Making Access Possible

Mozambique

Financial Inclusion Country Report

2014

cenfri
The Centre for Financial Regulation & Inclusion

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PARTNERING FOR A COMMON PURPOSE

Making Access Possible (MAP) is a multi-country initiative to support financial inclusion through a process of evidence-based country diagnostic and stakeholder dialogue, leading to the development of national financial inclusion roadmaps that identify key drivers of financial inclusion and recommended action. Through its design, MAP seeks to strengthen and focus the domestic development dialogue on financial inclusion. The global project seeks to engage with various other international platforms and entities impacting on financial inclusion, using the evidence gathered at the country level.

The cover symbol

Through the MAP programme, we hope to effect real change at country level and see the impact of financial inclusion on broader national growth and development. The cover graphic features the Devil Thorn, a flower synonymous with Mozambique. The flower symbolises growth and development while the circle represents inclusive growth. Each flower is an example of the successful growth in a unique environment. By combining the flower with the currency symbol of Mozambique we represent the characteristics of the country, linking financial inclusion with successful growth.

ABOUT MAP MOZAMBIQUE

This Diagnostic report presents a comprehensive analysis of the financial inclusion environment in Mozambique as part of the Making Access Possible (MAP) Mozambique initiative. MAP will be used to inform the Mozambican government's approach to financial inclusion. In 2014, the Ministry of Finance formally requested FinMark Trust's support for its ongoing financial inclusion agenda. It was agreed that the MAP study will form the basis for the development of a multi-stakeholder roadmap for financial inclusion, which in turn will be leveraged as a vehicle towards an integrated financial inclusion strategy in Mozambique.

The MAP Diagnostic comprises a comprehensive country context, demand-side, supply-side and regulatory analysis. The supply-side analysis covers the markets for payments, savings, credit and insurance, respectively. Hence the report provides an understanding of access to financial services in a broad context. The demand-side component includes an analysis of access, usage, perceptions and attitudes of financial services by different target groups. The demand-side analysis draws from quantitative data provided by the Mozambique FinScope Consumer Survey 2011 and qualitative research in the form of focus group discussions, immersion visits and key informant interviews.

The MAP methodology and process has been developed jointly by UNCDF, FinMark Trust (FMT) and the Centre for Financial Regulation and Inclusion (Cenfri) to foster inclusive financial sector growth.

THIS REPORT WAS PRODUCED BY THE CENTRE FOR FINANCIAL REGULATION AND INCLUSION (CENFRI).

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We would also like to thank the various people we met with from government, financial services

providers, industry bodies, technology providers, telecommunications operators and donor agencies for their time, the critical insights that guided this research and their efforts to extend financial services to the excluded.

Abbreviations and Acronyms

ATM	Automated Teller Machine
BdM	Banco de Mocambique
Cenfri	Centre for Financial Regulation and Inclusion
ISSM	Institute of Insurance Supervision of Mozambique
KYC	Know Your Customer
MAP	Making Access to Financial Services Possible
MSME	Medium Small and Micro Enterprises
POS	Point of Sale
UNCDF	United Nations Capital Development Fund
ZAR	South African Rand

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EXECUTIVE SUMMARY

Mozambique is a country on the move. Since emerging from its long civil war in the 1990's, the country has liberalised its economy, initiated the construction of new infrastructure on a vast scale and instituted extensive public reform. The financial sector, in particular, has seen far reaching changes. Not only were several state-owned financial institutions privatised, but many new financial institutions have emerged. The economy responded with strong growth, averaging 7.5% in real terms between 2005 and 2014.

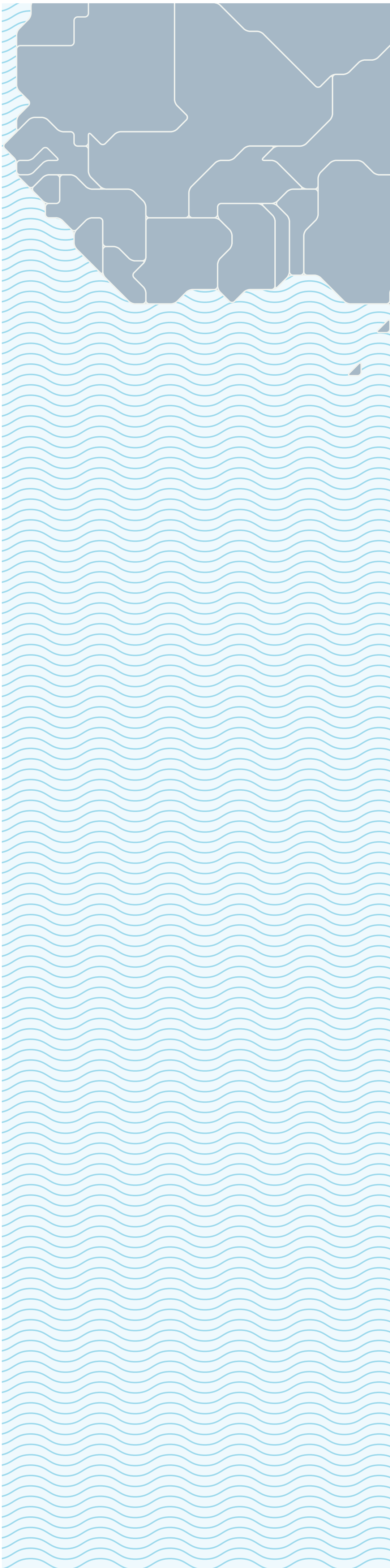
This report asks a simple question: to what extent has the liberalised, fast growing economy and the rejuvenated and reformed financial sector succeeded in delivering financial services to the people of Mozambique? Put differently, how inclusive is financial sector development in Mozambique?

To answer this question, the United Nations Capital Development Fund (UNCDF), FinMark Trust and the Centre for Financial Regulation and Inclusion (Cenfri) partnered to undertake a Making Access to Financial Services Possible (MAP) diagnostic in Mozambique in 2013-14. MAP combines a comprehensive analysis of the demand for, supply and regulation of retail financial services in a specific country with a dialogue process among the main stakeholders in the financial sector. In this manner it seeks to both assess the current state of access to and usage of financial services, and identify opportunities for the extension of financial services to improve individual welfare and wider economic growth.

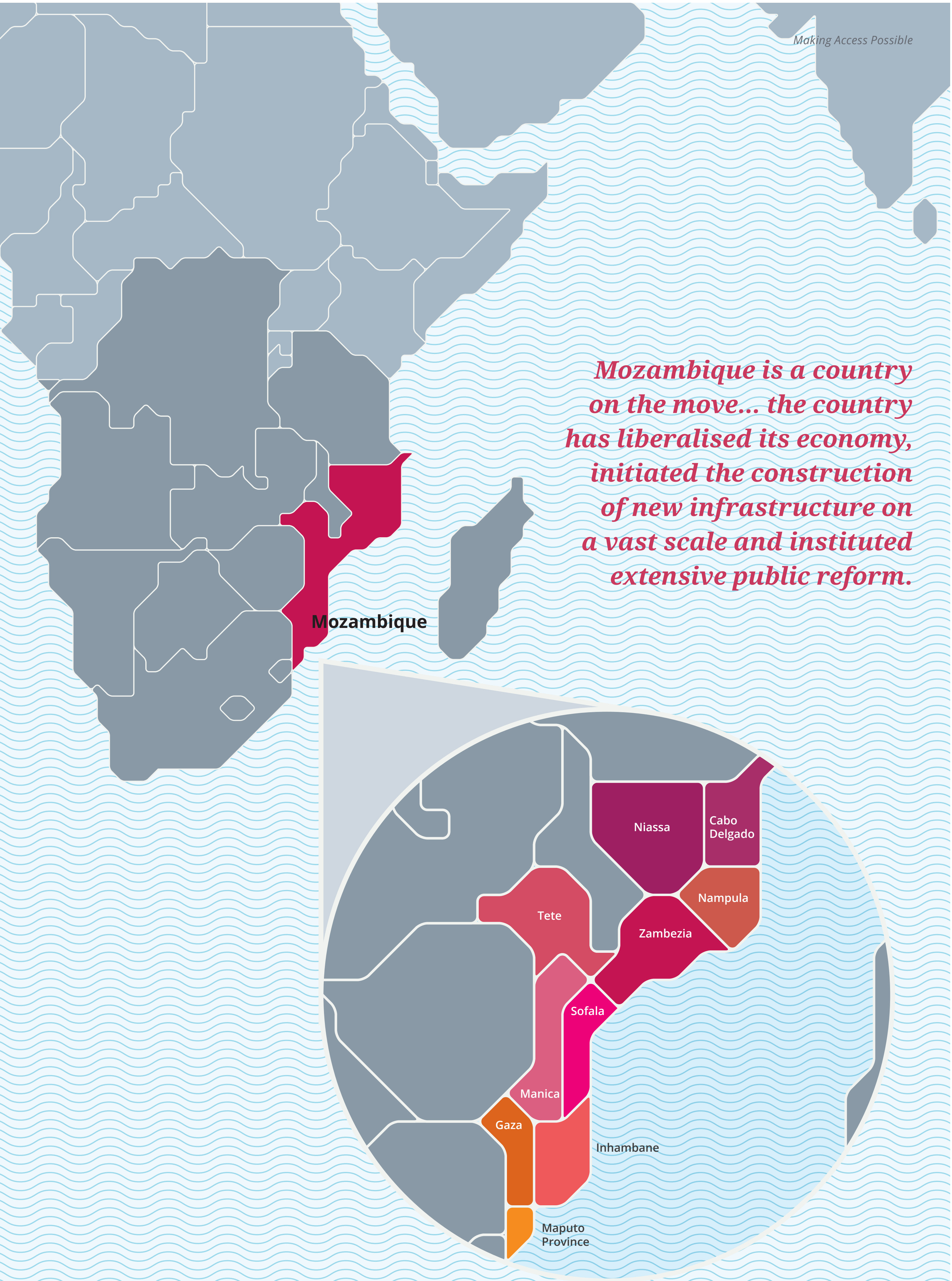
MAP Mozambique was able to draw on a number of primary data sources to create the most comprehensive picture yet of financial inclusion in Mozambique:

- FinScope consumer surveys[1] from 2009 and 2014 provided comprehensive, nationally representative surveys of consumer realities, perceptions of financial services, needs, access to and current usage of all categories of both formal and informal financial services. Comparison of the two surveys enabled an assessment of progress over the five year period.
- FinScope MSME survey conducted in 2012 provided data on the use of financial services by Micro, Small and Medium Enterprises.
- Qualitative demand-side research consisting of 60 individual interviews, 6 focus groups and 36 market place interviews was used to interrogate specific target market segments Interviews and focus groups in the Northern provinces focused on adults involved in agriculture, in the central provinces the focus was on tourism, and in the south the focus was on urban traders in Matola and Maputo.
- Supply-side information was drawn from financial sector data obtained from the Banco de Mozambique (BdM), the Institute of Insurance Supervision (ISSM) and individual financial institutions.
- A market scan of entry-level financial products was undertaken in 2014 to determine, among other things, available products in the market and eligibility requirements that may pose barriers to accessing these products.
- In-country consultations with public, private and non-governmental organisations were undertaken in 2013 and early 2014.

1. FinScope Consumer Survey is national representative survey – www.finscope.co.za



Mozambique is a country on the move... the country has liberalised its economy, initiated the construction of new infrastructure on a vast scale and instituted extensive public reform.



1 Financial inclusion policy

The Government of Mozambique has expressed a strong commitment to build an inclusive financial sector. The Mozambique Financial Sector Development Strategy articulates a number of strategies to achieve a goal of no less than 35% of the adult working age population having physical or electronic access to at least one financial service provided by a regulated financial institution by end 2020. These strategies include the development of financial sector infrastructure, including payments systems, building a microfinance sector, promoting rural financial services, and enhancing financial literacy and consumer protection.

2 Market findings

Increase in banked population. FinScope 2014 found significant growth in financial inclusion since 2009. Figure 1 below shows that the banked population increased from 12% to 20%. Adults served exclusively by other formal financial services, such as microfinance operators, insurers or mobile money operators, increased to 4% from almost nothing[2]. The current 24% of adults reporting formal access brings the country within striking distance of the 35% target set by the government for 2020.

Growth in financial inclusion reaching a ceiling. However, MAP reveals two major challenges with the current growth of financial access. Firstly, Mozambique is close to reaching a ceiling for formal access beyond which it will be very difficult to grow. Secondly, the character of formal financial inclusion as it evolved in Mozambique delivers limited value to households and does not make the contribution to the country's growth and development that it should.

Stark urban rural divide limiting expansion of formal financial services. Figure 1 below shows that nearly two times as many urban adults as rural adults report using any kind of financial services, reaching as high as four times for financial services offered through banks. Unless determined action is taken by both government and financial services providers, it will be very difficult to break through the barriers that obstruct financial access for the bulk of the rural population. Two thirds (67%) of Mozambique's 14.43 million adult population resides in rural areas. Only 13% of them have access to formal financial services, compared to 44% of the urban population. FinScope 2014 revealed that half of the rural population never travels to a bank branch, ATM or other financial institution, whilst 80% of urban adults do. Those who do want to reach a bank branch or ATM in rural areas usually have to travel more than one hour, effectively making it unaffordable. Large components of the rural economy is not even monetised. Of those who farm, 41% do so entirely or largely for subsistence and 26% of the population receives their income or other support in both cash and in kind. The remaining economic exchanges take place in cash. Most rural Mozambicans thus live in a pre-financial society, drawing on their local community and family to survive and deal with risk events. The financial sector is not evolving in a direction where it can serve the rural population effectively any time soon. Moving beyond the 30% to 40% level of formal access will thus require significant changes in infrastructure and supply of financial services.

Informal services meet most of the population's financial service needs. MAP revealed that bank accounts are overwhelmingly used by clients to meet two needs – to send or receive remittances within the country or to receive a salary. Beyond these two uses, formal financial services serve very few needs - payments, credit, savings or risk management - of the country's population. The bulk of the nation's financial services needs are met through informal services, of which cash transactions and informal savings

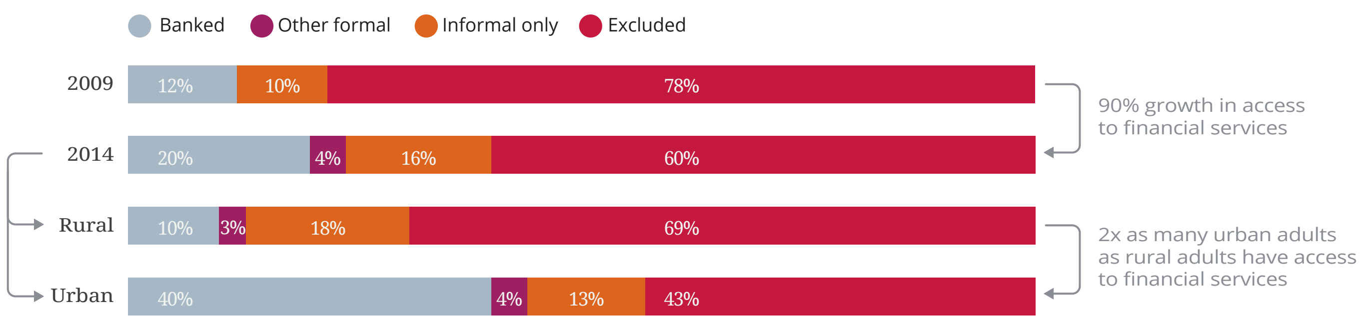


Figure 1: Mozambique financial access strands
Source: FinScope Consumer Survey 2009, 2014.

2. The access strand is inclusive from the banked side, i.e. those indicated as banked, may also use formal non-bank or informal services.

Those who do want to reach a bank branch or ATM in rural areas usually have to travel more than one hour, effectively making it unaffordable.

through xitiques are by far the biggest. Figure 2 below deconstructs the access strand to show how many people use both formal and informal financial services. It highlights that when taking into account total usage more people use informal services than formal services. Further, most adults who report using formal financial services use only one, but use more than one informal service, with almost all their transactions done in cash and not electronically.

MAP reveals that informal financial services provide a high adoption threshold which formal providers need to overcome if they want to capture the informal market. The extent of this barrier to the adoption of formal services is illustrated in Figure 2 which shows that salaried and government workers, the highest income and most formalised of all market segments in Mozambique, make extensive use of informal financial services despite their unhindered access to banking products. As will be seen later, there is little evidence that financial infrastructure and service delivery in rural areas will lift formal financial services over the adoption threshold in the next 5 – 10 years under current conditions.

To understand these dynamics better and explore alternative options to widen (give access to more people) and deepen (get those with access to use a portfolio of products) financial access, MAP disaggregated the adult population into discrete target markets based on main source of income.

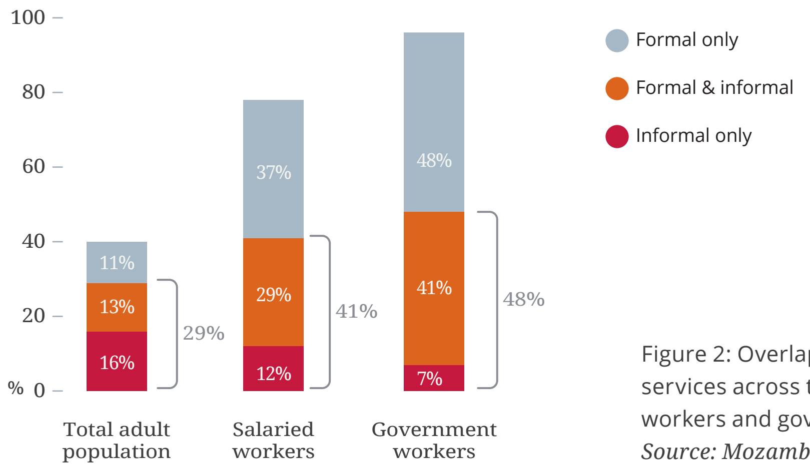


Figure 2: Overlap of formal and informal financial services across total adult population, salaried workers and government works
Source: Mozambique Finscope Consumer Survey 2014

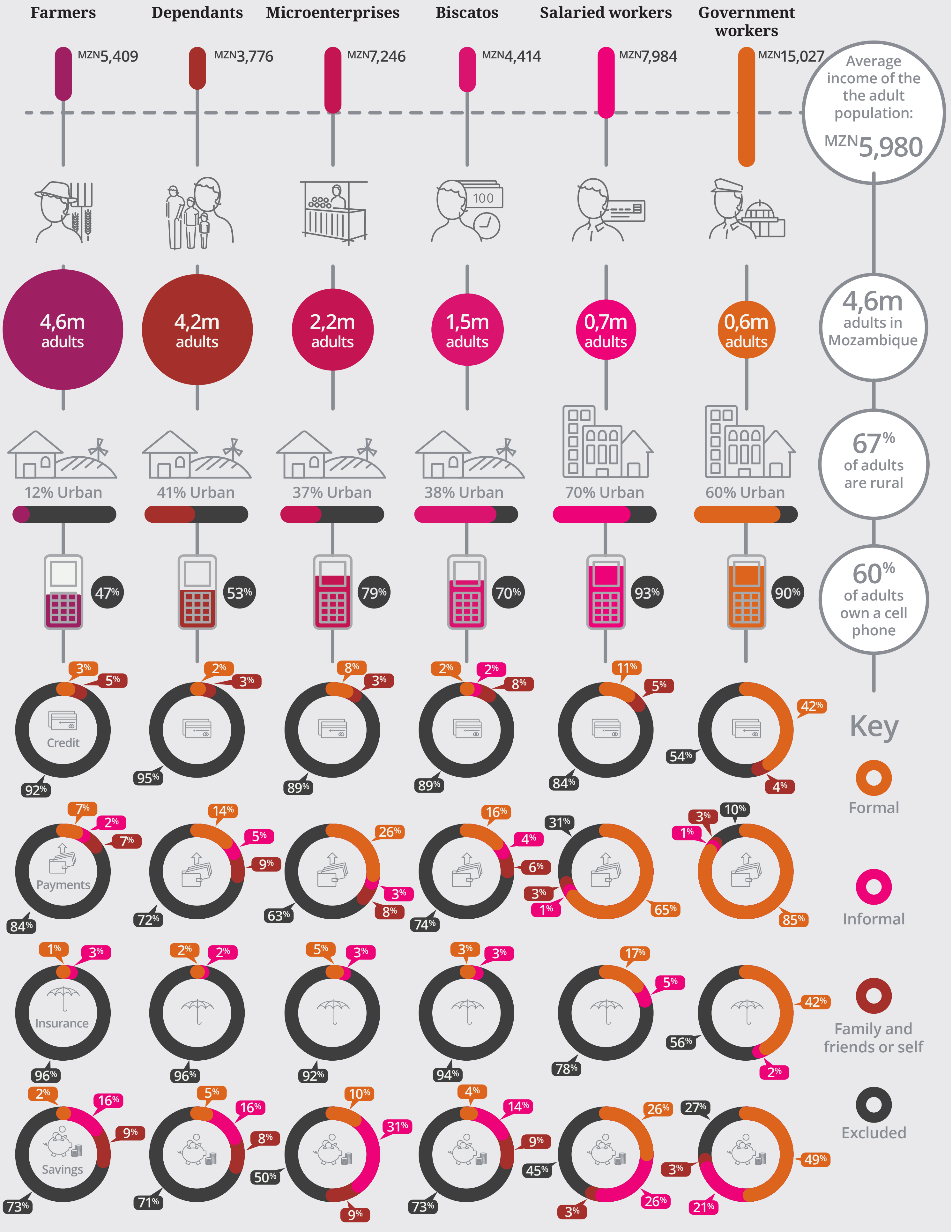


Figure 3: Target market infographic

Source: Mozambique Finscope Consumer Survey 2014

3 The Mozambican Consumer

MAP identified six discrete target markets and developed a demographic and financial access profile for each (see Figure 3). The six target markets are:

- ***Farmers***, i.e. those that derive their main income from agricultural activities or fishing, 88% of whom live in rural areas.
- ***Dependents***, who rely on their households for money and sustenance or to pay their expenses. Those whose main income is remittances also fall in this category. Dependents are mostly women (67%) and mostly young, the biggest age category being 16 – 20.
- ***Microenterprises*** represent those who receive their primary income from their own business. Half of this target market (49%) is women.
- ***Biscato***, the local term used for piece job workers, have a lower income than farmers, but a higher education level.
- ***Salaried workers***, which include only private sector salaried employees to distinguish them from government workers whose average monthly income is almost double that of their private sector counterparts (MZN 8 000 vs MZN 15 000).
- ***Government workers***, who have the highest incomes and best financial access of the entire population, but constitute the smallest target market at 4% of the total adult population. Together with the 5% salaried workers, the formally employed constitute only 9% of adults.

Farmers the largest target market. Unsurprisingly, farmers are the largest target market at 32% of the adult population. The surprising development, though, is that FinScope revealed that from 2009 to 2014, adults deriving their primary income from agriculture-related activities increased by 40%, well above the growth rate of the overall population over the same period. The only other target market that increased disproportionately since 2009 is government workers, who grew by 60%. This suggests that Mozambique's economic surge has failed to pull any significant numbers into formal employment outside of government. More people are being pushed into agriculture to survive where access to formal financial services is the lowest.

The farmers target market includes only those that derive their primary income from agricultural. However, more than 50% of all target markets indicated that they are involved in or connected to agriculture in one way or another, confirming that agriculture remains the lifeblood of the Mozambican economy. The link between the formally employed and agriculture is particularly strong, with payroll lenders reporting that a large proportion of their clients, which are exclusively government employees, use their credit facilities to buy agricultural inputs. The same goes for microfinance providers. A significant proportion of what is reflected in BdM statistics as personal loans is therefore in fact agricultural credit.

Three promising target markets. Government workers, salaried workers and microenterprises are the most promising target markets for improved financial inclusion in the foreseeable future. These three target markets report the highest current access to formal financial services, with almost 90% of government workers and 70% of salaried workers having access to formal services. MAP shows that at least half of adults included in the microenterprises target market should be categorised as survivalist entrepreneurs. Survivalist entrepreneurs are entrepreneurs out of necessity rather than choice with no option for a wage or salary income. This group of entrepreneurs report a similar financial access and usage profile to dependents or Biscato. The remainder of the microenterprise target market, considered aspirational, take up enterprise out of choice and report higher levels of financial services usage, similar to that of salaried and government workers. Further, the bulk of the adults in these three target markets (government workers, salaried workers and aspirational microenterprises) are located in urban areas within easier reach of formal providers.

These three target markets, which jointly comprise about 17% of Mozambique's population, merit priority attention not only because they are feasible to reach, but also because they provide a channel for sustenance and financial services to a significant portion of the rest of the population. For example, 57% of government workers remit money to someone elsewhere in Mozambique. At least one in three persons in these target markets have more than one income, implying that financial services, particularly personal credit, provided to them reach agriculture and microenterprises. More directly, the qualitative research revealed that many of the agiotas, or informal money lenders, are in fact formal employees who conduct informal money lending operations to earn additional income. The formally employed is thus a major financial services gateway to the other target markets.

Yet, these priority target markets are currently thinly served with financial services. Whereas more than 40% of government workers have access to credit, mainly due to the growth in payroll credit over the past five years, formal credit to salaried workers and aspirational SMEs is about 10%. Their usage of formal savings is even less and only government workers have any significant take-up of insurance.

What is the ability of the formal financial sector to reach these three core target markets and, beyond them, the other target markets of which more than 85% are currently excluded from formal financial services and more than 50% from formal and informal financial services?

4 Drivers of financial inclusion

MAP identified four drivers impacting the expansion of financial access to the majority of adult population:

1.

Citadel economy confines formal providers to urban areas. A number of factors converge to make it difficult for formal financial providers to provide services much beyond the main urban areas. Although being addressed, the infrastructure deficit beyond urban areas remains acute. Only a quarter of rural Mozambicans live within 2 kilometres of any road in the classified road network. If it is hard for citizens to travel in rural areas, it is even harder for financial institutions to install and maintain basic financial infrastructure to serve these people. This is illustrated by the fact that 47% of all bank branches, 45% of ATMs and 60% of POS devices are concentrated in Maputo City and Maputo Province, with less than 5% of these contact points present in Cabo Delgado, Zambezia, and Niassa respectively. Even within these provinces access to financial services is concentrated in urban areas. Figure 4 illustrates this by comparing the percentage of adults living within 30 minutes of a bank branch to the number of adults considered financially included across and within provinces in Mozambique.

The citadel walls are reinforced by Mozambique's parallel legal system, with civil law governing the formal urban economy, and customary courts, recognised in the 2004 Constitution, prevalent in rural areas. The customary courts have jurisdiction in small value civil claims and are the de facto means of dispute resolution for most Mozambicans. Yet, financial transactions involving formally regulated institutions are almost exclusively contracted under civil law processes. These do not coincide with localised community customs and values. The result is that formal financial inclusion is concentrated in urban areas, while the customary courts underpin the healthy growth in informal financial services both in rural and urban areas. Engendering an understanding of legal pluralism in formal financial institutions presents a significant hurdle to increasing formal financial inclusion.

These two structural divides between those inside and those outside the citadel walls, are exacerbated by the way in which the economy has developed over the past two decades. With an average education level of 1.2 years, most rural Mozambicans simply do not possess the skills to take jobs in skills intensive megaprojects or the services sector developing in the larger cities. Available credit is also being sucked out of rural areas to megaprojects and urban areas, with only 3.5% of credit going to agriculture in 2013 compared to 20% in 2000. Since income is probably the largest single driver of usage

Even the small number of employees that receive their salary in cash prefer to withdraw it immediately and conduct the rest of their transactions in cash.

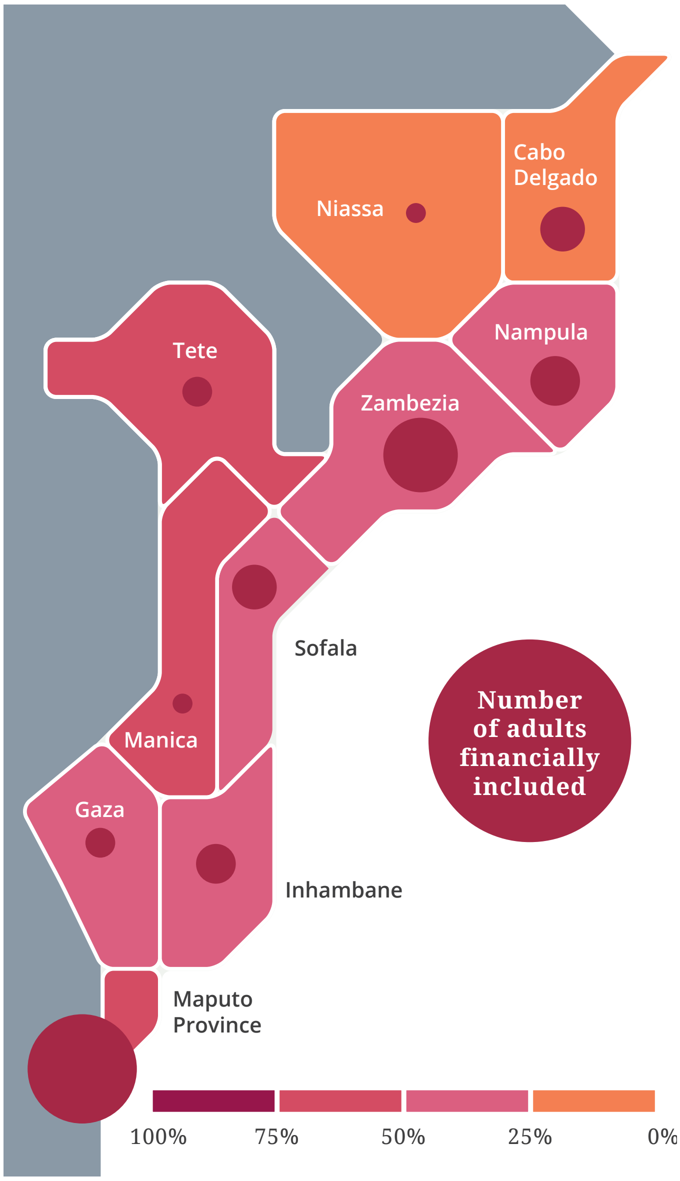


Figure 4: Percentage of adults living within 30 minutes of a bank branch compared to the number of adults financially included across and within provinces in Mozambique
Source: Mozambique Finscope Consumer Survey 2014

of financial services, the income divide between rural and urban areas is mirrored in their demand for formal financial services. The level of under-development in rural areas finds expression in a very low demand for financial services. An unmet demand for formal financial services is normally articulated through the use of informal services. Yet in rural Mozambique more than 50% of the adult population do not even use informal financial services, cash payments excluded.

2.

A starved cash ecosystem. The ability for an individual to connect with an electronic payments network, even if only to make a cash deposit or cash payment that is recorded in electronic value, provides the entry point for that individual to access formal financial services. If such cash to electronic value (and vice versa) access points, such as bank branches, bank agents, mobile money agents, ATMs or POS devices, are inaccessible or unable to fulfil their encashment function, it is virtually impossible to move a market to formal financial services. This barrier is acute in a market such as Mozambique, where the bulk of all transactions happen in cash and 66% of the population transacts exclusively in cash.

MAP reveals that even the small number of employees that receive their salary in cash prefer to withdraw it immediately and conduct the rest of their transactions in cash. The international yardstick for the level of adoption of digital commerce in retail economies is the ratio of POS transactions to ATM transactions. Predominantly cash-based economies like India report around 7 POS transactions per ATM withdrawal, and the G20 countries around 16. The Mozambican figure is 0.36, reflecting an overwhelming preference for cash and very low adoption of digital services.

Changing to digital payments will require some significant shifts. Mozambique does not have a real time, verifiable merchant payment system that is accessible and reliable enough to reduce payment risk at point of delivery. The retail payment systems that do exist are not interoperable, making an already narrow footprint even narrower. The 1300 ATMs that do exist are not able to carry the load for current demand, particularly during paydays. For many people who have to travel far to an ATM or bank branch, receiving their salary electronically is a hardship rather than a blessing.

Cash that is available is sucked into urban areas, because electronic payments for bulk purchases are not available. For example, service stations pay for fuel deliveries in cash. These and other bulk cash payments syphon off much of the available cash, leaving rural areas cash starved. This pushes rural areas further below the minimum encashment floor required to support digital payments.

3.

Banking regulation undermines the extension of cash infrastructure. Aviso 5/2009 was intended to increase transparency and reduce fees by prohibiting banks from charging any fees on cash deposits or withdrawals at bank branches. However, because banks are unable to recover these encashment costs for ATMs, Aviso 5/2009 has had the unintended consequence of dissuading banks from establishing encashment facilities and extending cash infrastructure in many rural and logistically difficult areas throughout Mozambique.

Instead, Aviso 5/2009 encourages branch-based transactions, which are the most expensive mode of banking. Further, because providers are prevented from charging certain fees, they must recover costs through different fees. This has resulted in misalignment in pricing of products and services. For example, banks cross-subsidise encashment with other higher margin fees such as statement and electronic banking ad valorem charges. This prevents banks from instituting a fee structure that would encourage a transition to digital transactions.

This is reinforced by banking regulations which also stipulate strict, extensive and indiscriminate requirements for bank branches, which effectively preclude banks from exploring partnerships with alternative distribution entities. There is also no regulatory framework for remittances, e-money and cross-border payment services, which creates uncertainty for providers and discourages investment in products dependent on electronic payments.

4.

A capital constrained financial sector. Bank capital is primarily tied up in high-earning opportunities, much of which indirectly relates to the megaprojects. The majority of banks, both large and small, must syndicate in order to finance fuel imports, the increased demand for which has been driven partly by the megaprojects. As foreign fuel purchases must be made in USD, banks must provide guarantees that are also denominated and ring-fenced in USD. Given the size and costs of fuel imports, this blocks off large amounts of capital from banks' balance sheets which cannot be put towards other activities, such as retail credit. Also attracting a lot of capital, credit is extended for high-value commercial or construction activities, many of which are ancillary to the megaprojects. Capital is further constrained by minimum reserve requirements for 8% of banks' daily liabilities, which must be deposited in cash, interest-free, with the central bank. With these factors absorbing and constraining capital, it is not surprising that the banking sector is neither geared towards nor focused on lower-value retail credit.

Despite significant advances in the financial services footprint and offering since the beginning of the century, these four forces conspire to place a ceiling on the ready extension of financial access in Mozambique. However, there are medium and long term strategies to lift this ceiling.

5 Financial inclusion priorities

The long-term project

The long-term extension of financial access in Mozambique will closely track the long-term restructuring of the macro economy. As physical and digital infrastructure expands into rural areas, education is extended and the government succeeds in growing agriculture and economic sectors outside of the extractive industries, incomes beyond urban areas and megaprojects will start growing. This will increase the demand for financial services.

For the foreseeable future, financial access will thus remain hostage to the macro economy. This should not detract from the significant intermediate advances that can be made in the financial sector itself.

Intermediate advances

However, some significant advances in financial access can be made, building on the momentum of the past five years. These relate to particular constraints on the financial sector which, if lifted, will make it easier and more cost effective for financial institutions to provide retail services across all product categories:

1. Facilitate interoperability in the retail payment system. When the electronic payment system is as restricted as it is in Mozambique, the over-riding strategy must be to make that which you have go as far as you can. Mandated interoperability across all the retail payment networks, including mobile payments, will benefit all financial institutions and increase the shift to electronic transactions.

2. Allow banks to price for cash. Evidence across multiple MAP countries shows that low income clients are prepared to pay higher than normal fees for services that are convenient to them. The notion that low cost banking transactions serves to extend financial access is therefore misplaced. Financial access will be extended far quicker if banks are allowed to price for cash transactions. This will make it viable for them to extend their infrastructure which will improve convenience for clients. This will require the regulators to revisit Aviso5/2009.

3. Improve liquidity of formal providers. As long as much of the capital of banks are tied up in the financing of fuel imports and mandatory deposits with the central bank, the retail credit market is unlikely to grow. There are strong structural economic reasons for these current provisions and they cannot be changed overnight. However, a signal that they will be relaxed gradually will prepare the financial sector to start building a serious credit policy, which is not currently evident.

4. Reduce client barriers seated in regulation. The new KYC regulations in Mozambique opens the door for proportionality by eliminating the requirement for showing proof of address for occasional transactions below a defined threshold. However these simplified KYC measures are not available for ordinary bank relationships such as for deposits or credit. Applying such simplified KYC requirements to other types of bank products or accounts would reduce eligibility barriers and benefit more customers.

5. Create sound regulatory frameworks for important product categories such as mobile money, cross-border remittances and microinsurance. The lack of clear regulatory frameworks for mobile money, cross-border remittance and microinsurance has created a gap in the market for these important products. Regulators need to create an appropriate space to incentivize providers to offer these services.

Normal business

Irrespective of any progress with the intermediate or long-term strategies, substantial advances in financial access can be made within the current framework. This should be based on an understanding of the behaviour of the different target markets and the powerful, but generally “hidden”, dynamic of intermediated access. By serving those within the “citadel”, financial providers are indirectly channelling credit and payment services to other target markets outside the “walls”. Households in Mozambique are currently far better at distributing financial services than formal providers. These informal market dynamics must be leveraged for the growth of the economy.

Much can therefore be gained by extending access to the three priority target markets – government employees, salaried workers and aspirational SMEs – and serving them with better products. Government policy and private providers should focus on these gains that are within reach, rather than the long reach rural strategies which will require shifts in the macro economy and infrastructure before they can be cost effectively pursued.

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