The Kenya Financial Sector Deepening (FSD) programme was established by the UK’s Department for International Development (DFID) programme in 2001 to support the development of financial markets in Kenya. In 2005 we were constituted as an independent trust under the supervision of professional trustees, KPMG Kenya, with policy guidance from a Programme Investment Committee (PIC). Our aim today is to help realise a vision of an inclusive financial system to support Kenya’s goals for economic and social transformation. We work closely with government, financial services industry and other partners across key economic and social sectors. The core development partners in FSD Kenya are currently the Bill and Melinda Gates Foundation and the Swedish International Development Agency (SIDA).
2018 Annual report
Table of contents

01 DIRECTOR’S NOTE 3
02 OUR APPROACH 4
03 OUR STRATEGY 5
04 INCLUSIVE FINANCE? RESULTS FROM FINACCESS 2019 6
05 OUR PORTFOLIO 10
06 THE 4TH FSD ANNUAL LECTURE 22
07 KEY FINANCIAL RESULTS & INCOME STATEMENT 24
09 THE TEAM 28
Creating value through inclusive finance
Excitement over fintech reached fever pitch in 2018 notwithstanding the puncturing of the Bitcoin bubble at the start of the year. And there are good reasons to be excited by the potential for new technologies to change the financial sector in a positive direction. However as with much new technology the outcomes are by no means assured.

FSD’s work is increasingly focused on trying to help harness the on-going disruption of the sector in a way which will create real value for people. Seven years ago we were involved in the birth of digital credit in Kenya. Today there is a vibrant and competitive market for digital credit. Our research has found many ways in which this has had a positive and empowering impact in people’s lives. But overall it remains a very mixed story and we are certainly now seeing signs of a dark side emerging. We are convinced in FSD that active measures to mitigate the potential harm – especially for the poorest – are now needed through appropriate regulation of market conduct. On the positive side, experimental work in many areas of the real economy from agriculture and energy to healthcare and education are starting to show how fintech can be used to create value. This year’s report shares some of the stories of our work with partners aimed at exploring the frontiers of how we can create a better kind of financing. While our contributions are modest, we see ourselves as part of a bolder movement to realise a brighter vision for the financial system as an enabler of sustainable human development.

David Ferrand
Director
FSD’s work is based on a market system development approach – often referred to as “making markets work for the poor” (M4P). This approach has emerged as an increasingly influential development paradigm over the last decade. It emphasises the development of sustainable and scalable market systems in a way that benefits poor people, offering them the capacities and opportunities to enhance their lives.

Building on a detailed understanding of market systems and a clear vision of the future, we seek to address the underlying systemic constraints as a means to bring about large-scale and sustainable change. This approach provided the original impetus for the establishment of FSD Kenya and has guided our activities for the past eighteen years. Making markets work for the poor starts with an interrogation of how markets are currently working, where the poor are situated within them and what will determine future development trajectories. Looking at the market system as a whole helps us understand the current state and potential future of inclusive finance in Kenya.

The starting point for analysis is with the core function of markets: transactions between supply and demand. The basis of any transaction is the creation of value for those engaging in it. From the perspective of the demand side, the first question to consider is the purpose - what does a financial service usefully enable in the real world? Then if financial services are to become truly relevant to all Kenyans, affordability is critical. The current costs of many formal services will need to reduce further. Finally, the participants in a financial transaction need to trust that the other party will honour its side of the deal.

The potential for services to create value through useful solutions to real world problems at an affordable price with confidence in the outcomes is heavily determined by the market’s supporting functions and rules.

The supporting functions include:

- **Industry infrastructure** such as the payments system, data/information sharing mechanisms, security depositories and collateral registries; and **Service markets** most notably the ability to outsource functions to specialist players to exploit scale and specialisation efficiencies.

- **Laws and regulation** – the rules and enforcement – are the most prominent rules of the game impacting on financial markets. But the **informal rules** – habits and norms, attitudes and mental models – are equally important in shaping market outcomes.
The Government of Kenya has established a long-term vision to “create a globally competitive and prosperous nation with a high quality of life by 2030”.

Vision 2030 emphasises that all Kenyans should enjoy a high quality of life. The link between financial market development and poverty reduction is the sole rationale for the FSD programme. In looking to the future, we need to ask what constrains the sector from making a transformational impact on lower-income markets. For too long there has been an implicit assumption that the only binding constraint was cost. While it is certainly true that reducing costs is an important objective, experience in Kenya and elsewhere has shown that it is not enough to realise far-reaching change. Furthermore we cannot focus only on the direct impact of finance on low-income households. Improving economic opportunities and delivering vital services to the poor depend on the financing of critical economic and social sectors.

Reiterating our approach to market development, we believe that inclusion depends on developing financial solutions which address real world problems. In other words, we need financial services which do useful things for people and businesses. Low levels of utilisation of many services often reflect that the current services are simply not especially useful. Services also need to be underpinned by a strong degree of trust. Addressing these three elements we believe is the key to developing a financial system which delivers real value to low-income people. The result should be sustainable improvement in their lives through facilitating growth, improving resilience and allowing people to make better choices which directly improve their quality of life.
Inclusive finance?
Results from FinAcess 2019

Kenya’s financial sector has tripled its reach in just 13 years with 83% of the population now formally included. Meanwhile, the informal sector remains strong, with over half the population using informal solutions. Exclusion has gone down to just 8% who use no financial devices at all.

Figure 1: Usage of formal and informal financial solutions (% adults 2006 - 2019)

Gaps in access

Formal access for the poor has risen steeply from 10% in 2006 to 70% in 2019 closing the inclusion gap between the wealthy and the poor (see below for definition). Women now have similar levels of formal inclusion to men with only a 6% difference between them.

Figure 2: Gaps in inclusion by wealth and gender (% adults 2006 - 2019)

1. Using the Poverty Probability Index (PPI) the population was divided into 5 wealth quintiles. In this report, we compare the wealthiest 20% (average monthly household expenditure KSh 34,000) and the poorest 40% (average monthly household expenditure KSh 13,000).
Borrowing and saving trends

Kenyans are primarily savers, but borrowing is rising rapidly. Over 70% of the population are saving formally or informally and 50% of the population currently have a loan.

Figure 3: Usage of savings and credit (% adults 2006 - 2019)

<table>
<thead>
<tr>
<th>Year</th>
<th>Savings prevalence</th>
<th>Borrowing prevalence</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>65</td>
<td>36</td>
</tr>
<tr>
<td>2009</td>
<td>83</td>
<td>38</td>
</tr>
<tr>
<td>2013</td>
<td>66</td>
<td>28</td>
</tr>
<tr>
<td>2016</td>
<td>80</td>
<td>34</td>
</tr>
<tr>
<td>2019</td>
<td>70</td>
<td>50</td>
</tr>
</tbody>
</table>

Savings device use

54% of Kenyans save on their digital wallets, making mobile money the most widespread savings device. Use of informal savings has declined, and the use of other formal devices has remained stagnant.

Figure 5: Change in use of top 6 savings devices (% adults 2016 - 2019)

<table>
<thead>
<tr>
<th>Device</th>
<th>2016</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mobile phone</td>
<td>43</td>
<td>54</td>
</tr>
<tr>
<td>Chama Secret hiding place</td>
<td>40</td>
<td>29</td>
</tr>
<tr>
<td>Mobile banking</td>
<td>17</td>
<td>17</td>
</tr>
<tr>
<td>Sacco Bank</td>
<td>13</td>
<td>11</td>
</tr>
</tbody>
</table>

Debt stress

67% of borrowers experienced at least two symptoms of debt stress including: default; being overleveraged; and selling assets/borrowing/cutting expenditure to repay loans.

Figure 4: Percentage of borrowers experiencing debt stress (2019)

- Default on a loan: 18
- Debt repayments > 50% monthly expenditure: 24
- Sell assets, borrow, reduce food expenditure: 51
- Any 2 signs of debt stress: 67

Borrowing device use

Digital borrowing is rising fast, driving up formal borrowing rates. 9% of Kenyans currently have a mobile banking loan and 7% currently have a loan through digital apps. However, the biggest leap is in the use of shopkeeper goods on credit, this is now at 29% possibly a reflection of economic stress.

Figure 6: Change in use of top 6 borrowing devices (% adults 2016 - 2019)

<table>
<thead>
<tr>
<th>Device</th>
<th>2016</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shopkeeper credit</td>
<td>10</td>
<td>29</td>
</tr>
<tr>
<td>Loan from Chama</td>
<td>8</td>
<td>10</td>
</tr>
<tr>
<td>Family &amp; Friends or neighbour</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Mobile banking</td>
<td>6</td>
<td>8</td>
</tr>
<tr>
<td>Sacco</td>
<td>5</td>
<td>7</td>
</tr>
<tr>
<td>Bank</td>
<td>10</td>
<td>8</td>
</tr>
</tbody>
</table>
Financial wellbeing

83% Kenyans are financially included but only 22% are financially healthy, indicating that uptake of accounts alone will not deliver the dividends we seek for improved well being.

Figure 7: Percentage of adults classified as financial healthy (2016-2019)

39%

22%

2016

2019

The dimensions of financial health – ability to manage day to day, ability to cope with risk, Ability to invest in the future – have all declined since 2016. In particular, there has been a marked decline in people’s ability to invest.

Figure 9: Ability to manage day to day, manage shocks and/or invest in the future (% adults 2016-2019)

Gaps in financial wellbeing

There is still a substantial gap in financial wellbeing between rich & poor and men & women.

Figure 8: Percentage of adults classified as financial healthy by wealth category (2019)

52

19

24

Poor

Wealthy

Women

Men

In 2019, half the population said that their financial situation had worsened. In 2016, a third claimed that this was the case. This corroborates the decline in financial health indications.

Figure 10: Over half the population claim that their financial situation has worsened (% adults 2016 - 2019)

51

34

28

Worsened

Remained the same

Improved

Ability to manage day-to-day

Ability to cope with shocks

Ability to Invest in future goals

2016

2019
Meeting financial needs

Figure 11: Use of formal, informal or non-financial solutions to meet needs (% adults experiencing liquidity distress, shocks or investing in goals 2019)

- 62% of the population had trouble meeting daily needs
- 36% of adults experienced a shock
- 59% of adults are investing in goals

The disconnect between rising financial inclusion and decline in financial health is partly related to the relatively limited role of formal finance in helping people to meet their needs.

- Kenyans mostly use informal solutions such as assistance from friends and family to deal with their daily needs.
- Non-financial solutions also play an important role, including working more and selling assets.
- Formal finance plays a more limited role, but formal savings is important, especially for investment.

Legend:
- Non-financial:
  - Worked more/cut expenditure
  - Sold assets
- Informal:
  - Informal saving
  - Informal borrowing
- Formal:
  - Formal saving
  - Formal borrowing
  - Insurance
FSD Kenya works to support the development of a financial system which delivers real value to low-income people by addressing the barriers of usefulness, affordability and trust. Our work is organised into four focal areas of work. It starts with creating a clear, shared, long-term vision in Kenya for the financial services sector and its developmental role. This will help shape the specific rules of the game for the market – laws and regulation – and the evolution of financial sector infrastructure. The ability of market players to deliver real value will be determined by the incentives and opportunities created by the rules and infrastructure. But it also depends on improving the market capacity to create better financial solutions to real world problems. The following pages illustrate key initiatives in each area.
Long-term policy and research

Shared vision across stakeholder groups of how the financial system should develop to support national development objectives and specifically the reduction of poverty.

Regulation

Supportive policy and regulatory environment in which the formal rules that govern the financial system shift incentives in favour of low-income consumers and smaller-scale enterprises.

Industry infrastructure

Efficient and open finance industry infrastructure supporting increased competition, expanded services and lower costs.

Innovations

Market capacity and incentive to innovate financial solutions for real world problems of poor households and the economies of the poor.
Open finance: giving consumers control over their own data

The ownership of personal data has become a major issue worldwide with significant implications for the future of the digital economy and beyond. Open finance models are based on consumers rather than providers determining who can access their financial data and for what purposes.

Nowadays, financial service providers use everything from our social media accounts to the content of our text messages to determine what products to offer us. But the details on data use are often buried in long terms and conditions few of us read, leaving consumers without control of their financial information. FSD Kenya’s open finance research aims to increase choice and competition for financial services by giving consumers greater control of their financial information.

Currently many providers do not let consumers freely share their information, or only let consumers share this data with a few partners the provider—not the consumer—selects. This limits consumers’ free choice and has hindered competition in Kenya. But what if a consumer could put all of their financial information in one place, and get competing offers from many different providers at the same time? Imagine how competition in car insurance renewals might change if all insurers had access to the same information, and the consumer could compare multiple offers on a single platform? That is the dream for open finance, and these models are already being implemented in places like the UK, Mexico and Australia.

In 2018 we began exploring the potential of open finance for Kenya. Our initial analysis suggests that Kenya has all the right ingredients for open finance—fast-innovating digital finance sectors, consumers willing to experiment with new products and legacy competition issues that are hindering consumer choice. Looking at current opportunities for change we engaged in the policy discussions around proposed new legislation on data protection. In the coming year we will look at how open finance thinking relates to the government’s flagship project on next generation digital finance.
Improved access to market data can support value adding finance for low-income Kenyans through better informed policy and business decisions. The FinAccess survey provides the most comprehensive data on financial inclusion and has now been firmly adopted by the market.

FSD has been involved with FinAccess since 2005 when the survey was founded to track the status of financial inclusion and identify barriers and opportunities to improve access and use. The survey was established under a public-private partnership with the aim of encouraging use of the data by policymakers and financial service providers. In the early days, FSD played a significant role in funding and overseeing execution of the survey. But our aim has always been to step back over time.

2018 marked a watershed in achieving the sustainability of FinAccess. Central Bank of Kenya (CBK) and the Kenya National Bureau of Statistics (KNBS), who have been centrally involved from the outset, took over much of the resourcing and management of the fifth round of FinAccess. Alongside the public funding, four industry players also contributed in this round. FSD made up the deficit, now a mere 15% of the total budget.

Achieving sustainability depends not only on the finance but also building the capacity to deliver a quality product. The commitment by the KNBS to the survey has created the research skills needed to underpin its rigour. Meanwhile the Central Bank’s research department provides the sectoral expertise needed to guide the survey design and analysis.

Renewed interest from industry sets a promising stage for the future. Individual players will be given the opportunity to sponsor new products that will increase the value of FinAccess. Salient market issues can be tackled by drawing on other data sets and using rapid tailored surveys. The FinAccess study into digital credit funded by FSD and launched in 2018 illustrates the approach. Drawing on the FinAccess sample, a follow-up phone survey allowed us to probe more deeply into the explosion in consumer credit offered through digital channels.
Kenya’s financial sector regulators have successfully applied a ‘test and learn’ approach to innovation over the past decade. The Capital Markets Authority (CMA) is now pioneering a more structured approach to encourage the development of financial technology (fintech) through the creation of a regulatory ‘sandbox’.

There seems little doubt that the ‘test and learn’ approach applied in Kenya has paid dividends. Where many other regulators on the continent simply applied existing rules strictly to proposed new mobile money schemes, the Central Bank of Kenya provided enough latitude to allow a business model to emerge. It was then able to practically assess the risks and establish an appropriate regulatory response. This worked well when there were relatively few credible ideas and firms for the regulator to oversee. The fintech revolution has changed that with many new prospective players seeking regulatory approval. A sandbox is a purpose-built framework that enables a firm to test an innovation on a limited basis, before obtaining full regulatory approval only if the test is successful.

While the term ‘sandbox’ might be new, the concept itself is not. In the pharmaceutical industry before a new drug is rolled out, tests are performed in a restricted and controlled environment. The UK’s Financial Conduct Authority (FCA) has pioneered the use of sandboxes in the financial sector. Three quarters of the firms admitted in the first cohort completed testing, with 90% of these firms going on to market launch. About 40% of firms confirmed receiving investment during sandbox tests. Participants reported that the constant and open dialogue with the regulator enabled them to develop more rigorous business models and processes.

Seeking to stimulate innovation in capital markets, CMA decided to establish the first regulatory sandbox in Kenya. During 2018, with support from FSD Kenya and the Consultative Group to Assist the Poor (CGAP), CMA developed its core policy guidance. This establishes a clear process for how fintechs apply to join the sandbox and perform tests while protecting consumers and other stakeholders. Implementation is expected to start by mid-2019.
Amplifying our social media voices to improve consumer protection

Every day in Kenya thousands of consumers take to Twitter and Facebook to raise problems they have had with a financial service. These social media posts, if properly organised and analysed, offer a new tool for improving consumer protection in Kenya.

In 2018, FSD Kenya partnered with Princeton University and CitiBeats, an artificial intelligence text analytics platform, to measure consumer protection issues in Kenya using people’s opinions and experiences expressed on Twitter. This tool allowed our team to easily sort tweets into nine key consumer protection topics, and see which topics were most common with different providers. We were also able to track spikes in tweets with different providers over time, to quickly identify issues as they pop up.

![Figure 12: Spike in Tweets to a major retail bank regarding charges](image)

Just as useful as the numbers that our analysis produced were the stories. Using a new handle @pesastory, we also sparked conversations on Twitter, asking Kenyans to share issues they have faced on topics such as loans, fees and charges, or customer service. One of our conversations revealed a serious concern—missing money in people’s bank accounts. Using @pesastory we were able to highlight a case where money had been removed from a customer’s account by a branch manager.

The study has demonstrated a valuable new way to gain insights into consumer experiences and problems. In 2019 we will work with regulators and industry to see how these approaches can be integrated into market monitoring processes to enhance consumer protection.
Despite recent progress in the development of digital financial services in Kenya, we remain some way from a fully interoperable payment system. Much attention is given to the technical aspects of interoperability – how one system is able to link to another. But this is often the easier part of the problem to solve. Many components of the wider payment system – debit cards, mobile money schemes, automated teller machines (ATMs) – are already technically interoperable. But usage remains limited. Consumers face tariff barriers which discourage day-to-day usage. Carrying out transactions across providers can be complicated. Frequently users aren’t aware that it is even possible to transact across provider systems. Underlying these problems is the need for collaboration across multiple players whose business interests may diverge – at least in the short-term.

Several initiatives are underway to tackle the underlying collaboration challenge. At a policy level, the recently established Vision 2030 flagship project on digital finance establishes interoperability as a core objective. In parallel the East African Community is seeking to establish regional interoperability across digital payments. A new National Payments System (NPS) strategy is under development by the Central Bank of Kenya to steer the payments industry towards a robust, open and efficient system. Government is building on the progress already made with the eCitizen platform aiming to digitise all remaining government services. And the industry is responding. Payment service providers offering instant payments have come together under the auspices of the Payments Association of Kenya (PAK) to establish a new payments clearing house. This will promote infrastructure sharing and improve efficiency. FSD Kenya has been supporting these initiatives in various ways through research, seed-funding and technical assistance. Much remains to be done but the future looks bright.
Social protection payments: Inua Jamii

Safety nets are essential to fighting poverty and vulnerability among the poorest households. The government has created a comprehensive National Safety Net Programme (NSNP) to improve and enhance social protection delivery across the country. Delivering this programme successfully depends on an effective payment solution.

NSNP consolidated earlier social protection schemes into a single programme – Inua Jamii. FSD was asked by the Ministry of Labour and Social Protection to support the design of a new solution to deliver payments under Inua Jamii. The aim was to provide beneficiaries with a better experience and help improve overall programme efficiency and effectiveness.

In order to deliver these aims the new payments approach sought to leverage the considerable consolidated buying power of the new programme and encourage competition among providers. While in the early days of social protection many areas of the country had very limited coverage, the expansion of mobile phone and data enabled agent banking has changed that. Rather than selecting a single payment service provider, the new approach includes a number of providers able to meet the minimum criteria. Beneficiaries make the choice of which one to use and will have the option of switching every year.

Following a competitive bidding process, four payment service providers were selected: Kenya Commercial Bank, Co-operative Bank of Kenya, Post Bank and Equity Bank. As projected, the government was able to achieve significant cost savings through better pricing. Gains are also expected through improved process efficiency building on past experience and scale economies. The first programme to be implemented was the recently introduced universal pension, targeting 500,000 senior citizens. Other programmes will follow with over one million beneficiaries set to be paid by the end of 2019.

The impact on beneficiaries is fundamental. Use of multiple providers with extensive networks is expected to help reduce travel times and costs for beneficiaries. The simple right to choose empowers beneficiaries and the resultant competitive pressure is expected to give rise to improved customer service. However, nothing can be taken for granted. Routine client satisfaction surveys will be undertaken to assess performance and ensure that minimum service levels are achieved.
Apollo Agriculture is a technology start-up seeking to dramatically improve farmers yields by offering the right combination of farm inputs, advice and financing. Using a combination of technologies - agronomic machine learning, remote sensing and mobile phones – Apollo delivers an optimized package of support to smallholder farmers on a commercial basis.

After Apollo’s first season of experimentation, they encountered a challenge that they had not anticipated in the distribution of the farm inputs. While they had been able to recruit agricultural input dealers to manage last-mile distribution of inputs to farmers, these dealers often did not have sufficient capital to keep enough inputs on hand. This resulted in delays in delivery, frustrating farmers as planting must coincide with the rains. After a joint problem-solving session with FSD, we codesigned an experiment to provide trade capital to dealers using a simple scorecard based on transactions and the number of farmers assigned to the store. FSD covered some of the operational costs for recruiting new dealers and a small guarantee in case of losses for Apollo since trade finance was not part of their initial business structure.

The experiment confirmed the hypothesis that inserting trade credit into Apollo’s process would add value for the dealers as well as the farmers. Of the dealers that received trade credit, less than 1 percent delayed repayment of the credit and all of the supplies were provided to the more than five thousand Apollo farmers in 2018, paid for, or returned to Apollo. Unlike the previous season, farmers were able to access inputs as soon as they were approved without having to wait or return to a dealer later. One dealer was able to triple their business with Apollo thanks to the provision of trade credit. It is not possible to confirm whether the score card accurately predicted different levels of risk, given that all dealers repaid. However, this will be further tested in the next iteration of the pilot which will reach a larger number of dealers and provide higher levels of trade credit per dealer.

"Of the dealers that received trade credit, less than 1 percent delayed repayment of the credit. Apollo was able to increase the number of farmers borrowing by over 400% in 2018."
Building livelihoods: poultry rearing

In his 2016 letter, Bill Gates celebrated the miracle of chicken rearing for improving the livelihoods of low-income households. FSD tested the potential for a market-based approach to small-holder chicken rearing.

A small experiment was conducted to finance sixty farmers in one of Kenya’s semi-arid counties to undertake chicken rearing. The experiment included support on the necessary know-how, feeds, vaccination and marketing. While the financing could readily be provided on a sustainable basis.

Gates’s case for advocating chicken rearing was based on four observations:

- Chicken are both easy and inexpensive to take care of;
- Chicken represent a good investment;
- Rearing of chickens empowers women; and
- Increased regular protein intake from meat and eggs is good for child health.

How did these play out in our experiment?

**Easy and inexpensive:** The cost of vaccines and feed over a 16-week cycle are manageable and can be included in a financial product that was affordable to the families. For many of the households, the opportunity cost is not excessive as the work is near other household chores that need to get done. In addition, the critical skills of brooding and vaccination are easy to acquire.

**Good investment:** In the FSD experiment, 30 farmers received 1-day old chicks and 30 farmers received 1 month old “pullets”. Those that received 1-day old chicks eventually made a 30% return on investment. Those that purchased the 1-month old pullets, suffered higher than normal mortality and in the 16-week cycle were unable to recoup their investment. In short, there is evidence of a potential business model here with room for use of financial solutions like insurance to mitigate some of the risks.

**Women’s empowerment:** Anecdotal evidence from the short experiment suggests that women are more likely to get involved in rearing and sale of chicken as an economic activity. 87% of those who reared day old chicks were women and 64% of those who reared one-month old pullets were women. Whether this translates to long lasting empowerment will require a longer study period.

**Improved child health:** This was not measured during the 16-week experiment as validation will require study over consecutive testing periods.
Graduation programmes seek to help the poor ‘graduate’ out of poverty by developing income generating activities. While many pilots have been successful around the world, the challenge is achieving scale and sustainability. FSD Kenya has been working with CARE since 2016 to test a market-based approach in Marsabit.

The graduation approach pioneered by the Bangladesh based NGO, BRAC provides a carefully delivered package of cash stipends, savings, skills training and an asset transfer supported by constant coaching and mentoring. It is carefully designed to tackle the multiple barriers faced by very poor people in building their livelihoods.

Government funded social protection programmes now provide regular stipends to many low-income people in Kenya, giving them a basic platform on which to build. The pilot targeted beneficiaries of the Hunger Safety Net Programme (HSNP) in Marsabit county. Community-based facilitators were identified and trained to provide mentoring and coaching. Routine mentoring and coaching visits to individual households typical of the BRAC model are a key cost driver. In this pilot, the beneficiaries were mobilised into savings groups which in addition to providing financial services are the primary avenue for delivering support to the households. Instead of an asset transfer in cash or kind, FSD Kenya partnered with Equity Bank to provide credit to the beneficiaries to start income generating activities. Activities supported include petty trading, small livestock (sheep and goats) trade and bead-making.

Not surprisingly, some participants were at first apprehensive about borrowing, having observed the experiences of their neighbours running into problems taking loans from formal providers. The community-based facilitators helped allay these fears and the number electing to borrow and develop income generating activities has gradually increased. Some are now in their second cycle of borrowing. Anecdotally, the loans are valued by the participants and most borrowers are managing to repay their loans.

The project aimed to facilitate market linkages to support the purchase of commodities and sale of the livestock at better prices. Common interest groups have been formed and connected to Tosha, a local institutional trader supported by the Kenya Market Trust, and the Kenya Livestock Marketing Council (KLMC) to enable goat trading outside the local market. The project has also facilitated the collection of livestock market price data and dissemination by Radio Jangwani, a local station.

The remaining year of the pilot will be focused on refining the financing and market linkage components which are at the heart of creating a sustainable approach. Many challenges have been encountered in execution and the results are as yet far from conclusive. Nevertheless, the pilot provides some encouraging pointers to how a scalable market-based graduation approach can be developed.
The inevitable: a glimpse into the future of fintech

FSD Kenya annual lecture on financial inclusion 2018

In his delivery of the 4th FSD Kenya annual lecture on financial inclusion internationally recognised entrepreneur and business leader, Julian Kyula, discussed the world of fintech from an African continent perspective and the journey we must embark on to participate in a rapidly changing digital world.

Julian Kyula is one of Kenya’s most successful fintech entrepreneurs. In 2010 Julian started Mobile Decisioning - or MODE - in Nairobi. Within eight years when Julian successfully exited, he had established MODE as a leading global provider of airtime credit operating in more than 20 countries, disbursing more than 6 million loans per day, lending more than $800m last year.

While pointing to the explosion of investment in fintech across the world, Julian emphasised his core belief that what we are seeing here is in investment in learning and experimentation, quoting Silicon Valley entrepreneur Steve Blank: “a start-up is a temporary organisation used to search for a repeatable and scalable business model”. With the costs of launching a tech start-up having reduced by several orders of magnitude over the last decade, the disruption is only set to increase. Digital banking start-ups are now challenging traditional institutions and the world of finance is already changing.

Julian discussed the world of fintech from an African continent perspective. “The research and data presented ... should not come as a shock to those who see this tech world unfolding. However, and we can agree, the world is shifting; data patterns are morphing and the tools to understand it are a marvel. Do we play or do we spectate? From lending, to blockchain, regtech to payments, billing and capital markets; insurance and so on – wherever you play, there is an inevitable disruption coming. And this time the one continent that should create its own digital future is sitting on digital gold! Let’s participate, disrupt and enjoy doing it.”

The full video, a summary video, photos and the presentation are all available at fsdkenya.org/the-4th-fsd-annual-lecture.

“The world is shifting... [and] this time the one continent that should create its own digital future is sitting on digital gold! Let’s participate, disrupt and enjoy doing it.

– Julian Kyula, Techpreneur
Key financial results

Income

FSD ended the year with a surplus of KShs 947 million. This was attributed to core funding received from Gates Foundation (KShs 401m) and restricted funding from SIDA (KShs 322m).

FSD also recognised incomes from restricted funding for the Hunger Safety Net Programme (KShs 2,067 million) from DFID. In conformity with statement of financial accounting standard, and as per donor requirements, these funds are recognised as income only when expenses are incurred. Additionally, FSD earned a total of KShs 82 million in interest income from the cash held on fixed deposit.

Expenses

Total programme expenditure for the year was KShs 2,667 million (9% below budget). Management expenditure was KShs 138 million (5% below budget) for the year due to lower spending on administration costs and office procurement.

Income statement - Audited
For the year ended 31st December 2018

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>INCOME</strong></td>
<td>KSh millions*</td>
<td>KSh millions*</td>
</tr>
<tr>
<td>Grants</td>
<td>2,468</td>
<td>2,816</td>
</tr>
<tr>
<td>Other income</td>
<td>62</td>
<td>100</td>
</tr>
<tr>
<td>Finance income¹</td>
<td>20</td>
<td>46</td>
</tr>
<tr>
<td>Unrealised foreign exchange gain</td>
<td>-</td>
<td>63</td>
</tr>
<tr>
<td><strong>TOTAL INCOME</strong></td>
<td>2,550</td>
<td>3,025</td>
</tr>
<tr>
<td><strong>EXPENDITURE</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>PROJECT EXPENSES</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Core projects²</td>
<td>410</td>
<td>635</td>
</tr>
<tr>
<td>Designated projects³</td>
<td>2,067</td>
<td>2,267</td>
</tr>
<tr>
<td><strong>Total project expenses</strong></td>
<td>2,477</td>
<td>2,902</td>
</tr>
<tr>
<td>Administrative expenses</td>
<td>138</td>
<td>145</td>
</tr>
<tr>
<td><strong>TOTAL EXPENDITURE</strong></td>
<td>2,615</td>
<td>3,047</td>
</tr>
<tr>
<td>Unrealised foreign exchange losses</td>
<td>52</td>
<td>0</td>
</tr>
<tr>
<td><strong>TOTAL COSTS</strong></td>
<td>2,667</td>
<td>3,047</td>
</tr>
<tr>
<td>Surplus/(deficit) for the year</td>
<td>(117)</td>
<td>(22)</td>
</tr>
</tbody>
</table>

* Columns do not add up due to rounding

¹ Finance income includes interest earned on FSD funds.
² Core/non-designated projects are funded by donors through unrestricted funds. Unrestricted funds have no conditions regarding the projects they can be used on.
³ Designated projects are funded through restricted funds. Restricted funds can only be used on the projects specified by donors.
### Balance sheet - Audited
**As at 31st December 2018**

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ASSETS</strong></td>
<td><strong>KSh millions</strong>*</td>
<td><strong>KSh millions</strong>*</td>
</tr>
<tr>
<td><strong>Non-current assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Property and equipment</td>
<td>28</td>
<td>36</td>
</tr>
<tr>
<td>Intangible asset work in progress</td>
<td>3</td>
<td>-</td>
</tr>
<tr>
<td>Long term loan</td>
<td>38</td>
<td>38</td>
</tr>
<tr>
<td><strong>Total non-current assets</strong></td>
<td><strong>69</strong></td>
<td><strong>74</strong></td>
</tr>
<tr>
<td><strong>Current assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Receivables</td>
<td>13</td>
<td>1</td>
</tr>
<tr>
<td>Short term deposits</td>
<td>62</td>
<td>234</td>
</tr>
<tr>
<td>Bank and cash balances</td>
<td>1,700</td>
<td>1,477</td>
</tr>
<tr>
<td><strong>Total current assets</strong></td>
<td><strong>1,775</strong></td>
<td><strong>1,712</strong></td>
</tr>
<tr>
<td><strong>TOTAL ASSETS</strong></td>
<td><strong>1,844</strong></td>
<td><strong>1,786</strong></td>
</tr>
<tr>
<td><strong>RESERVES AND LIABILITIES</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Reserves</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accumulated fund</td>
<td>947</td>
<td>1,088</td>
</tr>
<tr>
<td><strong>Current liabilities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unexpended projects fund</td>
<td>679</td>
<td>562</td>
</tr>
<tr>
<td>Accruals</td>
<td>143</td>
<td>83</td>
</tr>
<tr>
<td>Tax liability¹</td>
<td>75</td>
<td>75</td>
</tr>
<tr>
<td><strong>Total current liabilities</strong></td>
<td><strong>897</strong></td>
<td><strong>720</strong></td>
</tr>
<tr>
<td><strong>TOTAL RESERVES AND LIABILITIES</strong></td>
<td><strong>1,844</strong></td>
<td><strong>1,808</strong></td>
</tr>
</tbody>
</table>

* Columns do not add up due to rounding

---

¹ This amount is an accrual of taxes on which FSD has applied for exemption from the government pending finalisation of the exemption application.
The Team

Amrik Hayer
Head, Knowledge

Apphia Ndung’u
HSNP support officer

David Ferrand
Director

Duncan Oyaro
Project manager, Innovation

Edoardo Tololo
Research economist

Fausto Njeru
Finance officer

Felistus Mbole
Head, Poverty impact

Francis Gwer
Policy analyst

Geraldine Makunda
Project manager, Market information