

embracing informality

designing financial services for China's marginalized

January 2013 | By Patrick Ainslie, Sarah Fathallah, and Panthea Lee



Despite China's meteoric economic rise, huge swaths of the population have been left behind. Before the 1978 market reforms, citizens could at least rely on the *tie fan wan* ("iron rice bowl") for jobs, rations, and retirement regardless of their economic standing. However, social support programs have steadily disintegrated in the years since, leaving many rural and poor citizens with neither jobs nor government support.

Driven by a lack of opportunity, 250 million migrant workers have left rural areas to take part in the country's manufacturing boom. Often, even when they find work, their lives are just as defined by poverty and instability as those they left behind.

Financial services are a key leverage point for individual economic mobility, yet banks are becoming scarce in rural areas. More than 30,000 branches in poor and rural regions have closed over the last few years, leaving more than 64 percent of these populations unbanked. Creating new, innovative access to savings accounts, loans, and other financial products could provide the opportunities and stability people need to improve their own futures.

This is not just a moral imperative, it is also a significant market opportunity. These large sections of the population could quickly transform into a growing and sustainable consumer base for savvy and forward-thinking financial service providers who can recognize the latent potential and make strides to meet their diverse needs.

this study

With the support of the Institute for Money, Technology, and Financial Inclusion (IMTFI), Reboot undertook this study to develop and share a deep understanding of the daily lives of China's marginalized. Our goal is to inform the development of new financial services that can tap into this immense potential market and, in doing so, greatly increase these populations' access to economic opportunity and security.

We focused on three marginalized groups of the Chinese population:

migrant workers: The engine of the manufacturing economy, 250 million people strong.

rural villagers: An aging population that survives primarily on money sent home from migrant-worker family members.

ethnic minorities: China's 55 minority ethnic groups, who face restrictive government policies and cultural marginalization.

our findings

Based on 113 interviews and in-country field research, Reboot has uncovered three key findings for any service provider interested in serving this market:

1. Build on informal services,
2. Leverage existing social connections, and
3. Meet people's everyday needs.

Following these directives requires an empathetic understanding of users' daily lives and needs, but this modest investment of time and attention is more than repaid through the increased likelihood of rapid and successful user adoption.

1. build on informal services

Disconnected from formal financial services provided by regulated providers, such as commercial banks or insurance companies, our target populations meet their needs instead through networks of informal services facilitated by social connections. Lacking regulation, these informal services—such as rotating savings and credit associations (*hehui*), or loan sharks (*gao li dai*)—can be exploitive, overpriced, insufficient, and/or unreliable.

Yet our research shows that people often prefer informal services, for several reasons:

convenience: Most informal service providers are individuals that a user already sees in his or her day-to-day life; for example, a traveling veterinarian may also loan his clients money.

ease of use: Paperwork, regulations, and fees are all opaque and intimidating to these target populations. Informal providers, where transactions are enforced by relationships not regulations, can process transactions with just a handshake.

trust: Informal services are built on powerful and longstanding social connections. People feel that their informal service providers can be trusted because their personal and family reputations are on the line.

We found that these factors can impede the adoption of new, formal financial products; people are not likely to risk their financial lives on something new and untested, especially from an unknown institution or organization.

Therefore, we recommend, first and foremost, that service providers design their products to complement—not compete with—existing informal services. By building new services into existing networks of relationships, such as by using an informal service provider as a delivery agent, formal service providers can greatly increase these populations' trust in new products and accelerate adoption.

2. leverage existing social connections

Unofficial and official mass migration has strained, although not completely severed, the traditional Chinese family structure. Migrant workers save and send money back to support their families, and few lay roots in the cities in which they work (which often change each season). China was once a network of walled cities, but is now a web of tethered networks.

Thus, traditional, geography-based definitions of markets are futile. Service providers seeking to accommodate these populations must focus on the human networks that connect them.

These tethers are especially apparent in one particular, widespread system of informal service providers: the *laobans*, or managers, who arrange contracts with employees and take responsibility for recruiting and managing hundreds of temporary workers. Most *laobans* are connected to their workers by only a few degrees of separation, some even hail from the same village. Because *laobans* control worker payments, many workers ask them to provide financial services, such as holding their savings or transporting funds home to their families. The relationship is clearly unbalanced—one worker claimed he could ask his *laoban* for his savings any time, but then confessed he felt social pressure not to ask too frequently—yet it is an arrangement that millions feel comfortable with.

A *laoban* is a prime example of an informal service provider that can be recruited to increase market awareness and trust among our target populations, and to serve as a delivery agent to increase user adoption rates.

3. focus on people's needs

For those with limited economic means, stable services are critical. Consistent, predictable service delivery enables consistent, predictable life patterns, which may alone be enough to improve livelihoods even without increases in income.

Our target populations clearly crave stability: China's 38 percent household savings rate, the highest in the world, reflects people doing their best to brace against economic shock. This desire is a powerful motivator that service providers should focus on when communicating about new services.

Even more importantly, providers must actually deliver the stability they promise. For people with limited economic means, and who have an outsize reliance on a limited number of formal services, the risk of change is a critical one. Service providers must understand that they run the chance of deeply undermining the lives of those already most marginalized. And, as word-of-mouth marketing is the fastest and most effective for such populations, failing to deliver stability can detrimentally inhibit the adoption of any new product.

the financial services landscape in China

Recent public- and private-sector investments, as well as certain conditions in the country, suggest that China is ripe for the development of inclusive financial services:

- Mobile phones have become a critical tool in developing inclusive financial services worldwide; with over 1 billion mobile phone users, China is leading the world in mobile use.
- 83 percent of commercial banks are partially or entirely government controlled, but the government has demonstrated an openness to banking innovation through diverse private-sector partnerships.
- State-owned China Mobile, the world's largest mobile carrier, recently purchased a 20 percent stake in the Shanghai Pudong Development Bank, and the two are collaborating on branchless banking products.
- China Mobile is also partnering with China UnionPay, the country's only bank card organization, to deploy SIM cards that can handle mobile payments.
- China Unicom, another state-owned telecommunications operator, is also deploying a mobile payment system in Sichuan targeting 5.5 million subscribers in the province.
- The People's Bank of China, the country's central bank, intends to launch mobile money pilots in China's rural areas. Participating service providers include the Agricultural Bank of China, the Postal Savings Bank of China, and China UnionPay, as well as all three mobile network operators.

These conditions are promising for innovation but not necessarily inclusion. Experience and inertia often encourage businesses to develop services tailored only for those high on the economic spectrum. We make the previous recommendations with the hopes that a private interest will tailor its business model to empower this large, untapped market segment.

designing a new mobile remittance service

To illustrate how our recommendations may be operationalized, we have designed a hypothetical prototype for a new financial product for China: a mobile remittance system.

The Chinese market is primed for the deployment of a national, mobile-based remittance system with potential applications for both peer-to-peer and business-to-consumer usage models. We have designed this prototype, which we call M-Fu, to inclusively reach our target populations. (*Fu* means “to pay”, “to deliver”, or “to entrust” in Mandarin.)

M-Fu offers an easy way for anyone to send and receive money. A typical user might be a migrant worker in need of a secure method of sending money home so he or she can avoid carrying on their person. M-Fu works by leveraging existing networks of *laobans* and their workers. To build a user base, *laobans* act as agents and receive a small commission for every worker they sign up. The

money is transferred through a government-regulated network that alerts the recipient of new funds via SMS. The recipient can then collect the funds at M-Fu agent locations, based out of mom-and-pop stores in rural villages nationwide.

If all goes to plan, how many users can we expect? Let's say through extensive and effective marketing, half of all 250 million migrant workers in China become aware of M-Fu; one in four of those may actually try it. Based on the strength of the service experience, imagine half of those who try M-Fu become repeat users: That represents a potential core client base of over 15 million users, with an annual transaction value nearing USD 8 billion (RMB 51.7 billion).

Additional details of the design of the service are covered in this report. We have designed this service not as an ironclad recommendation, but to demonstrate possibilities and spark discussion.

conclusion

By understanding the lives of China's poor in the rapidly changing economy, and by designing services that align with the social networks and informal services on which people currently rely, we can help lift millions of previously neglected Chinese citizens into the stability they need to improve their economic situations, and help them seize the opportunities they need to thrive. In return, the visionary service providers who do so will have a head start in building long-term relationships with this vast market segment.