

FSD News



EDITORIAL

There is little doubt now that mainstream banking in Kenya has the mass retail market firmly in its sights. Equity Bank, whose recent rapid growth has been founded on providing good basic banking products at an affordable price, was awarded the Kenyan Bank of the Year in this year's Banking Awards. In his keynote speech at the awards ceremony, Maina Mwangi of Renaissance Capital, noted that while ten years ago the major banking institutions were shrinking their branch networks, today we see the leading banks rediscovering the retail customer. We will need to wait for the results from the national FinAccess survey later this year to see the impact on overall levels of financial inclusion but in the last two years we've seen the number of bank accounts in Kenya increase by over 65%.

Good news indeed but there is still a long way to go if a majority of Kenyans are to access appropriate and safe financial services. Reaching even the average income Kenyan raises the question of affordability. To put some numbers on this we probably need to see the average cost of a transaction drop from a current minimum of around KShs 20 to below KShs 10 if we want to see a majority of Kenyans banked. New technologies offer considerable promise for reducing costs. ATMs are now ubiquitous and the numbers in use grow by the month, mobile phones are being used as a channel to allow customers to access services and branchless banking using retail agents is set to provide services deep into rural areas where branches would not be viable. A growing concern for FSD however is whether Kenya is set to reap the full potential of all these new approaches. There are considerable scale economies available if the new systems are shared by players across the financial system rather than used as a basis for competitive differentiation. The key issue here is inter-operability. Technologically the barriers can be overcome. The challenge is finding commercially viable routes to sharing this new infrastructure.

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NEWS AND VIEWS

Creation of the Financial Education partnership

Following earlier workshops on financial education a further stakeholder meeting was held in July. Three objectives for financial education were agreed: (i) Foster informed use of financial services (ii) Improve financial management, and (iii) Consumer protection.

It was decided that a public private partnership the Financial Education Partnership (FEP) would be formed to establish the foundations for a comprehensive programme of financial education in Kenya. Membership is open to all and there are currently seven private sector organisations and six public (or public-private) organisations involved. A smaller taskforce was established. If you are interested in joining the FEP or you would like to receive a copy of the report 'Financial Education in Kenya' please contact caroline@fsdkenya.org.

International trade finance

Export oriented small and medium enterprises (SMEs) are anticipated to play an increasingly important role in Kenya's future growth. The Government's Private Sector Development Strategy (PSDS) Implementation Plan has identified access to appropriate trade finance as a potential constraint to realising this growth. In response FSD's GrowthFin programme commissioned a study by specialists to assess the position and make recommendations for actions to strengthen the supply of trade finance to SMEs. Findings from the study were discussed with industry stakeholder at a workshop in July. Many positive features of the market in Kenya were noted with a strong level of interest evinced by banks in both the SME segment and trade finance. Some conservatism was also observed, with some banks reluctant to recognise the intrinsic self-liquidating characteristics of trade finance, often seeking additional collateral which can restrict access. A wide range of recommendations were put forward for consideration by various stakeholders. The report will be available shortly.

Credit bureau regulations gazetted

The regulations for the licensing of credit bureaus by the Central Bank of Kenya were gazetted in May. This represents a critical development in the enabling environment for financial services in Kenya. Once bureaus have been licensed, commercial banks in Kenya will be

required to share information on loan defaulters. This will create a significant disincentive to default reducing loan screening costs and the burden of write-offs on the sector.

Credit scoring for SME lending

Credit scoring is widely used in many countries, such as the United States, to help assess SME credit risk more cost effectively. As yet few institutions in Kenya have made use of the approach and it has been identified in the PSDS as a possible way to improve access to finance for SMEs. FSD's GrowthFin programme recently commissioned a specialist team to explore the potential use of credit scoring in SME finance in Kenya. The team found strong interest and discussed its conclusions with stakeholders at a workshop in July. While some of the large international banks are able to develop their own custom scorecards, few other lenders have the necessary volumes of SME lending or institutional resources to take this route. Credit bureaus offer the potential to overcome this constraint by offering generic credit-risk scores, providing a potentially cost-effective tool for all lenders. Extending the sharing of 'positive' credit reference information clearly presents a challenge but one which is worth tackling given the potential benefits. The full report from the study will be published shortly.

HIV AIDS study

The extent of the impact of HIV-AIDS in Kenya is now widely appreciated. It is no longer regarded as only a health issue but one which cuts across society and the economy. Less clear however is how the financial sector can practically contribute here. FSD Kenya undertook a study to assess the prospects for developing financial services in Kenya which can contribute to the prevention of HIV transmission or mitigate the economic impact of HIV/AIDS. Following extensive individual consultations with stakeholders, a workshop was held in Nairobi during July to discuss the findings. While there were a number of focussed financial sector programmes tackling the issues in Kenya, few of these have been able to reach real scale. A number of ideas for programmes with prospects for impact and scale-up were discussed including insurance, workplace support, linkages with social protection programmes and agricultural value chain finance. We expect to publish the study report during this quarter.

POST-ELECTION CRISIS: SUPPORT TO THE FINANCIAL SECTOR

The crisis arising from the general election held in Kenya at the end of 2007 has had a disastrous impact on the livelihoods of large numbers of Kenyans. Inevitably many, if not most, of these were among the more vulnerable and poorest in society. While recent growth data shows that the economy as a whole was impacted significantly it is clear that the informal sector in areas affected by the violence have been especially badly hit. Reports from affected areas indicated that in some cases whole markets have been destroyed. Even when the violence subsided, economic activity was subdued as a result of the persistent threat of its return. Ethnic tensions remain, notably in Rift Valley and Western provinces.

Impact on the financial sector

The impact on commercial banking which provides the core of Kenya's financial system has so far been relatively limited. It has however been much greater on micro-finance institutions (MFIs) and savings and credit co-operative societies (SACCOs) operating in the affected areas. Many of their members suffered. Tragically in some cases this involved the loss of life. Others were internally displaced, fleeing the violence and reliant on either relatives or makeshift camps for survival. A significant number have yet to be resettled, remaining in camps. Many people's livelihoods were affected with the destruction of houses, business premises and assets, stock and loss of business. This inevitably gave rise to loan repayment problems and a deterioration in the quality of affected portfolios.

The Association of Microfinance Institutions (AMFI) took a lead in co-ordinating an industry response to the crisis, taking a strongly demand driven approach. AMFI is well placed to co-ordinate much of the activity on behalf of the industry. Co-ordination among donors was vital to ensure that appropriate resources were brought to bear, the transaction costs for the industry minimised and that approaches did not contradict one another. The first step taken by AMFI was to commission a rapid situational analysis from MicroSave Consulting Ltd to understand the position in more depth. Responding to this analysis and subsequent consultation with industry stakeholders, an AMFI led programme was developed. There are four elements to the programme supported by FSD Kenya:

(i) Peace building

Consultations with the industry indicated that promoting peace and reconciliation in communities was among the

most urgent requirements. Re-building trust within groups across ethnic divisions is vital to future operational effectiveness. Work is now well advanced in developing an industry-wide programme for the promotion of peace and reconciliation through MFIs. A workshop was held by AMFI bringing together its members and specialists on peace and reconciliation work in Kenya. Following this a comprehensive participatory study was undertaken. This sought to identify the causes of post-election violence and its socio-economic impacts on MFIs as a basis for identifying the opportunities for peace-building by MFIs, the requirements and recommendations for the way forward. The study found a clear opportunity for the industry to contribute to the reconciliation and reconstruction efforts in Kenya. In order to assume this role MFIs will need skills in Conflict Prevention, Management and Resolution (CPMR). It will also require the development of internal structures within institutions to support this work. The next step, already underway, is to design and pilot an appropriate MFI training programme.

(ii) Liquidity support

The initial analysis pointed to the need for liquidity support among a number of the smaller institutions with significant portfolio concentration within the most affected areas. It was clear that the largest nationwide MFIs and low-income market oriented banks were able to handle the financial impact within existing resources and established financial relationships. Given the availability of considerable liquidity in the Kenyan financial system the emphasis has been not to seek new sources of funding but finding ways to direct the available liquidity to the institutions needing it. While there are already a number of wholesale institutions addressing the MFI and SACCO market in Kenya, lending to institutions who were worst affected entails accepting a greater degree of risk than would normally be faced. Two existing wholesale providers, Equity Bank and Oikocredit, working in partnership with AMFI, US Agency for International Development and FSD Kenya, will be expanding their

lending to MFIs and SACCOs. The facility put in place will enable Equity and Oiko to finance institutions whose risk profile has worsened as a result of the post-election chaos.

(iii) Re-capitalisation

For institutions most severely affected the capital base will have been eroded as a result of higher than usual loan loss provisions. In some instances future viability could be undermined without a fresh capital injection. One specialist wholesale finance institution already addressing the sector, Jitegemee Trust Limited (JTL), is now providing equity or quasi-equity finance for MFIs and SACCOs. As part of the post-election crisis programme FSD Kenya is providing JTL with additional financial resources to allow it to expand the availability of equity/quasi-equity financing to MFIs and SACCOs. This allows strong institutions which have suffered capital depletion to obtain the new capital they require from a strong local partner.

(iv) Technical assistance

Finally technical assistance is being offered by AMFI under the programme to help institutions adjust to the shock experienced. There was an immediate need to provide support to MFIs to adapt their products to the needs of clients in the post-crisis period. Inevitably client needs will have changed - dramatically in some cases - and it is important that any rescheduling of loans or refinancing reflects these needs. Two industry wide workshops have already been delivered on product refinement and market research. Both were well attended and favourably received. A number of institutions will face severe capacity challenges in adapting to the changed circumstances. Post-crisis institutional assessments were offered to help institutions in identifying the issues which need to be tackled. A number have already been completed. Under the component AMFI invited proposals from its members for individual support. The first round of support grants have now been approved. Looking to the future, support will be offered to strengthen institutions' preparedness for managing future crises and disasters.

EVENTS CALENDAR

Aug 25 – Sept 5	Applied Microfinance Institute, Accra, Ghana
Sept 2 – 4	SACCO Cap Training on Credit Administration
Sept 8 – 19	School of Applied Microfinance, Mombasa, Kenya
Sept 18 – 20	Boulder - Bergamo Forum on Access to Financial Services, Bergamo, Italy
Oct 13 – 17	SACCO Cap/CGAP Training-of-Trainers
Oct 20 – 24	WOCCU Africa SACCO technical Congress, Banjul, The Gambia