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M-PESA Mobile Money

A Case Study in Blue Ocean Strategy

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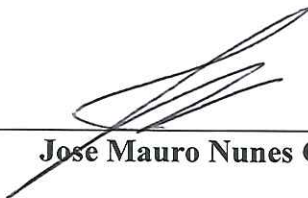
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Abstract

The recent and widespread availability of affordable mobile phone technology in developing countries has paved the way for the development of a number of mobile money and electronic remittance services. One of the most successful of these services is Safaricom's M-PESA program, launched in the East African nation of Kenya in March 2007. Since then, the program has successfully enrolled over 15.2 million users, transferred more than US\$1.4 trillion in electronic funds, and contributed significantly to poverty alleviation and financial inclusion efforts in Kenya. M-Pesa is a mobile phone based money transfer system in Kenya which grew at a blistering pace following its inception in 2007. This case study will analyze the critical factors that make M-PESA such a unique success in Kenya specifically.

Introduction

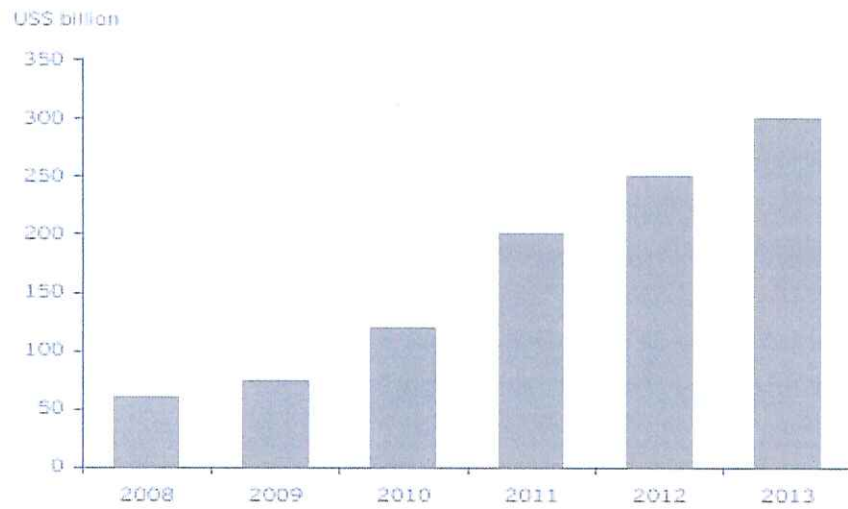
Background of the Case Study

A 2014 report by the World Bank (World Bank Global Financial Development Report 2014) measured financial inclusion around the world found that 1.3 billion adults in developing economies pay utility bills in cash and more than half a billion pay school fees in cash. Between 2011 and 2014, 700 million adults became account holders while the number of those without an account—the unbanked—dropped by 20 percent to 2 billion. What drove this increase in account ownership? A growth in account penetration of 13 percentage points in developing economies and innovations in technology—particularly mobile money, which is helping to rapidly expand access to financial services in Sub-Saharan Africa. M-PESA is the largest mobile-phone based electronic payments system in Sub-Saharan Africa & very specifically in Kenya. Surveys of users show it is a highly valued service, and Safaricom continues to expand the range of applications for which it can be used. This paper utilized case study methods to investigate how Safaricom, the mobile operator that owns M-PESA may have used Blue Ocean Strategy to innovate, reconstruct market boundaries and re-define the industry.

In early 2007, the leading mobile operator in Kenya, Safaricom (part of the Vodafone Group) launched one of the most successful implementations of a mobile money transfer service, M-PESA. The product is called M-PESA since “Pesa” is the Swahili word for money and the “M” is for mobile. The service has grown rapidly since launch, and is currently used by over 8 million subscribers. M-PESA, the mobile banking and payment system in Kenya represents the gold standard for innovative financial services. Tailor-made

for the Kenyan society, where many feel formal bank accounts are out of their reach while mobile phone technology has become pervasive, M-PESA creates an environment where even the most poverty stricken resident of a remote African village can become “financially included”. A product of collaboration between mobile phone giant, Vodafone, and local service provider, Safaricom, M-PESA has become ubiquitous to everyday life in the East African nation. All that is needed for participation is a basic mobile phone, technology that almost every household is now able to obtain. Using data preloaded on the SIM card, M-PESA utilizes a SMS based interface to transmit money virtually to other phones. To load money into one’s virtual account, a customer visits one of Safaricom thousands of agents and exchanges currency for e-money that is automatically deposited into their account. Customers can transfer money to anyone who owns a mobile phone. This generates a seismic shift in how money is managed and payments are made in Kenya. The operation is built around convenience, security, and low prices. M-PESA reveals the new opportunities and reduction in risk a competent mobile service can provide to those excluded from traditional financial products and services that the residents of developed nations take for granted. As such it represents a revolution in financial inclusion in emerging markets and a probable model for many other countries. (Mas and Amolo, 2010)

While the number of mobile money deployments has experienced explosive growth, the number of active mobile money users has not grown on the same trajectory in almost all countries. Kenya however has been able to see tremendous growth of the mobile money transaction and also the value of transactions has increased. Figure 1 below shows that mobile money transaction dollars increased from \$50 billion in 2008 to \$300 billion in 2013. The trend is expected to increase exponentially in the next few years.



Source: Juniper Research

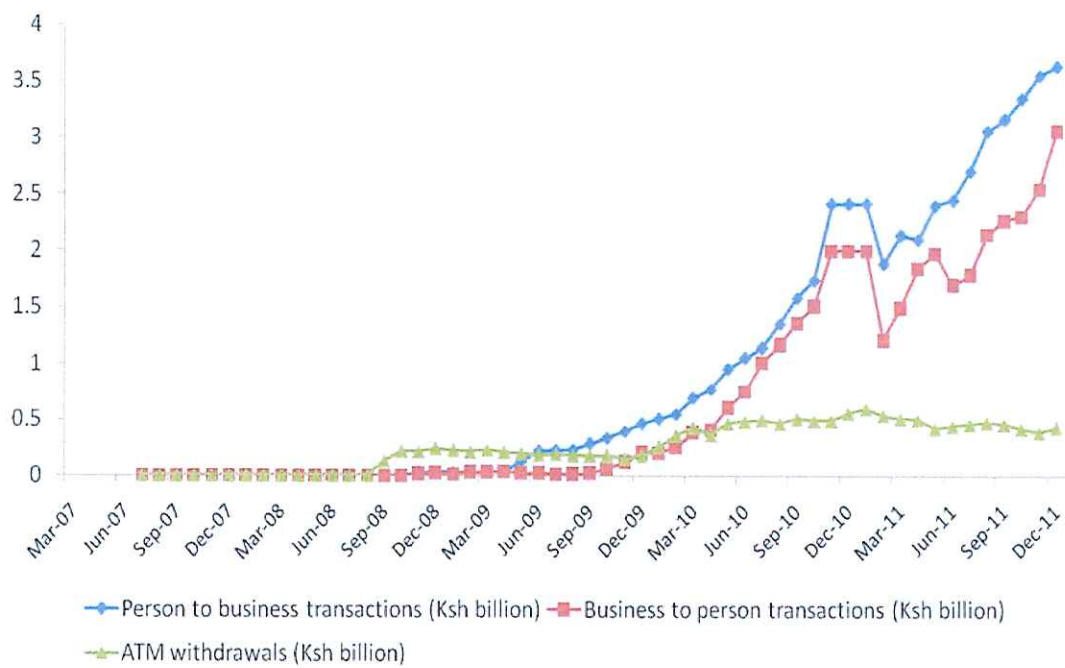


Figure 1 Mobile Money Growth in USD \$ & Volume of mobile Money Transactions

Despite the widespread knowledge that mobile money is the way humans will conduct financial transactions in the future there is little research done on what conditions are necessary for this innovation to be born and succeed like M-PESA.

Scope of the Study

The study targeted Safaricom limited, a company listed in the Nairobi Securities Exchange. The research and literature review entail analysis of the Blue Ocean Strategy book, journals and newspaper prints that reflected various strategies implemented with M-PESA mobile money. This paper utilized case study methods to investigate how Safaricom, the mobile operator that owns M-PESA may have used Blue Ocean Strategy to innovate, reconstruct market boundaries and re-define the industry.

Objective

The objective of this case study will be to analyze the critical factors that make M-PESA such a unique success in Kenya specifically.

Methodology

The M-PESA case study was grounded in the scientific blue ocean methodology which studied hundreds of companies and determined certain factors that contribute to their very unique success in their various markets. The markets also known as oceans are the result of specific sequence of actions that each company undertook in becoming successful. I examined the M-Pesa mobile money through the blue ocean strategy lens by taking a top to bottom approach. I identified the factors that made M-Pesa so

successful then compared them to the criteria set forth in the blue ocean strategy framework. The comparison resulted in my conclusions at the end of this paper.

Literature Review

The term Blue Ocean is derived from a book by W. Chan Kim and Renee Mauborgne that describes how companies traditionally work in “red ocean” conditions where businesses viciously fight against each other for a share of the marketplace. INSEAD Professors W. Chan Kim and Renée Mauborgne brought to the world Blue Ocean Strategy (Kim & Mauborgne, 2005) based on their over decade-long research on key strategic moves spanning more than a hundred years and thirty industries. It challenged the tenets of competitive strategy, the then dominant school of strategy, and called for a shift of focus from competition to creating new market space and hence making the competition irrelevant. Coming with proven analytical frameworks for creating and capturing blue oceans, the blue ocean strategic approach made a paradigm shift in the field of strategy.

The authors argue that in order to analyze businesses successfully you have to realize that the universe consists of two distinct kinds of space which can be grouped into two categories; red oceans and blue oceans. Red oceans represent all the industries in existence today in the known market space. In red oceans, industry boundaries are defined and accepted, and the competitive rules of the game are well understood. Here, companies try to outperform their rivals in order to grab a greater share of existing demand. As the space gets more and more crowded, prospects for profits and growth are reduced. Products turn into commodities, and increasing competition turns the water bloody. Blue oceans denote all the industries not in existence today—the unknown market space, untainted by competition. In

blue oceans, demand is created rather than fought over. There is ample opportunity for growth that is both profitable and rapid. (Harvard Business Review, 2011)

The authors of the Blue Ocean Strategy studied over 150 blue ocean creations in over 30 industries, using data stretching back more than 100 years. They analyzed companies that created those blue oceans and their less successful competitors, which were caught in red oceans. In studying the data, they have observed a consistent pattern of strategic thinking behind the creation of new markets and industries, called blue ocean strategy. The logic behind blue ocean strategy parts with traditional models focused on competing in existing market space. Indeed, it can be argued that managers' failure to realize the differences between red and blue ocean strategy lies behind the difficulties many companies encounter as they try to break from the competition. (Kim & Mauborgne, R, 2005)

The blue oceans stand for completely new and undiscovered markets and opportunities with new value creations, new customer bases and no competition. Demand is created, growth is profitable and rapid, competition is irrelevant, and rules of the game are not set. Blue Oceans signify potential of profitable growth, and infinite scale. Red oceans represent the traditional existing industries and known market space, where industry boundaries are defined and accepted, competitive rules of the game are known, outperform the rivals to grab a greater share of existing demand at a crowded market space. The prospects for profits and growth are limited. (Kim & Mauborgne, 2005)

Figure 2 below illustrates how effective and successful blue ocean strategy has been for business ventures. In a study of 108 companies the authors found that,

“most companies seem becalmed in their red oceans, 86% of new ventures were line extensions—incremental improvements to existing industry offerings—and a mere 14% were aimed at creating new markets or industries. While line extensions did account for 62% of the total revenues, they delivered only 39% of the total profits. By contrast, the 14% invested in creating new markets and industries delivered 38% of total revenues and a startling 61% of total profits.”
(Kim & Mauborgne, 2005)

FIGURE 1. The Profit and Growth Consequences of Creating Blue Oceans



(Source: Kim & Mauborgne, 2004)

Figure 2 Profit in Blue Oceans

Blue Ocean Strategy Framework

The blue ocean strategy framework consists of six core principles in order to be effective:

- a.) Create uncontested market space
- b.) Make the competition irrelevant
- c.) Create and capture new demand
- d.) Break the value/cost tradeoff
- e.) Align the whole system of a company's activities in pursuit of differentiation and low cost

Figure 3 below illustrates the main differences between companies that pursue red ocean strategy vs a blue ocean strategy company. Blue oceans focus on new opportunities, new market spaces and creating value.

Figure 3 Red Ocean Vs Blue Ocean

Red Ocean Strategy	VS	Blue Ocean Strategy
Compete in existing market space.		Create uncontested market space.
Beat the competition.		Make the competition irrelevant .
Exploit existing demand.		Create and capture new demand.
Make the value-cost trade-off.		Break the value-cost trade-off.
Align the whole system of a firm's activities with its strategic choice of differentiation or low cost .		Align the whole system of a firm's activities in pursuit of differentiation and low cost .

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Sequence of Blue Ocean Strategy

Companies need to build their blue ocean strategy in the sequence of buyer utility, price, cost, and adoption. This allows them to build a viable business model and ensure that a company profits from the blue ocean it is creating. W. Chan Kim and Renée Mauborgne argue that with an understanding of the right strategic sequence and of how to assess Blue Ocean ideas against the key criteria in that sequence, companies can dramatically reduce business model risk and ensure that both the company and its customers win as it creates new business terrain. The starting point is buyer utility. Does your offering unlock exceptional utility? Is there a compelling reason for the mass of people to buy it? Absent this, there is no blue ocean potential. The last step in the sequence is to address adoption hurdles. What are the adoption hurdles? Blue ocean strategy is complete only when you can address adoption hurdles in the beginning to ensure the successful actualization of your idea. (Kim, W & Mauborgne, 2005) Figure 4 below reflects the sequence of blue ocean strategy in determining the viability of a blue ocean idea.



Figure 4 Blue Ocean Sequence

Value Innovation

Value Innovation, is a cornerstone of blue ocean strategy. It is the simultaneous pursuit of differentiation and low cost, creating value for both buyers and the company. Because value to buyers comes from the offering utility minus its price, and because value to the company is generated from the offering's price minus its cost, value innovation is achieved only when the whole system of utility, price, and cost is aligned. (Kim & Mauborgne, 2005) Value innovation is the blue ocean strategy perfect balancing act between cost savings and creating buyer value as seen in Figure 5 below.

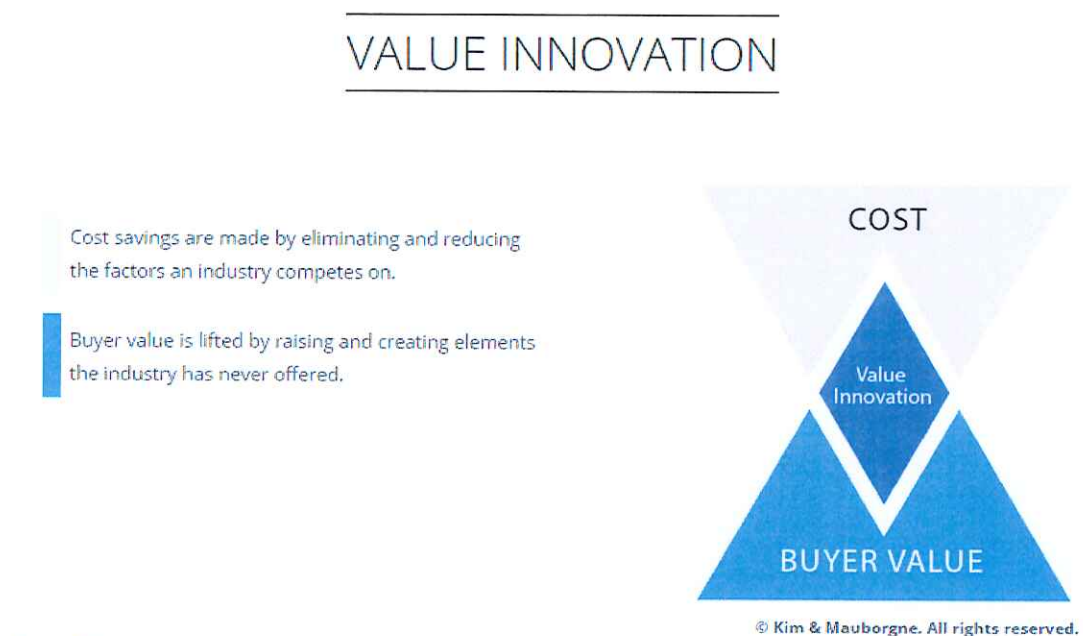


Figure 5 Blue Ocean Value Innovation

Analysis of Blue Ocean Strategy with M-Pesa

Creating M-PESA Blue Ocean

Safaricom, the parent company that owns M-Pesa created a blue ocean not competing in the red ocean with banks and telecommunications corporations but by creating uncontested mobile banking market space. The phenomenal success of M-PESA's mobile payments system is the quintessential example of blue ocean strategy. The ability to transfer small sums of money provides maximum utility to poor people in remote areas at a low cost which results in large profits for the company. Built on a mobile phone platform, M-PESA filled that niche, enabling customers to send money and store money through a simple interface. The service has been wildly successful. Launched in 2007, the number of subscribers surpassed 9 million in late 2009. Recent figures indicate that M-PESA handles \$320 million in person-to-person transfers a month, or roughly 10 percent of Kenya's GDP on an annualized basis. (World Bank, August 2010)

M-PESA Structure

There are three basic transactions that customers conduct with M-Pesa (Safaricom 2009). A customer may deposit money at an M-Pesa outlet in return for e-float (called a "cashin" transaction). The customer is required to show a valid identification document, and his identity and the amount of the deposit are logged in a book kept at the outlet. Upon receipt of the money, the M-Pesa agent enters the customer's telephone number and deposit information into his/her cell phone, and the customer waits at the outlet window until he/she receives a confirmation text message that e-float has been deposited. Unless the system is

running slowly (which happens occasionally), the whole transaction takes about a minute or less. A customer may exchange e-float for cash at an M-Pesa outlet (called a "cash out" transaction.) Again, the customer must show a valid identification document, and the transaction is logged. The customer informs the shop clerk how much cash he/she wants, then chooses "withdraw cash" on the M-Pesa menu on his phone, enters the amount to be withdrawn (plus the relevant fee), and enters the agent number (Safaricom, 2009). The agent then receives a text indicating that the transaction is complete, and the agent then gives the appropriate amount of cash to the customer. This whole transaction takes about one minute. Finally, a user may transfer e-float from his/her phone to another phone. This transfer can also be referred to as "person-to-person transfer," even though one or both of the parties may be an institution or firm. The user enters the phone number of the recipient and the amount to be transferred on his/her cellphone. The sender and recipient each receive a text message stating that money has been transferred (Safaricom, 2009).

These three basic transactions can be combined in a number of ways. For example, a user may deposit cash and send the full amount deposited to another user, who can then withdraw the full amount transferred. This is referred to as "deposit-transfer-withdraw." Alternatively, a user who receives a transfer from one person may transfer the e-float to some other user instead of withdrawing cash. E-float could circulate in this manner indefinitely, like conventional cash. A third usage possibility is where a user deposits cash and then later withdraws the money him/herself without having transferred it. Anecdotally, it is said that people do this for safety when they are traveling (Vaughan, 2007; Morawczynski, 2009).

All M-Pesa e-float is backed 100% by deposits held at three commercial banks in Kenya. Interest earned on these deposits is donated to a charity, which allows Safaricom to avoid being regulated as a bank. The pricing structure of M-Pesa is also very simple and intuitive.

Growth of M-Pesa

M-Pesa allows users to exchange cash for "e-float" on their phones, to send e-float to other cellular phone users, and to exchange e-float back into cash. The story of the growth of mobile telephones in Africa is one of a tectonic and unexpected change in communications technology. From virtually unconnected in the 1990's, over 60 percent of Africans now have mobile phone coverage, and there are now over ten times as many mobile phones as landline phones in use. The growth of M-Pesa is startling, within eight months of its inception in March 2007, over 1.1 million Kenyans had registered to use M-Pesa, and over US\$87 million had been transferred over the system (Safaricom, 2007). By September 2009, over 8.5 million Kenyans had registered to use the service and US\$3.7 billion (equivalent to 10 percent of Kenya's GDP) had been transferred over the system since inception (Safaricom, 2009). This explosive growth was also mirrored in the growth of M-Pesa agents (or service locations), which grew to over 18,000 locations by April 2010, from a base of approximately 450 in mid-2007 (Safaricom, 2009 and Vaughan, 2007). By contrast, Kenya has only 491 bank branches, 500 postbank branches, and 352 Automated Teller Machines (Mas and Ng'weno, 2009). While the mobile telephone is within sight of becoming a mature business, e-money services like M-Pesa are still in their early days and are continually evolving in response to competitive pressures and customer needs.

M-Pesa Transfers

M-Pesa is “mobile money” and it refers to the convergence of mobile telephony and financial services. Following Heyer and Mas (2010) “mobile money” includes three elements: an electronic stored value account linked to a user’s mobile phone; mobile phone software (or “application”) that allows users to manage their accounts, and a network of agents where users can exchange between cash and electronic value. The software can afford a variety of uses, such as the ability to check a bank account balance via text message, the means to pay with or send money from a digital account on a mobile phone, or the practice of receiving insurance or credit products over the mobile network. Assessing the diversity, Gencer (2011) separates mobile money into mobile payments, mobile finance, and mobile banking.

Safaricom’s service is capable of each of these functions. One of the reasons mobile money has attracted considerable attention is the expectation that it can provide affordable financial services to previously excluded populations, Ivatury (2006). A considerable amount of literature on financial inclusion emphasizes that “banking the unbanked” can lead to better decision-making, more efficient markets, and various other development goals (Collins et al. 2009). The M-PESA application connects to the Safaricom network and uses the SMS protocol to communicate with the central servers (that record transactions) and other phones (such as for a peer-to-peer value transfer). A user registers for M-PESA at any one of 20,000 licensed agents. The process is free and only requires the customer’s name, government ID number, and mobile phone number (Mas & Radcliffe 2010).

Impact of M-PESA

Prior to the introduction of M-pesa, individuals used a mixture of informal and formal channels to transfer money. Larger bus companies such as Akamba Bus Company or Scandinavia Bus Company offered formal money or parcel transfer services, where recipients would collect the funds at a designated bus terminal. However, smaller bus companies or independent mini-bus operators (*matatus*) would perform these transactions informally, and in some cases the bus driver would carry the funds with the promise to deliver them. In other cases, individuals would disguise money transfers as packages and place them on the bus for delivery to the designated terminal (Kabbucho *et al.*, 2003 and Morawczynski, 2009). The post office offered a variety of different money transfer products including instant money transfer which would be delivered to the post office closest to the recipient (Kabbucho *et al.*, 2003). Banks and money transfer companies such as Western Union or Moneygram also offered transfer services, although their outlet or branch networks were not as extensive as the post office's. Other formal methods such as sending money through banks or money transfer companies like Western Union were less common with less than 10 percent using these methods to send or receive funds.

The inception of M-Pesa in 2007 dramatically changed the money transfer market. In less than two years since its inception, M-Pesa was the leading money transfer method with over 50 percent sending money via M-Pesa and over 65 percent receiving funds through the system in 2009. The emergence of M-Pesa as the dominant money transfer mechanism virtually eliminated the use of post office products, bus companies, and formal channels such as Western Union and banks, where between 3.5 percent and 0.4 percent of individuals now use these methods to send or receive money. However, sending and receiving funds through

friends remains a popular means of money transfer, where 33 percent of individuals send money via a friend and 22 percent receive funds through a friend in 2009

Approximately 50 percent of Kenyans have used M-Pesa, with close to 38 percent formally registered with Safaricom. As discussed in Aker and Mbiti (2010), M-Pesa users are more likely to be younger, wealthier, better educated, banked, employed in non-farm sectors, to own cell phones, and to reside in urban areas. Higher and lower socio-economic status individuals use M-Pesa to purchase airtime, save and store money while travelling, send money to relatives and friends and use M-Pesa to pay wages than their respective employees.

M-Pesa Value Innovation

In order to maximize value innovation in blue ocean strategy, costs must come down while buyer value is increasing. M-PESA pricing is made transparent and predictable for users. There are no customer charges for the SMSs that deliver the service, and instead fees are applied to the actual customer-initiated transactions. All customer fees are subtracted from the customer's account, and outlets cannot charge any direct fees. Thus, outlets collect their commissions from Safaricom (through their master agents) rather than from customers. This reduces the potential for agent abuses. Customer fees are uniform nationwide, and they are prominently posted in all outlet locations creating trust between the user and the product offering. In order to increase buyer value M-PESA chose to specify its fees in fixed currency terms rather than as a percentage of the transaction. This makes it easier for customers to understand the precise cost of each transaction and helps them think of the fee in terms of the transaction's absolute value. It also helps them compare the transaction cost against alternative and usually costlier money-transfer arrangements. Since the per transaction cost is

low for both the user and Safaricom compared to the industry while also increasing the trust in buyer value, M-Pesa creates a blue ocean.

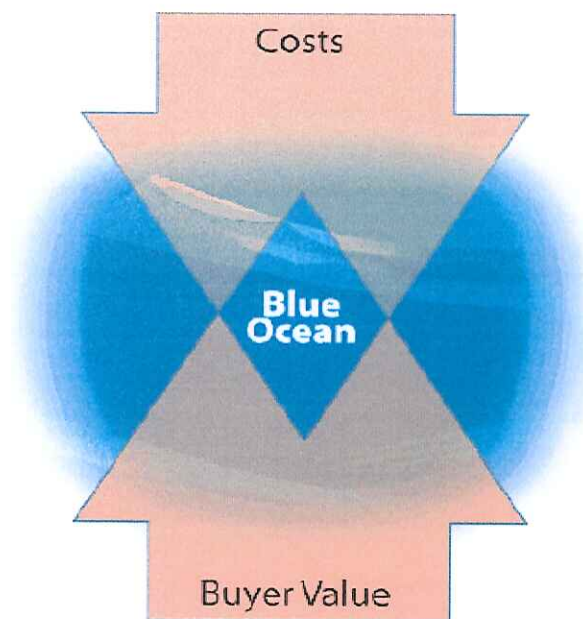


Figure 6 Blue Ocean Costs & Buyer Value

Increasing Buyer Value – M-Pesa

In order to increase buyer value & customer satisfaction, Safaricom understood that the primary role of the mobile phone is to enable the creation of a retail outlet-based channel for cash-to-digital value conversion. And, for this cash-to-digital conversion to be broadly available to the bulk of the population, it had to develop a channel structure that could support thousands of M-PESA stores spread across a broad geography. To achieve this, Safaricom built four elements into its channel management blue ocean execution strategy:

- (i) engaging intermediaries to help manage the individual stores, thereby reducing the number of direct contacts it had to deal with;
- (ii) ensuring that outlets were sufficiently incentivized to actively promote the service;
- (iii) Maintaining tight control over the customer experience;
- (iv) Developing several different methods for stores to re-balance their stocks of cash and e-value.

The M-Pesa network of stores was able to match up the buyers primary need with Safaricom core services and in doing so was able to gain and keep new clients that the rest of the industry deemed to be unreachable in the banking and mobile sectors. The M-Pesa network of stores could be considered blue oceans that increase the buyers' value perception dramatically while keeping costs low.

Conclusion & Recommendations

As the developed world begins to rebuild the recently collapsed global financial system, the financial architecture in parts of the developing world is being rapidly transformed. As the costs of mobile phone technology have fallen, and as the technology has been adapted to support financial services, mobile banking innovations have begun to spread across and within poor countries. The low cost, and the widespread unmet demand for financial services, as captured by low rates of bank access, means that mobile banking has the potential to reach remote corners of the socio-economic, as well as geographic spectrum. Potential appears to be realized in Kenya through M-PESA, a mobile banking system operated by Safaricom Limited. It is estimated that M-PESA reached nearly 40 percent of the adult population after a little more than 2 years of operation. Part of this success is due to a rapidly expanding network of M-PESA agents, who now number over 15,000.

M-PESA is an innovation that clearly dominates its money-transfer predecessors on virtually all dimensions. Users say it is faster, cheaper, more reliable, and safer, and a very large majority report that they would suffer significant negative consequences if it were to be shut down. These expressed preferences suggest that M-PESA is valued more by individuals than it costs.

The Blue Ocean Strategy factors and sequence were parallel to the actions that have made M-pesa such as success since

- a.) M-pesa created uncontested market space
- b.) M-pesa made the competition irrelevant
- c.) New demand is constantly being created & captured and finally

d.) The whole system of Safaricom activities aligns with M-pesa mobile money.

Whether viewed through main indicators or detailed strategy maps, Safaricom M-Pesa product is a very good example of a blue ocean strategy implementation. The product is a clear opposite of any red ocean market spaces occupied by the competition in the industry, it created and captured new demand and resulted in cost savings while increasing buyer value.

The challenge going forward is to remember that most blue ocean's turn into red oceans after many years of unprecedented growth. M-Pesa needs to continually innovate in order to stay ahead of any new blue oceans that may result from various challenges they are facing as the product grows. The current challenges include

- a.) Regulatory treatment of money transfer may change
- b.) Clients are not able to create savings since they can only transfer their cash
- c.) Trust in M-PESA may erode since deposits are not supervised by the Central bank.

The opportunities for more blue oceans abound for M-Pesa as a product since the World Bank estimates over 2 billion people lack basic financial inclusion. If a product like M-Pesa was available to all of them it would indeed be the largest blue ocean.

Glossary

ATM – Automatic Teller Machine

M-PESA – Swahili word for Mobile Money

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