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MFIs and Mobile Phones
A powerful combination for Myanmar?

A Policy Brief on the regulatory aspects and potential of mobile financial service delivery by microfinance institutions for access to finance and socio-economic emancipation of rural and low-income households in the Republic of the Union of Myanmar

Executive summary

There is huge potential in allowing capable microfinance institutions and mobile network operators to use mobile financial services to provide international and local remittances. The potential is in the socio-economic enhancement of rural households, and the catalysing effects on financial sector effectiveness and economic growth in Myanmar. This on top of benefits that mobile financial services have upon the sustainable and effective provision of savings, credit and insurance services by lowering transaction costs for rural and urban households and financial service providers.

The Myanmar financial sector authorities have made huge steps forward to providing an enabling regulatory environment that allows for unleashing this potential. This paper aims to illustrate those issues that require further clarification and request such clarification, and give publicity to existing opportunities.

Introduction

On the 29th of July 2016, the new government of President U Htin Kyaw and State Counsellor Daw Aung San Suu Kyi issued its economic policy document. Since then, the government has received criticism for the lack of specifics, and the State Counsellor admitted not to be fully happy with some of the response the new government has given, so far, on questions and demands from the business community.[1]

This Brief has been inspired by the State Counsellor's speech made on the 22nd of October, and is a response to her call for the development and business communities for input on the government's efforts to achieve inclusive economic growth. It aims to make a proactive contribution to policy development and take steps toward the achievement of the government's objectives, i.e. to enhance access to finance for the rural population, economically active households and micro enterprises.

The Brief, on the subject of mobile financial services (MFS) and microfinance institutions (MFIs), targets both the financial sector policy makers and private sector actors that have it within their means to enhance financial inclusion through application of available MFS technology; the Central Bank of Myanmar (CBM), Microfinance Supervisory Committee (MFSC)[2], the Financial Regulatory Department (FRD) of the Ministry of Planning and Finance, the Mobile Network Operators (MNOs) and MFIs.

It aims to point out some of the existing regulatory and procedural issues to consider; to spell out the apparent legal space for MFI involvement and give publicity to it – not all MFIs (nor MNOs for that matter) seem fully aware of the precise regulatory situation; indicate market demand and opportunities in which MFIs to engage; and illustrate the potential positive effects on the socioeconomic well-being of rural and low-income households, financial sector development and economic growth in Myanmar.

Mobile financial services: a political priority

The demand for, and supply of financial services, has been diagnosed comprehensively and in detail as part of the "*Making Access to Finance Possible (or MAP)*" exercise for Myanmar.[3] The government's policy document on enhancing financial inclusion, which was based on MAP's results, identified the development of mobile financial services as a key, immediate priority toward enhanced access to finance for the financially excluded portion of the Myanmar population.[4] This priority has since been confirmed in the Myanmar National Economic Policy document issued on 29 July and in public statements by the CBM governor and deputy governors.

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[1] Speech by State Counsellor Daw Aung San Suu Kyi on 22 October in MICC II in Nay Pyi Taw.
[2] The MFSC is the main policy maker, and highest regulatory and supervisory body with regard to MFIs, and is chaired by the Union Minister of Planning and Finance. See Chapter IV of the Microfinance Business Law (2011).
[3] See for the diagnostics: http://cenfri.org/making-access-possible/map-myanmar; and for a video summary of results: https://www.youtube.com/watch?v=2k2v0Ii_w2E.
[4] Myanmar Financial Inclusion Roadmap: http://www.uncdf.org/en/myanmar-financial-inclusion-roadmap

The market potential

In Myanmar, 70% of people live in rural areas, and 58% of adults make a living from (often unproductive) agricultural activities. Counting those who are dependent on the income of other household members (e.g., spouses), the total percentage of people who depend on agriculture is even higher. Because of a combination of the risky nature and low productivity of agricultural activities, combined with rural households' need to maximise income from its available members' human resources, there has been a trend for younger members to move to urban areas in Myanmar and Thailand, to raise and diversify household income. In considering only international migration and incoming remittances are, the numbers are staggering.

The World Bank's Migration and Remittances Factbook for 2016 officially estimates the value of incoming international remittances at USD 3.5 billion in 2015, about 5% of Myanmar's GDP, generated by 3.1 million migrants. The Factbook, however, has made the caveat that true numbers can be expected to be much higher in cases where migration and remittances are highly informal, such as in the situation of Myanmar.[5] A 2012 World Bank publication on the issue concluded that the real amount of remittances is about double the official number, which would put the true number for Myanmar at USD 7 billion for 2015, or about 10% of GDP.[6]

These data, combined with the overwhelming information on the high level of informality of remittance methodologies, suggest a large untapped market that could well be served by formal financial service providers, such as banks and MFIs.

In fact, there is a range of policy recommendations to that effect, including those made by MAP, and related studies, that emphasise use of mobile-phone based technologies. Such technologies have been enabled by the successful roll out of an effective and low-cost mobile-phone telecommunication services infrastructure and high levels of adoption of mobile phone technology by the Myanmar population: the 2016 LIRNE Asia MIDO survey estimated household mobile ownership at 83% and household smartphone ownership at 65%.[7]

Impact on financial sector access and transaction costs

MFS technology holds the potential to dramatically increase financial sector access, both through non-financial agents that provide cash-in and cash-out functions, and through the mobile phones themselves. For Myanmar, where the number of financial sector access points is low (particularly in rural areas), and transactions costs high, MFS serves to solve both.

This paper primarily focuses on the direct effects of MFS in enabling remittances and rural households' socio-economic emancipation. However, we emphasise that MFS can greatly enhance access to savings, credit and insurance products, as well as their quality and usage. MFS allows for making many small payments at low cost and at great convenience, enabling a

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[5] In line therewith is the estimate of the International Organization for Migration, which says that 10% of Myanmar's population, about 5 million people, live outside of Myanmar.
[6] "Gaining from Migration: Trends and Policy Lessons in the Greater Mekong Sub-region", World Bank 2012.
[7] LIRNEasia 2016 MIDO survey Myanmar http://lirneasia.net

channel for payments of interest, instalments, insurance premiums and - perhaps most importantly - savings.

The socio-economic relevance for rural and low-income households

The relevance of remittances for rural households is reflected in survey results - for many rural households, remittances constitute a main source of income. MAP found that 12% of households had received remittances from within Myanmar alone and MAP data suggests that as many as 25% of households are receiving remittances overall. A regional household survey in a rural area found that remittances made up 22% of the incomes of overall surveyed households, with income from agriculture only slightly higher at 24%.[8]

The impact on economic growth and financial sector development

In addition to the direct importance of remittances for recipient households, remittances have (strong) positive impact on both financial sector development and on economic growth. As research has shown, in countries where the financial sector is less developed, remittances perform a role as a substitute for financial sector services in supporting economic growth[9]. At the same time remittances stimulate uptake of deposit and credit services, intermediated by the banking sector of the recipient country.[10] The labour migrant population and incoming remittances constitute not only a strong foundation in terms of income and social insurance for lower-income and rural households, but also present an enormous opportunity to enhance economic growth through additional investments, financed by recipient income and catalysed financial sector intermediation.

Space for involvement of banks and MFIs to enhance financial inclusion

In 2011 the government prioritised MFIs as a means to provide formal financial services to "*the basic-class people*", i.e. the lower-income part of the populace. Banks, with the exception of the state-owned agricultural policy bank Myanmar Agriculture Development Bank (MADB) are primarily involved in financing large companies and conglomerates, and some high net worth individuals. Being constrained by an artificially set 5% interest rate spread and strict collateral requirements, banks have had little space for manoeuvring, even if they wanted to downscale.

Currently, banks are allowed to accept moving assets as collateral yet are still restrained by the 5% cap. Some banks, in particular Yoma Bank and CB Bank, have shown interest in reaching out to (M)SMEs and economically active households. The main way of operating in this space is

[8] International Food Policy Research Institute, the Centre for Economic and Social Development, Mon State Government and Michigan State University, 2016 (http://www.ifpri.org/blog/revitalizing-agriculture-rural-myanmar). The study in Mon State also found that 31% of adults aged 15-45 were abroad and that 50% of households have a family member that has migrated.

[9] "Remittances, Financial Development, and Growth", prepared by Paola Giulia and Marta Ruiz-Arranz, authorized for distribution by Eswar Prasad and Arvind Subramanian, Research Department, IMF Working Paper, December 2005.

[10] "Do Workers' Remittances Promote Financial Development?", Reena Aggarwal (McDonough School of Business, Georgetown University), Asli Demirgüç-Kunt and Maria Soledad Martinez Peria (The World Bank), World Bank Policy Research Working Paper 3957, July 2006. We mentioned this earlier in the Brief.

through hire-purchase constructions (which are not bound by the gap) induced by the gracious support of development partners in the form of credit guarantees, technical assistance, and grant funding.

Apart from some hire-purchase products, the under-limit on the size of loans issued by banks is still around USD $50,000, an amount too large for the majority of both the enterprise community and the general population. For the longer-term future, CBM has indicated that it will allow liberalisation in some parts of the retail market, including market-based pricing of interest rates on deposits and credit. For now, however, even with a view to the medium term, banks are not the natural partner for the lower-income part of the population, especially the rural population and including the large number of micro enterprises that together make up an overwhelming majority of the financially excluded population. Financing the excluded groups requires specific organisational competencies, expertise, and systems that can not and should not be expected to develop overnight.

By definition, MFIs are the natural partners of many of the currently excluded groups. MFIs can only provide uncollateralised loans of amounts up to USD $4,000. Targeting formally excluded groups is the foundation of their business proposition. MFIs are allowed to make 2.5% in interest per month and can levy fees, allowing them to compensate for higher operational costs and risks involved in delivering smaller-sized financial services to clients with lower incomes.

Myanmar has the benefit of having around a dozen foreign-owned MFIs that have been successful in their home countries (and some other foreign countries) and have the strategic and funding partners, expertise, systems and financial strength that allows them to scale up their activities in Myanmar on relatively short notice. Some of those have been involved in the delivery of MFS. Examples include ACLEDA in Cambodia; Vision Fund in Tanzania; and BRAC in Bangladesh and Uganda. Dawn MFI (ACCION) even has a Digital Solutions Group in its worldwide organisation For Myanmar. This international presence brings a great opportunity to leapfrog existing impediments such as lacking physical infrastructure and brick-and-mortar branch networks. Some local MFIs also seem to have the capacity to and are working on MFS.

There is a great potential in enabling and supporting MFI involvement in the delivery of MFS in Myanmar. MFIs are the natural partner for many of the financially excluded households in rural areas for whom remittances are so important as an income source and as social insurance. On top of that, incorporating remittance delivery through MFIs has the potential to catalyse financial sector development and economic growth, and enable low-cost, safe, good-quality, effective and accountable financial transactions.

The legal situation for MFIs to provide remittance services & MFS

The jurisdiction of the CBM over payment systems and financial institutions' involvement in MFS is detailed in the Law on the Central Bank of Myanmar, the Financial Institutions Law and the MFS regulations based thereon.[11] Unlike banks, however, MFIs are not governed by the Financial

[11] Central Bank of Myanmar Law (No.16/2013, 11/07/2013); Financial Institutions Law (No. 20/2016, 25/01/2016). For banks, non-bank financial institutions and MNOs that would like to provide e-money or MFS, the legal

Institutions Law, but rather by the Microfinance Business Law and the MFSC Directives based thereon.[12] Do these allow MFIs' engagement in providing remittance services? And MFSs?

The Microfinance Business Law allows MFIs to "*carry out remittances,*" but only based on prior approval of the MFSC.[13] Until recently, the MFSC didn't allow MFIs to provide remittances.[14] That has changed as recently as the 29th of August 2016. In a Directive issued that day, the MFSC stipulated that MFIs seeking to provide remittance services should submit their business model and plans for approval.[15]

Earlier - and this is seemingly not much known or publicised - MFIs were in principle already allowed to provide MFS, but not to use it to provide remittance services.[16] Under the heading "*Mobile payment system for MFIs*," the Directive stipulates:[17]

> *"Apart from local and international remittances, Microfinance Institutions can utilise mobile payment systems when performing microfinance activities." "The following terms and conditions are to be abided by in exercising mobile payment systems:*
>
> *(1) To introduce Mobile Payment Systems, firstly MFIs have to apply to CBM and the Ministry of Transport and Telecommunication (MoTT);*
> (2) *MFIs must firmly follow the CBM Directive related to Mobile Banking (No.4/2013, 03/12/2013)".*

Now that the new MFSC Directive has withdrawn the limitation on the provision of remittance services by MFIs, the potential of MFI involvement in MFS and remittances – i.e. that which is described earlier in this Brief - could and should be unleashed. So what are procedural issues for MFI involvement?

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framework is given in Sections 128-132 of the Financial Institutions Law, and the regulations and directives that have been based thereon: CBM Directive on Mobile Banking (No. 4/2013, 03/12/2013) and CBM Regulation on Mobile Financial Services (No. FIL/R/01/03-2016, 30/03/2016).

[12] Article 2 (jj) juncto article 19 (a) of the Law on Financial Institutions. MFIs are categorized as Scheduled Institutions, which are financial institutions that have been established under a law other than the Financial Institutions Law and provide financial services for a specific group or a community. In the case of MFIs, The Microfinance Business Law defines the group as "*the public, including low-income peasants, labourers and vendors who reside in rural and urban area*". Careful reading suggests this group consist of the entire (adult) population of Myanmar and really isn't a specific group, which the definition of Scheduled Institutions has suggested.

[13] Microfinance Business Law (No.13/2011, 30/11/2011), Sections 2 and 29.

[14] MFSC Directive No. 2/2011, 23 Dec 2011.

[15] MFSC Directive No. 3/2016, 29/08/2016, Article 2 (f). Remittances are included in the "*other services*" category the article mentions.

[16] MFSC Directive No. 3/2014, 13/10/2014. Article 2 (C 1-5). Article 2 C.3-5 state: *"(3) The Microfinance Law, including its procedures and directives, must be followed precisely; (4) In order to protect the clients' benefit, MFIs are required to have a plan to deal with issues rising from clients' limited knowledge on Mobile Payment System and or technical incompetency of the system. (5) Directives related to mobile payment system, occasionally issued by MFSC, MFI Development Supportive Committee and FRD, are to be followed exactly. Information on mobile payment system may be demanded and supervised."*

[17] Non official translation.

Procedures and requirements

As we can see from the previous paragraphs, the procedures and requirements for the license to provide MFSs and the one to provide remittance services are different. The former requires "*application*" to CBM and the Ministry of Transport and Telecommunication (MoTT); the latter to "*submit an application (to MFSC) with a business model and a business plan*."

MFIs and remittances

So far, MFSC hasn't issued any details on rules or principles that will guide its decision to allow remittance services, which generates significant regulatory uncertainty for MFIs. We call upon the MFSC to provide these regulations and principles, upon MMFA to advocate on behalf of MFIs, and on development partners to support MFSC and FRD on the issue.

MFIs and MFS: Questions Remaining

Similarly, there is a need for clarity on what it means for an MFSC Directive to refer MFIs to the CBM (and MoTT) for MFS licensing. The following pertinent questions remain unanswered: Is the CBM amply aware of this Directive? Will the CBM accept applications from MFIs? Will, and should, the CBM apply its Mobile Banking Directive to MFIs' request? If the CBM issues licenses to MFIs, does this mean it will require MFIs to report to the CBM and accept CBM supervision? If it issues licenses to MFIs, will the CBM inform and coordinate with MFSC on supervision?

We have not yet been able to probe the issue conclusively in preparing this Brief and call upon the MFSC and CBM to provide clarity in their coordinated efforts. We also call upon the MMFA, and individual MFIs, to probe the issue by simply applying, and for development partners to address the issue with MFSC through FRD.

When speculating on the CBM's position and reading its Mobile Banking Directive (which, according to MFSC's Directive should be the CBM's basis to decide on MFI MFS license requests), we consider that it is based on the Financial Institutions Law, which isn't applicable to MFIs. The CBM Mobile Banking Directive's article that describes its jurisdiction, similarly does not include Scheduled Institutions (the category which contains MFIs). It is possible that the CBM never intended for its Mobile Banking Directive to be applicable to MFIs. The time is right to probe and clarify these important issues.

Allowed services

The requirements for MFI licenses to provide remittances, and the requirements for MFIs to provide MFS, are distinct and issued by different agencies based on different regulations. Then what, exactly, are the services each of the separate licenses would allow?

License to provide remittances only

If an MFI obtains a license from the MFSC to provide remittance services, but does not simultaneously obtain a CBM license to provide MFS, we would make the assumption that all activities aimed at providing Mobile Banking Services as described in CBM's Directive (please find them summarized in the next paragraph), including the use of agent and Point-of-Sale devices, would not be allowed.

License to provide MFS only

If an MFI obtains a license from the CBM to provide MFS, but does not simultaneously obtain an MFSC license do provide remittance services; what is the MFI allowed to do? Article 2 of CBM's Mobile Banking Directive details the following categories of services that licensees are allowed to provide:

(a) Local Remittance and Remittance from abroad.
(b) Deposit and withdraw cash through agents, branches of banks, ATM, branches of Mobil Operator.
(c) Payment from person to economic business (for example- payment for bills, payment for goods and services)
(d) Payment from economic business to person (for example- payment of salary, profits, and refund for insurance).
(e) Payment from Government to person (for example- wages and salary, pension, other allowances).
(f) Payment from person to Government (for example- Tax, revenue).
(g) Payment between persons. (payment and transfer between each mobile bank account to other)
(h) Micro loan, surplus loans, other small payment like as insurance premium.

We deduce that, in such a case, an MFI would be allowed to provide all services mentioned under both, and to engage in cooperation with agents in providing microfinance services.[18] Here again, however, explicit clarification is needed.

The case to allow MFS-licensed MNOs to receive an MFSC MFI license

Another interesting case is that of Mobile Network Operators (MNOs) that have been licensed to provide MFS based on the CBM's 2016 MFS Regulation.[19] What would likely be the response if such an MNO were to request an MFI license, having met all requirements?

The combination of having insight into a customer's financial transactions would be of great value in making the credit assessment and allocation decision, reducing information asymmetry and allowing the MFS-based MFIs to strongly contribute to enhanced access to finance for lower-income and rural households. This could be based on detailed insights into their repayment capacity, further enhancing responsible lending. The options for clients to make smaller, convenient savings payments, and pay interest and instalments easily, transparently and with low transaction costs, creates a strong proposition for the socio-economic enhancement of the households. It would also help to streamline the supervisor.

What then if that MNO, after first having received its MFS license from CBM[20] and second its MFI license from MFSC, were to request a Mobile Banking license from CBM[21] and a license to

[18] Article 10 of CBM's Mobile Banking Directive.
[19] CBM Regulation on Mobile Financial Services (No. FIL/R/01/03-2016, 30/03/2016).
[20] Ibid.
[21] Based on CBM's Mobile Banking Directive (of December 2013).

provide remittances from MFSC[22]? There seems nothing standing in the way of a progressive MNO (or nonbank financial institution for that matter) to pursue such a path - and it would certainly have benefits. The bank-led mobile banking model allows for a much higher wallet size and for making and receiving international remittances. Currently MNOs licensed under the MFS Regulation of 2016 are only allowed to provide remittance services in Myanmar. The regulatory space for MNO-based MFS providers to accept a larger wallet size than the currently allowed MMK 200,000 per day and to receive international remittances would greatly enhance their impact.[23]

Issues for discussion and next steps

As regulator and market participants familiarise themselves with the new there will no doubt be challenge. There will and should be adaptations over time, and the opportunity for the regulator to build experience and trust.

Currently, however, there is a need for further clarification by the financial sector authorities and further coordination between the MFSC and CBM. There also is a need for strict prudential supervision and monitoring, to weed out unwanted market behaviour and actors that could damage trust in the financial system. The paper in hand aims to contribute to the learning curve and ongoing discussion on how to build a strong and reliable sector, something both regulators and the large majority of well-intended and capable MFI owners and managers wish to achieve.

The regulatory framework is making large steps forward in creating a space for capable providers to engage in and provide desperately needed financial services - this is promising. There is huge potential in allowing capable MFIs and MNOs to provide international and local remittance services (and MFS) both to boost the socio-economic well-being of lower-income and rural and to support sustainable development and continued economic growth.

For more information, visit our website: www.uncdf.org/myanmar or contact UNCDF Myanmar Country Coordinator Paul Luchtenburg by writing to 6 Natmauk Road, Tamwe Township, Yangon 11211.

[22] Based on MFSC Directive 03/2014, 29/08/2016.

[23] See CBM Regulation on Mobile Financial Services (No. FIL/R/01/03-2016, 30/03/2016).