGY OF PAKISTAN

The persistence of financial exclusion in the face of long-standing efforts to promote inclusion pointed the need to develop a comprehensive National Financial Inclusion Strategy (NFIS). The NFIS provides a vision that underlies the NFIS, a framework and a road map for priority actions aimed at addressing constraints and significantly increasing access to, and usage of, quality financial services. The strategy guides efforts to promote financial inclusion over the five years (2015-2020). It includes targets and objectives that are being monitored, but it was intended to be a living document that can be adjusted as required.

The NFIS has been agreed to at the national level following extensive consultations and collaboration with Ministry of Finance (MoF) and the Securities and Exchange Commission of Pakistan (SECP) while the objectives are fully consistent with the Government of Pakistan's Vision 2025, which calls for enhancing access to credit for SMEs and focusing on financial inclusion. Successful implementation will require the commitment and active engagement of key stakeholders from both the public and private sectors.

The stated vision for financial inclusion in Pakistan is: ***“individuals and firms can access and use a range of quality payments, savings, credit and insurance services, which meet their needs with dignity and fairness”***.

The key enablers of NFIS are;

- (i) Public and private sector commitment to the NFIS and coordination
- (ii) Enabling legal and regulatory environment
- (iii) Adequate supervisory and judicial capacity
- (iv) Financial payments and information and communications technology (ICT) infrastructure.

The key enablers support targeted actions – the drivers – aimed at increasing access and developing an ecosystem of financial services that will have the quality and features required by the Pakistani population and enterprises. These drivers are:

- (v) Promoting DTAs and reaching scale through bulk payments
- (vi) Expanding and diversifying access points
- (vii) Improving capacity of financial service providers
- (viii) Increasing levels of financial capability.

The network to distribute financial services in Pakistan was falling short, particularly in rural areas, and it didn't permit all firms and individuals, especially women, to have easy and convenient access to even basic accounts. Hence, the NFIS prioritized the need to increase and diversified financial service access points such as bank branches, bank agents, ATMs, POS, mobile money agents and remote access through mobile phones and the internet.

## **CURRENT LANDSCAPE OF FINANCIAL SERVICES –OVERVIEW**

In 2017, Pakistan's Central Bank, the State Bank of Pakistan (SBP), continued to prioritize financial inclusion as a key element of its national development program and the 2015 National Financial Inclusion Strategy. The World Bank also supported these financial inclusion efforts through an ongoing partnership program. SBP and its partners continued to focus on digital financial services (DFS) as a means to expand financial inclusion.

The SBP's 2017 published National Telecoms Policy which aims to address existing gaps and improve avenues for innovation and market entry by nontelecom providers.

The enforcement of SBP's regulations on the use of biometric verification for all Over-The Counter (OTC) transactions contributed to an increase in registered users of mobile money by making OTC transactions more difficult. Revision in Banking regulations, biometric verification for OTC transactions is expected to increase compliance with the SBP's Know Your Customer (KYC), Anti Money Laundering (AML) and Combating Financing of Terrorism (CFT) guidelines.

- SBP launched the **Asaan Remittance Account** in December 2017. These accounts have a simplified one-page application form with basic information. The account is designed to facilitate P2P transfers of home remittances. The maximum credit balance limit is PKR 2 million (\$17,200), and a cash withdrawal limit as well as fund transfer limit of PKR 50,000 (\$430) per day
- SBP plans to launch the **Asaan Mobile Account Scheme**, which will allow anyone with a basic mobile phone to open a mobile money account using a USSD code. The Asaan scheme is expected to facilitate conversions from OTC to mobile wallets.

The Government of Pakistan took new measures to address the limited mobile internet connectivity. According to a 2016 GSMA report, Pakistan ranks low on infrastructure, affordability, consumer readiness and content, relative to its neighbors.

- In April 2017, the Government of Pakistan launched a \$130 million Financial Inclusion and Infrastructure Project focused on improving access to digital payments and advancing access to credit for small- and medium-sized enterprises.
- In an effort to expand the supply of telecom financial services and facilitate branchless banking, in April 2017, the Pakistan Telecommunications Authority (PTA) began offering licenses to Third Party Service Providers (TPSP) for the operation of telecom financial service applications.

A large and persistent gender gap in economic participation works against financial inclusion, particularly the lack of women-owned physical capital, as well as social norms that limit women’s economic empowerment. Financial service providers are testing new digital products on the market.

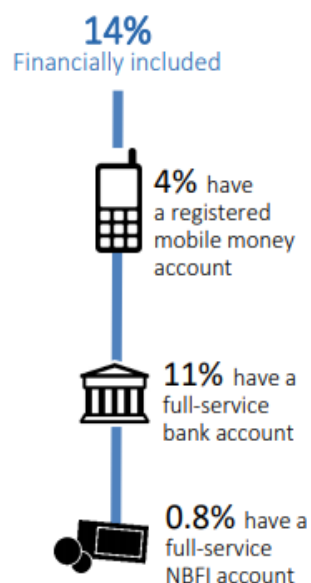
- The Pakistan Post and Karandaaz Pakistan are partnering to digitize the Pakistan Post’s money order services.
- The National Bank of Pakistan (NBP), a state-owned commercial bank, and Karandaaz are partnering to support DFS through the implementation of an Application Programming Interface (API) management platform. API will enable the NBP to automate and digitize government-to-person (G2P) and person-to-government (P2G) transactions.
- Master Card is collaborating with Pakistan’s NADRA Technologies to enable electronic payments using national ID cards. This functionality will allow citizens to conduct financial transactions, receive government payments, and send and receive remittances using their unique 13-digit national identification card number.

## NOTABLE STATISTICS OF FINANCIAL INCLUSION IN PAKISTAN

### Increase in Financial Inclusion:

Pakistan achieved real gains in financial inclusion in 2017. Financial inclusion increased by 5 percentage points, from 9% of adults in 2016 to 14% in 2017<sup>13</sup>. This gain was the first statistically significant change in the proportion of adults who are registered users of full-service financial accounts that the FII (Financial Inclusion Insight) program has recorded in five years of annual surveys in Pakistan.

- Both banks and mobile money drove the gain in financial inclusion. Access and trial users of mobile money grew 4



<sup>13</sup> Financial Statistics Insight 2017

percentage points, from 9% of adults, who accessed mobile money services in 2016 to 13% in 2017.

- Registered users of mobile money also increased by 3 percentage points, from less than 1% of the population in 2016 to 4% in 2017.
- In 2017, 11% of the adult population had a registered full-service bank account, up from 9% in 2016 and 7% in 2015.
- Full-service nonbank financial institution (NBFI) account users are nearly undetectable using nationally representative survey methods; less than 1% of the adult population had a registered NBFI account in 2017.

### **Gender Gap:**

The gender gap remains an enormous barrier to women's financial inclusion and economic empowerment; 20% of men are financially included compared to only 7% of women. Men also have much higher readiness for adopting digital financial services.

- The gender gap in access to a mobile phone is 13 percentage points: 84% of men versus 71% of women have access.
- The proportion of men with SIM card ownership is double that of women: 78% of men versus 39% of women own a SIM card.
- Text messaging – a key indicator of capability to use digital financial services – is twice as prevalent among men: 68% of men versus 34% of women have ever sent or received a text message.
- As on Oct-Dec 2017, the Branchless Banking accounts comprised of 29.9 million male and 7.3 million female accounts. Punjab became the top contributor in female accounts by registering 466,273 new female accounts during the quarter. Province-wise segregation of data reveals that Punjab maintains the highest female inclusion ratio (21.7% female vs. 78.3% male accounts), followed by Sindh (18.7% female vs. 81.3% male accounts) and Azad Kashmir (18.4% female vs. 81.6% male accounts)<sup>14</sup>.

### **Active Users:**

Active users of a registered financial account increased 5 percentage points, from 8% in 2016 to 13% in 2017. This gain was driven by both banks and mobile money. Nearly all of those who became registered mobile money users in the year between the 2016 and 2017 surveys used their accounts actively.

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<sup>14</sup> Quarterly Branchless Banking Newsletter, State Bank Of Pakistan, Oct-Dec 2017

## **Advanced Users:**

Advanced users increased from 7% of adults in 2016 to 10% in 2017. Saving, bill pay, receiving wages, and receiving government benefits were the main activities of advanced users. 10% of Pakistani adults, over 10 million people, are advanced users of financial services, using their registered accounts for activities beyond account management and person-to-person transfers. 81% of advanced users, representing around 8 million people, reported saving money via a variety of methods.<sup>15</sup>

## **TECHNOLOGICAL INNOVATION IN FINANCIAL INCLUSION**

Technology plays an important part in improving the financial inclusion. Mobile technology and its large scale penetration is a fine example. The first product which went popular worldwide was M-Pesa. M-Pesa of Kenya spread quickly and became one of the most successful mobile based financial services. In 2007 on an average number of registration to M-Pesa in Kenya exceeded 5000 per day, by 2009 around 7.9 million M-Pesa accounts are registered. Customers in Kenya started using M-Pesa for their day to day activities, as there was no hard currency involved resultantly there was less risk of theft. Due to increase in M-Pesa outlets demand, banking agents increased, which ultimately increased job opportunity in the country. M-pesa is a simple mobile banking application in which customer can send money to any individual or can purchase items by doing transaction with M-Pesa application. One of the main reasons for M-Pesa growth in Kenya is due to increase in growth of mobile communication in late 2000's. Secondly, the product was simple to use and affordable for the locals. It provided choices of product which customer can choose. It facilitated easy cash convertibility due to availability of large number of M-Pesa outlets. Regulators encouraged this mobile financial services across the world.

After success of M-Pesa many countries adapted the idea of branchless banking. As per current trend the future of branchless banking looks bright. A lot of technological innovation will be coming in future to boost financial inclusion. To support these initiatives, apart from government, there are some international agencies which also work for financial inclusion, namely World Bank, CGAP, Bill and Malinda Gates Foundation. After the M-Pesa, many companies in Kenya are investing in branchless banking. New products have been launched which are similar to M-pesa like IKO-Pesa also known as orange money. Other countries also developed mobile banking solutions with the help of service providers and banks e.g. Easy Paisa in Pakistan, EKO in India, G-Cash in Philippines etc.

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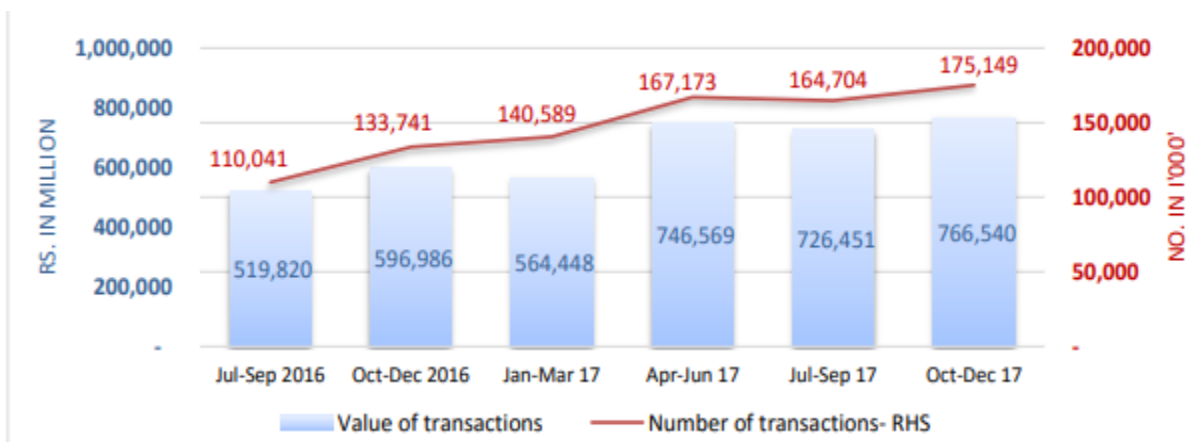
15 InterMedia/ Gallup Pakistan

## BRANCHLESS BANKING, PAYMENTS AND DIGITAL TRANSACTION SERVICES

Pakistan is one of the fastest growing markets for branchless banking in the world. The catalyst for this growth was the introduction of the Branchless Banking Regulation in 2008, which allowed banks and MFBs to leverage mobile phone communications and distribution networks to bring financial services closer to customers. In addition, SBP has made proactive regulatory decisions since 2008 which have facilitated a range of sustainable branchless banking business models. The mobile network is well developed, and while access is not always present for all household members, 9 out of 10 households do have access to a mobile phone and SIM card.

Graph<sup>16</sup> below depicts the steady growth in the value and volume of branchless banking transactions in Pakistan.

**Volume and value of branchless banking transactions 2016-2017**



### Composition of Volume & Value of Transactions:

Branchless Banking (BB) transactions are divided into two major categories;

- Agent related (for liquidity purpose)
- Customer Oriented: It is further divided into Over The Counter(OTC) and Mobile-Wallet transactions. OTC transactions involves Funds transferred through CNIC, bill payments & mobile top-ups and social welfare payments whereas cash deposit & withdrawals, funds transfers and mobile top-ups are the major contributors in m-wallet transactions.

Following table shows the quarter wise comparison and break-up of overall BB transactions with their respective share and percentage change.

<sup>16</sup> Quarterly Branchless Banking Newsletter, State Bank Of Pakistan, Oct-Dec 2017



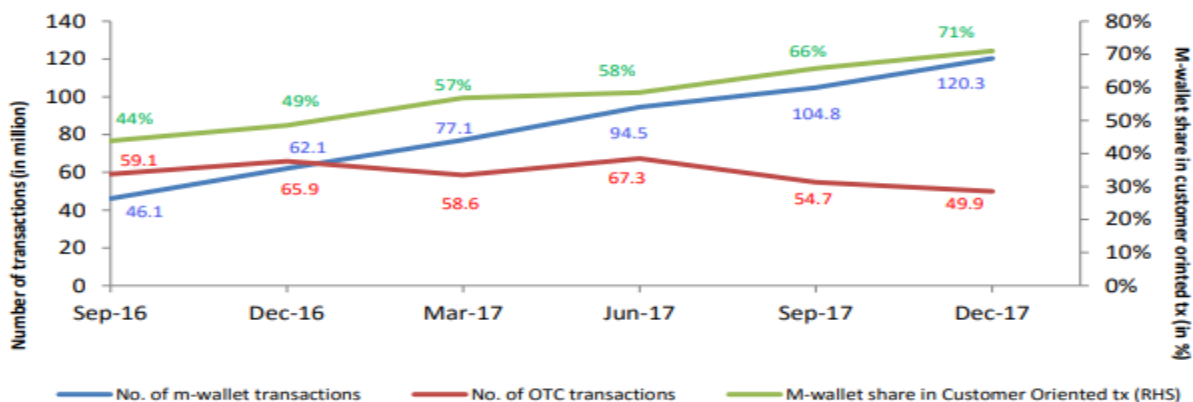
Type of Transactions	Volume (No. in Million)		Change in %	Value (PKR in Billion)		Change in %
	Jul-Sep 2017	Oct-Dec 2017		Jul-Sep 2017	Oct-Dec 2017	
Customer Oriented	159.5	170.3	6.8%	444.6	492.6	10.8%
Agent related (for liquidity purpose)	5.2	4.9	-5.8%	281.8	273.9	-2.8%
<b>Total BB Transactions</b>	<b>164.7</b>	<b>175.2</b>	<b>6%</b>	<b>726.4</b>	<b>766.5</b>	<b>6%</b>

There are 120 million SIM card holders in Pakistan, only 7% of Pakistani adults use mobile money either through their own or others' accounts. Just 0.4% of adults have registered mobile money accounts.

SBP and industry have been striving to introduce the M-wallets as an easy and convenient way to conduct transactions. It is encouraging to see that these efforts are bearing fruits, as the m-wallet channel is constantly gaining share in customer oriented transactions from the OTC channel. During the recent years, M-wallet share has crossed 70% mark for the first time in history, ending at 71% during the end of Oct-Dec 2017 quarter. It is important to note that the M-wallet share was only 13% in customer oriented transactions during Jan-Mar 2015 quarter. Since then, a significant rise in wallet-to-wallet transfers (96%), mobile top-ups (98%), utility bill payments (76%) and pension payment through M-wallets (74%) has been witnessed.

OTC transactions currently represent 80% of all transactions versus only 14% of transactions are direct wallet-to-wallet (account-to-account). However, wallet-to-wallet transactions are growing in both volume and value thanks to increasing use of e-wallets for mobile top ups and bulk payments. The main driver for growth in value has been bulk payments (e.g. government to person, G2P) and cash deposits or withdrawals. Growth in volume can be largely attributed to mobile top-ups, which accounted for a 40% growth in the number of transactions in Q1 2014.

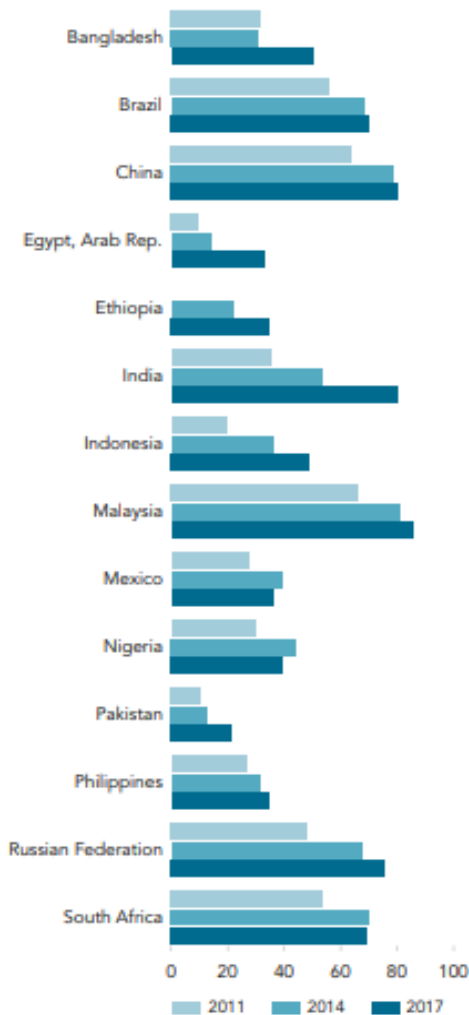
Periodic trend of M-wallet to OTC transaction relative share is as follows;



## GLOBAL TRENDS AND COMPARISON WITH REGIONAL COUNTRIES

### Account ownership has grown in some developing economies, stagnated in others

Adults with an account (%)



Source: Global Findex database.

Note: No data are available for Ethiopia for 2011.

Globally, the share of adults with an account rose from 51 percent (2011) to 62 percent (2014) and then to 69 percent (2017). Among developing economies, the growth in account ownership has been far from uniform. In India, the share of adults with an account has more than doubled since 2011 to 80 percent. An important factor driving this increase was an Indian government policy launched in 2014 to boost account ownership among unbanked adults through biometric identification cards. This policy benefited traditionally excluded groups and helped ensure inclusive growth in account ownership. Between 2014 and 2017 account ownership in India rose by more than 30 percentage points among women as well as among adults in the poorest 40 percent of households. Among men and among adults in the wealthiest 60 percent of households, it increased by about 20 percentage points. Indonesia also saw equitable growth in account ownership among men and women as the overall share of adults with an account rose from 20 percent in 2011 to 49 percent in 2017.

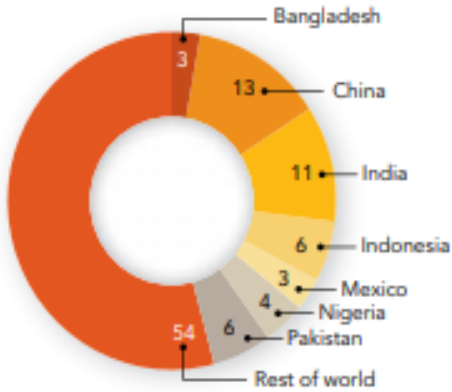
Some economies have had gains in account ownership but missed out on opportunities for greater progress because women were insufficiently included. In Pakistan, for example, account ownership has doubled since 2011, though it started from a low base of 10 percent. But while it surged among men, it stagnated among women. In Ethiopia account ownership has raised by 18 percentage points among men since 2014, roughly twice the size of the increase among women. Bangladesh has also had uneven progress, with slower gains among women. Yet the picture is not entirely bleak in these economies. Most have seen account ownership rise among women and poorer adults. But more inclusive growth in account ownership would have led to faster overall progress. Account ownership has remained largely unchanged in developing economies where it was already about 70 percent or more in 2014, such as Brazil, China, Malaysia, and South Africa.

1. Pakistan lags behind India and the South Asia and East Asia and Pacific regional averages in individuals' usage of accounts with formal financial institutions. Income is also associated with the use of financial

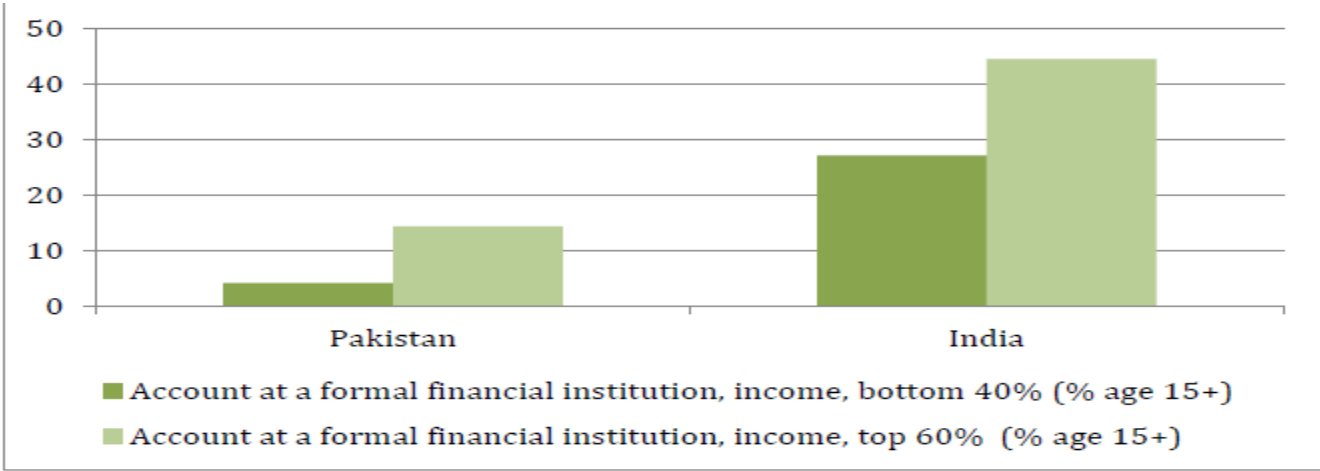
services. The gap between the access rates of the lowest and highest income quintiles in Pakistan is double than that of India.

**Proportion of adults (age 15+) with an account in a formal financial institution:**

In 2017, globally, about 1.7 billion adults remain unbanked; without an account at a financial institution or through a mobile money provider. In 2014 that number was 2 billion. Nearly half of unbanked lives in just following seven economies<sup>17</sup>.



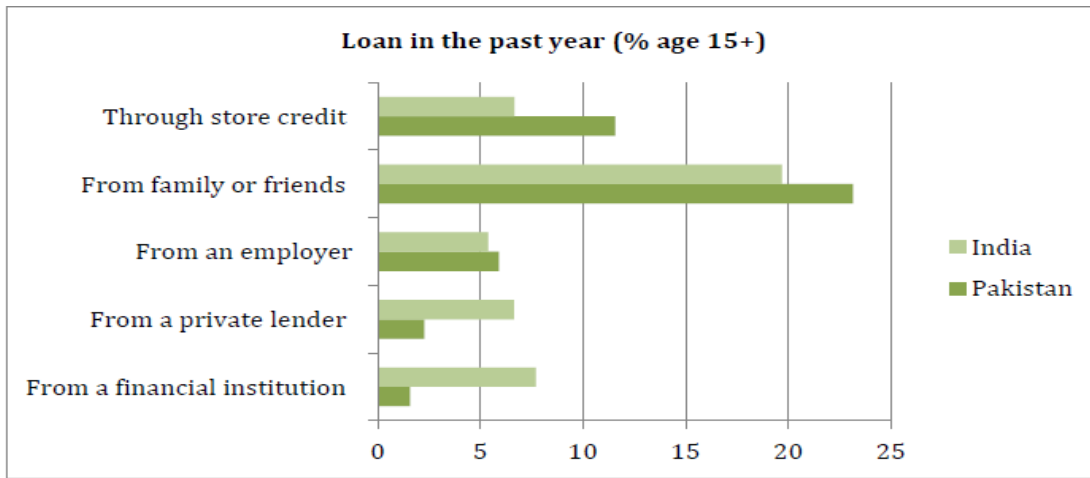
**Comparison of Account at Formal Financial Institution by Income Quintiles:**



Usage of a bank account also increases with the level of education. The percentage of adults with a bank account in urban areas (15.4%) is twice that of rural area residents (7.2%). The gaps between urban and rural residents are much wider than in India.

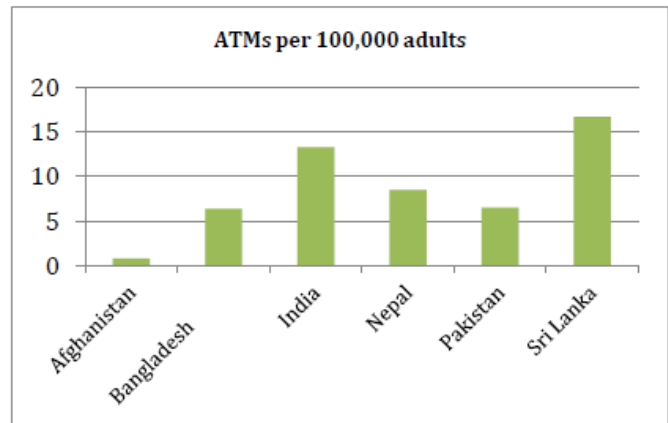
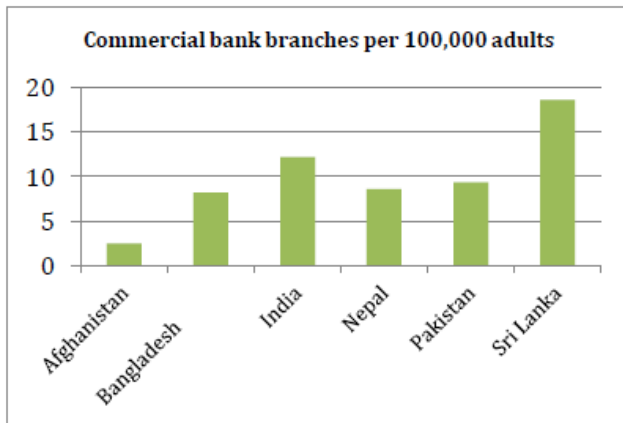
- One-third of the adult population borrows, but less than 2% uses a formal financial institution to do so. Access to credit increases with age and education. Borrowing is mostly informal. Figure below shows the importance of borrowing from friends (23%) and shopkeepers (13%). The percentage of informal borrowing is lower in India. On the other hand, Pakistan lags behind India in borrowing from a private lender (3% versus 7%) or from a financial institution (2% versus 8%). These findings reinforce the importance of the informal sector in Pakistan.

<sup>17</sup> Global Findex data base 2017



Source: Findex 2011

3. On the supply side, proximity to financial services has traditionally been a key determinant of access. Pakistan has roughly the same number of bank branches and ATMs per 100,000 inhabitants as most countries in South Asia. The recent development of branchless banking has increased access points considerably. While there were just 6.6 bank branches per 100,000 adults in 2014, there were 152 registered agent outlets (up from just 15 in 2011). Nonetheless, the agent network still falls short of achieving full national distribution. There has been little growth in rural settings where the absence of formal financial services is more acute. A geo-spatial mapping of access points would be helpful to determine how many individuals may remain excluded due to lack of physical access.



## **ROLE OF ZTBL IN FINANCIAL INCLUSION**

Since its inception, ZTBL made significant contribution in providing credit to agriculturists and landless rural poor. It emerged as the single largest institution in the country for supply of agricultural credit and transfer of agricultural technologies to the farmers through Mobile Credit Officers(MCO)who deliver credit with technology at the doorstep of farmers and they are aimed at making maximum number of farmers banked.

A paradigm shift has been envisaged pursuant to the vision of CEO/ President of the Bank to bring unbanked segments of population especially in rural area, particularly poor and marginalized groups through the continuum of sound financial access. The objective is to provide equitable and efficient market based financial services to the otherwise excluded poor and marginalized population including women and young people. Enabling the bank to expand its banking services to tap 78% unbanked population.

The Bank has been playing an instrumental and proactive role in modernization of agriculture, boosting productivity and enabling growers, particularly landless poor and small land holders to increase their farm productivity and hence income. The Bank holds the largest agriculture credit market share, in terms of outstanding loan portfolio in the industry with total outstanding portfolio of Rs. 159 billion (as of December 31, 2017) with total clientele base of approximately one million farmers, with more than 90 % clientele comprised of small/subsistent farming community. Bank disbursed 97.128 billion and served 304,877 borrowers during the year 2017. The Bank disbursed a major portion of its funds towards production loans amounting to Rs. 74.429 billion constituting around 77% of total disbursement to meet the input credit requirements of farmers. An amount of Rs.22.699 billion constituting 23% of the total agricultural credit was disbursed for development purposes including tractors, tube-wells, farm equipment, livestock, poultry farming etc.

### **Bank' s Lending Schemes under Financial Inclusion Initiatives**

ZTBL is extending following financing facilities in Balochistan & KP categorized under Production and Development Loans.

#### ***Schemes under Production Loan:***

- Sada Bahar Scheme
- Kissan Dost Scheme

#### ***Schemes under Development Loan:***

- Red meat financing package for Sheep Goat Rearers
- Asan Qarza Scheme (for rural youth - 18-35 years old)
- Khawateen Rozgar Scheme
- Tobacco Barn Financing Scheme

- Khushk Ratab Scheme
- Tahahfuz-e-Ajnas Scheme
- Warehouse Receipt Financing Scheme
- Financing for Ostrich Framing
- Kissan Dost Scheme

Moreover, realizing the potential and increasing demand for the value addition, the Bank has emphasized on the area and developed its lending products for promotion of value addition sector and to broaden the financial services outreach to those who currently are deprived of financial services due to lack of bankability and non-availability of required banking products at their door step

In addition to this the bank has initiated value chain services and plan to launch following value chain products in near future;

- Financing for Agriculture Implements (Farm Mechanization/Stocking of Machinery)
- Warehouse Receipt Financing
- Financing to Service Providers
- Rent – a – Cow (Financing for Dairy / Milk & Allied Products)
- Financing Livestock (Poultry/Dairy/Fisheries)
- Value Chain Contractor Farmer's Financing

#### **Other Initiatives:**

The regional experiences and undertakings for the development of agriculture especially in South Asia region reveals that any desired level of sustainable agriculture sector growth and uplift of rural house hold income requires broadening the banking and financing services matrix. There is need for uplifting the set of services offered to ZTBL target market, special emphasis has been laid by the management of the bank for bring ZTBL in line with the spectrum of agriculture banking services in vogue as success stories in South Asia region. Therefore, certain initiatives have been undertaken to make ZTBL competitive in the agriculture financing industry.

- Initiation of Alternate Delivery Channel
- Launch of Islamic Banking as a tool to broaden Financial Inclusion
- Installation of Automated Teller Machines “ATM”
- Development of new deposit products such as ZTBL Assan Remittance Account, ZTBL Business Value Account, Kissan Assan Karobar Scheme, Senior Citizen Account, Junior Account etc.
- Dissemination of Agriculture Technology
- Establishment of Call Centre

## **Role of MCO at ZTBL in Financial Inclusion**

- Establish door to door contact with the farming community
- Provide technical and financial support
- Guide farmers on lending products and lending process
- Create awareness on various products of the Bank
- Effective and proper utilization of Bank's Loans
- Guiding farmers about latest farming techniques and technologies
- Other financial services of the Bank.

## RECOMMENDATIONS

Following suggestions are proposed that may gear ZTBL towards increased financial inclusion:

- Number of branches in remote areas may be increased with robust role of MCO in identifying financially excluded households and assess their banking, credit and other non-financial service needs via field studies of village economy and households' economic profiles
- Bank may focus more on products which should be simple, affordable, and should have high utility.
- Bank may do regular surveys in villages for understanding the financial needs of the rural population.
- Customer feedback surveys may be conducted about the product and services of the Bank.
- Opening of Bank Accounts without minimum balance condition should be allowed at all branches of remote areas where population is financially excluded.
- Since credit need of small and medium size farmers is both for investment and production purposes, therefore at least 25% credit should be for production purpose under subsidized interest rates (subsidy to be paid by the federal government).
- In order to protect the outlay of banks in agricultural loans, it is proposed that the bank in collaboration with National Insurance Corporation should prepare and introduce a scheme i.e. crop insurance for other crops like gram, oilseed crops, potato etc. besides five major crops of cotton, wheat, rice, sugarcane and maize. The average portfolio size of the Bank for minor crops is Rs.500 million per annum.
- Develop public-private partnership with the provincial governments like e-credit scheme of Punjab and dairy scheme of AJK on subsidized basis to support small farmers in a manner, where the mark-up portion on the loan may be chipped in by provincial governments. At present negotiations with provincial government of KP are also in progress on the same lines with ample room to explore further opportunities/collaboration.
- An agri credit card scheme may be extended to the farming community of Pakistan with credit limit (kharif and rabi) based on the size of land holding and productivity of the land and other collateral assets.
- In addition to the provision of production loans, there is considerable need to provide loans for marketing, storage and processing of agricultural produce i.e. promoting value chain financing.
- With the active cooperation of Provincial Government and manufacturing companies of the fertilizers and other chemical inputs, following facilities may be established at all union councils for the benefits of local farming community. (i) soil and water testing laboratories (ii) Agricultural



extension centres (iii) Pool of agricultural machinery for hire (iv) Repair workshops and depots of fertilizers (of all types) and of agro-chemicals (v) marketing committees for fruits, vegetables and other perishables through market and also marketing through processing plants.

- To render better service and to foster the growth of exclusive customer-banker relationship, the area of operation of each branch of the potential area may be extended to a union council or patwar circle. Within that union council, it should be the exclusive responsibility of the designated bank branch to ensure that the genuine agri credit requirements of all farmers of that area are properly met.
- It is important to ensure that credit disbursement has a correlation with the farming requirements at individual and collective level.
- Advertising campaigns are needed to create “awareness” among all categories of households in villages on the availability of banks financial services and procedures to avail them. For this purpose, village level seminars and meetings can be organized, details be released in all local print media, regular and frequent advertisements can be given on electronic media, leaflets can be distributed, success stories be featured on a regular basis.
- Geographic discrepancies in agri credit disbursement may be minimized as major agri credit lending remains skewed towards big provinces.
- Digitalization of land records and titles can help in better distribution of agri credit. It can also help loan recovery and keeping bad debts low.
- The Advances to Credit Ratio stood at 56pc in 2017-18, it may be increased in all provinces and regions to support local economies.
- Bank may overcome its infrastructure gaps to achieve agri credit target
- In order to encourage borrowers in regular repayment of their loans, incentives for regular/old borrowers on their previous repayment performance may be extended.
- Group lending may be encouraged.
- New and innovative credit lending products such as green banking products should be offered to the farming community.
- Paradigm shift is required to move towards cash flow based lending instead of asset based lending.
- Loans should be extended to promote women entrepreneurs who are involved in cottage industries related to agriculture and allied activities.

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