



# Developing a Digital Financial Services Strategy in Nepal

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Nepal

Facts and figures

## Scaling up digital financial services in rural areas

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Nepal is a landlocked country with picturesque, mountainous terrain. The geographical diversity makes it a challenging place for digital financial services (DFS) deployments, mainly because of low population density, poor connectivity and infrastructure-related challenges. While it is a young, growing nation, the vast majority of the population remains financially excluded. DFS can play a key role in changing this landscape and offering adapted and affordable services to economically poor Nepalese people.

To pave the way for the spread of DFS, Nepal Rastra Bank released electronic banking guidelines in 2012. The guidelines were prescriptive and focused on developing an agent network in rural areas only. At present, there are 12 active deployments by banks/ financial institutions (FIs) with more than 1000

registered agents; however, none have been able to achieve significant scale nor exhibit precursors to large-scale success.

To support further development of services and enable market players to reach scale, Mobile Money for the Poor (MM4P) organized a workshop exploring DFS entry strategies and has been interacting with the players through various studies conducted over the past several months.

Entry strategies proposed for DFS in Nepal are discussed in this briefing note, including the strategies' related factors and customer segments. Key factors include expansion strategy, anchor products, distribution channel and interoperability and vary based on socio-economic conditions, DFS regulations and the current state of deployments.

## Key factors

### Expansion strategy

Two broad strategies that can be adopted by FIs are the following:

- Horizontal model (penetrate on a wide scale).
- Vertical model (penetrate with depth).

#### Horizontal model

Focused on driving the top line and volume by expanding outreach across rural and urban locations, the key factors to consider for this model are the following:

- Focus on driving payment transactions such as these:

- Person to person, both international and domestic, where doorstep delivery of the service and savings are important.
- Business to business, in arrangement with large corporates, creating efficiency in supply chain for dealer network by reducing cost of cash.
- Conduct mass marketing to drive uptake, especially above-the-line marketing.
- In communication, highlight pain points that the product offering addresses for customers with respect to transactions.

### 27.8 million

Total population

### 35%

Financial inclusion rate

### US\$ 694

GDP per capita

### 22.9 million

Mobile phone penetration



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**Vertical model**

Focused on driving the bottom line and value by expanding the reach of several products and services but at key strategic locations in a limited geographical area, especially in economically active markets, the key factors to consider for this model are the following:

- Focus on integration of product offering through a transaction value chain that will reduce the cost of setting up an agent network. It also creates balance by ensuring continuous use of agent channel and allows customers to develop trust in service, which further allows the FI to serve customers with a range of financial products, including credit, insurance, savings and remittances. Such an approach could be seen with these:
  - ↳ Microfinance, where digitising disbursement and repayment creates efficiency for microfinance institution and paves the way for the FI to offer new services.
  - ↳ Agriculture or non-agriculture value chains, which ensure a captive customer base riding on thriving economic activity and allow portfolio diversification opportunities for FI both through upstream and downstream arrangements.
  - ↳ Government-to-person payments, received on a regular basis, which not only allow for distribution of payments but also can be leveraged for developing credit and saving offerings that are based on ensured future cash flows.
- Conduct concentrated advertising focused on products to drive usage, especially below-the-line marketing.
- In communication, focus on customer needs and wants and, at the same time, on raising financial competence of clients.

The above-mentioned models can only succeed when they are developed along with other elements like the following:

- Design value propositions that motivate agents to drive uptake and usage of products, and treat the agents as customers themselves.
- Ensure the agent management system focuses on continuous training, monitoring and service support.
- Ensure real-time and seamless transactions, and ensure timely payment of commissions to agents.

No FI in Nepal has a double-digit market share. Thus, their ability to scale up on their own will always be limited and resource mobilization for agent banking channels will always be a challenge. In such a scenario, the key to sustainable development will be the ability to leverage and collaborate with other FIs and non-FIs, in order to build a robust agent infrastructure that fulfils customers' needs.

**Anchor products**

The growth of an agent banking model is rooted in need-based products and services that pull in customers. To design anchor products, it is important to segment the customer base and identify key needs. The products may differ based on the segment and the outreach model chosen. Some of the crucial elements are the following:

- Horizontal model: primary anchors may be quantitative (e.g., price, speed of delivery).
- Vertical model: primary anchors may be qualitative (e.g., design, customer experience).

Other elements may include cost, risk plus the perception of risk, accessibility, usability, etc. Choices can be clearly outlined while keeping the customer at the centre of the process and developing products accordingly.

**Distribution channel**

There are limits to the scale of growth that can be achieved if FIs develop and manage an agent network on their own. It is imperative to leverage the existing agent infrastructure to achieve maximum success. FIs often start from scratch to build an agent channel that they own completely; however, that approach is counter-productive and a lot more can be achieved by collaborating, building an interoperable structure and sharing agents. FIs can look at arrangements with companies that manage remittances, agriculture inputs or consumer goods, appoint them as super-agents and allow them to manage agents in a limited geographical area.

FIs can control all banking related functions directly, while distribution channels can be managed and supervised either directly or through an intermediary. Other housekeeping functions such as marketing, in-field servicing and monitoring of agents, assistance with agent identification/on-boarding, liquidity management and training can be outsourced. This division of responsibilities will sharpen focus, enable growth and make the business profitable.

**Interoperability**

Most FIs in Nepal have already chosen channel-level interoperability, which is linked to the servicing of the product on offer and includes intra-bank channels like interoperable ATMs, branches and agents. Given the geographical constraints, it will be essential for FIs to collaborate when they scale up their pilots in order to develop a DFS ecosystem—to manage costs, improve services and grow the market. Other forms of interoperability, either at the agent level or technology level, will be driven as the market becomes efficient and the players/outside forces become more interested in driving volume in an efficient manner.

In addition to understanding the building blocks discussed in this note, each FI needs to understand its revenue streams and cost structures based on its business plan. It is important to answer questions such as these:

- Which aspect of the business, if any, will be subsidised?
- What will be the pricing?
- How will sufficient numbers of customers be attracted?
- How will a network of agents be set up?

A clear financial model will direct proper allocation of resources, assist in planning operations and activities and drive partnerships.

A combination of the above building blocks and clear financial models will define the direction that FIs must take in order to expand through an agent channel and achieve their goal of fully functional financial inclusion for the low-income segment of their customer base.

**Key stakeholders**

**Regulator**



- Nepal Rastra Bank

**Main banks**

- Rastriya Banijya Bank Limited
- Nabil Bank Limited
- Nepal Investment Bank Limited
- Everest Bank Limited
- Himalayan Bank Limited



**Mobile network operators**



**Market share**



**Digital financial service providers**

- Laxmi Bank Limited
- MEGA Bank Nepal Limited
- Prabhu Money Transfer Limited
- Citizens Bank International Limited
- Siddhartha Bank Limited
- Global IME Bank Limited
- eSewa
- Everest Bank Limited



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