

Exploring barriers to remittances in
sub-Saharan Africa series

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Remittances in Nigeria

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Acronyms

| | |
|---------|--|
| AML/CFT | anti-money laundering and the combating the financing of terrorism |
| ATM | automated teller machine |
| BVN | bank verification number |
| CBN | central bank of Nigeria |
| CIFT | inter-bank fund transfer |
| DMB | deposit money bank |
| EFT | electronic funds transfer |
| FATF | financial action task force |
| KYC | Know-your-customer |
| MFB | microfinance bank |
| MMO | mobile-money operator |
| MNO | mobile network operator |
| MTO | money transfer operator |
| NACS | Nigerian automated clearing system |
| NCS | Nigerian central switch |
| NEFT | NIBSS electronic funds transfer |
| NFIS | national financial inclusion strategy |
| NIBSS | Nigerian inter-bank settlement system |
| NIMC | national identity management commission |
| NIN | national identity number |
| NPS | national payment system |
| OTC | over-the-counter |
| POS | point-of-sale |
| PSB | payment service bank |
| PSM | payment systems management |
| RBA | risk-based approach |
| RSP | remittance service provider |
| RTGS | real-time gross settlement |
| SANEF | shared agent network expansion |
| SDG | sustainable development goals |
| SSA | sub-Saharan Africa |
| SWIFT | society for worldwide interbank financial telecommunication |
| USD | US Dollar |
| USSD | unstructured supplementary service data |

Key definitions

| | |
|------------------------------------|--|
| Mobile-money operator (MMO): | A licensed mobile-money service provider that develops and deploys financial services through mobile phones and mobile telephone networks. |
| Mobile network operator (MNO): | A company that has a government-issued licence to provide telecommunications services through mobile devices. |
| Remittance service provider (RSP): | An entity providing services that enable the transfer of remittance funds. |

Source: Authors' own based on AFI (2013)

About the barriers to remittances in sub-Saharan Africa series

At the time of writing, the average cost of remittances to sub-Saharan Africa (SSA) was 9.3% of the value of the transaction, compared to the global average of 6.9% (World Bank, 2019). Informal flows are rife, especially in SSA, and the trend is increasing in many corridors. High amounts of informal remittances, coupled with the high cost of formal remittances are indicative of a formal market that is not functioning optimally to serve people's needs. The G20 and the Sustainable Development Goals (SDGs) made it an explicit target to reduce the price to between three and five percent of the transaction value. However, a fine balance needs to be struck between lowering the cost and keeping remittance business profitable for providers, especially in hard to reach areas, so that access for rural consumers is not compromised. To do so, there needs to be an understanding of the market impediments preventing formal costs from decreasing and hindering access for consumers.

This note is the sixth in a series of seven notes that explores the barriers to remittances in SSA to conclude on what is required to enable the formal market to fulfil its true potential.

The series is organised as follows:

- Volume 1 provides an overview of key remittance corridors in SSA, from the perspective of both the receiving and sending countries. It analyses the correlation between migration and remittances and introduces a categorisation of countries.
- Volume 2 outlines and ranks the market barriers to the efficient flow of remittances in SSA, drawn from existing literature and in-depth stakeholder interviews.
- Volumes 3 to 6 explore how the barriers manifest in the region by presenting four country case studies from SSA: Uganda, Ethiopia, Côte d'Ivoire and Nigeria.
- Volume 7 draws conclusions and recommendations for SSA on how to overcome the barriers to reduce informality and costs without compromising access in the region.

This note explores the state of the remittance sector in Nigeria and unpacks the key barriers and enablers to the development of the formal remittances market, drawing on in-country stakeholder consultations from February 2018 and desktop research.

1. Introduction

A lifeline for households. Remittances are defined in the International Monetary Fund’s sixth edition of the Balance of Payments and International Investment Position manual as “all current transfers in cash or in kind made or received by resident households to or from non-resident households... [or] current transfers made by employees to residents of another economy” (IMF, 2013). Remittances can take many forms but are typically associated with working migrants that send regular amounts of money to support their families and communities back home. The advantage of these payments is that they usually flow directly into the hands of households, which increases household income and reduces the likelihood of households falling into poverty (International Organisation for Migration, 2005). This monetary support has positive effects on both education and health outcomes, and it has been shown to support human capital development particularly in children (Gupta and Pattillo, 2009; Hassan, et al., 2017).

Nigeria’s remittance inflows impressive yet informality dominates. Volume I of this series (“Where are the flows?”) revealed how Nigeria dwarves all other African countries in terms of volume and value of remittance flows. Their diaspora remains closely tied to home even after many years abroad and sends an increasing number of funds to support families and friends. While formal flows are high, informal flows are said to be even higher, causing a strong, competitive informal sector in money transfers. Formal remittance prices, especially between Nigeria and other African countries are still exorbitant and show a lack of competition. Despite the high remittances inflow into Nigeria, poverty and inequality are still prevalent, and the country is yet to make efficient use of remittances like other developing countries. This report is therefore aimed at understanding the market conditions for remittances: what drives the high rate of informality and what are the cost drivers for providers?

Case study outline. This case study outlines the barriers and enablers of remittances in Nigeria. It is organised as follows:

- Section 2 introduces the remittance sector in the country, including remittance flows, the actors, the regulatory framework, and the infrastructure underpinning the money transfers.
- Section 3 discusses the country-specific remittance barriers and enablers in terms of business case, regulation, infrastructure and consumer-facing elements.
- Section 4 offers recommendations and conclusions for actors already active in the market and for those who wish to enter.

2. Remittance sector overview

2.1. Remittance market

Nigeria's remittance inflows highest in Africa; high prevalence of informality. Remittance inflows into Nigeria are by far the highest in Africa. In 2017, they were the sixth-highest in the world¹. Figure 1 shows that in 2018 USD 24.2 billion was remitted to Nigeria – a 9% increase from 2017. The Central Bank of Nigeria (CBN) attributes this growth to improved global economic conditions (CBN, 2017). These impressive flows constitute just under one third of total formal remittance flows into Africa and are ten times higher than those of Senegal, which is the second highest recipient in SSA. Remittances were worth 5.9% of the Nigerian GDP in 2017 (World Bank, 2017). This is an impressive figure given that Nigeria is Africa's largest economy. Capital flows in general, and remittances in particular, have accelerated rapidly since 2005 due to the opening of the Nigerian capital market, and the country is considered to have joined the ranks of frontier markets² (IMF, 2016). Various sources report that the flows are vastly underestimated, however, with as much as 50% of remittances entering the country through informal channels not captured in the official data (Iheke, 2016). Remittance outflows stood at around USD275 million in 2017, making Nigeria a clear net recipient of remittances³ (World Bank, 2017).

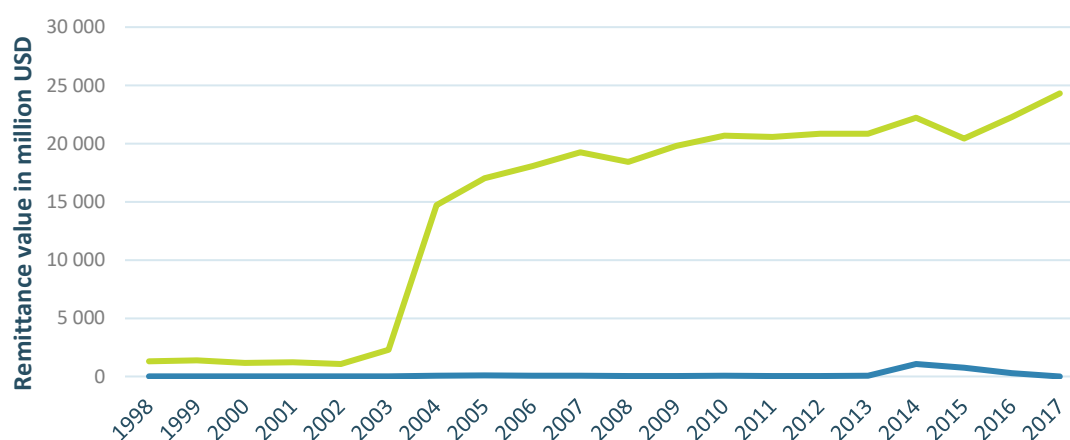


Figure 1. Nigeria remittance inflows and outflows over time

Source: World Bank Migration and Remittances Data, 2018

Diaspora widespread; highest inflows from USA and UK. Estimates suggest that currently around 15 million Nigerians live abroad, or around 8% of the total Nigerian population (Vanguard, 2017). The diaspora is widespread but can mostly be found in developed countries in Europe and North America as well as other West African states. Figure 2 shows that most Nigerian migrants live in the USA, UK and neighbouring Cameroon, collectively making up

¹ After India, China, the Philippines, Mexico and France (World Bank, 2017).

² Frontier markets are economies with access to international capital markets and domestic financial markets that are deep and open relative to other low-income developing countries (IMF, 2016).

³ Analysis of Nigeria's capital flows is subject to limitations in the data, as inflows are generally captured more comprehensively than outflows are. This has in the past been a contributing factor in the large, negative errors and omissions reported in balance of payments data (IMF, 2016).

almost 50% of Nigerians abroad. In line with migration, the diaspora in these three countries also send by far the highest amount of formal remittances back home – close to USD13 billion collectively (World Bank, 2017)⁴. Nigerian migrants are often well educated and highly skilled. In the USA, they are the immigrant group with the highest level of education in the country (Chron, 2018). This profile allows the diaspora to send larger amounts of money back home compared to other SSA countries due to higher average earnings. Their close family and cultural ties translate into sustained remittance flows even from second or third generation Nigerians (Hernandez-Coss & Egwuagu Bun, 2006).

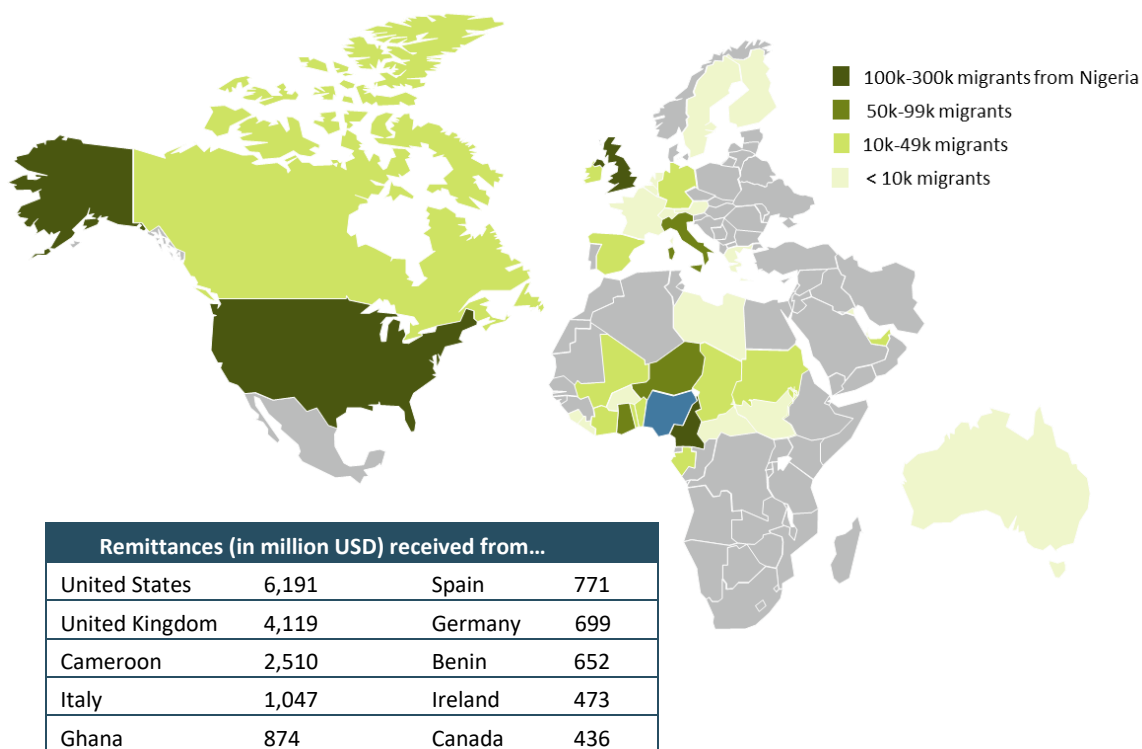


Figure 2. Nigerian documented migrant stocks abroad and top 10 countries sending remittances to Nigeria

Source: World Bank, 2017

Internal migration substantial. Within Nigeria migration is also substantial, especially from rural into urban areas. Nigeria has a relatively large network of urban centres scattered across all regions of the country and the rate of urbanisation is over 4% per year (CIA, 2018). Despite the extent of migration within Nigeria, little to no data exist about the aggregate volume of internal migration or remittances. Yet, anecdotal evidence suggests that most of those who move out of the rural communities maintain strong links to their places of origin (Mohapatra & Ratha, 2011). In a continuously growing and worrying trend, conflicts, especially in the North-East of the country, have led to a large number of internally displaced Nigerians. The Boko Haram insurgency has left over 1.9 million Nigerians internally displaced since 2014. In addition, over 228,000 Nigerian refugees have fled to neighbouring Chad, Niger and Cameroon in 2017, living in vast refugee camps (UNHCR, 2018). The high number of migrants and

⁴ Following the collapse of oil prices and the austerity measures adopted by successive Nigerian governments to correct the macroeconomic imbalances of the late 1970s and early 1980s, economic conditions deteriorated for a large proportion of the population. What followed was massive emigration of Nigerians, driven by the prospect of higher wages elsewhere. Nigeria's geographic and ethnic diversity plays out in most national issues—including migration and remittances. For example, within their broader Nigerian immigrant communities, Ireland has attracted a particularly strong community from southwest Nigeria, and the USA a large contingent from southeast Nigeria (Agu, 2010).

refugees, both domestic and cross-border, calls for an array of cost-effective and convenient remittance solutions for the Nigerian population.

Informal channels and MTOs dominate cross-border flows. While no official data on informal mechanisms exist, it is estimated that an additional 50% of the formal remittance flows into Nigeria are transferred informally, as outlined above. There are several ways of transferring money this way. One of the most popular method of the diaspora in the UK, for example, is sending cash with friends or family travelling back home. Others rely on trader relationships or value transfer systems to offset import payments with remittances in Nigeria (Hernandez-Coss & Egwuagu Bun, 2006). Informal remittance service providers often have sophisticated back-end and accounting systems, using Naira accounts opened in local banks to pay out proceeds to the beneficiaries while channelling the foreign currencies to fund the parallel market (CBN, 2014). Stakeholders also suggest that cross-border remittances are partly happening on the back of illicit financial flows (Stakeholder interviews, 2018). In terms of formal providers, there are currently 35 money transfer operators (MTOs) licensed to conduct international remittance transfers (CBN, 2016). Nigerian banks, also called deposit money banks (DMBs), are prohibited from operating as MTOs but can act as MTO agents (CBN, 2014). Of the 21 DMBs, 19 offer remittances via MTOs⁵. Neither the post office nor any mobile-money operator (MMO⁶) are currently offering cross-border remittance services. Essentially all formal international remittances are received into bank accounts or over the counter (OTC) via MTO agents.

Banks and informal channels dominate domestically. The channels most commonly used for sending and receiving money within Nigeria are bank transfers and via family/friends. According to Findex (2017), 51% of Nigerian adults sent or received remittances in the past year. Of those who did, 46% indicated having used an account. Thirty-six percent (36%) sent or received funds in person or in cash only. Only 14% used a mobile phone; 2% used an MTO service. While there is considerable growth in using a mobile phone as a transfer mechanism (a 14% increase since 2014), Nigeria is far behind markets like Ghana, Uganda or Kenya. In Uganda, for example, 82% of adults sent or received money via a mobile phone in 2017 (FSD Uganda, 2018).

Remittance costs competitive in UK and USA yet exorbitant in Cameroon corridor. Prices to send USD200 from the USA to Nigeria are quite competitive with an average cost of just over 5% of the transfer value. Competition in this channel is high with many providers offering transfer services, both via the internet and OTC agents. The UK-to-Nigeria channel shows slightly higher costs of almost 6%⁷ despite the fact that there are even more operators available to consumers than in the USA-Nigeria channel. Digital MTOs charge between 2.2% and 5% while transfers via traditional OTC MTOs set consumers back by between 6% and 12%. Yet, the latter have a larger cash-out footprint. The Cameroon-Nigeria channel is by far the most expensive channel of the three, with an average cost of over 11%. Only three providers offer their services⁸ and the dominant OTC MTOs charge close to 14% and 15.5%, respectively (World Bank, 2018). While the cost of remittances in the case of the Cameroonian corridor is likely to be a major deterrent of using the formal remittance system, it would seem that this is less likely in the UK and USA corridors.

⁵ Information obtained from the banks' websites.

⁶ There are 21 licensed MMOs in Nigeria, six of which are initiatives by banks. They only operate domestically, however.

⁷ Average for second quarter of 2018.

⁸ While the cheapest provider states that it charges only 1%, the foreign exchange margin is not transparent, meaning that the RSP could be charging the consumer an exorbitant amount hidden in the exchange rate.

2.2. Regulation

This section focuses on the regulatory background to conduct remittance services in Nigeria. It highlights the regulation around licensing, government policies, know-your-customer (KYC) requirements, anti-money laundering, and regulation for innovation.

Tight exchange rate management by CBN results in parallel market and lower consumer confidence. The Nigerian remittance sector is governed by the central bank and is bank-led. The banking sector is one of the most dominant and regulated industries in the country and the CBN regularly interferes, especially with regard to foreign exchange controls⁹. As Nigeria's economy is heavily reliant on oil, representing over 90% of the country's total export revenue or just under 9% of GDP, the recent collapse in world oil prices resulted in an abrupt decline in foreign currency revenues. This triggered an erosion in Nigeria's foreign currency reserves. In April 2017, the CBN introduced the investors and exporters window to boost liquidity in the foreign exchange market, trading the Naira at ₦360 to the USD. The official exchange rate was fixed at ₦305/USD1. The very prominent parallel market for foreign exchange, however, traded the USD at ₦362 - ₦364, making it more profitable to use this mechanism to exchange foreign currency. The weaker exchange, high inflation (over 15% at the end of 2017) and high interest rates negatively impacted on consumer confidence in the formal sector in Nigeria (KMPG, 2018, InterMedia, 2018).

Comprehensive set of regulation exists yet it frequently changes. There have been many amendments, retractions and revisions to money transfer guidelines over the years in order to stabilise the financial system, impacting remittance providers. Regular amendments can lead to uncertainty in the sector, impacting investments and scale of flows. Based on the many regulations and guidelines governing the remittance sector¹⁰, the following key policies on licensing, agent banking and anti-money laundering and the combatting of terrorist financing (AML/CFT) are worth highlighting:

- **MTO licensing.** In order to obtain an MTO license for cross-border remittances, the applying institution needs to be present in at least seven countries and have a minimum capital requirement of ₦2 billion (around USD6.5 million¹¹) for domestic applicants. Partnerships with foreign entities providing middle mile services require a letter of no objection from the CBN. Unlike DMBs, microfinance banks (MFBs) cannot be MTO agents. MTOs must sell any foreign currency to their agent banks, which then exchange it into Naira based on a weekly hard peg issued by the CBN. Outbound transfers are capped at USD1,000 per quarter per person (Stakeholder interviews, 2018)¹², which explains the low amount of outward remittances.
- **Mobile money and payment service bank licensing.** Only DMBs or corporate organisations specifically licensed by the CBN can apply for an MMO license, excluding mobile network operators (MNOs). The role of MNOs is restricted to providing infrastructure to MMOs.

⁹ In August 2018, CBN accused the South African telecommunications operator MTN of allegedly illegally repatriating over USD8 billion between 2007 and 2015 and asked for a return of the money. The dispute is ongoing but hints at the intransparent developments in the foreign exchange market and accompanying regulatory framework for service providers (Fawehinmi, 2018).

¹⁰ Namely the 2009 AML/CFT Regulation, the 2013 Guidelines for the Regulation of Agent Banking and Agent Banking Relationships, the 2014 Guidelines on International Money Transfer Services and the 2015 Guidelines on International Mobile Money Remittance Service.

¹¹ Using ₦305/USD1 as per official exchange rate in 2017.

¹² In mid-2016, the CBN issued but then backtracked on a new directive that stipulated MTO requirements of USD1 billion in net worth and operations spanning 20 countries as well as 10 years of experience. If this directive had remained in place, only Western Union, MoneyGram and RIA would have been able to continue operations in the country. However, the directive stopped the other RSPs' transfers for a month, resulting in reputational damage (Kazeem, 2016, Stakeholder interviews, 2018).

MMO licenses require minimum capital of ₦2 billion (around USD6.5 million). The maximum transfer amount via Unstructured Supplementary Service Data (USSD) is ₦100,000 (around USD320). In order to offer cross-border remittance services, a provider needs to have an MMO license or a newly created payment service bank (PSB) license¹³. Under the MMO license the applicant needs to have a staggering minimum net worth of USD1 billion, partner with a DMB in Nigeria, and operate in at least 20 countries with 10 years' operating experience. PSB applicants require a minimum capital of ₦5 billion (around USD16.6 million). PSBs are expected to leverage on mobile and digital channels to enhance financial inclusion with a focus on high-volume, low-value transactions. MNOs¹⁴, among other providers such as MMOs, fintechs, and retail chains, are eligible to apply for a PSB license that includes provisions for electronic wallets, carrying out only inbound cross-border remittances services and accepting deposits through agents. No credit may be issued by PSBs.

- **Agent banking.** Agent exclusivity was abolished in 2008¹⁵ to end the oligopoly of two international MTOs that had been dominating the market (Aigbomian, 2016). Licensed deposit-taking financial institutions such as banks, MFBs and the post office, as well as PSBs and MMOs can deploy agents to conduct money transfer services¹⁶. Transactions at an agent need to be real-time. Agents are not allowed to charge fees for cash-out transactions. While the licensing framework around agent banking is quite conducive to the market, agent penetration in Nigeria is still low compared to its neighbours. This issue is discussed in more detail in Section 2.3.
- **AML/CFT requirements.** Nigeria is moving towards a risk-based approach (RBA) in AML/CFT through gradually training financial institutions on how to assess their risk. RBA in KYC is mandated by regulation. However, until the risk factors are better assessed, RSPs are not strictly following a principles-based approach. Instead they fall back on rules-based compliance, including tiered KYC requirements¹⁷. There are three levels of KYC requirements for consumers:
 - **Level 1.** Allows customers to open accounts at a financial institution, PSB or MMO with basic customer information that does not need to be verified. The maximum balance of the account is ₦300,000 (around USD984) and the customer can transact up to a daily limit of ₦50,000 (around USD164). The customer is not required to have a bank verification number (BVN). Section 2.3 explains the BVN system further.
 - **Level 2.** Medium-level accounts require a customer to provide evidence of basic customer information, i.e. a BVN. The daily transaction limit is set at ₦200,000 (around USD655) while the maximum balance is ₦500,000 (around USD1,640).
 - **Level 3.** High-value accounts require full evidence of customer documentation, including proof of address. Transaction limits are set at ₦5,000,000 (USD16,400) and the balance is unlimited.

Competing NPS bills. No national payment system (NPS) act currently exists, but there are two competing bills: the NPS Bill of 2017 and the Payment Systems Management (PSM) Bill of 2017.

¹³ Guideline FPR/DIR/GEN/CIR/07/018. The guidelines provide that PSBs will operate mainly in rural centres and unbanked locations and must have at least 25% of their “financial services touch points” (to be defined by the CBN) in these areas. Further, they must establish ATMs, operate through banking agents in accordance with the CBN Guidelines for the Regulation of Agent Banking and Agent Banking Relationships in Nigeria 2013, and use other channels, including electronic platforms, to reach out to customers (Aluko & Oyeboode, 2019).

¹⁴ MTN Group announced that it will apply for a mobile banking licence in Nigeria at the end of 2018 (Moneyweb, 2018).

¹⁵ Directive BSD/DIR/CIR/GEN/VOL 2/017

¹⁶ Three agent tiers exist: Super-agent (agent networks that establish a collection of outlets), sole agent (a singular agent who does not delegate powers) and sub-agent (agent networks that are under direct control of a super-agent).

¹⁷ 2013 Circular FPR/DIR/CIR/GEN/02/001 and subsequent amendments in 2017

These bills have similar objectives, but they have different implications for the regulation of the Nigerian NPS. The harmonised PSM Bill appoints the CBN as the only authority for “management, regulation and oversight of the payment system, with a Payment Scheme Boards and a Strategy Committee”. However, the NPS Bill 2017 allows an association of payment system participants to act in a self-regulatory capacity. Under the PSM Bill, the CBN is empowered to give authorisation, refusal or revocations to operate or participate in the Nigerian NPS, but the bank is given no such authority under the NPS Bill. This responsibility rests with an association of payment system participants. Essentially, the NPS Bill allows the payments industry participants to regulate themselves. However, international best practice is that the CBN should oversee the payment system (Cooper, et al., 2018).

Regulation for innovation: new sandbox for fintechs introduced. CBN and the Nigerian Inter-Bank Settlement System (NIBSS) established a regulatory sandbox in 2018, namely the “Financial Industry Sandbox”. The objective of the sandbox is to empower fintechs to come up with innovative digital products that will enhance financial inclusion in the country. The PSB licence was created as a result of the sandbox (Abubakar, 2018). The full effect or success of the sandbox is yet to be seen in the market.

2.3. Infrastructure

This section focuses on the Nigerian payment system conditions as the basis for efficient remittance provision. It further describes the status of the financial access points, mobile network, internet, electricity and road infrastructure.

CBN’s cashless society vision pushes electronic payment infrastructure development. In 2007, CBN launched the Payment Systems Vision 2020¹⁸, which identified a series of recommendations to increase the resilience of the payments system infrastructure to encourage the usage of electronic payment methods. In addition, CBN introduced the use of credit and debit cards as well as electronic fund transfer (EFT) as part of the “cashless policy” in 2012. This implied a cash handling charge on daily cash withdrawals to reduce the amount of physical cash in the economy and promote electronic transactions (CBN, 2012).

Modern, well-structured NPS to support remittances. Nigeria has modern, well-utilised NPS to support the transition away from cash and consists of a large number of players. Twenty-five (25) banks, 50 licensed payment service participants¹⁹ and just over 3,900 other licensed financial institutions²⁰ participate in the NPS.

NIBSS facilitates cooperation among competitors in the NPS. NIBSS, owned by the DMBs and the CBN, ensures cooperation among payment service providers in the non-competitive space of the retail portion of the NPS (Cooper, et al., 2018). It plays a central role in the NPS as it runs the Nigerian automated clearing system (NACS) and the Nigerian central switch (NCS). The NPS is made up of a variety of additional infrastructure elements such as the inter-bank fund transfer (CIFT), NIBSS instant payment (NIP), NIBSS electronic funds transfer (NEFT), automated teller machines (ATMs) and point of sale (POS) devices to support remittances in the form of

¹⁸ Available at <https://dfsobservatory.com/content/central-bank-nigeria-nigeria-payments-system-vision-2020>.

¹⁹ Includes four domestic card schemes, 21 MMOs, three payment solutions providers, 14 payment terminal service providers, six switches, and two third-party processors.

²⁰ Includes over 950 MFBs and over 2,800 bureaux-de-change.

cash, cheques, EFTs, mobile payments, internet transactions and international payments via SWIFT²¹. The most important and innovative infrastructure elements are:

- **NACS.** NACS, introduced in 2002, is the automated clearing system of the entire banking and financial industry for both debit and credit transfers, as well as derivatives/image paper-based instruments (cheques).
- **NCS.** The central switch was implemented in 2010 and serves to interconnect and interoperate between the various players in the financial system, including banks, mobile payment operators, non-banking financial institutions, payment terminal providers, card acquirers, government institutions etc. All financial service providers are required to connect to the switch. Usage of the NCS has grown rapidly over the years, with payments valued at USD171 billion processed through the switch in 2016 (Cooper, et al., 2018).
- **CIFT.** The CBN inter-bank fund transfer is the Nigerian real-time gross settlement system (RTGS), interfacing with the T24 System core banking application. All DMBs and Discount Houses are direct participants. The T24 System is a significant development of the Nigerian NPS, as it allows 24/7/365 online operation, which removes the need for end-of-day processing. The RTGS system also facilitates straight-through processing between CIFT and core banking applications. It uses the SWIFT messaging format and operates on the SWIFT network. CIFT checks all the boxes for a central bank system with dynamic securities management linked to the RTGS system, which makes it efficient for banks to remain invested in interest-bearing securities while still having access to the value (Cooper, et al., 2018).
- **NIP.** Introduced in 2011, the NIBSS instant payment system is a point-to-point funds transfer service that guarantees instant value to the beneficiary. It is a real-time, online, bank-account-number-based, inter-bank credit transfer. NIP is offered on mobile, internet and branch banking platforms for individual and corporate clients. Settlement occurs once per day in the NIBSS third clearing cycle at 4.30pm. The ability to receive instant payments regardless of which bank the payment is sent from or which payment channel is used is highly innovative. In a market where a high incidence of fraud and rent-seeking undermines trust in formal institutions, the instant receipt of funds builds trust in the reliability of the payment system. The almost instantaneous transfer of value also brings the value proposition of digital payments closer to that of cash (Cooper, et al., 2018).
- **NEFT.** The high-volume batch payment method, NEFT is a typical ACH system that supports both credit and debit payments. NEFT transactions settle in two of the three daily settlement sessions of NACS. Settlement 1 (10am) and Settlement 2 (3pm) offer same day value for ACH credits. There is no value limit (minimum or maximum) on NEFT payments. NIP usage in both volume and value is around seven times higher than that of NEFT due to its larger value proposition (Cooper, et al., 2018).

BVN facilitates ease of onboarding. The BVN system was established in 2014 and is a centralised biometric financial identification system, which allows customers to be identified across financial institutions. Under this system, customers become interoperable with the banking and payment system as a whole. BVN data is stored in a central database at the NIBSS, which allows authorised financial institutions to authenticate customer information against this database to prepopulate their product and account applications. The BVN currently uniquely identifies 33.3 million customers across the banking system and increases the effectiveness of

²¹ The Society for Worldwide Interbank Financial Telecommunication (SWIFT) provides a network that enables financial institutions worldwide to send and receive information about financial transactions in a secure, standardised and reliable environment (SWIFT, 2010).

KYC. The goal going forward is to authenticate transactions without the use of cards, using only biometric features (Cooper, et al., 2018). BVN data is being used to feed the national identification number (NIN) database, which aims at establishing the identity of every Nigerian citizen and ties together all records of an individual in the database. The roll-out of the NIN is still slow (Fatokun, 2018).

Fragmented ID systems. Nigeria operates a fragmented identity landscape. About 13 or more identity programmes are run by different government agencies. Most identity systems are not interlinked. The different programmes are geared towards issuing an identity card. Citizens thus have to carry multiple identity cards for different uses. No single identity registry has reached full scale. As of 2019, the National Identity Management Commission (NIMC) had only about 35 million records on their system and is still facing hurdles in rolling out the national ID cards (NIMC, 2019).

Financial access points low yet new agent strategy promises expansion. The number of financial access points, including bank branches, ATMs and agents in Nigeria is low when compared to other SSA countries, particularly in rural areas. Despite a relatively conducive regulatory and licensing regime, agent penetration is still low. A geospatial mapping exercise found that there are approximately 17 active financial access points per 100,000 adults in Nigeria, compared with 181 in Kenya, 116 in Uganda and 44 in Bangladesh. Less than half of Nigerian adults are aware of a bank branch within 30 minutes of where they live or work (EFInA, 2017). In January 2018 Nigeria had an agent force of less than 30,000 agents, whereas the estimated requirement to effectively serve the nation was pegged at about 180,000 (Sustainable and Inclusive DFS, 2018). In a push to expand the agent network, the CBN announced in March 2018 that it had reached an agreement with DMBs, MMOs and super agents to push for a roll out of a 500,000-strong agent network under the new Shared Agent Network Expansion (SANEF) programme to bring financial services to the estimated 50 million underserved Nigerians (Komolafe, 2018). However, the meagre commission structure for cash-in and cash-out services for agents does not incentivise an expansion of the agent network. MNOs cannot use agent networks for digital financial services, except under the super agent license. Furthermore, the super agent framework is not yet trusted or fully understood by stakeholders (CBN, 2018).

Fairly good mobile network and internet penetration. Ninety-nine percent (99%) of Nigeria's population is covered by a mobile network signal, compared to 89% in Kenya and 87% in Ghana (World Bank, 2016). However, stakeholders suggest frequent network downtime, especially in rural areas. Nigeria has an internet penetration rate of 48%, with about 92 million Nigerians having access to the internet. With that, Nigeria is ranked as Africa's highest internet-using country, making up roughly 27% of the continent's total usage, followed by Egypt, Kenya and South Africa (IT News Africa, 2017). The high mobile network and internet penetration is a good foundation for digital remittances if uptime can be guaranteed.

Electricity and state of the roads less impressive. In contrast to the internet penetration, only 60% of the Nigerian population have access to electricity. In comparison, 80% of Ghanaians are covered. Forty-one percent (41%) of the Nigerian rural population has access to electricity, slightly higher than in Kenya (39%) but much lower than Ghana (67%) (World Bank, 2016). The road network in Nigeria is quite extensive yet the road conditions are often poor (Styles, 2018). Both electricity and road infrastructure are necessary pre-requisites for efficient and effective remittances delivery given that the majority of transactions are still conducted in cash. In the absence of electricity, providers need to make diesel generator provisions to ensure that consumers are able to cash in and cash out their digital value. Conducive road conditions are necessary to enable providers to stock their ATMs.

2.4. Consumer

This section describes some attributes of the Nigerian population, including literacy rate, financial inclusion and uptake of mobile money, which impact remittance service provision.

Large population and increasing extreme poverty rates. Nigeria is the seventh most populous country in the world with an estimated population of around 199 million. A staggering 88.2 million people (or over 44% of the population) are estimated to live in extreme poverty²², making Nigeria the country with the most people in extreme poverty in the world, having just overtaken India. This problem is likely to worsen in the light of the major population boom in the country. It is set to become the world's third largest country by 2050 in terms of population (Kazeem, 2018). Half of Nigerians live in rural areas (CIA, 2017). The literacy rate is 60%, much lower than Kenya (78%) and Ghana (77%) (Index Mundi, 2018).

Low rates of financial inclusion. According to the Access to Financial Services in Nigeria 2016 survey, of the 94.6 million adults²³, the proportion of financially excluded increased from 39.5% in 2014 to almost 42% in 2016 (EFInA, 2017). The gender gap is immense: while 51% of men have a financial or a mobile money account, only 27% of women do (Klapper, 2018). This goes against the overall trend in Africa where especially mobile money has improved the financial inclusion of many adults. The decrease of financial inclusion in Nigeria is attributed to the growth in the adult population outpacing that of the banked population and a decline in the contribution of MFBs to formal financial inclusion. Nigeria's financial inclusion strategy (NFIS), which is undergoing a revision process, prioritises financial inclusion through innovation. The country is not going to reach the ambitious targets in financial inclusion set out in 2012, which were aiming for an inclusion rate of 80% of the adult population (CBN, 2018).

Low uptake of mobile money. According to Findex 2017, 21% of adults in SSA have a mobile money account – an increase of almost 50% since 2014. In Nigeria, however, mobile money account ownership is stagnant at around 6% of adults. While roughly seven out of ten adults own a mobile phone, including 35 million unbanked adults and 20 million women, only 1% of adults signed up for mobile money services in 2016. This represents only a 0.2% increase since 2014 (EFInA, 2017). The low uptake of mobile money is partially due to the bank-led structure of the Nigerian market, with banks not prioritising this form of product delivery. There is a big opportunity for mobile money to increase financial inclusion and remittances delivery (Klapper, 2018, EFInA, 2017). Especially USSD services are increasingly popular in the country.

²² Living in extreme poverty as defined by the World Bank is living under USD1.90 per day (World Bank, 2015).

²³ In the EFInA Access to Financial Services in Nigeria 2016 Survey, adults are classified as people 18 years of age or older (EFInA, 2017).

3. Market barriers and enablers

The barriers described in the following sections reflect the findings from interviews conducted with regulators and remittances and payments service providers in the remittance value chain in Nigeria in February 2018. These barriers were considered by industry stakeholders to be either cost drivers, impediments to accessing services or as hindering market development.

The market barriers and enablers are presented through four different lenses. **Business case or commercial** factors are those that impact on a provider's ability to offer services at different costs or expand their access points. **Regulatory** implications relate to specific clauses relevant for cost of and access to remittances. Remittances need to be set in an adequate environment to be able to be accessed by all – hence the **infrastructure** factors describe the supporting conditions in Nigeria. **Consumer-related** issues highlight the realities for the consumer on the ground that can act as drivers or barriers for using formal remittances.

3.1. Business case/commercial

As Nigeria is a net recipient of cross-border remittances, convenient and accessible cash-out options is a major determinant of market share in the remittance market. The underdeveloped financial access infrastructure means that informal mechanisms, which are more accessible and convenient, dominate and outcompete formal RSPs. But even within the formal sector competitive barriers arise. Partnership issues due to lack of trust, reliable data or limited capacity around integration increase provider costs and impact remittance prices for consumers. Each of these business case or commercial factors are discussed in turn:

Informal market impacts formal RSPs' profitability. All interviewees raised the degree of informality in the remittances market as a major barrier. Formal RSPs often struggle to compete with informal providers given that informal remittances are conducted on the back of trading relationships and offer a better exchange rate than on the formal market. Many stakeholders lamented that the limitations around the foreign exchange spread allows only for a two-Naira charge on the dollar. The high level of informality means that formal providers compete for a much smaller pool of formal funds (and foreign exchange), which reduces the profitability of RSPs. It also means that less funds are available for intermediation in the formal sector (Stakeholder interviews, 2018).

Lack of international MTO competition. There is a major lack of competition in intra-Africa channels. Given the regulatory limitations around money transfers, banks prefer to serve corridors where they can earn hard foreign currency and do not see as big a business case in illiquid or volatile corridors. This promotes a tendency towards an oligopoly in many intra-Africa corridors involving Nigeria, leading to high prices for consumers and high barriers to entry for new providers. Given the sheer size of the population, marketing campaigns to drive uptake and awareness around new solutions are hugely expensive (Stakeholder interviews, 2018).

Costly agent management. Customers still largely prefer to send and receive remittances in cash with very few keeping their funds at financial institutions or in e-wallets. This requires a heavy reliance on agents to facilitate money transfers. Agent liquidity, recruitment, supervision, remuneration, the training of agents as well as fraud prevention were raised as

major cost drivers by providers. The following factors were highlighted during stakeholder interviews as significant cost drivers:

- **Liquidity management.** In rural areas it can be difficult for RSPs to ensure effective liquidity management, especially in regions where the number of agents, MFBs and bank branches is low. Some RSPs deploy super-agents or regional cash hubs to ensure better cash reticulation. Furthermore, a small number of RSPs are increasingly using retailers and petrol stations as liquidity partners; however, this practice is still emerging as those retailers are mostly present only in the main towns.
- **Training.** Agents need to be continuously trained on how to deliver new products and how to comply with AML/CFT regulation to remain compliant with the law, especially in light of the frequent regulatory changes. Furthermore, stakeholder interviews suggest that while exclusive partnership agreements have been abolished, agents tend to have a preferred service provider and it is hard to shift their mindset or incentivise them to use the newer products or providers. There is a distinct lack of supervision on agent exclusivity issues.
- **Recruitment.** There is a high turnover in agents, meaning that there is a constant need to recruit new agents and train them. Recruitment in rural areas is reported to be difficult. The tariff structures for agents (in line with the CBN Guide to Bank Charges) do not give profitable commissions for potential agents. This demotivates existing agents and deters potential agents from entering the agent banking business. Most businesses that meet initial requirements qualifying them as potential agents are constrained by the lack of adequate capital to provide agent banking services, especially in the rural areas where the service is needed the most. This is because these agents lack sufficient funds to meet the liquidity demand of cash-in, cash-out and other agent banking services. The documentation required to become an agent is cumbersome, even for those situated in urban areas, deterring recruitment (EFInA, 2016).
- **Fraud.** Fraud by agents, especially in digital channels, has direct financial consequences for RSPs but also carries a reputational risk where customers are cheated by an agent in a position of trust. Especially older customers are still wary of electronic channels and are easily turned off by incidences of fraud, which then fuel the uptake of informal mechanisms. In order to decrease the incidence of fraud, more supervision is necessary which adds another substantial cost layer for providers.

Cybercrime on the rise through the internet, increasing costs of doing business. Many stakeholders mention a steep increase in cases of cybercrime connected to their business. Nigerian internet scams are notorious worldwide, resulting even in its own category of scams (“Nigerian scam” or “419 scam”²⁴). CBN reports DMBs in Nigeria lost around USD7.1 million to fraudsters in 2016 – an 82% increase in the number of reported cases between 2015 and 2016 (Onuba, 2017). Social engineering attacks conducted via emails, SMS and calls are the number one cyberthreat being faced in Nigeria today, resulting in reputational risk and increased cybersecurity and agent and customer education costs (Stakeholder interviews, 2018).

Hardware and system integration costs often prohibitive. While the level of innovation in Nigeria is far more advanced than in many other SSA countries, the associated hardware costs around some innovative solutions remain high. BVN onboarding equipment costs around ₦1.6 million (around USD5,300) per point. QR code readers and equipment for agents are also expensive. Coupled with the poor electricity coverage in some areas, operational costs tend to

²⁴ The “Nigerian prince” scam is among the top five largest revenue sources for Nigeria. For this scam, the consumer is contacted by somebody requesting help in recovering a large sum of money. They claim that if the consumer helps them by providing banking account information or money to pay fees, they will be rewarded with a substantial portion of the money (Finder, 2018).

be high in the country. There is an array of fragmented IT systems in banks and FinTechs that require integration when partnering up. Stakeholders report not only expensive integration issues but a lack of IT capacity at many remittance companies (Stakeholder interviews, 2018).

Security in insurgency areas. The insurgency of the jihadist group Boko Haram in the Lake Chad basin since 2009 poses enormous security and governance challenges for RSPs whose service is regularly interrupted through violence and destruction. This threat to security impacts both operational costs, the ability to recruit more agents and the trust of consumers (Stakeholder interviews, 2018).

Lack of reliable data constrains business case development. There is limited and inconsistent data on formal and informal flows, meaning that use case development is costly for providers. Banks especially do not understand the lower-income market very well given that they target higher earners and corporates (Stakeholder interviews, 2017).

3.2. Regulation

Nigeria has a vast set of regulations governing the remittances sector, comprehensively covering almost every aspect of the industry and showing great appetite for innovation. Positive highlights in regulation include mandated interoperability of payment players, the existence of KYC tiers while RBA is implemented, allowing e-signatures, the creation of only eight balance of payments codes for reporting, and a regulator that is open to stay on top of innovation. However, the detailed regulation and frequent amendments also cause a high level of disruption with most stakeholders identifying regulation as their main impediment to doing business. It has also done little to increase financial inclusion in the country. The issues of exchange rate management, capital outflow controls, lack of competition, regulatory changes, lack of RBA, and the need for proof of address are discussed in turn below.

Tight exchange rate controls negatively impact formal providers. There is a direct link between exchange rate management and formal remittances. Formal remittances to Nigeria decreased from USD21 billion in 2015 to an estimated USD19 billion in 2016. A significant decline in foreign exchange revenue, caused by the fall in oil prices, resulted in tighter capital controls and a managed exchange rate policy. These changes resulted in large black-market premiums in the foreign exchange markets of 33%, diverting a large part of formal remittances to informal channels (World Bank, 2017). Stakeholders name foreign exchange controls as the single most expensive driver of their business (Stakeholder interviews, 2018).

Control of capital outflows fuels informality. The limit of USD1,000 per person per quarter for outbound transfers seriously hampers formal flows and fuels informality. Many stakeholders raised that capital controls impact their business model given that the small sum is often not worth the hassle for consumers who prefer to use informal mechanisms without capital caps (Stakeholder interviews, 2018).

Lack of competition through regulation. International MTOs need to register in Nigeria instead of simply partnering with a local DMB, which can act as a deterrent to market entry given the increased licensing cost and compliance burden. Licensing requirements are high by African standards. Minimum capital requirements, years of operation and multi-country presence requirements present a barrier to entry in the MTO, PSB and MMO licenses, reinforcing the lack of competition in the sector in many corridors. Perhaps a better form of risk mitigation or more tailored prudential requirements are more appropriate to encourage more competition, Fintechs do not play as major a role in the remittances space in Nigeria as they do in other sectors or countries. It remains to be seen if the new PSB license that is also available to

fintechs will bring the desired increase in competition. Domestically, the dominance of banks in remittances is fuelled by the limited involvement of MNOs in remittances due to only being allowed to provide the infrastructure for such payments. The new PSB license paves the way for MNOs to offer financial services, including in-bound remittances, yet does not allow the sending of remittances outside the country. While the effects of the new PSB license are expected to be positive for financial inclusion and digitisation domestically, the restriction on outbound transfers is likely to present an obstacle to increased uptake compared to informal channels (Stakeholder interviews, 2018). The regulatory framework's tendency towards single use case business models seems to have the tendency to unnecessarily fragment scale in flows, increase the cost of doing business and hinder access expansion instead of fuelling investment into more robust and accessible services.

Frequent regulatory changes cause uncertainty and erode trust. The CBN regularly issues changes, new guidelines and directives in the money transfer sector. There is a tendency to overregulate and impose rather stringent requirements, which can hamper innovation²⁵. The move towards creating a regulatory sandbox for fintechs shows the appetite for innovation, yet it runs the risk of overregulation based on past behaviour by the CBN. Several stakeholders mentioned that the unlevel playing field in the sector when it comes to consultations of regulatory changes by the CBN with many providers not being consulted before a proposed change. The frequent changes cause a loss in trust in the formal system by consumers. The lack of regulatory impact assessments and unpredictable change decreases the incentives for investment into a vital sector (Stakeholder interviews, 2018).

RBA is required, yet not applied, in KYC due to lack of country risk assessment. The anti-money laundering regulations state that financial institutions are to adopt a RBA around KYC. To date, financial service providers have faced challenges in developing a risk-based KYC approach due to the lack of data on national, sectoral and customer and product-specific money laundering and terrorist financing risks. As a result, RSPs have largely maintained the status quo on relying on the KYC tier requirements, which do not provide for a KYC process that is proportional to a client's risk or meets consumer needs (Stakeholder interviews, 2018).

BVN as the only form of ID allowed currently causes exclusion. Regulation stipulated that only BVNs are allowed as a form of identification in opening financial accounts. Given the limited roll-out of BVNs, this requirement presents a large barrier to accessing formal remittance service by consumers who do not have a BVN yet (Stakeholder interviews, 2018).

Insistence on proof of address cumbersome for providers and consumers. While the BVN was meant to ease the onboarding of consumers and reduce fraud, KYC barriers are still high. This is because both when registering as an agent as well as when wanting to obtain a BVN as a consumer, the respective regulation requires proof of address. Only 39% of Nigerian adults own both an ID and have proof address²⁶. The value of addresses in proving identity in terms of AML/CFT is heavily contested as it adds limited identification value and is not robust nor reliable given documentary exceptions. Requiring proof of address to open financial accounts hence leads to exclusion of consumers who do not have access to such documents and tends to fuel the use of informal channels (Cooper, et al., 2018). The use of informal channels in turn

²⁵ For example, a directive, which mandated MTOs to remit foreign currency to the local banks for disbursement in Naira was released in 2016. This prevented a number of MTOs who operated through foreign exchange swaps with local partners from doing business in Nigeria. In addition to the directive, MTOs looking to operate in the country had to have a net worth of USD1 billion, operations spanning 20 countries and a minimum of ten years of industry experience. As a result, only three cross-border MTOs were left in the country. One month later this directive was reversed. The damages can be felt in the industry to this day. Stakeholders reported a big financial loss as their operations were interrupted for a whole month causing an erosion of trust and investor uncertainties. Informality rose sharply according to interviewees.

²⁶ ID here refers to any form of ID, including BVN, NIMC ID, handwritten state IDs etc.

decreases cost effectiveness and business case viability. While Level 1 accounts do not require this documentation, the functionality of those accounts is very limited (Stakeholder interviews, 2018).

3.3. Infrastructure

Nigeria's middle mile infrastructure is well-built out and is one of the best positioned on the continent to incorporate and drive innovation in the payment system. The planned RTGS system with other West African nations will drive even higher scale and cost effectiveness in the region. A lot of other countries can learn from Nigeria's set up. This includes the BVN system, increasing convenience for the consumer once enrolled, the instant payments through NIP and the interoperability facilitated by NIBSS. Yet, several obstacles remain in terms of remittance infrastructure that hamper the expansion of formal remittance services. The lack of access points, lack of identification database harmonisation, subpar mobile network and electricity uptime, as well as settlement in only Naira are highlighted in turn below.

Access point expansion via agents still slow. Despite the fact that agent banking guidelines were released in 2013, the agent network is still way below the size of its potential of the market. Given that banks are the main access point for most formal remittance senders and recipients, a lack of banking agents limits the expansion of formal remittance uptake, especially in the Northern parts of the country. According to interviewees, financial services are still mainly utilised by the banked population. Agent banking is a mass market channel targeting the financially excluded, lower-income market. Most banks in Nigeria still shy away from this market segment, preferring to focus on high-wealth, corporate target markets, i.e. are not pushing their agent network expansion. It is yet to be seen whether the SANEF programme is finally able to increase agent numbers substantially (Stakeholder interviews, 2018). With the new PSB license, MNOs are now also incentivised to increase agent expansion. Banks are likely to see major competition from MNOs in conducting remittances, forcing banks to increase their agent network. Road, electricity and mobile network infrastructure development will be crucial in supporting the agent expansion. Research from Kenya has shown that banking agents can form a hub supporting MNO and PSB agents as well as wholesale businesses in a radius from 5km to 15km each, which is far beyond the current business case for a banking agent (Munoz Perez, et al., 2019). It enables the expansion away from single to multiple use-case business.

Inefficiency due to lack of harmonisation between biometric systems. Besides BVN, biometrics are collected for a variety of purposes, such as national ID, SIM registration, vehicle registration, immigration, national elections and others across private-sector and government agencies. The different biometric systems in the country are not yet fully harmonised or interoperable, which is inefficient. Nigeria's NIMC has already started the process of harmonising these biometric databases and, to this end, has collected 15 million BVN records and harmonised 12 million of these to the national identity database²⁷. In addition to this, NIMC has already enrolled 30 million Nigerians into the national identity database and aims to enrol 15 million more before the end of 2018 (Adewumi, 2018; Akowe, 2018; Advocaat Law Practice, 2018). Stakeholders lamented that the quality of MNO databases is subpar compared to that of banks (Stakeholder interviews, 2018). Yet due to the foresight of maintaining almost all the same fields in MNO and KYC onboarding, the potential exists to become interoperable

²⁷ Due to the inefficiencies of these non-harmonised biometric data collection methods, President Buhari issued a directive ordering the harmonisation of all the disparate identification data into the National Identity Database, under NIMC's management, by 2020 (Adewumi, 2018; Advocaat Law Practice, 2018). Although the NIMC Act of 2007 gave NIMC powers to enforce the National Identity Number (NIN) as the required form of ID for financial services, it has only recently been enforced; and some DMBs, have recently begun the migration from BVN to NIN as the primary form of ID (Opusunju, 2018).

with the high-quality enrolments and to enter a process of resampling where records or templates are poor.

Electricity cuts and network downtime increase operational costs and damage trust. Frequent power cuts and network downtime in both rural and urban areas decrease the value proposition for digital solutions in remittances. Stakeholders revealed that these infrastructure challenges have negative implications in terms of consumer and agent trust as POS devices, mobile money services and USSD solutions all require a stable electricity or mobile network connection. Solutions in the form of generators are costly (Stakeholder interviews, 2018).

Settlement in Naira impacts profitability. Settling in Naira was raised as a concern by stakeholders as this makes them vulnerable to exchange rate fluctuations. Naira settlements do not allow for adjusting fees along a spread and hence providers are limited in the fees they may charge consumers (Stakeholder interviews, 2018).

3.4. Consumer

Nigerian consumers, especially in urban areas, are often miles ahead in terms of making use of internet services compared to other African nations. USSD services are common and well-used and e-commerce is on the rise. Yet, the digital expansion is highly unequal both in terms of gender and location. Mobile phone penetration is high yet mobile money use extremely low. The lack of digital use cases, lack of trust and fraud are discussed in more detail below.

Lack of digital use cases reinforces customer cash preference. Consumers' preference for cash or OTC remittances is exacerbated by an absence of digital use cases (Stakeholder interviews, 2018). Remittances are often the first point of exposure to a digital financial service for many consumers. If the central bank and providers want to encourage consumers to keep their received values in digital wallets and accounts in line with their cashless policies, they need to be able to meet consumer needs just as well as cash can (Bester, et al., 2016). However, this is currently not the case in Nigeria. Especially in rural areas, digital value cannot be used to pay for most items (Stakeholder interviews, 2018). USSD services are becoming increasingly popular but mostly in urban areas. Until the payment value chain is fully digitised, providers have to make costly provision for better integrated cash handling including convenient points of encashment. Formal remittance senders are often bound by cash-out options of recipients, i.e. the convenience for the recipient dictates the remittance channel and instrument. The remittances ecosystem in Nigeria plays a vital role in attracting more formal remittances going forward.

Mobile phone ownership high yet financial inclusion low. Given the low access point penetration in Nigeria and the associated queuing in branches, consumers are moving away from opening bank accounts. Most adults own a mobile phone but conduct almost no financial transactions on those devices. Lack of BVNs, the limited engagement of MNOs in the mobile money space, and lack of trust are the main drivers of this phenomenon according to stakeholders.

Financial literacy low, increasing operational costs. In addition to the low literacy rate, in 2017, only 16% of Nigerian adults were financially literate (InterMedia, 2018). The lack of financial literacy requires expensive and extensive education campaigns, especially by digital RSPs without a large agent force to assist consumers with transactions. Combined with frequent power and network cuts, services run the risk of losing consumer trust if the service does not meet people's needs or is not simple enough (Stakeholder interviews, 2018).

Lack of trust in formal financial services fuels informality. Frequent regulatory changes, tight exchange rate management and rent seeking increase the distrust of Nigerian population in the formal financial system. Stakeholders mentioned that the informal sector is often trusted more than the formal system given that it meets people's needs better, circumvents KYC requirements and offers a level of privacy. Strong consumer protection mechanisms are needed, and enforcement of such policies guaranteed to build trust in the formal system.

ID forgery threatens compliance by providers. The many different customer databases and ID systems leave room for forgery. Stakeholders lament the degree of ID forgery among their client base. Continuous training of staff and supervision systems are necessary to ensure compliance with AML/CFT regulation as accepting a fake ID can carry fines for the RSPs.

4. Conclusion and recommendations

Nigeria's vast flow of inward remittances as well as the high number of personal transfers within the country present an exciting opportunity for the country's economy. Instead of solely focusing on oil revenues and being dependent on the oil market, remittances offer diversification. They are direct developmental flows in the hands of those who need the funds most, and already contribute a substantial amount to GDP. Nigerians therefore have a strong incentive to develop this sector further and ensure that remittance flows continue to increase. While the NPS is highly developed and innovative, including the BVN and mandated interoperability, several impeding factors in regulation and infrastructure cause remittance costs to remain high and drive informality in the sector.

This case study presents the main challenges that remittance providers are currently facing in the market. The business case issues encountered mostly relate to bank dominance, the agent management costs, the lack of competition, cybercrime and system integration issues. Regulatory challenges exist around the participation of MNOs, KYC regulation and the lack of the implementation of the RBA as well as the tight exchange rate and capital outflow control. Infrastructure issues arise from the small agent force, competing biometrics systems, the lack of a digital ecosystem, as well as the limitations of the mobile, road and electricity networks. Consumer-facing barriers include the lack of financial inclusion, illiteracy, lack of trust in the formal system and fraud. Informality in Nigeria is especially driven by the tight exchange control environment.

To bring more funds into the formal system to increase the scale of flows and ultimately reduce the cost, the following actions by policy makers, regulators and the private sector could be considered. These are presented in the order of importance:

- 1. *Incentivise MNO participation in remittances to increase access points and drive digitisation.*** Mobile money growth in Africa has mainly been driven by MNOs. While Nigeria's mobile money market is dominated by banks and technology companies, it has become clear that financial inclusion numbers have not increased through this approach. The main reason is the absence of a sizeable access point network accessible to all Nigerians. Convenient cash-in and cash-out options for remittances are vital in driving formal uptake and to reach scale to make business profitable for providers. The newly created PSB licence allows MNOs a greater role in financial services and it should be closely monitored whether the license creates the desired effect towards a more cashless, financially included population. It could be considered whether the current cash-in, cash-out commission structure for agents is appropriate to drive expansion.
- 2. *Consider revising licensing requirements to increase competition and lower costs.*** The regulator could consider revising the regulatory requirements around money transfer licensing. Capital requirements are high compared to many other SSA countries, increasing the barriers to entry of new entrants. For agents, a framework around e-float to obtain cash is necessary to ease liquidity management and make agents less reliant on bank infrastructure.
- 3. *Incentivise more use cases for mobile money to reduce the need for cash.*** Current use cases for mobile money are limited, which entrenches the consumer need to cash-out the received digital funds. Instead of focusing on only digital merchant payments to drive the

demand for digital value alone, it could be considered to digitise the entire payments value chain to decrease the consumer need to hold cash. Government-to-person payment efforts could be expanded to drive the uptake of digital services if this is in line with cash infrastructure expansion to ensure that people can trust that digital value can always be converted to physical currency. Every rollout of digital financial services could emphasise the network use cases including digital value acceptance, liquidity and encashment points so as to not lead to consumer lock-out or hardship and to provide real utility to digital value.

4. ***Potential to establish feedback loops with private sector before issuing new directives to avoid confusion.*** The regulator could consider an improved framework to collect feedback on proposed regulatory changes to decrease the frequency of regulatory revisions and alterations. Regulatory impact assessment could deliver insights as to the gaps in regulation to avoid stagnation and unintended consequences. A stakeholder working group that meets regularly could provide a good forum to raise and understand issues in the market.
5. ***Consider conducting detailed retail risk assessment to guide the application of RBA and allowing alternative IDs to ease the burden on consumers.*** Ideally, the RBA to AML/CFT is adequately implemented at regulator, FSP and RSP levels to ensure proportional KYC requirements for consumers. The regulator could hence consider the adequate assessment of AML/CFT risks within the country via a detailed risk assessment exercise. Sending and receiving low-value funds by lower risk consumers, does not necessarily require the same level of identification certainty or verification as higher-value transfers by higher risk consumers. Key to the adoption of proportional KYC requirements by providers is the implementation of a principles-based concept of identification. This includes the elimination of the proof of address requirement when opening financial institution accounts given its ineffectiveness in risk mitigation. In the absence of full BVN penetration in the country and given the fragmentation in ID databases so far, other identification measures could be employed where a sufficient identification confidence level exists between one or more identifiers or identification elements to enable universal consumer access. In addition, the requirement of a proof of address when opening financial institution accounts could be assessed and potentially revised given its very limited robustness and effectiveness in risk mitigation.
6. ***Harmonisation of biometrics systems to increase use cases and formalisation.*** The lack of full ID penetration either through the national ID or BVN initiatives, as well as the fragmented ID databases drive the cost of doing business for providers and place a burden on consumers. A push to consolidate all existing information can ease onboarding of consumers and add use cases for an ID database for providers. In terms of expensive onboarding systems for the BVN, stakeholders could consider a subsidised programme to roll-out the equipment to key strategic locations across the country.
7. ***Consider improving data collection and quality.*** Because of exchange rate fluctuations and the many competitive options in the informal market, remitters have more incentives to use informal channels. Improving the quality of the central banks' collection of data on formal and informal remittances could improve trust and business case building by providers in the sector. All stakeholders could make use and develop more consumer surveys to understand the consumer better and improve service offering.
8. ***Consider revising capital outflow limits for remittances to drive the use of formal mechanisms.*** In order to make the formal remittance sector more attractive for consumers and increase the business case for providers to serve consumers, policy makers could consider the revision of capital outflow controls. The USD1,000 limit on outflows presents an obstacle for both consumers and providers. It drives informality, which defeats the

objective of the regulation. A potential avenue could be to conduct a regulatory impact assessment to assess the effectiveness of the existing regulation with a view to potential revision of the regulation.

- 9. Consider legalising and licensing the buying and selling of foreign currency at the adequate exchange rate to incentivise formal use.** The overvalued Naira causes a shadow foreign currency exchange market that negatively impacts on the formal providers' business case and reinforces the reliance on informal mechanisms. An appropriate exchange rate policy has the potential to incorporate substantial informal flows into the formal system. A pegged exchange rate with daily moving averages that allows for more flexibility in spread could be considered. In addition, an 'Authorised Dealer with Limited Authority' license framework could be adopted. In South Africa and Zimbabwe, this framework has proven successful from both risk and compliance perspectives.
- 10. Improve electricity and network coverage/uptime to drive quality of service.** In addition to an expanded agent network and digital use cases, electricity and mobile network improvements are vital. These two infrastructure pieces are key in driving more innovation and trust in the remittances sector if formal mechanisms want to seriously compete with the more trusted informal services.

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About Cenfri

The Centre for Financial Regulation & Inclusion (Cenfri) is a global think-tank and non-profit enterprise that bridges the gap between insights and impact in the financial sector. Cenfri's people are driven by a vision of a world where all people live their financial lives optimally to enhance welfare and grow the economy. Its core focus is on generating insights that can inform policymakers, market players and donors who seek to unlock development outcomes through inclusive financial services and the financial sector more broadly.

About FSD Africa

FSD Africa is a non-profit company that aims to increase prosperity, create jobs and reduce poverty by bringing about a transformation in financial markets in sub-Saharan Africa (SSA) and in the economies they serve. It provides know-how and capital to champions of change whose ideas, influence and actions will make finance more useful to African businesses and households. It is funded by the UK aid from the UK Government. FSD Africa also provides technical and operational support to a family of 10 financial market development agencies or "FSDs" across SSA called the FSD Network.