M-Payments in M-BRIC

How to best leverage the upcoming opportunity

Mobile financial services are experiencing a global surge, especially in emerging markets. Global total transaction volume is expected to reach approximately USD 280 billion by 2015. Clearly, there is an enormous potential for M-payments in M-BRIC countries, but how to best capture it? This article provides an overview of the best entry strategies and indicates how players in each country must consider specific local requirements in order to succeed in the m-payment market.

Transformational mobile financial services are a true convergence between the telco industry and the financial sector. Both industries have recently discovered new user potential in the practically unaddressed segment at the bottom of the pyramid – consisting of hundreds of millions of people in M-BRIC and representing the largest opportunity in their regions.

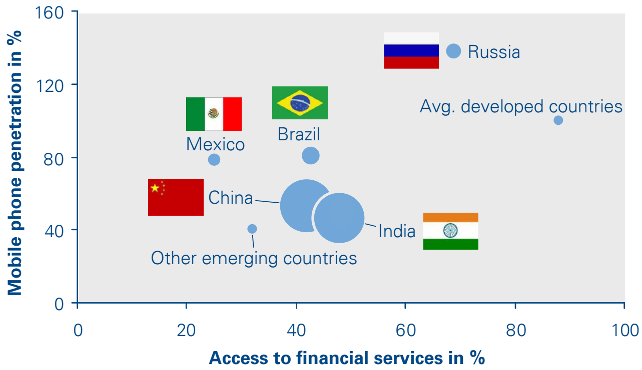
This viewpoint is based on qualitative interviews with numerous leading experts and CEOs from diverse industries, as well as a range of industry reports and case studies. For more details on the global m-payment market, please refer to our M-Payment Report Update 2009.

M-BRIC's high market attractiveness

M-BRIC countries are highly attractive markets for mobile financial services. Currently, only 32 million people in M-BRIC (42% of which are in India, 20% in China, 18% in Brazil, 12% in Russia and 8% in Mexico) use these types of services. We project that this number will increase to 290 million users (10% of total M-BRIC population) by 2015, representing a compound annual growth rate of 58%. These users are expected to conduct a total of 20 billion transactions in 2015, with India at 8 billion and China at 6.9 billion.

As every second person owns a mobile in these markets, potential entrants would not have to supply additional devices. In terms of the banking sector, over 70% of the population is currently excluded, which provides an opportunity for an alternative access to financial services. Although Russia is an exception with 140% mobile penetration and 70% of the population being banked, Russia's banking services are inefficient and many people are underserved. Therefore, mobile financial services have a great potential in Russia (see figure 1).

Figure 1. Mobile phone penetration vs. access to financial services



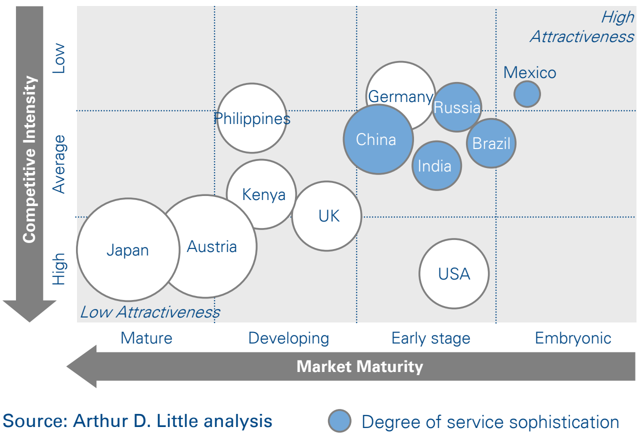
Source: Arthur D. Little analysis

These favorable preconditions and a low level of market maturity enable new entrants to actively shape the m-payment market. Moreover, competition among service providers is much lower than in advanced m-payment markets like Austria or Kenya (please refer to figure 2 overleaf).

M-BRIC – Different standards for different markets

M-BRIC is not a homogenous market, so each country needs to be analyzed independently in terms of its entry barriers and opportunities. China's telco and banking industry is highly consolidated, relative to the fragmented Russian market where there are many active local players (1,200 banks). Mexico has already implemented new regulations as of March 2010, which provide ample scope for players, but it will take some time for the market to mature as they need to prove themselves.

Figure 2. Attractiveness matrix



Source: Arthur D. Little analysis

Despite the varying market conditions, the size of the opportunity is reason enough to analyze these markets together.

There is a substantial base of people with a low-income spread across immense distances in these countries, in contrast to most other emerging markets. For that reason, there is a need for a more extensive distribution network, especially in rural areas. Furthermore, over 90% of all transactions are done in cash, which is perceived to be high-risk.

Mexico's regulations make a promising start

In Mexico, m-banking and top-ups are the only m-payment services currently available. Therefore, little experience with consumer adoption exacerbates problems with usage prediction and the design-of-use cases.

Opportunities for MNOs and third party providers exist due to a fundamentally altered regulatory environment. A legal loophole was created that allows bank-independent service providers to actively participate in the financial sector. They can play the role of niche banks (capital, rights and responsibilities are limited) and switches, which are also limited to m-payment transactions. These developments will further strengthen MNOs, and will give non-banking entities the ability to offer a variety of services, while only marginally integrating banks.

Brazil's government needs to free up regulations

The merchant network, consisting of micro-entrepreneurs that run small shops around the country, needs better rural coverage, especially in the North and Northwest regions. These businesses cannot be motivated to provide cash conversion for m-payments given the bureaucratic hurdles, such as costly licenses, as well as issues with cash handling. Additionally, in rural areas they can neither balance cash and e-float, nor convert money due to geographically dispersed bank branches.

The Brazilian government currently provides low-value, monthly payments as part of the social payment program, which total USD 5.9 billion p.a. These payments are currently made via lottery kiosks (68%) to mainly rural dwellers, and symbolize a significant opportunity for m-payments.

Players can profit from cooperation with aggregators to set up a network and, with the government, engage key accounts, which use m-payments on a large scale.

Quotes on the Markets

Russia

"Russia, in which most of population has no bank offices in even reasonable driving distance is a huge opportunity for remote payment services, and mobile payments are, definitely, a first option"
Victor Dostov – President at Russian Electronic Money Association

Brazil

"Governmental actions to decrease financial exclusion as well as private sector pressure will lead to a bank-lead m-payment development"
Sandro Roberto Pereira, IBM Solutions Executive

India

"Regulation today favors bank led schemes for inclusion whether they are supported as banked, pre-paid or no-frills bank accounts over non-bank schemes to do cash-out and P2P. 2012 will be a year in which we expect to see huge growth"
Aditya Menon, Executive Director & Global Head of Product Management, Obopay Mobile Technology India

Mexico

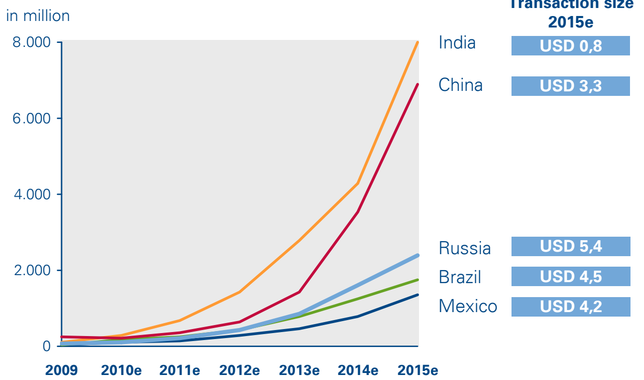
"The new financial regulations together with the current technological infrastructure of the country will permit practically any adult in Mexico to have an electronic purse"
Carlos Marmolejo Trujillo, General Director of Systems Supervision, National Banking and Securities Commission (CNBV)

Russia's inefficient banking system calls for alternative channels

Russia's MNO-led mobile payment market is already proven with roaring numbers. The decentralized, inefficient banking system drives people away from traditional banks towards mobile financial services. Business-to-consumer (B2C) payments have the greatest potential, as there is a ten times higher number of automated cash-in machines (ACMs) than cash-out points (ATMs). This symbolizes a significant opportunity to send money directly to people's m-payment account.

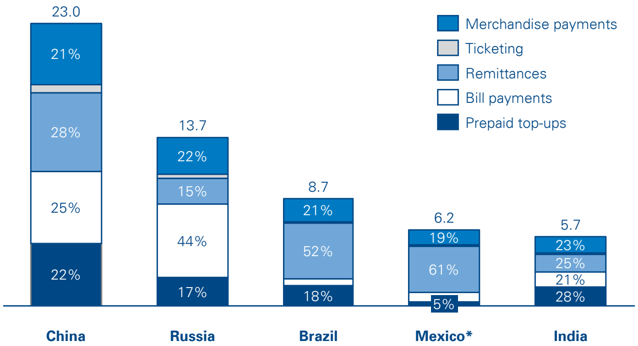
The hurdle for financial institutions is an opportunity for bank-agnostic players. The success of sophisticated services is already proven, reaching a total transaction volume of over USD 300 million in 2009. The relatively high income per capita in Russia drives spending, which results in an average transaction size of merchandize m-payments of USD 5.

Figure 3. Number of transactions and average transaction size, 2009-2015e



Source: Arthur D. Little analysis

Figure 4. Mobile payment transaction volume by country and services in billion USD, 2015e



* international remittances (starting from 2013)
Source: Arthur D. Little analysis

India's banks lead the competition

While banks in India have been early adopters in m-banking alerts, actual transactions on the mobile are rare. Banks in India have not gained traction in m-payment products because of a lack of marketing and sales effort, as well the inability so far to utilize channels beyond their bank branches to acquire consumers. Banks, however, have a competitive advantage over non-banks because they can capitalize on the cross-selling potential via micro-loans and can offer both disbursement notification and options to repay via mobile. Therefore, non-banks face an uphill task in monetizing their cost of consumer acquisition.

An important hurdle for user adoption is the exclusion of many Indians from banking services due to the lack of an official ID. It is unattractive for non-banks to pay the required user registration (about USD 20) as the cost is higher than the revenue potential from the customer in the short to medium term.

Banks also have an option for opening No Frills Accounts, which are "Light Bank Accounts" that limit the total amount transacted per annum. Prepaid accounts offered by banks have a transaction limit of USD 1,200 per transaction. Non-banks however, are limited to prepaid wallet size of only USD 120, which makes it far less competitive.

As soon as regulations allow for a larger wallet size, MNOs' market share can increase dramatically, because they can leverage their reach and distribution, which encompass millions of outlets.

China searches for new ways to develop m-payment

In China, mobile payments are still in their infancy. A variety of players, however, such as MNO's, independent service providers and banks, have already deployed a variety of technologies. Therefore, competition in the market is high. Advanced NFC and RF-SIM (radio frequency SIM) technologies for mobile financial services represent a big hurdle, as the ecosystem is still premature for such technologies. In addition, the rollout requires expensive POS devices.

As channel competition is intense, banks and MNOs seem incapable of sharing the cake. Inconclusive negotiations on the division of power and profit are hindering further development. In response, the biggest Chinese operator pro-actively bypassed the contentious point by simply buying shares in their negotiation partner in the banking sector. As a result, the MNO obtained a strategic hold on the bank and became the leading player in commercial mobile payment services on the market.

Recommendations for potential market entrants

Arthur D. Little has identified specific recommendations for each of the five markets analyzed.

Mexico calls for action, now

The Mexican market is the best option for a fast market entry, as regulations are already in place to facilitate entry of non-banks and enhance the chances for MNOs and third party providers. First movers will have a significant advantage.

Players should focus on top-ups and merchandise payments since these services will grow quickly, expected to reach about $1.2 billion in 2015. Merchandise payments require relevant B2B partnerships to successfully gain critical mass, which is vital as the currently limited m-banking services cannot drive demand.

Partnerships with money transfer providers in US, especially in California, Arizona, New Mexico and Texas, will be key in order to enter the international mobile payment remittance market in the Mexico – US corridor, which is expected to amount to USD 5 billion in 2015. Today every Mexican receives USD 245 p.a. on average, compared to Brazil with USD 26.5.

Brazil's banks will take the lead

Financial institutions are getting plugged into the system more intensively as regulations increasingly require their participation. Developed banking sectors like Brazil's should leverage this progress, occupy a strong position and take the lead. Banks should identify and approach the most valuable potential key accounts for both bulk payments and money collection services, to ensure scalability.

In order to address the upcoming demand for peer-to-peer transactions (P2P) that are expected to amount to USD 4.5 billion once regulations are in place, players should set up a very strong merchant network in cooperation with existing national and local networks by using aggregators.

Russia's MNOs to come to power

The inefficient banking system provides opportunities for non-banks. Russia is well positioned to develop mobile bill and utility payments (USD 6 billion in 2015), due to its strong coverage of cash-in points. This is an attractive opportunity for MNOs to strengthen their market position, if they focus on B2C transactions in cooperation with banks and non-bank payment operators, which are developing rapidly in Russia.

India's P2P services will have the lion's share

M-payments in India will be bank-led in the upcoming years, as banks use m-payment for regions where they do not offer ATMs or branches. Players should focus on top-ups and bill payment services in the next two years. They should then extend their focus on domestic P2P remittances, which are expected to amount to the lion's share of transactions by 2012, and will reach 1.5 billion in 2015. In addition, banks can increase their scale by targeting local SMEs and distributors, offering them less cumbersome cash handling through the use of m-payment.

China's service providers should focus on SMS-based solutions now

Existing technology, without an immense price tag, can be used to address China's rural areas. Such a network could be quickly and cheaply deployed to provide an SMS-based mobile payment system in remote areas.

Scalability and performance need to be ensured for the 6.9 billion transactions expected in 2015, especially when it comes to the IT architecture and billing systems. Data transfer disruptions due to network congestion need to be prevented, as they would impact consumer trust.

Non-banks should consider investing in the banking sector in order to be involved in strategic decisions. A large share of m-payment service users (36.7%) prefers to use platforms run by banks rather than by other players. China's biggest mobile operator has provided a successful case study. We are convinced that such a relationship provides a model for other operators and banks.

Conclusion

Players who aim to become a global leader in mobile payments cannot avoid entering M-BRIC. They need to invest substantially if they want to enter one of the world's five most attractive m-payments markets. Anticipating changes in regulations and responding to country-specific market and consumer characteristics is key. Players must act now, either becoming operational in the next year in order to gain a foothold, or by investing in infrastructure and partnerships in order to reap the benefits after 2013.

Contacts

Dr. Karim Taga
Managing Partner Austria
TIME Practice
taga.karim@adlittle.com

Thomas Kuruvilla
Managing Partner TIME and S&O practice
+971 50 9571 520
kuruvilla.thomas@adlittle.com

Authors

Dr. Karim Taga, Dr. Nicolai Schaettgen, Asli Ayaz, Stephanie Ludwig

Arthur D. Little

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