

COMMENTARY

Evolution of M-Pesa from a person-to-person platform to a sophisticated fintech

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In just about a decade and a half, M-Pesa has evolved massively. Today, it has a lot more capabilities and functionalities. This has seen it transform from a one person-to-person money transfer platform within the country into a sophisticated fintech platform. Presently, it supports electronic payments, airtime top up/transfers, mobile banking, digital lending, international remittances and fintechs, among other functions.

It has generated massive economic rents distributed through the platform. To date, on average Ksh7.5 billion or (\$75 million) are transacted on the platform daily.

This growth has progressed through six evolutions. M-Pesa has significantly impacted retail electronic payments system, inclusive financial services, improved livelihoods, spurred innovative digital financial solutions, inspired changes to the monetary policy framework and supported an e-Government services platform. As the evolution continues, it is important to keep track.

It all started in 2007. Beginning as a mobile money system, it influenced financial inclusion through a diversity of financial services that continue to be easy to reach. This platform and a savings culture that has evolved has contributed towards tackling poverty sustainably and enhanced market accessibility. In this first-evolution phase, many of the unbanked, who had been excluded from the formal financial system, could now save securely without enduring the cost of servicing an account, minimum balance requirements or a trip to the bank. With these micro-savings, they could accumulate savings and assets that would cushion them from negative shocks or accumulate capital for investment. M-Pesa heralded their entry into the formal financial system.

This led to the second evolution of M-Pesa, during which even more innovative solutions emerged, mostly based on partnership with financial institutions. This saw the emergence of a virtual banking system, allowing for a standalone savings account or one linked to a personal savings account. Alongside this was electronic retail payment for goods and services, through Lipa na M-pesa.

With the emerging partnership with financial institutions, the natural pro-

gression for the third evolution was unlocking short-term digital credit. This meant that participants in the virtual platform could save and borrow on the same platform. This was pushed further to the frontier by the virtual platform using savings and transactions data to generate credit scores that provided a basis for assessment, pricing and distributing of short-term credit. This in turn revolutionised lending and greatly boosted economic activity, particularly for small businesses.

In addition to evolving locally and impacting the economy, the fourth evolution of M-Pesa took it beyond borders, to support cross-border payments and international remittances. This immediately transformed the informal Hawala money transfer system to a formal and convenient remittance system in the phone. It also positively impacted the regulatory regime as demand for regulations grew to cope with these innovations and more intensive use of technology to monitor the money-transfer market, strengthening Anti-Money Laundering/ Combating the Financing of Terrorism (AML/ CFT) efforts.

Riding on the M-Pesa platform, uptake of fintech has increased, marking the fifth evolution of the platform. There is increased uptake in the use of mobile

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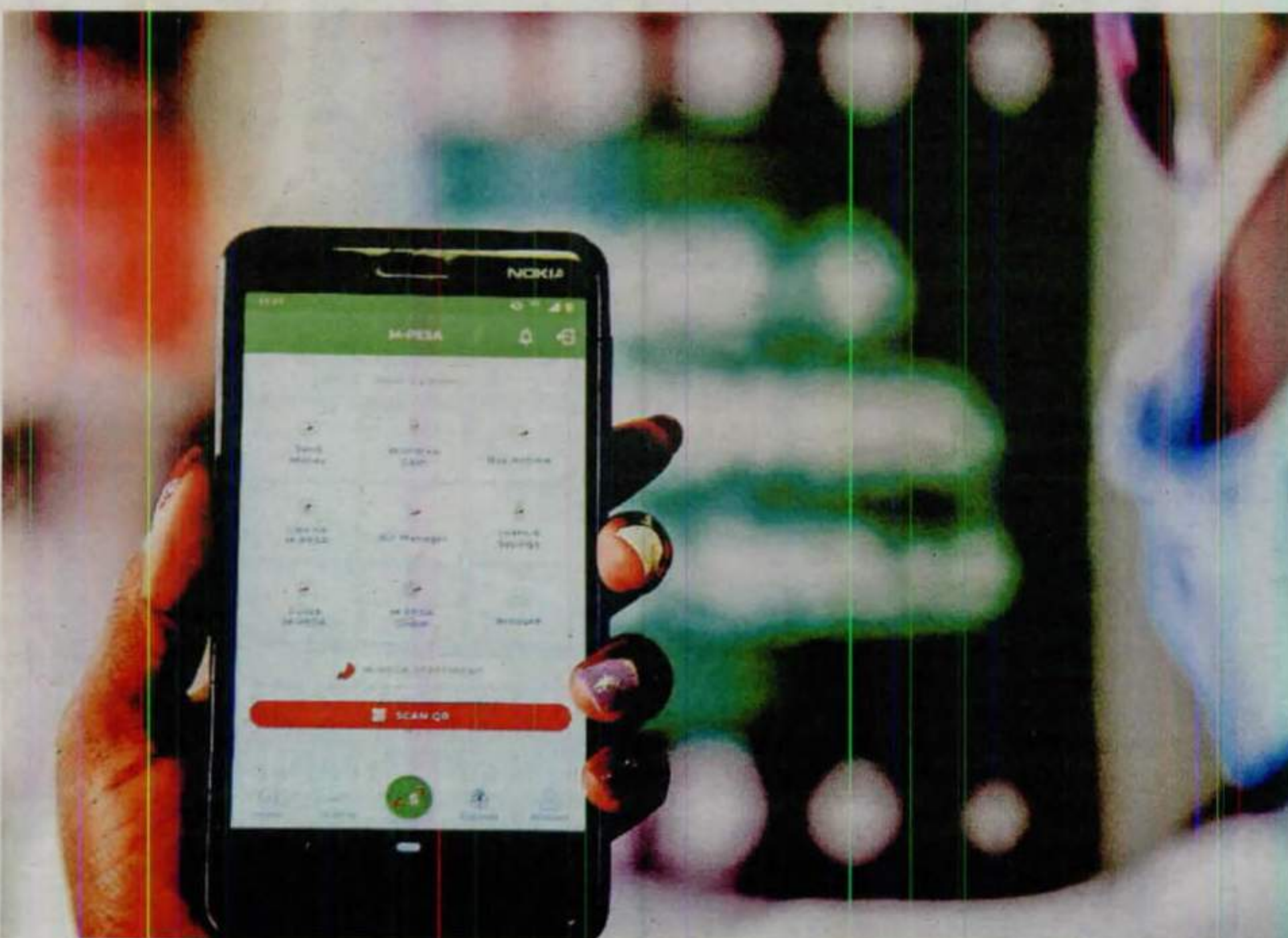
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networks and mobile embedded systems, the use of big data and data analytics, and cloud computing, and crowdfunding. On its own, M-Pesa is a fintech product too. It performs a fintech's typical essential roles for the financial industry: Reduction of transaction costs and enhancing efficiency; improving business and risk management; and financial.

The sixth evolution of M-Pesa has been its impact on the monetary policy framework and beyond. The benefit of innovation transcends financial inclusion, leading to a better monetary policy environment. The evolution of the velocity of money seen in the mid to late 2000s depicts different regimes — financial development and less cash changing hands. In addition, the rising money multiplier could imply that the Central Bank of Kenya (CBK) may have lost control of money supply process, but that was not the case, it reflected financial innovation in the market. Consequently, targeting broad money via reserve money as an intermediate target was inadequate and perhaps obsolete. This led to change in monetary policy framework in 2009 with CBK adopting Net Domestic Assets in place of Reserve Money. This allows a more forward-looking monetary policy that accommodates pre-commitment of a targeted inflation rate and so creates an environment of policy clarity.

Going forward, the M-Pesa platform is likely to be more dynamic. It has created endogenous demand for a national strategy on financial inclusion, cutting across the financial sector. Several banks and Telcos have replicated the product and its platforms. The cut in costs of financial transactions has led to the emergence of an efficient, effective, and real time payments and settlement platform allowing financial inclusion. All it requires now to sustain this development is a complete physical infrastructure for connectivity and a strong regulatory and institutional capability to support and protect the market.

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Safaricom recently introduced an updated mySafaricom App for its customers. Pic: Diana Ngila