

EDITORIAL

Last month saw the first international fibre optic going live, finally providing eastern Africa with a high speed internet link to the rest of the world. This has created a new buzz around information and communication technology (ICT) in Kenya and so I'm again focusing on technology. Arguably it isn't so much the international link which will directly impact on financial inclusion but the 'pull' effect on improving domestic communications across the country. A widening network of domestic fibre optic is now providing the backhaul (the 'main roads' for data), while wireless technologies are offering the 'final mile' (or 'feeder roads') covering an increasing proportion of the population.

As the results of the FinAccess 2009 survey show (discussed in more detail on the next page), the promise of technology to transform the financial landscape is already being met. In just two years the mobile phone based M-PESA system has grown to become a major player in the small value retail payments market. Other mobile operators have launched or plan to launch rival systems. Currently focussed on providing domestic money transfers, these new systems have the potential to impact across the whole retail financial system.

The Budget saw the government introduce legislation in the Finance Bill to permit banks to use agents. As the experience from Brazil has shown, this can dramatically change the way in which banking services are delivered. Using low cost wireless point-of-sale (POS) devices, thousands of shops and other outlets across the country could become points of presence for banks. This potentially offers a much lower cost and more accessible channel to the market.

At this stage it still isn't clear where these developments will finally take us. The 'high road' would see transaction costs reducing by an order of magnitude, enabling millions to access better and safer financial services. Equally though it is possible to at least conceive of a 'low road' in which the potential is lost as a result of a lack of interoperability between rival systems, failure of effective competition or an inappropriate regulatory framework.

David Ferrand
Director

NEWS AND VIEWS



A typical M-PESA cellphone interface. Sending money to provide monthly regular support to family members is currently the most popular use of M-PESA in Kenya.

Mobile banking

FSD Kenya has recently completed research on the use of M-PESA in Kenya on behalf of the Central Bank of Kenya. At the end of 2008 Safaricom offered service through 6,104 M-PESA agents, a figure which compares well with the 876 bank branches and 1,424 ATMs country wide. The survey suggests that customers are using M-PESA as a complement to their existing financial services. FinAccess data shows a tendency to use a mix of products and services from formal and informal providers to meet financial service needs. The most popular reason for sending money was to provide regular support to the recipient, usually monthly. Almost half of these transfers were sent to parents living away from the sender's household, the next most significant were other relatives living away from the home. The majority of remittances were sent to family members. When users of M-PESA were asked to compare the service with their previous national money transfer service over 95% of users found that M-PESA was faster, more convenient, safer and cheaper. Given this competitive position the strong growth in M-PESA user numbers becomes much easier to understand.

Towards an effective collateral process

The Central Bank of Kenya (CBK) and the Kenya Bankers Association (KBA) with GrowthFin support recently commissioned a comprehensive study of the collateral

process in Kenya. Its aim was to determine if constraints to the effective working of the process imposed costs that put borrowing out of the reach of many small and medium sized businesses. The study scheduled to be launched in August reveals that Kenyan borrowers presenting collateral face pre-disbursement costs of 5.7% of the loan amount and up to 90 days from application to disbursement.

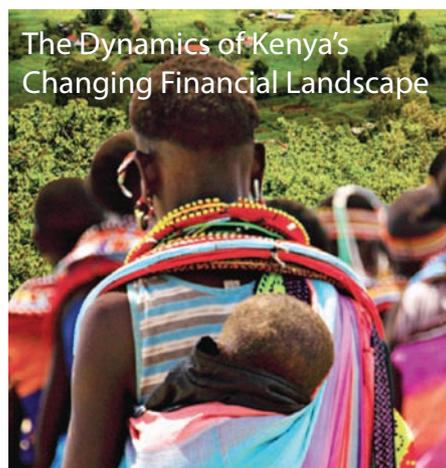
The cost to financial institutions in enforcing collateral is equally onerous and can take as long as 5 years before recovery. The report identifies a weak and dispersed legal framework as a major constraint with over 20 different laws and regulations that relate to the collateral process. Among other key constraints are convoluted processes of conveyance, poor enforcement mechanisms, ineffective and dispersed system of registries and weak property rights.

Without reform of the process, Kenya will lag behind in the development appropriate finance for SMEs that make use of alternative or non-traditional forms of collateral including invoices, warehouse receipts, leased assets etc. A number of recommendations are made in the study. The CBK and KBA will be at the forefront of tackling the necessary reforms with the aim of creating a more efficient and effective collateral process.

Group savings and loans associations (GSLs)

Group savings and loans associations (GSLs) are a simple financial intermediation model where members of a group (usually between 10 and 20) contribute equal amounts of savings or their multiples during meetings which are held weekly, fortnightly or monthly. The savings are then loaned out to members of the group at an agreed interest rate, building up the group's funds. The members' passbooks are the core form of documentation although in some GSLs a simple ledger showing each meeting's transactions is also kept. At the end of every 12 or 18 month period, an action audit is done and the savings together with interest from loans are distributed to the members in proportion to their savings. The GSL is then dissolved but reforms immediately. Research has shown that due to the simple nature of model, GSLs continued functioning well and independently following initial support in form of training. CARE Kenya with FSD's support has designed and is currently implementing a GSL development project which is testing cost-effective ways of delivering training to GSLs. Results from the project will be shared with other GSL implementing organisations semi-annually in forums to be organised by CARE.

FINACCESS 2009



The results of the second national survey on access to finance in Kenya, FinAccess 2009, were launched in June by Professor Njuguna Ndung'u, the Governor of the Central Bank. These show that Kenya has made considerable progress in improving access over the two and a half years since the last study which was undertaken in 2006.

What is FinAccess?

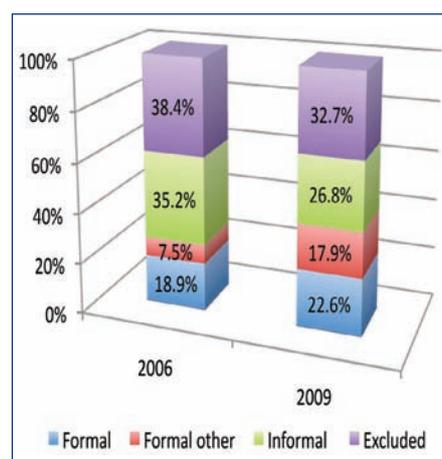
FinAccess is a public-private sector initiative, jointly managed by the Central Bank of Kenya (CBK) and FSD Kenya. Financial sector institutions, government ministries, development agencies and research institutes came together to drive the process in the Financial Access Partnership (FAP). The survey was undertaken by the research company, Synovate (formerly Steadmans), in February and March of this year with technical support from the Kenya National Bureau of Statistics and FinScope, a specialist international agency. Funding was provided by FSD Kenya, CBK, Commercial Bank of Africa, Equity Bank and Ministry of Finance.

Based on a large-scale national survey, FinAccess provides detailed information on the use of financial services in Kenya. People across the whole country, from all walks of life, were asked detailed questions about which services they use and why. Results from the first study (FinAccess 2006) showed that this information is invaluable to both policymakers and financial institutions. The data has been used to inform key policy such as the Vision 2030 and helped guide banks, micro-finance institutions and others in developing new products and services.

Key findings

The overall findings on access to finance in the study are summarised in the chart. It shows some very encouraging developments. The level of financial exclusion - that is people without access to any form of financial services -

has fallen from 38.4% to 32.7% of the population. The usage of banking services has increased markedly, from 18.9% to 22.6%. However the dramatic change came in access to 'formal other' institutions - increasing from 7.5% to 17.9%. Combined the results mean that the total proportion of people 'formally included' (that is able to access a service from formal sources; banks, SACCOs, MFIs and money transfer operators such as M-PESA) has increased significantly over the last two and a half years, from 26.4% to 40.5%.



Much of this dramatic change can be attributed to M-PESA which has changed the landscape of domestic remittances in Kenya. In the 2006 survey just 16.5% of respondents received money transfers but by 2009 this figure had grown over three times to 51.8%. In 2006 the most popular means of transfer was using friends and family members but, after its launch, M-PESA has now become the most popular means of money transfer, now used by 39.9% of all adults.

While money transfer is clearly an important and much needed service, it is only one part of the financial service picture. Access to savings, credit and insurance are key elements of a complete service offer. It is encouraging to note the strong expansion into previously un-served

markets by a number of banks, led by Equity Bank, over the last two and a half years. This increase, while lower than the dramatic expansion in the money transfer area, does represent a very substantial gain in a relatively short period and one which results in access to a much broader range of services.

The results show the proportion of those who are classified as 'informally included' has reduced significantly - from 35.2% to 26.8%, reflecting the growing numbers who are now counted as 'formally included'. Interestingly however this hasn't translated into a decline in the overall usage of informal services - rotating savings and credit associations, welfare and clan groups etc. The overall level of usage of these mechanisms remained virtually unchanged with just over 50% of Kenyans using them. So while there is a trend towards greater use of formal services, many people continue to make use of informal mechanisms.

The way ahead

Professor Ndung'u observed at the FinAccess launch that: "over the last five years Kenya's financial landscape has considerably changed. The financial system is now offering a wide range of financial services to more Kenyans and to a wider geographical coverage than ever before. FinAccess 2009 marks a major contribution towards improving our understanding of the dynamics of the changing financial landscape in Kenya."

This understanding is important to both financial institutions in identifying new opportunities and the government in developing the policy and regulation needed to support a rapidly developing market. In the short term we'll need deeper analysis of the new data to understand the full implications, while in the longer term the survey will need to be developed and periodically repeated. A summary of the 2009 survey results is already available in an initial report on www.fsdkenya.org/finaccess/index.html or on request from FSD or CBK. More in depth analysis is well underway and will also be made available shortly.

EVENTS CALENDAR

- 8th – 9th Sep** **Promoting Financial Capability and Consumer Protection – A step towards Financial Inclusion in Africa**, Making Finance Work for Africa (MFW4A) and GTZ Ghana, Accra – Ghana (Email: Karen.Losse@gtz.de)
- 7th – 18th Sep** **School of Applied Microfinance courses**, Mombasa – Kenya (www.samtraining.org)
- 14th – 16th Sep** **Alliance for Financial Inclusion Global Policy Forum**, Nairobi – Kenya (Email: nancy.widjaja@afi-global.org)
- 21st – 22nd Oct** **AMT 2009 Microfinance Investor's Fair**, Nairobi – Kenya. Contact Emma-Jayne Paul, AMT Coordinator (Email: info@amt-forum.org, Web: www.amt-forum.org)

FSD Kenya is an independent Trust established to support the development of inclusive financial markets in Kenya

4th Floor Kenya Re Towers, Off Ragati Road, Upper Hill | P.O. Box 11353, 00100 Nairobi, Kenya

T +254 (20) 2718809, 2718814 | +254 (724) 319706, (735) 319706 E info@fsdkenya.org W www.fsdkenya.org