

## EXECUTIVE SUMMARY

# Building Digital Bangladesh: The Way Forward for Digitizing Payments

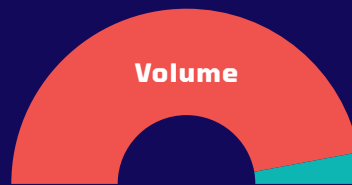
NOVEMBER  
2016



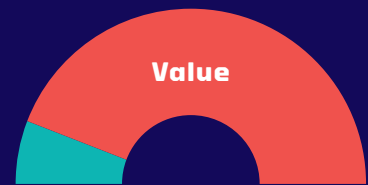
BETTER THAN CASH  
ALLIANCE



■ Cash  
■ Electronic



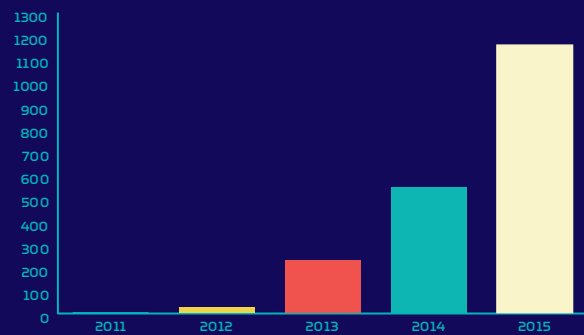
Bangladesh conducts  
**4.4 billion**  
 transactions annually.  
**94%** are in cash



**\$44 billion**  
 annually flows through  
 electronic channels,  
**12%** of all value

## PROGRESS IS BEING MADE

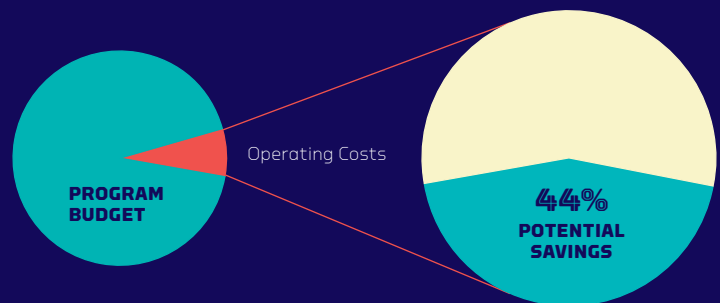
**Mobile money transactions** have grown from nothing in 2011 to over **1 billion per year**



## AND OPPORTUNITIES EXIST TO INCREASE ELECTRONIC PAYMENTS

By digitizing major social transfers, Bangladesh could save **\$146 million annually**

Retail payments make up half of all transactions and less than **3% are made electronically**



THIS REPORT WAS AUTHORED BY  
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Cover photo: ©Government of Bangladesh

## BANGLADESH

Country  
Diagnostic

This Diagnostic Report shows Bangladesh is making significant strides toward a digital economy, and outlines specific policy measures that can underpin further digitization of payments into the future. Led by initiatives from the Bangladesh government and supported by private sector innovations, the country has seen impressive growth in mobile financial services in particular, and a rising appetite for digital payments more generally. However, this Diagnostic Study also shows that Bangladesh is just commencing its journey toward a fully inclusive digital payments ecosystem, and that significant barriers remain. To overcome these barriers and support further progress, this report recommends as top priorities the completion of Bangladesh's National ID system, as well as reforms to improve regulation and make it easier for all forms of digital payments to move across channels and platforms. Putting in place these measures can play a powerful role in driving financial inclusion, economic growth, and cost savings for Bangladesh's government, businesses, and individuals at a time of rapid, positive change across the country.

# 1. EXECUTIVE SUMMARY

Shifting payments from cash to electronic forms helps drive greater financial inclusion and economic opportunity in many countries. The government of Bangladesh is laying the groundwork through regulatory measures, and an innovating private sector is also driving the shift from cash to digital.

Although all forms of digital payments have been increasing in Bangladesh, the mobile financial services (MFS) industry in particular is notable for its rapid expansion. Government-to-Person (G2P) digital payments have also grown significantly, and further digitization of G2P payments could save an estimated US\$146 million annually across six major social safety net programs, translating to 44% of total operating costs or 3% of the combined annual budget of the six programs.<sup>1</sup>

However, the overwhelming majority of payments in Bangladesh are still made in cash. Achieving further progress will require continued efforts by the government to implement policies that create enabling conditions and evolve the regulatory environment in order to overcome key barriers such as the need to achieve more competition, and more interoperability enabling payment transactions between different service providers and platforms.

This report measures the state of the shift from cash to digital payments, assesses the trajectory of Bangladesh's shift, identifies specific barriers to digitization, and recommends specific actions that government and the private sector can take to guide future policymaking.

# KEY FINDINGS

- **A major shift to digital payments from governments and businesses to individuals is possible in Bangladesh;**

however, the following needs to be considered:

- The continued transition to digital government and company salary payment is an important step for a successful shift toward a cashless economy
- There is strong justification for the digitization of the social safety net and other government transfer programs, including both program management functions and payments
- Private sector payments are set to shift, but incentives are required to drive full adoption

- **The overwhelming majority of the payments made in Bangladesh are still made in cash.** The analysis of the currently available payment data indicates that government entities, businesses, and individuals make only 12% of payments by value (equating to \$44 billion of \$367 billion total annual payments), and only 6% of payment by volume (around 260 million or 4.4 billion total payments) by electronic means.

- **The increase in the number of MFS (mobile financial services) available indicates a trend in changing consumer behavior regarding digital payments.** According to Bangladesh Bank (the central bank), 18 banks are operating MFS as of December 2015 and transactions have grown an average of 120% since 2011, averaging US\$1.3 billion per month. Although still a small proportion of the overall economy, the data suggests a strong interest among individuals, businesses, and institutions in Bangladesh to transact by a variety of digital forms.

- **MFS are a key driver of the increasing number of person-to-person payments, but availability of appropriate platforms will be critical to more widespread adoption.** The rapid growth of MFS has been in part driven by a significant move toward electronic remittances. However, this growth has slowed the last couple of years due partly to uncertainty related to MFS regulation changes proposed in 2015, particularly in relation to ownership structures, and the need to transition the market from over the counter (OTC) transactions to mobile wallets.

- **There is a need to improve the business case for private sector actors to embrace digital payments.** Cost structures associated with digital payments for private sector actors, including fees charged by banks particularly applied to higher-value transactions, are areas that warrant further examination.

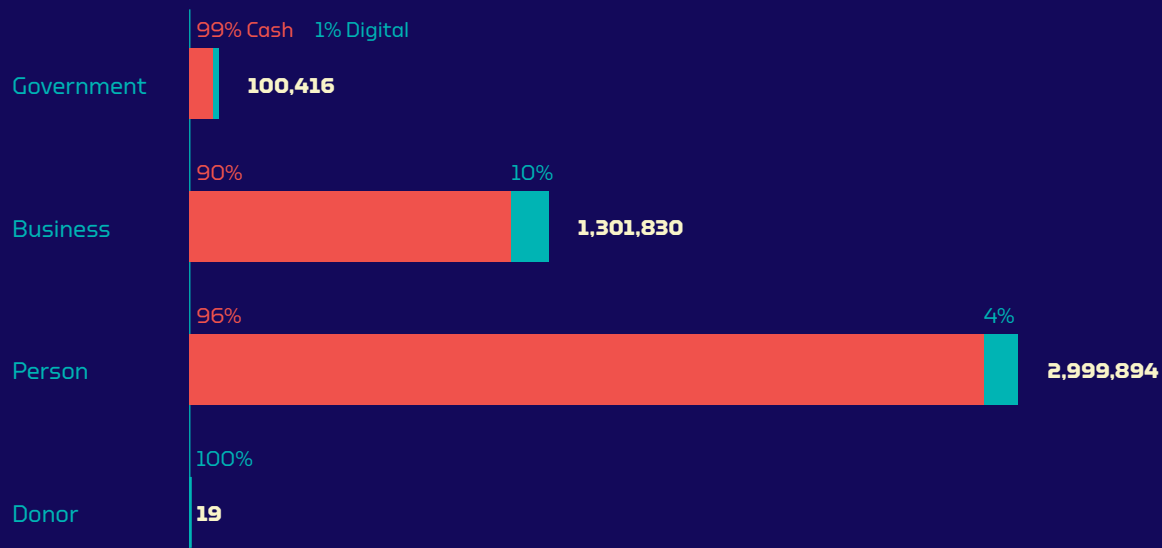
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The government of Bangladesh is laying the groundwork through regulatory measures, and an innovating private sector is also driving the shift from cash to digital. However, **the overwhelming majority of payments are still made in cash.**

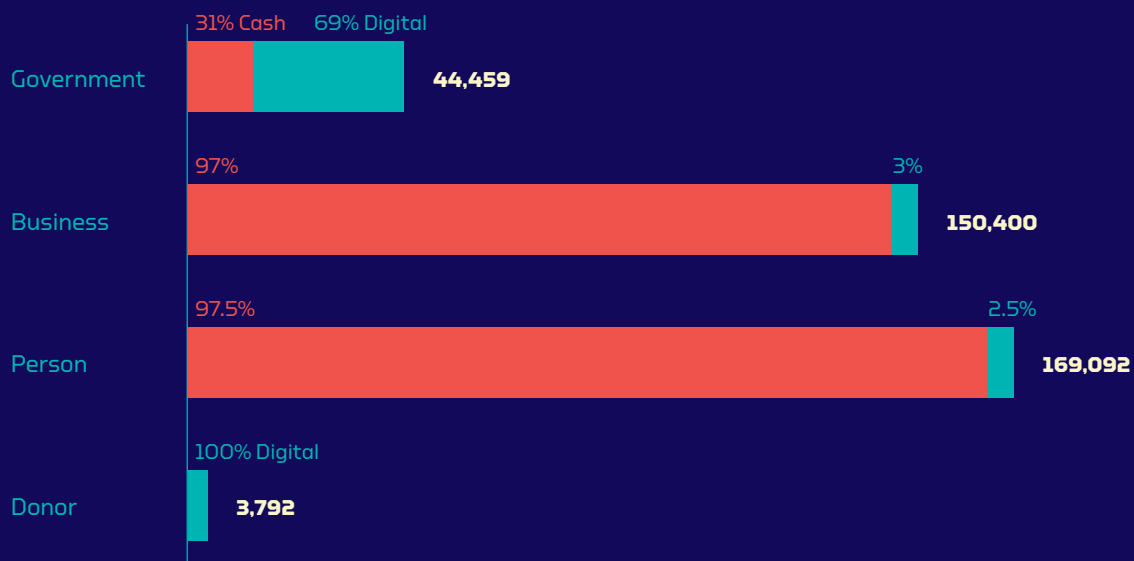
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There is **strong justification for the digitization of the social safety net** and other government programs.

## VOLUME (TRANSACTIONS, THOUSANDS)



## VALUE (US\$, MILLIONS)







18 banks are operating mobile financial services as of December 2015 and **transactions have grown an average of 120% since 2011.**

### Government payments:

- **An estimated 69% of the value of payments made by governments are digital.** This accounts for approximately US\$45 billion but only constitutes around 1.1% of the number of transactions made by government on an annual basis, illustrating the significant potential for further digitization of government payments to help build out the digital payments ecosystem in Bangladesh.
- **While 69% of the value of all payments by government are electronic, the corresponding figure for electronic G2P salary payments is about half that amount, at 36%.** This indicates that the infrastructure for G2P salary payments is already in place, but further measures are needed to enable more employees to be paid digitally, whether through bank accounts or other means.
- **Electronic payment of conditional cash transfers or other social program payments is in its very early stages in Bangladesh, at less than 1% of payments by volume.** Electronic payment of pensions has not yet started, but a database for automated pension payments is under construction.

## Business payments:

- **There is an opportunity for businesses to increase the number of payments they make and receive digitally.** Formal business payments represent around US\$150 billion, or about 40% of total value of payments in Bangladesh. However, only an estimated 10% of the number of transactions originating from businesses to individuals (B2P) and 2.6% of all Person-to-Business (P2B) payments are made over electronic channels. There is also an opportunity to incentivize adoption and digitize payments in the informal sector, which currently includes nearly 6 million micro, small, and medium enterprises (MSMEs), accounting for 25% of GDP and employing at least three-quarters of the total workforce.<sup>2</sup>
- **While most Government-to-Business (G2B) payments (90%) have now transitioned to digital channels, payments from Business-to-Government (B2G) have not transitioned at all (0%).** There is an opportunity for government and businesses to work together to support this latter transition.





### Individuals:

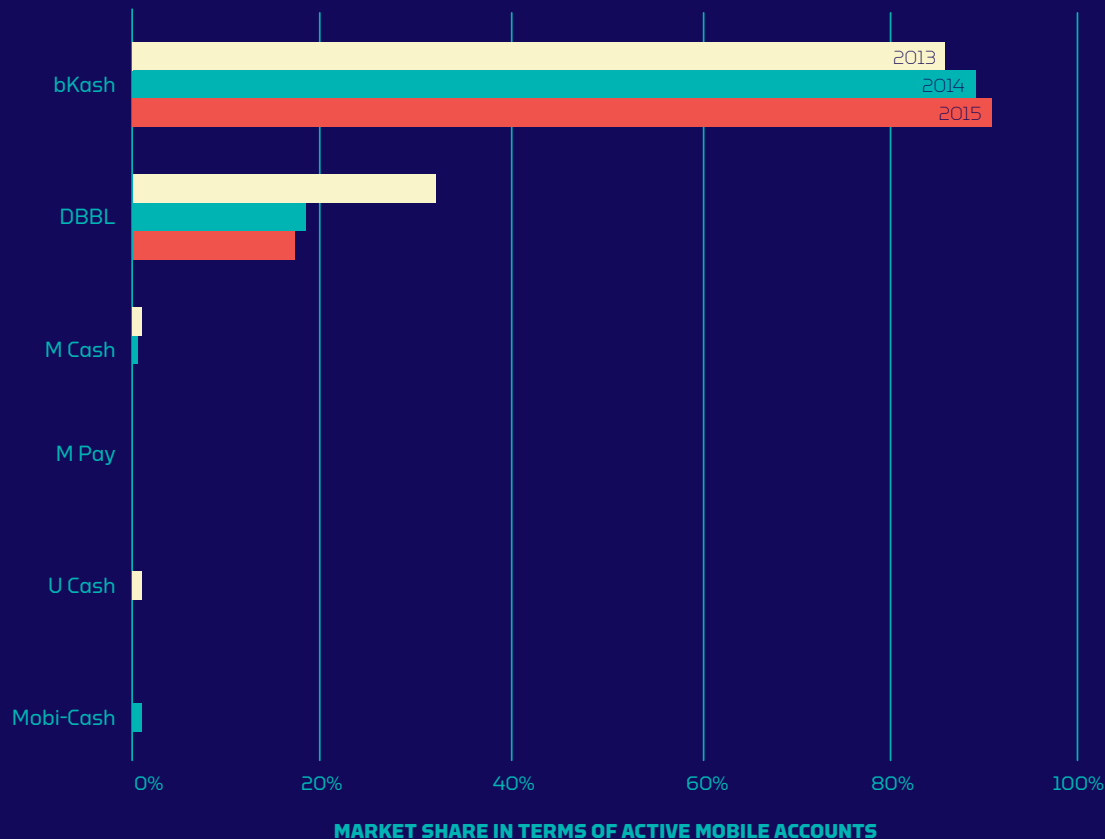
- **At present, over 95% of the overall number of individuals' payments is made in cash.** Payments made by individuals – (P2B), Person-to-Person (P2P), and Person-to- Government (P2G) – account for US\$170 billion.
- **Migration from rural to urban areas has significantly increased domestic remittances in Bangladesh.** However, 90% of this segment of the population is yet to transition to digital payments. To expand adoption, it will be important to increase platform interoperability, improve product innovation across multiple use cases, and address the misperception that cash is a low-cost way to transact.
- **The shift to digitizing payments such as bill payments is likely to be slower and more incremental than the shift for other payment types.** Only 8.4% of all utility bills are paid electronically, and only 2.6% of all P2B payments overall are made over electronic channels in Bangladesh. Individuals make hardly any payments to government electronically. This is in part due to the following factors:
  - Business is driving remote electronic bill payment, but government is not playing a significant role at this stage
  - A lack of confidence in electronic payments from payers and merchants is hampering progress
  - End users are open to using MFS, but do not always find them easy to use, highlighting the need for user-friendly products and improved services across a wide variety of use cases, including for very low-income users and unbanked or under-banked users

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# MFS MARKET LANDSCAPE IN BANGLADESH

Source: Intermedia



**Bangladesh's mobile financial services market is currently heading toward a damaging monopoly situation,** which may lead to price increases and other negative consequences for consumers.

# KEY RECOMMENDATIONS

The report highlights three specific actions that government and the private sector can take to further catalyze Bangladesh's shift to digital payments. The report also addresses some of the key barriers such as the lack of platform interoperability and the need to achieve more competition in the market. Importantly, these steps should be viewed as starting points on the payment digitization roadmap. They do not need to be completed in sequence. In fact, the first step of developing a National Identification System is already underway.



**Fully implement a National Identification System and integrate it with key services. Bangladesh now has a National ID (NID) database currently holding information on 96 million people in the country.**

In 2015-16 it connected to the biometric re-registration of SIM cards. With support from the World Bank, the government has recently embarked on a new project that will issue a smart card containing added biometric information. A lack of shared infrastructure such as an NID has been identified as a key barrier to G2P and B2P payments in Bangladesh as in many other economies. Once NID in Bangladesh is fully implemented and the necessary access is provided to certified government and business entities, it has the potential to greatly improve access to and adoption of digital financial services.



**Improve the regulatory environment to achieve more competition in the MFS market. Bangladesh's MFS market is currently heading toward a damaging monopoly situation, which can result in a range of negative consequences for consumers.**

This trend currently presents potentially the most significant barrier to Bangladesh developing an inclusive digital payments ecosystem. Improving the regulatory environment to help achieve an adequate level of competition will allow systemic risks to be managed. It will also promote competitive pricing and greater product innovation, and will be a vital step in improving the business case for businesses to move toward digital payments. It will also be important to continue developing a policy framework that supports other digital and non-digital channels and infrastructure, in order to build a vibrant, long-term ecosystem. Digital payment networks, including cards, mobile, and other channels, can play an important role in ensuring access, effective services and scale, as well as building long-term infrastructure.



### **Improve interoperability to create an unrestricted flow of money among user accounts from different institutions or service providers and across multiple channels.**

Agent interoperability in Bangladesh allows a single agent to act for more than one service provider, as well as customer interoperability that allows one customer to access multiple accounts using one SIM card. However, a lack of platform interoperability in Bangladesh currently inhibits payment transactions between different service providers, and therefore severely limits the scope of different payments that can be made digitally. Given the increasingly monopolistic trend in the MFS market, there is not currently sufficient incentive for the market leader (with 90% of customers) to encourage interoperability. Moreover, the smaller players do not have a sufficiently strong voice to advocate effectively for interoperability. Given market forces by themselves are unlikely to drive sufficient progress in a reasonable timeframe, improving interoperability is a key policy focus of the Bangladesh government. Success in these efforts will help drive further adoption of digital payments. More active participation of Mobile Network Operators (MNOs), as well as the Bangladesh Telecommunication Regulatory Commission (BTRC), could facilitate faster and wider adoption of digital financial services.

Broader interoperability of this type allowing transactions across different kinds of accounts will ultimately deliver the greatest long-term benefit for users.

The interoperability needed includes the ability for payments to move across MFS, bank, and other platforms. This will also serve to improve the use cases described in this report because it increases choice leading to the most optimal method of payment. This report shows that Bangladesh has made significant progress in a short period of time in driving the adoption of digital payments, led by the a2i Programme of the Prime Minister's Office, Bangladesh government, and key innovators in the private sector. Further progress requires action to address key barriers and spur growth. Through its analysis and recommendations, this report aims to help policymakers and other stakeholders better understand and to take action to accelerate Bangladesh's path toward a responsible, effective, and inclusive digital ecosystem. This will help stakeholders in Bangladesh fully unleash the power of digital payments to drive economic opportunity and financial inclusion in a country in rapid transition, and with significant opportunities ahead to improve living standards and drive new sources of economic growth.



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## The Better Than Cash Alliance Research Series

Our case study and country diagnostic series seeks to highlight specific examples of shifts from cash to digital payments by governments, companies, and international organizations. Each case study and country diagnostic aims to provide insights for a wide audience on the factors that have helped or hindered the digitization process, and also present key results and benefits of the transition away from cash. We hope that readers will be able to adapt the lessons from these cases to their own contexts and local conditions.

## Bangladesh Project Team

The diagnostic process for this study involved desk research and many in-country discussions by a team of experts to gather data, assess the incentives of participants in the local payments context, and obtain the insights of local BTCA champions and stakeholders. This study also included a limited scope end-user survey. Each diagnostic country team includes local researchers with experience in the payments system and knowledge of relevant institutions and individuals. Content and data in this document are based on information gathered during the second quarter of 2016, and therefore represent data prior to this date.

## Acknowledgments

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### About The Better Than Cash Alliance

The Better Than Cash Alliance is a global partnership of governments, companies, and international organizations that accelerates the transition from cash to digital payments in order to reduce poverty and drive inclusive growth. Based at the United Nations Capital Development Fund (UNCDF), the Alliance has over 50 members, works closely with other global organizations, and is an implementing partner for the G20 Global Partnership for Financial Inclusion.

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