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FSD News

EDITORIAL

Once they are put into effect, recent changes inserted by MPs into the much delayed Finance Bill will have a profound positive impact on the provision of credit in Kenya. In response to a recent spike in lending rates, the MPs mandated, through changes to the CBK Act, that Banks must share both positive and negative information with each other. They also cleared the way for deposit taking microfinance institutions (DTMs) to join the bank database currently housed in two bureaus.

Until now Kenya had a negative only bank database. Effectively this meant it captured only the 5% of the borrowers who defaulted on their obligations. If your name was correctly listed then it would be unlikely that you would be granted further credit until you cleared the debt for which you had been listed. Soon all those who pay their debts on time and in full will also have the benefit of a listing showing they are good borrowers.

By capturing millions more records, banks will quickly be able to differentiate between good, average and poor borrowers. Bureaus will also use analytics to create predictions of default that will be captured in a score. After a while, those who have a good bureau score will receive more favourable treatment on any future borrowing requirements. Many will receive lower collateral requirements, lower interest rates and other better repayment terms.

Despite the particular mandate, DTMs will find it hard to remain outside positive information sharing for long because of the value of the information which they will not be able to use. Institutions only get to use positive information submitted by others if they submit positive from their own databases.

And there is more good news on the way. There is currently a bill in parliament to allow SACCOs and utilities to share information. These are all great developments and stakeholders need to be congratulated. The ultimate objective is to have all credit providers providing and using both positive and negative information. The urge will be so great to join that it may not be necessary to wait for a legislative or regulatory mandate.

James Kashangaki
Head, Inclusive Growth theme, FSD Kenya

NEWS AND VIEWS

Julie Zollmann from Bankable Frontier Associates (BFA) responds during the Q&A session at FSD's 9th Research Colloquium on 6th July, 2012 in Nairobi.

FSD's 9th research colloquium examines Kenya's path to a cash-lite economy

Building from the premise that cash has certain disadvantages - transaction costs, vulnerability to loss or theft, and geographic restrictions, FSD's 9th research colloquium featured a presentation by Julie Zollmann from Bankable Frontier Associates (BFA) which explored the potential opportunities and obstacles associated with reducing the use of cash in the Kenyan economy.

Julie's presentation was based on the results of an FSD sponsored scoping study that sought to understand cash flows in Kenya and identify the costs and benefits of a shift towards a cash-lite economy, particularly in terms of the impact on the poorest and most vulnerable segments of society. The study identified two main pathways to reducing the costs of cash: i) increasing the local circulation of cash; and ii) increasing the prevalence of e-payments.

Julie concluded her presentation by encouraging FSD and other public entities to conduct research that will help identify existing demand for e-payments and improve the attractiveness of e-payments where the business case for consumers and providers is weak. The research colloquium ended with insightful comments and questions from colloquium participants. Our in-depth article provides more details on the subject.

Health and Life micro-insurance project

Micro-insurance has attracted considerable interest in the local and international market as a risk mitigation tool for low income households. Determining which risks to prioritise for significant impact on livelihoods is a concern for the Government of Kenya, International Labour Organisation (ILO) and FSD Kenya. This is because severe illness, injury, death of a family member, man-made or natural disasters constrain the low income client's cash flow, liquidity and earning abilities. The Kenya micro-insurance landscape survey (2010) identified health and life insurance as anchor risks upon which micro-insurance can be further developed.

With the exception of compulsory micro-credit insurance, all other micro-insurance schemes in Kenya appear to be running on a pilot basis, with little evidence of scalability so far. The micro-insurance landscape survey (2010) further identified that policy and regulatory barriers, a poor reputation of the industry, supply and demand challenges need to be addressed to foster growth. Regulatory reforms have begun and there is concerted effort from the industry to regain consumer trust and confidence.

FSD in partnership with the Insurance Regulatory Authority (IRA) and ILO have embarked on a project that aims to explore the market potential for health and life micro-insurance products to reduce vulnerability among low-income households in Kenya. A project-briefing workshop for the industry was held in mid May, 2012 in Nairobi. The project is expected to assess the demand and supply of life and health micro-insurance; the policy, legal and regulatory framework for the two risks and give an in-depth analysis of the market for possible further engagement to develop the sector.

Centre for Branchless Banking

FSD's Centre for Branchless Banking (CBB) is playing an active role in pushing the national cash-lite agenda. As captured in Vision 2030, Kenya is moving towards a cash-lite economy through opportunities presented by mobile money. The CBB is involved in some of the most innovative developments in the market while supporting a wide range of partners including banks, telecommunication companies and investors. It aims to inform the market through knowledge generation and research in line with FSD's mission. The Centre is developing knowledge and expertise through action research around specific products, and commissioning large-scale studies to better understand the lessons learnt from five years of mobile payment systems in Kenya. In doing so it is also therefore well placed to play a role as an independent information hub on the Kenyan mobile money market, supporting researchers, policy makers and market players.

FSD Kenya
Financial Sector Deepening

SCOPING KENYA'S PATH TO A CASH-LITE ECONOMY

Research suggests that a shift from cash to electronic payments can save countries 1-2% of their GDP annually. Cash is an expensive and vulnerable payment technology that is a drag on economies and a barrier to financial inclusion. It's difficult to sustainably provide low income consumers a range of useful financial services given the high costs of managing in person, physical cash transactions.

Findings were recently presented from research commissioned by FSD to scope the current status of cash usage and circulation in a small Kenyan community. This was in order to build a research agenda for the promotion of an inclusive cash-lite society.

There are two main ways to move towards a "cash-lite" society, where the costs of moving and transacting in large volumes of cash can be reduced:

1. By increasing the recirculation of cash, such that cash is used in confined geographies and converted to electronic value when coming or going. This could be called, building "bridges to cash" via ubiquitous cash in locations.
2. Through useful, widely accepted electronic payments that substitute for cash in a wide range of transaction types.

The research looked closely at consumers, merchants, service providers, and financial instructions operating in a small (population 8,000) market town, a linked rural cattle market, and a large county hub, the nearest town with a range of bank branches.

The research showed that there is some progress on increasing recirculation of cash through itinerant market traders who deposit their earnings at M-PESA and bank agents at the end of the day and travel with only electronic value. But, these bridges to cash cannot work alone. In the research site, each of 13 M-PESA agents were bringing about KShs 440,000 in cash each week to their outlets from the county hub in order to accommodate withdrawals. Still, cash-out facilities cannot accommodate the scale of withdrawals for the large cash transactions, such as external traders buying cereals and mangos from local producers. M-PESA and bank agents allow customers to withdraw up to KShs 70,000-75,000, but a trader might make KShs 400,000 in cash payments to farmers in a single day.

Electronic payments are a necessary complement to cash recirculation. But, when examining transaction profiles of consumers, merchants, and service providers, the research team found that electronic payments were being used for only very specific types of transactions. Person to person transfers, for example, were indeed shifting to the M-PESA platform, and salaried workers were now largely receiving their incomes through electronic bank transfers.

However, most merchant and service provider transactions were still dominated overwhelmingly by cash. And, the purchase of stock from distant distributors and wholesalers was moving towards another costly payment device, cheques, rather than electronic payments.

The research indicated that cost, convenience, and reliability of electronic payments were important barriers to more prevalent usage, but so was trust. In large, infrequent transactions for the purchase of agricultural goods and livestock, for example, sellers expressed fear of being defrauded through an M-PESA payment promised by unknown and untrusted buyers.

Kenya is still some ways from an integrated electronic payments space that brings the benefits of ubiquitous electronic transactions all the way to the very poor. However, there are opportunities to work towards that vision by promoting de facto integration of existing payments devices and promoting greater use of electronic payments where demand is already ripe, for example in payments to casual laborers and farmers, between merchants and suppliers, and through government procurement. Given very small transaction sizes, retail transactions may be the 'last mile' payment type to tackle, but the first movement could come from agro-vets and supermarkets that experience high numbers of large transactions every day.

The presentation concluded by suggesting research activities that could be undertaken to remove more of the uncertainty around consumer response to electronic payments and pave the way for provider-led innovation in this space. Such studies would take a closer look at price elasticity of demand for electronic payments, model the speed of consumer behaviour change in response to product changes, and to take a closer look at how and when consumer behaviour begins to change across payment domains, for example from person to person electronic payments to person to merchant or service provider domains. For the full presentation and report, visit: *http://www.fsdkenya.org/news/9th_FSD_colloquium.php*

Julie Zollmann
Bankable Frontier Associates (BFA)

EVENTS CALENDAR

27 - 31 August	**Increasing agricultural input and output trade through innovative market information systems in Africa,** Nairobi - Kenya. For more information, email: *training@ifdc.org* Website: *www.ifdc.org*
13 - 14 September	**Kenya Bankers Association (KBA) Annual Research Conference,** Nairobi - Kenya. For more information, email: *info@kba.co.ke* Website: *www.kba.co.ke*