

# SERVING THE UNDERSERVED

How open banking can unlock the R446 billion\*  
informal sector in South Africa



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\* The value of the non-measured, informal and household economy is estimated to be at least R446 billion according to according to:  
<https://www.southafricanmi.com/estimating-the-size-of-the-informal-economy.html>



# Introduction

Broad consensus exists that small businesses and their unregistered counterparts in the informal economy are the key elements in improving the unemployment crisis and poverty in South Africa. The continued lack of relevant services aimed at the informal sector therefore represents a drag on growth and economic development.

The use of Application Programming Interfaces (APIs) to more freely exchange data and payments information, known as open banking, provides the opportunity for banks and non-banks to collaborate to boost innovation and provide more suitable services for the informal economy, whilst simultaneously expanding the market for financial services in South Africa.

This paper will begin by outlining the importance of the informal economy and the challenges faced by small businesses operating within this sector. We will then describe the concept of open banking using APIs and provide examples from other geographies. Finally, we will apply open banking principles to the South African context and identify potential open banking services that banks and others can develop to better serve the informal economy.



# The role and importance of the informal economy in South Africa

The informal economy, like its formal counterpart, is multi-faceted, comprising of different sectors or markets and engages in diverse activities. It can include, but is not limited to, informal labour markets, informal financial services, and informal businesses. Due to its heterogeneous nature, various definitions of the informal economy exist, and terms such as informality, informal economy, and informal sector are often used interchangeably. The International Labour Organisation (ILO) defines the Informal economy as including “all activities that are, in law or practice, not covered or insufficiently covered by formal arrangements” (International Labour Organisation, 2013). This definition includes informal employment and informal business. For the purposes of this paper the focus is on the economy created by informal trade. This includes employers, self-employed, and those who assist (unpaid) in household businesses that are not registered and/or not registered for income tax or value-added tax.

South Africa remains one of the world's most unequal societies. According to the Institute for Race Relations (IRR), Bloomberg ranked South Africa as the world's second most miserable country, in large part thanks to the unemployment rate, which they reported as being an unofficial 36.4% in 2018.

The informal economy in South Africa plays a pivotal role in job creation and income generation amongst the most marginalised in society. It is estimated to contribute 8% of GDP and supports 27% of all working people (Greve, 2017). According to Stats SA, approximately 1.5 million people run informal businesses in South Africa. The 2013 “Survey of Employers and Self-Employed (SESE)”, released by Stats SA, finds that almost 70% of people who start an informal business do so because they are unemployed and have no alternative source of income.

In addition to reducing poverty through job creation, street vendors play a key role in food security in South Africa and across the region. A survey of over 6,000 households in 11 cities across Southern Africa found that around 70% of

households buy food daily or weekly from informal outlets (Crush and Frayne, 2011). The study further found that the more food-insecure the household is, the more likely it is to buy food from informal vendors or traders.

However, there are negative impacts of having a large informal economy with negative outcomes including: low productivity levels; providing insecure, unstable and poor remuneration to workers; and lacking legislated protection for workers.

While it is not necessary for all businesses to formalise by registering with the Companies Intellectual Property Commission (CIPC), all are advised to register for tax purposes. In this lies much of the resistance from the informal economy. A large informal sector can have substantive fiscal implications when viewed from a tax revenue perspective. Additionally, large informal sectors also imply that copious transactions are omitted from official economic statistics rendering macroeconomic indicators vital for policy inaccurate and therefore potentially leading to sub-optimal policy decisions.

For market participants such as banks and fintechs, serving the informal sector is filled with challenges, and often cannot be done profitably using traditional business models. On-boarding customers can be difficult due to the lack of proper documents required for Know Your Customer (KYC) processes. The high use of cash can also present challenges to introducing forms of electronic payment such as cards or EFT. In a business context, the need for card acceptance devices such as terminals (or mobile phones with a dongle) may be prohibitive for small businesses. The result is that the informal sector effectively operates as a shadow market with little participation from formal financial institutions.

Its disadvantages aside, the informal economy is a key contributor to the reduction of poverty and unemployment in SA. In order to maximise the informal economy's contribution to economic growth, a greater focus on improving financial inclusion\*\* in this sector is required.

\*\* Financial inclusion involves ensuring that consumers and informal businesses have access to and can effectively use formal financial products: electronic payments, savings, credit, and insurance.

# How financial exclusion impacts the informal economy

**Informal businesses face a variety of constraints, making it harder for them to do business and grow. A recent IQbusiness study sheds light on the challenges that the informal sector faces with regards to access to financial services (Inclusive growth: The role of the informal economy 2018):**

**1**

## **Lack of access to formal financial services**

Banking hours and locations are also not always accessible for all informal traders. A lack of the required documents for KYC procedures also prevents many from being able to apply for accounts with banks.

**2**

## **Lack of access to business accounts**

Informal businesses primarily transact on a cash basis and tend not to use formal banking channels. Where the use of electronic payments, such as EFT, is present, these payments are made using personal bank accounts or wallets instead of business accounts. The use of a personal account for business expenses makes business accounting difficult. EFT payments are also only possible if the business owner has access to a personal bank account.

**3**

## **Lack of credit history and access to finance**

Lack of access to finance is often cited as the biggest operational constraint faced. Businesses in the informal sector operate on very low margins, with business owners finding it difficult to develop savings that would allow them to expand and grow. Smaller loans may not be available to this segment and organisations that offer small loans / microcredit are not able to assess the creditworthiness of these businesses, particularly if they operate exclusively using cash. SMEs (Small and Medium - sized Enterprises) generally require capital investment at the start-up and expansion phases, and while many informal business owners source start-up capital from family members or friends, expansion capital is not easy to come by. As a result, many simply remain hand-to-mouth businesses.

**4**

## **Lack of insurance**

Informal business owners find it difficult to obtain insurance that can protect them from the impacts of crime or natural disasters.

In addition to the above, these businesses do not have access to government support and they also struggle with access to markets, lack of technology, management skill gaps and infrastructure inadequacies. Informal businesses struggle to thrive and expand, which fundamentally limits their ability to improve their contribution to South Africa's economic growth.



# Improving financial inclusion for the informal economy

Improving financial inclusion and better serving the informal economy requires banks and non-bank payment service providers to have a firm understanding of the needs of consumers and businesses in this sector. Banks in particular may find that they lack the tools to meet the challenges of adequately serving these customers. With the advent of open banking and APIs, banks can now look

outside of their organisations to partners such as fintechs who may have the tools and know-how needed to develop products and services that meet the needs of the informal economy. This will improve the choice for South African consumers and businesses while also expanding market opportunities for banks and non-banks alike.

## How open banking is changing the global banking landscape

Open banking is an initiative that enables third party developers to build applications and services around financial institutions (FIs) by giving access to previously walled-off data. Open banking has become a hot topic in Europe and Asia, where the financial services industry and regulators are looking to increase competition and innovation, enhance security, and improve transparency. Open banking is enabled by the creation and adoption of APIs, which allow different software systems to communicate in a secure and standardised manner. This approach allows banks, system operators, fintechs, and other players to exchange data freely, openly, and securely. In particular, open APIs, which are developed for use outside of an individual organisation, are deemed key in fostering open banking. The degree of openness can range from making an open API available to specific partners and developers only; through to standardised, public APIs that are accessible to any party.

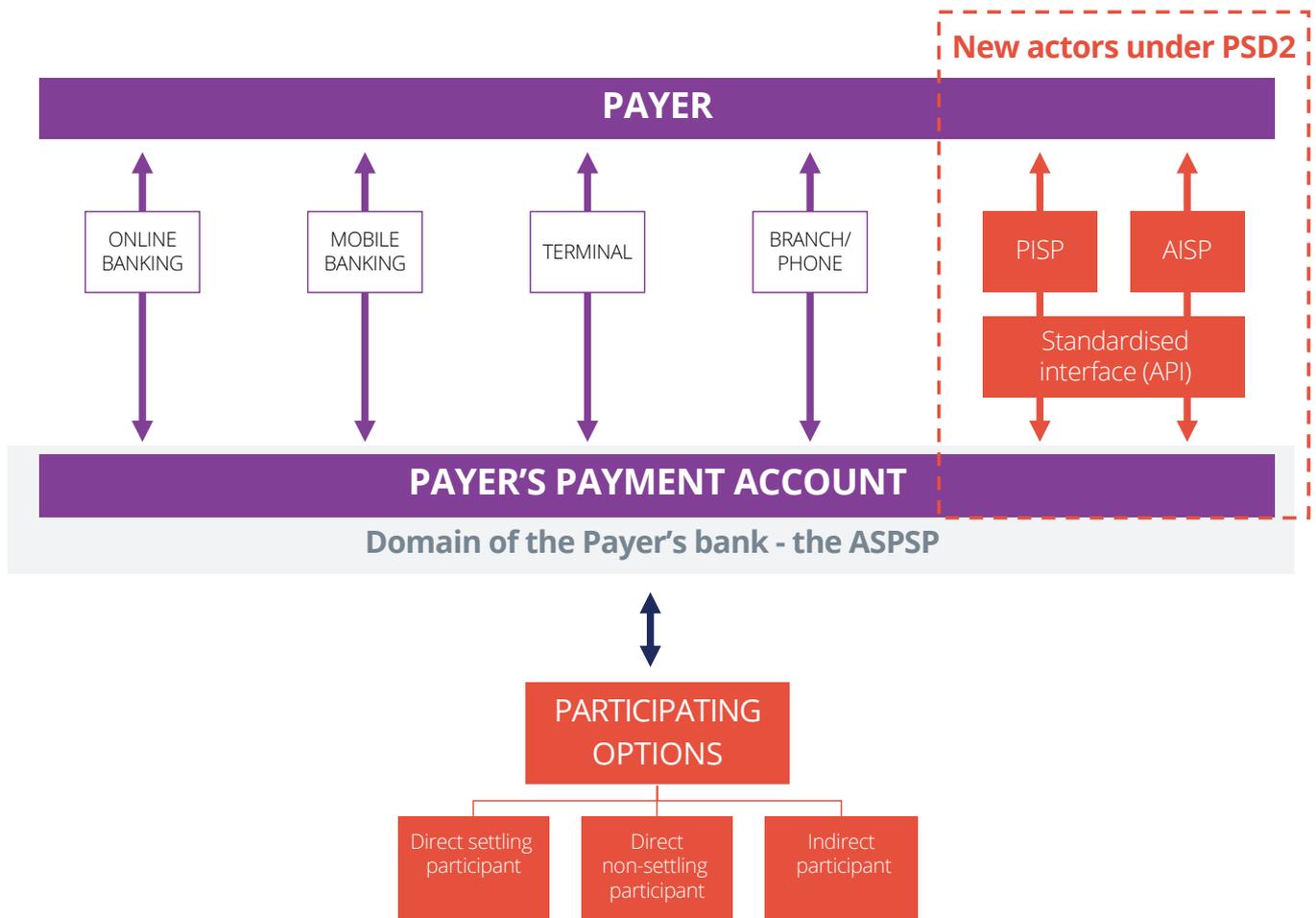
In essence, APIs provide third parties and customers with on-demand account information, on-demand payment initiation, and on-demand product marketing such as loans,

account optimisation, and savings plans. Open banking enables cost-effective micro-services that improve customer experience, enhance competition, and allows for new business models. Open banking is set to fundamentally change business models in financial services and open up new markets for banks and non-banks alike. The acceptance of open banking concepts and solutions, however, is critical to overall success and change. Innovation needs to be relevant to the South African context, easy to use, and compatible with informal business realities. A key factor here will necessarily be the education of informal business owners. For example, erroneous beliefs that money in the form of taxes will be automatically deducted from bank accounts – regardless of whether an income was earned or not – will hinder adoption. Lastly, open banking concepts should be recognised as a platform for innovation where the potential benefits are greater than the perceived risks – the whole will be greater than the sum of the parts.

# Expanding access to payment services

Access is a key issue in any payment system, but there are different types of access. The most basic type of access is to the central bank settlement system, allowing a financial services provider to directly settle payments on its own behalf. This option can be costly because it requires funding a settlement account at the central bank and following strict rules designed to maintain stability in the financial system. The next level of access is direct technical access to a retail payment system (such as the EFT system or a card network). Initiating banks send individual payment messages or bulk payment files directly to the infrastructure or to a sponsoring agent, which then forward these files to the payment infrastructure. This requires the sponsoring bank to keep additional liquidity in its settlement account to settle both its

own payments and those of the institutions that it sponsors. The third type of access is concerned with accessing accounts and information at individual financial institutions. In most markets around the world, financial institutions control which parties can have access to which accounts (for the purposes of initiating payments) and the information contained within them (for example, to analyse how money is spent). One of the key value propositions of open banking is easing access to accounts and information held by financial institutions and allowing third parties access to customer data to offer the end user improved services. With the end-user's consent, open banking has the potential to promote innovation by allowing new entrants to initiate payments or to use data to improve services to end users.



# Open banking in practice: A global movement

The move to open banking in Europe is mainly spurred by regulation, specifically the second Payment Services Directive (PSD2). The PSD2 is a directive that regulates payments and payments service providers within the EU and European Economic Area and is the single biggest initiative aimed at initiating open banking in global payments today. While the PSD2 covers many areas related to payment services (e.g. legal definitions of third parties and additional transparency on fees), the most relevant clause pertaining to open banking is the so-called “access to accounts” (A2A) clause. A2A mandates that any authorised third party (known as a payment institution, or PI) can access a customer’s bank account data if that customer gives consent to the PI. European banks are thus being forced to open up their systems to accommodate A2A and comply with the PSD2.

While the PSD2 does not explicitly mention APIs, it is commonly understood that APIs are the most feasible option for enabling third party access to customer bank accounts, whether to initiate a payment or simply to access the data contained within them. The European Banking Authority (EBA) has developed Regulatory Technical Standards (RTS) for APIs to be used by banks and PIs throughout Europe. While the RTS is different from standardised open APIs, it does pave the way for some standardisation of services when complying with the PSD2.

While the development of SEPA-wide public (Single Euro Payments Area), open APIs have not yet occurred, some SEPA bodies are attempting to boost standardisation and avoid a fragmented API environment in Europe. The Euro Retail Payments Board (ERPB), for example, has recommended the development of a common API standard for Europe and the European Payments Council (EPC) has established an API Evaluation Group to evaluate proposed standards for open, public APIs in Europe. Some EU countries such as the UK have established national projects aimed at developing open APIs. The Open Bank Project – begun before the PSD2 was passed – is a collaborative effort by the UK’s largest banks, regulators, and third parties aimed at developing public APIs for use by

all regulated providers (third parties authorised to access bank account information). As part of the project, the UK’s Competition and Markets Authority (CMA) established the Open Banking Implementation Entity (OBIE) to oversee the project. The Open Bank Project had a managed roll out in January 2018 (in line with PSD2 go-live), and full implementation of the project occurred in April 2018.

Other countries, such as Canada, Australia, and Singapore, are also discussing or even implementing open banking concepts. Australia’s federal government, for example, has mandated that the country’s major banks open up access to banking data for credit and debit cards, deposits, and transaction accounts by 1 July 2019, with mortgage information following on 1 February 2020. While Canada is not as advanced in its open banking regulations as Australia, the ongoing modernisation undertaken by Payments Canada has led the Canadian government to consider the merits of implementing open banking there. Lastly, the Association of Banks in Singapore (ABS) has released a playbook that is intended to help banks in Singapore and the ASEAN region implement APIs to foster an open banking environment.

The use of APIs in financial services is not limited to collaborative efforts among banks. Individual banks can also develop APIs to create marketplaces that allow third parties to develop innovative new services for the bank’s customers. In markets such as the United States, some banks are opening up their banking platforms using APIs despite the lack of corresponding regulation forcing them to do so. Wells Fargo Bank has developed APIs to allow for various types of services, including account aggregation, viewing account balances, and checking the status of payments. According to an interview with Wells Fargo, there are even plans to allow for loan applications via APIs. By developing APIs and opening them to third parties, Wells Fargo can outsource innovation to more agile players such as fintechs while retaining their customer relationships.

While some banks see open banking as a threat to legacy revenue and business models, some forward-thinking banks see open banking as creating potential to outsource innovation and product development to more agile players such as fintechs. Open banking using APIs can enable banks to remain competitive while allowing fintechs to expand the reach of their products and services. The combined effect of this is improved choice and lower costs for consumers and businesses, which promotes better overall outcomes in financial services.

The following table lists various services in the open banking space and provides examples of companies providing these services from various countries.

## Open banking services

TOPIC	DEFINITION	EXAMPLES
<b>Banking-as-a-Service or Banking-as-a-Platform</b>	These terms are synonyms. These are platforms created by fintechs which then license out the usage of these platforms. Sometimes the fintech behind the platform has a banking licence, which it allows others to use, while other times the fintech does not. In essence, these services are similar to traditional outsourcing services, except the usage of APIs and modular services allows for customisation in an unprecedented way.	With a banking licence includes Fidor Bank and solarisBank (both from Germany); without a banking licence includes Mambu (Germany) and Emid (South Africa)
<b>Digital on-boarding</b>	These are services that allow banks to on-board end users digitally, thereby easing the process. This is usually done via webcam on a desktop or a mobile device.	IDnow (Germany), pbdigital (South Africa)
<b>Branchless banking</b>	Banking actions that are done outside of banking, such as online via a desktop or a mobile device. Branchless banking is used by both traditional banks with an online presence and digital-only banks.	Digital-only: N26 (Germany), Revolut (UK), Fidor (Germany), Tyme Digital, Azar Bank (both South Africa) Online banking: most banks already have some type of branchless banking options
<b>Lending</b>	Instead of filling out reams of paperwork in order to receive a loan, APIs are allowing fintech lenders to gather digital information via APIs (e.g. bank account information, social media information for small businesses, etc.) and base loan decisions on non-traditional information. This allows them to serve previously neglected communities. Other forms allow for pre-approved loans at the point-of-sale.	Kontomatik and BBVA (available in Mexico, Spain, and the USA), Nobuntu (South Africa)
<b>Business banking</b>	Many of these technologies allow for small and informal businesses to more easily operate by cutting out red tape, easing access, and being more user-friendly than traditional banking technology.	Tyme Digital (South Africa); Sasfin (South Africa); Kontist (Germany)

# Using open banking to promote financial inclusion in South Africa

In South Africa, open banking has the potential to help banks and non-banks reach new customers and expand the overall market for financial services. South Africa faces challenges that many of the countries currently implementing open banking concepts do not, including widespread exclusion of the informal economy from the formal financial sector. These issues, however, do not mean that South Africa would not benefit from implementing open banking and further modernisation through digitalisation. Promoting openness

among financial institutions could promote innovation in products and services available to end users in South Africa in both the formal and informal sectors and help narrow the gap between the banked and unbanked. Furthermore, opening access to bank information could promote innovation in the wider financial sector, leading to the creation of new companies and increasing digitalisation.



# Developing new banking services

Open banking allows financial institutions to pursue more customer-centric product development strategies, as opposed to the less flexible, product-based approach that banks have traditionally taken. This is key in a market like South Africa where existing bank products are not adequately serving the needs of the informal economy. By increasing digital payments and branchless banking, lowering costs, and expanding the scope of financial services for the majority of South Africans, the industry has the opportunity to make a substantial impact on the growth and functioning of this sector.

Moving more services to a digital format would decrease the cost of servicing low-balance accounts, allowing banks to lower prices and make having a bank account both more affordable and convenient. The increased convenience of digital services would allow for cost savings in other areas, too. The implementation of open banking concepts and access to account information, specifically via APIs, takes some of the burden of innovation off the banks and allows new players, such as fintechs, to fill market gaps by partnering with banks. Fintechs are known for their ability to bring products to market quickly, and by collaborating with banks, the two can benefit from each other's strengths. The bank shares its user base and reach within the market, and the fintech shares its creativity and technological agility. They also mitigate each other's weaknesses – complex and siloed legacy systems from banks hinder innovation and fintechs lack the user base and reach that banks have.

These partnerships have the ability to reach previously underbanked and underserved groups in South Africa by providing services that meet their needs in an easy, user-friendly way that is cheaper than traditional financial products and services. For example, challenger banks such as N26 in Germany focus solely on creating a compelling user experience and relentlessly outsource all non-core functions, using APIs to access them.

N26 uses banking-as-a-service providers like Mambu (also from Germany) to provide their core banking platform. This allows N26 to focus its efforts on providing customer service and integrating additional services onto its platform rather than building, processing and maintaining its own back-office. N26 also outsources its Know Your Customer (KYC) process to yet another fintech, IDnow. This allows N26 to on-board customers within minutes using a smartphone with an internet connection, saving both the bank and the end user's time, and offering superior customer service via increased convenience. Being a digital-only bank allows N26 to save considerable costs on traditional branches, which allows it to offer customers a basic bank account that is free, something that could help traditionally underbanked populations in South Africa by giving them access to electronic payments, savings platforms, insurance, and other digital services enabled by banking APIs.

For the fintech firms, such as Mambu and IDnow, partnering with banks offers the ability to innovate and offer their products to an expanded user base. This symbiotic relationship also benefits consumers by giving them easy and convenient access to products and services at a cheaper price while also offering these products and services with quicker turnaround time than would normally be experienced at a traditional bank. The net result is improved choice, lower cost, increased convenience, and greater speed in financial services. These services, however, are not limited to Western Europe and are expanding in developing countries: Emid, a digital technology company that offers banking-as-a-service and various other SaaS (software-as-a-service) solutions offers similar services to Mambu, whereas pbdigital offers digital on-boarding and KYC solutions by directly connecting to South Africa's Home Affairs database. South Africa can also capitalise on the different ways in which open banking and APIs are creating new business models and create win-win businesses.

# Better serving the informal economy in South Africa

There are a range of services that APIs and open banking policies could offer end users in South Africa. Some of these services are already on the market today but are inaccessible to portions of the population, while others are active in other markets but not currently South Africa. In this section we will discuss the various types of services that South Africans, both consumers and small-scale entrepreneurs, could benefit from. A few of these services include:

- **Personal financial management**
- **Market intelligence and analysis**
- **Comparison and purchase offerings**
- **Credit scoring and loans**
- **Real-time payments**
- **Payment initiation services**

## Personal financial management tools

APIs allow for new products to be created, such as personal financial management tools that allow end users to collate information from multiple accounts into a single user interface. These financial management tools, besides collating what used to be scattered information, offer users key functionality such as budgeting, tracking bills, tracking investments, obtaining a credit score, and other tools to manage finances. This type of tool, such as Intuit's Mint, are helpful for people living under a budget but also for small businesses that need the flexibility and ease of use that API integration offers. Banks, by offering this type of product to their customers, can build up a relationship with end users and offer them value-added services, which gives the end users an incentive to stay with that bank.

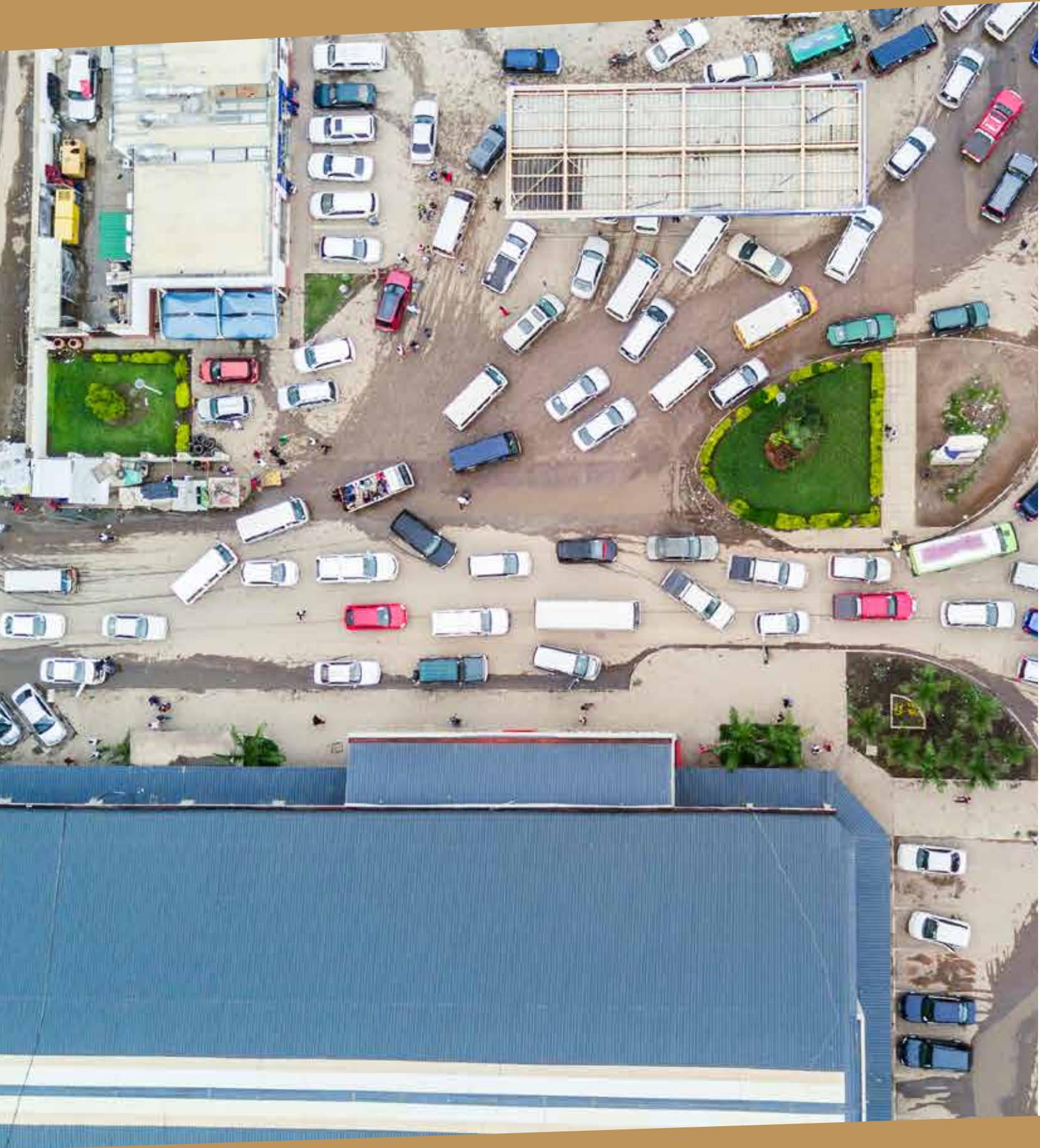
Combined with a smartphone, these new tools can help solve some of the problems rampant in underbanked communities. For example, many small entrepreneurs have trouble getting small loans due to a lack of credit history or have problems

reconciling accounts. These tools provide a much quicker and more accurate overview of business expenses, allowing entrepreneurs to see what parts of their businesses are profitable and how much they can afford to save. This type of financial management also helps small businesses with expansion, which is a key goal for many in the informal economy.

Because this type of tool requires the end user to have an account, its existence could incentivise small entrepreneurs to open a business account.

## Market intelligence and analysis

APIs allow for big data analytics to offer unprecedented market information to banks' business customers. Companies like Meniga, which is already active in the South African market, do this by collecting and anonymising bank payment data through APIs. Data aggregation allows Meniga to offer businesses market research and then tailor this information into a marketing strategy, growing a business' potential market and increasing its conversion rate. More specifically, Meniga helps businesses conduct market research, follow consumer trends, improve their marketing by sending targeted offers to consumers and adjust their business product offerings accordingly. This type of information could be extremely useful for small businesses active in South Africa's large informal economy because many small entrepreneurs lack the time and resources to hire help to work on advertising and market intelligence. While many small entrepreneurs have expressed a desire to grow their business, many rely on word-of-mouth, which has an inherently limited potential. An API-powered platform that can offer helpful information with only limited input from small business owners can go a long way to growing a small business, whether or not it is active in the formal economy.



# Using open banking to promote financial inclusion in South Africa

## Comparison and purchase offerings

APIs are a great tool to collect and display data from many different sources in an easy and understandable way. Product comparison websites such as Raisin and Savedo in Germany offer banks the ability to reach a wider audience by advertising their product offerings using APIs rather than relying on the manual collection of data from the source, which can quickly become outdated. For consumers and small businesses, this means that they can conveniently compare similar products without having to go to different websites. This allows banks and financial institutions to advertise their products on a central platform, making their products and services more visible to the general public without having to worry about advertising and without having to worry about their offers becoming outdated. This allows end users to view a range of different products and services and choose the right one for them.

While Raisin and Savedo offer financial products, it is very easy to imagine an API-powered site comparing products in the local South African market that caters to small businesses or the underbanked. Products such as current accounts, savings accounts and small business accounts all easily lend themselves to comparison websites targeting the underbanked in South Africa. This could allow small business owners to have a clear, up-to-the-minute view of evolving bank and non-bank products and help them better understand when it may make sense to open a business account instead of using a personal bank account or dealing exclusively in cash.

The availability of these products in a digital format could also be a further step in promoting more formal financial inclusion for both underbanked individuals and small businesses that could greatly benefit from financial products tailored to their needs. Other products, such as credit cards tailored to SMEs, could also be shared on the platform, allowing SMEs access to products they may not otherwise have been aware of.

## Credit scoring and loans

Many informal small businesses in South Africa lack access to financing due to a lack of credit history and a credit score.

Digital banking and APIs are now allowing would-be lenders to use a simple bank account to check an entrepreneur's credit worthiness as well as creating online platforms for person-to-person (P2P) lending. Fintechs like Kontomatik in Poland allow potential lenders to use everyday bank account transactions to analyse small business or personal banking transactions to judge a person's financial health and to determine the amount that they can be lent. This process drastically cuts down the time required to process loan applications from days or even weeks to potentially hours or minutes, and in some cases even seconds. Algorithms assist lenders in categorising financial data, conducting KYC checks based on bank account information, and aggregating data into useful categories enabling quicker decision-making.

This same technology is being used to create credit scores for small businesses that may have had trouble getting one. German fintech Kreditech is using APIs and machine learning to serve the underbanked in various ways, including micro loans, micro installments, installments, POS financing, pre-paid cards, and external products via a marketplace. Kreditech's product, Monedo, caters to the underbanked by using non-traditional sources of information, such as social media information ("likes" that a restaurant may have, for example) in order to improve its decision-making and serve communities neglected by traditional market players. In parts of Africa, airtime purchases are being used as an indicator of affordability and creditworthiness. This presents an opportunity for Mobile Network Operators (MNOs) and banks to partner and could allow informal business owners to be assessed for micro loans.

# Using open banking to promote financial inclusion in South Africa

Lastly, these platforms can also connect individuals for P2P lending, allowing individuals to make and receive small loans without having to involve a formal institution. The potential benefit of small, P2P loans should not be underestimated in its potential to help traditionally underbanked communities. Companies like Nobuntu are helping to fill a market need by offering P2P social insurance programs that benefit the community.

## Real-time payments

One of the biggest challenges for many informal small businesses is fundamental to business and trade: sending and receiving payments. While cash is the original form of a real-time payment, the problems with using cash as a primary payment method are well documented: security, the need for proximity, the lack of electronic transaction records, and lack of scalability. The uptake of electronic payments by informal businesses in South Africa is hampered by a number of factors. The foremost issue is the need for a bank account to make electronic payments such as EFT, real-time payments, or accept card payments. Most South African businesses in the informal economy do not have a bank account, and many only have access to electronic payments if they use a personal bank account. The second issue is that even if a business is able to send an EFT payment or accept a card transaction, the funds may take a day or more to reach the beneficiary account. For small informal businesses operating on tight margins, locking up funds in payment systems can make it difficult to pay employees or suppliers. Some informal businesses could look to solutions from non-bank providers such as fintechs, but these are limited by the lack of reach of closed-loop systems. The final challenge is the prohibitive cost of electronic payments to informal businesses.

Some of these structural challenges could be overcome by expanding choice for informal businesses via open banking. For instance, banks could partner with fintechs serving the

informal sector to enable expanded reach for electronic payments using mobile wallets. This would allow small businesses to reap the benefits of electronic payments (particularly real-time electronic payments) without the high cost of initiating payments directly via a bank. One of the biggest benefits of real-time payments for small businesses are those related to liquidity management. Instead of having to worry about nights, weekends and holidays, real-time payments allow end users to pay for goods 24/7/365, giving them increased flexibility when making business-related payments. It also allows lower risk for entrepreneurs who are hesitant to carry large amounts of cash on them and increases the channels through which business supplies can be purchased (online as well as in-person).

Another issue surrounding payments for small businesses is the trust gap: one of the reasons that cards are so widespread is the guarantee of funds that card systems offer merchants. Real-time payments, on the other hand, can provide guarantee of funds (via instant notification) and do away with the delay. While real-time payments have the ability to be even cheaper to accept than card payments (from the merchant perspective), this is so far not the case in South Africa, although widespread adoption could make this more likely. This is a possible game-changer because businesses would save money by accepting real-time payments, increase flexibility in making and receiving payments, and get the benefits of having access to more formal financial products.

Another issue surrounding the initiation of real-time payments is that banks in South Africa have not set up an interbank proxy database which would make initiating real-time payments much easier. Easing payment initiation could go a long way to encouraging usage of the system, which could have lots of downstream effects including encouraging the opening of bank accounts among traditionally unbanked communities.

## Payment initiation services

Lastly, the growth of open banking and APIs has encouraged new types of payment initiation services to enter the market. While services like PayPal are by no means new, other companies such as Klarna have built additional services on top of the everyday payment, such as their “pay later” and “slice it” services, whereby consumers can wait up to 30 days to pay for an item or pay for items in instalments. These services are liked by merchants because the merchant receive funds normally and Klarna takes on the risk of receiving the funds from the consumers. Klarna uses APIs to embed itself in merchant websites and uses APIs for its various payment products, but there are many other companies now using APIs to initiate payments directly from consumer or business accounts. Furthermore, larger, more established tech companies such as Google, Alibaba, Facebook, Samsung, Tencent and Apple are all offering their own payment methods, both for online payments but also for POS transactions via NFC technology, QR codes, or mobile wallets.

Some of the payment methods require more open banking infrastructures and widespread API usage while others are simply new ways to initiate payments via card-not-present technology (such as mobile wallet solutions), but all of these new ways of initiating payments could help make non-cash payments in South Africa more feasible and bring down the cost of accepting non-cash payments, benefitting both consumers and businesses in the formal and informal economy.

# Conclusion

Open banking has the potential to promote financial inclusion in South Africa and help spur inclusive growth. By separating the production of financial services from distribution using APIs, banks can collaborate with non-banks to develop innovative financial services that can reach segments of the market that have previously been inaccessible. Banks stand to reap significant rewards from the move to open banking by seeing greater efficiencies, lower costs, and an expanded market for their services. Non-banks such as fintechs or telecommunications firms can team up with banks to offer services targeted at the informal economy. Retailers, many of whom currently offer closed-loop payment services, could also partner with banks to expand the reach of their services or access payment systems directly. Regulators could also play a role in the move to open banking, for instance by institut-

ing a more risk-based KYC regime that helps open up access to the informal economy for formal institutions such as banks. The move to open banking will open up new business models in payments and financial services and help give banks the flexibility to keep pace in the rapidly evolving financial services industry. It will also allow them to serve market niches that are not profitable or desirable under traditional business models. The ultimate beneficiary of the move to open banking will be consumers and businesses in the informal economy, who will have access to better services, lower costs, a more feasible path into the formal economy and better economic prospects.



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## About IQbusiness

IQbusiness is the leading independent management consulting firm in South Africa, helping clients overcome their business challenges and achieve better results. Since 1998, we have been enabling banks, insurance companies, retailers and others to take their products to market faster, improve customer satisfaction, upskill teams, eliminate waste and strengthen governance and compliance.

Drawing on our core strengths - consulting, research and contracting - we solve clients' problems by providing innovative, faster and more cost-effective services and solutions, backed by teams with real expertise and experience.

Although proudly South African, our perspective is international through the experience of our people, our clients and our business partners. IQbusiness is privately owned and fully empowered with a level 3 B-BBEE certification.

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## About Lipis Advisors

Lipis Advisors' core business is payment system analysis, design, and strategic advisory services for payment associations, clearing houses, banks, and software processors. We are payment systems experts and maintain the Lipis Advisors Global Payment Systems Analysis, one of the world's richest payment system information databases.

Our expertise and intellectual capital enable us to deliver robust analytical frameworks for the analysis of payment systems and products as well as support clients with payments system design, strategy, product development, organisational development, and supplier selection. Based in Berlin, Germany, our consulting supports dozens of internationally recognised clients. Lipis Advisors offers an unparalleled combination of expertise and experience in payment systems research and consulting.

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