AfricaNenda
ACCELERATING INCLUSIVE PAYMENT SYSTEMS

Toward the Bare Minimum in Policy to Unlock Seamlessly Integrated Retail Digital Payments Across Africa

Policy Note 1: Introduction

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Background: Accelerating digital financial inclusion in Africa for the realization of the African Continental Free Trade Area.

The African Continental Free Trade Area (AfCFTA) aims at accelerating intra-African trade and boosting Africa's trading position in the global market by strengthening Africa's common voice and policy space in global trade negotiations.[1] The successful implementation of the AfCFTA is intended to reduce trade barriers, leading to an increase in Africa's income by $450 billion by 2035.[2] Other benefits include creating more decent jobs, improved welfare and better quality of life for all Africans, and sustainable socioeconomic development.

Digital Trade was included in the AfCFTA Agreement through a decision of the African Union Heads of State and Government Assembly in February 2020 and is being implemented through negotiations. It is a fundamental component of the Agenda 2063, essential to boosting intra-Africa trade through expanded African markets for traders on the continent. This is in considering how the COVID-19 pandemic unlocked the demand for digital trading opportunities, and increasingly, more businesses continue adopting virtual business environments.

Successful implementation of the Digital Trade protocol of the AfCFTA mandate needs a thriving and more inclusive financial system, where significant value is to be unlocked for traders by enabling them to make or receive payments seamlessly in a manner that provides incentives, improves working capital through cost reduction, and drives the efficiency of payment processes.

What is at stake for Africa?

Africa has immense potential for immense economic growth and development; digital trade is a part of realizing this potential; therefore, robust policy and regulatory frameworks are crucial in enabling and accelerating digital financial inclusion to realize the AfCFTA agenda for Africa.

During the 2023 Spring meetings of the World Bank and International Monetary Fund in Washington, DC, Makhtar Diop, the Managing Director of the International Finance Corporation, expressed concerns that the AfCFTA might not become a reality unless laws and regulations are addressed. He highlighted that without a framework of laws and regulations that support intra-African trade, a Nigerian business owner, for example, would find it easier to do business with Europe than with other African countries, citing as reasons, Europe's well-developed regulations for free trade and a conducive environment such as a single market for financial services[3].

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[1] The African Continental Free Trade Area
[2] AU Summit 2023: Powering trade through AfCFTA
[3] IFC: AfCFTA is becoming a lot of talk — we need to fix regulations.

Europe is an often-cited example of significant progress in developing as a single regional market for financial services. The European Union (EU) has implemented policies and regulations through consultative processes to create a more integrated and efficient financial services market across its member states. As African countries and regions embark on their own process toward market integration, this series of policy notes will aim to make a case for critical considerations in designing policies and regulations that enable Africa to develop a seamlessly integrated payments system while sharing key learnings and benchmarks from Europe's journey for the benefit of the AfCFTA, for Africa's digital economy, and sustainable development.

What is the opportunity cost of a fragmented market?

Today, in 2023, customers of a majority of African financial service providers (FSPs) operating across multiple African countries face significant challenges in conducting cross-border transactions. Even FSPs operating in multiple countries have not yet integrated platforms that allow seamless transactions across countries for reasons attributed to variable requirements by different regulatory regimes and tedious, costly authorization processes to enable them to operate in several countries. These difficulties have cast into doubt the notion of a "Pan-African FSP"–whether bank or non-bank –when customers cannot easily access their mobile wallets or accounts and when they cannot conduct transactions across borders within the same provider institutions. Some key challenges that affect FSP operations in facilitating cross-border transactions include costly multiple liquidity requirements that tie up capital and the risks associated with these requirements, technological messaging standardization challenges, limited interoperability and complexities associated with different channels and instruments that limit efficiency. All the above challenges contribute to the current high cost of cross-border retail transactions and a limited focus on retail cross-border transactions as most FSPs pay attention to large-value, low-volume cross-border transactions.

In the subsequent policy notes in this series, we will discuss some implications of these challenges and the opportunities for improvement in the capacity of existing and future closed-loop payment systems.

How can Africa capture the benefits of seamlessly integrated payments?

In our analysis of the African landscape, we identified levers that are part of the macro policy that is needed across countries, to enable regulators, FSPs, and other stakeholders to take action to advance critical reforms and get ready for when change happens. The levers identified are:

1. FSP licensing and passporting;
2. Championing open finance; and
3. Developing robust regional data protection frameworks.

These levers are considered as part of the bare minimum because they represent three levels of innovation necessary for Africa; Launch stage (Licensing & Passporting), Scale (leveraging embedded finance through open finance capabilities to scale innovative digital financial services solutions), and consumer data and funds protection. We, therefore, considered other levers as an additive, and this policy note focuses on the bare minimum. This series will explore each of these three in detail in the subsequent notes.

1. FSP licensing and passporting

"FSP Passporting" refers to the practice of allowing FSPs authorized in one economic area's member state to operate in another member state without requiring separate authorization or, in some cases requiring, minimal additional authorization. This is made possible because the member states have harmonized their financial regulations and allow firms authorized in one member state to provide services across the economic region with minimal additional authorization. When FSPs are accorded this capability, they are considered to have gained passporting rights.

The current FSP licensing regime in Africa is fragmented: each country has its own rules and regulations. This makes it difficult for FSPs to operate across borders and for consumers to easily access financial services outside their home country or easily conduct cross-border transactions. Passporting is a valuable approach to defragmenting the financial services market in Africa. It minimizes the red tape for FSPs seeking authorization from regulators in different countries, which involves lengthy and costly processes. Passporting could accelerate the implementation of the AfCFTA by eliminating regulatory barriers to free trade between African member states and enabling a significant flow of related financial transactions.

A common licensing framework would make it easier for FSPs to operate across borders and for consumers to access and use a broader range of financial products and services. The Central Bank of the West African States (BCEAO) has strongly demonstrated the will to advance easy passporting rights to financial services providers within West Africa. This effort is already yielding results for the region and FSPs, as in the recent example of the license issued to Wave Money (Box 1).

Box 1 | Licensing and passporting rights: Central Bank of the West African States (BCEAO) issues E-money license to Wave Money[4]

- Wave Mobile Money offers inclusive and mobile financial solutions to millions of users across Africa. Wave's mobile money solutions allow users to save, transfer, and borrow money. Wave launched in Senegal in 2018 and grew into Senegal's largest mobile money provider, with more than 6 million active users by 2022.
- Wave became the first non-bank, non-telecom operator to be granted an e-money issuance license by the Central Bank of the West African States (BCEAO), which allowed them to operate in multiple West African Economic and Monetary Union (WAEMU) markets and achieve scale.
- Wave now has access to the eight WAEMU markets as a direct result of the passporting rights available to FSPs within the jurisdiction of the BCEAO.
- Working with the national directions of the BCEAO, Wave will extend operations in several countries in the WAEMU region leveraging this license.

[4] Wave Mobile Money becomes the first Fintech operating in multiple WAEMU countries to get an E-money license.

One of the critical levers used in Europe to create a single market for financial services is the harmonization of regulations and policies. The EU has implemented various regulations applicable across all member states, such as the Markets in Financial Instruments Directive 2014 (MiFID II) and Payment Services Directive (PSD2).[5] Such harmonization measures have helped to create a more level playing field for financial services providers and have made it easier for consumers to access a broader range of financial products and services across different countries, attributed to enabling high-quality integrated digital financial services ecosystems and interoperable products and services for all. For FSPs in the European Economic Area (EEA), once a firm is established and authorized in one European Union (EU) country, it can apply for the right to provide defined financial services across the EU or to open branches in other countries, with only minimal additional requirements. This authorization is the FSP "passport".

In our second policy note, we will take a closer look at the licensing and FSP passporting lever to highlight opportunity areas for Africa.

2. Championing open finance

“Open finance” refers to sharing financial services data between different FSPs, with the consumers’ consent. Open finance enables innovation by helping FSPs to understand customers better and address their pain points by offering solutions. It also helps FSPs to manage their operations better, reduce risk, and guide the evolution of business models. Open finance, therefore, has the potential to create a more level playing field for smaller FSPs (fintech entities) and to foster innovation and competition, leading to better consumer financial products and services. The result, of course, is accelerating financial inclusion.

Open banking, a component of open finance, is a relatively new concept that has been gaining traction in various regions worldwide, including Africa. The extent of open banking penetration in Africa can vary significantly from country to country, and it is still in its early stages. In some African countries, regulatory frameworks and infrastructure to support open banking are still being developed, while in others, progress has been made in implementing open banking initiatives. For example, South Africa, Nigeria, Kenya, and Ghana have shown promising developments in open banking.

In South Africa, the Payment System Management (PSM) Framework introduced by the South African Reserve Bank (SARB) has paved the way for open banking initiatives. Banks are required to provide access to customer transactional data to authorized third-party providers (TPPs) through Application Programming Interfaces (APIs); such access is one of the key principles of open banking.

Ghana has also taken steps towards open banking, with the Bank of Ghana (BoG) issuing guidelines on electronic payment services, including provisions for access to customer data by TPPs. Similarly, in Nigeria, the Central Bank of Nigeria (CBN) approved operational guidelines for open banking in 2023, the culmination of an open banking journey that began in 2017. The operational guidelines outline the framework for licensed financial institutions to provide APIs and share customer data with authorized TPPs in a secure and standardized manner. Nigeria has emerged as a hub for open finance, expanding the financial services

[5] The revised Payment Services Directive (PSD2) and the transition to stronger payments security

playing field to accommodate additional asset-light notable fintech entities and driving innovation.

Although commendable progress has been made in some countries in implementing open finance, it remains fragmented across countries. However, the full implementation of the AfCFTA presents a unique opportunity for Africa to establish a unified and comprehensive open finance framework. Such a framework would enable FSPs across the continent to securely share data, facilitating seamless access to credit by consumers across borders based on their financial history from various countries. This would also enhance payment systems within the continent as digital payments use cases grow, with the potential to boost trade finance amongst micro, small, and medium-sized enterprises (MSMEs) in Africa. Implementing a single open finance framework under the AfCFTA mandate can significantly boost financial inclusion and economic growth in Africa by fostering greater connectivity and interoperability among the continent's banks and financial institutions.

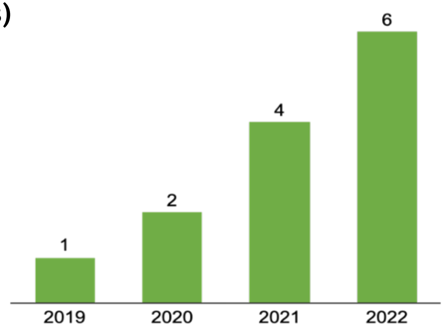
How did the EU achieve open finance at scale?

In 2015, the first iteration of open finance was born in Europe in the form of the Payment Services Directive (PSD) and, later, the revised PSD2. These unified regulations allowed FSPs and non-FSPs to access client banking information (with the client's consent) and make informed decisions about clients based on that information.

According to a *Statistica* report, the growth of open banking has been so rapid that Europe is expected to see nearly 64 million users in 2024,[6] an increase of more than 400% in 4 years. As of 2022, the United Kingsom's number of active open banking users reached 6 million, according to the Open Banking Implementation Entity (OBIE). Given that the population of the United Kingdom with any type of day-to-day bank account is 47m, 10.6% of the country's banked population is benefitting from open banking solutions.

Figure 1: Active open banking users in the UK (millions)

"With a record 1 billion API calls, 5 million open banking payments, and 6 million active users, it's clear that open banking is continuing to deliver added value to the UK's consumers and small businesses" - OBIE Executive.



Source: OBIE[7]

Industry players in Europe have been cited as saying that they have seen customer numbers grow significantly. They have undoubtedly seen open banking–enabled payments as a huge factor in this growth. They also report that innovative value propositions are being developed on top of open banking rails that will continue to benefit and transform government, retail, and business in general in the future. Furthermore, industry experts have indicated that lending is the next most robust use case after payments, because it would make it easier for Europeans to live in different countries without losing their credit histories.

[6] A look at Open Banking statistics across Europe.
[7] Three open banking milestones for May 2022.

3. Developing robust regional data protection frameworks

The increasing amount of data generated by financial services transactions creates a need for secure and reliable data storage. This is particularly important in cross-border financial transactions, where data sovereignty, privacy, and security are paramount. Consumer data protection best practices encompass four key levels: data processing, data residency, data localization, and data sovereignty. These terms will be thoroughly discussed in an upcoming policy note.[8] A common data storage framework would ensure that financial data is stored securely and in compliance with data protection guidelines.

The African Union (AU) has taken significant strides toward establishing a unified data protection policy across Africa. In collaboration with the Internet Society, the AU has developed the Personal Data Protection Guidelines for Africa.[9] Over the past decade, African countries have made progress in aligning their laws and regulations with the AU guidelines, covering areas such as cybersecurity, cybercrime, electronic transactions, and data protection. Presently, 33 countries in Africa have enacted data protection laws and/or regulations, albeit at varying stages of development. A few countries have also enacted laws on data localization in specific sectors like financial services and healthcare.

As part of this policy note series, we will share a map that reflects the current state of data protection laws in Africa.

In contrast to Africa, Europe has a unified common framework for data protection called the General Data Protection Regulation (GDPR).[10] The GDPR is applicable across all EU member states and provides a high level of protection for personal data. This has helped to ensure that financial data is stored securely and in compliance with data protection regulations, which is essential for building trust and confidence in the financial services industry.

Conclusion

Our series of policy notes are intended to invite and inform your consideration in exploring the following actions as we bring you more information about this ongoing transformation.

Regulators

- **Regulatory harmonization**: The policy notes will provide critical considerations for regulators to pursue efforts toward harmonizing regulations and standards across different jurisdictions to facilitate FSP passporting, hence supporting the implementation of the AfCFTA.
- **Regulatory cooperation and coordination:** Regulators may also find merit in establishing cooperative arrangements and information-sharing mechanisms to facilitate the exchange of information (data sharing) and data protection as part of the AfCFTA implementation.

[8] **Data processing** refers to the collection, transformation, and organization of raw data into meaningful information. **Data residency** refers to the geographic location of the data. **Data sovereignty** refers not only to the location of the data but also to the laws and regulations to which the data are subject at that location. **Data localization** requires that all data generated within a country's borders remain within those borders.
[9] Personal Data Protection Guidelines for Africa.
[10] GDPR.EU.

Financial Service Providers

- **Market access:** FSPs may leverage the policy notes to explore new markets and expand their operations across borders, focusing on subregions in Africa that already have an integrated finance market.
- **Market research**: FSPs could consider conducting market research, identifying potential opportunities, and developing business strategies to enter new jurisdictions and serve customers in different markets as part of preparations for the full implementation of the AfCFTA.
- **Technology and cybersecurity:** FSPs may begin simulating the required investment in technology and cybersecurity measures to comply with the regulatory requirements and protect customer data, in preparation for a possible single financial services market in Africa.
- **Compliance and risk management:** FSPs may consider establishing robust compliance and risk management frameworks to ensure they can meet the regulatory requirements and mitigate risks associated with operating true Pan-African institutions.

Finally, these levers are a few leading attributes of the bare minimum in policy to unlock seamless, integrated retail payments across Africa. We welcome the community for contributions to spur dialogue and action towards a robust African financial ecosystem. We believe that by putting these levers in place, Africa can unlock the potential of its financial services industry and drive economic growth and development across the continent.

We are looking forward to sharing additional notes focused on licensing, open finance, and data protection over the next three months.

Authors

Jacqueline Jumah and **Tochukwu Egesi**

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About AfricaNenda

AfricaNenda is an African-led team of experts committed to unlocking the potential of digital financial services for the financially excluded across the continent by accelerating the scale-up of instant and inclusive payment systems. AfricaNenda's approach is to provide public and private sector stakeholders with technical expertise and the capacity to reduce barriers to digital payments. AfricaNenda wants to enable everybody in Africa to make digital transactions seamlessly and at a low cost wherever they are on the continent by 2030.

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