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FSD News

EDITORIAL

Last month Kenya Women Finance Trust (KWFT) became the second micro-finance institution in Kenya to be licensed by the Central Bank of Kenya (CBK) as a deposit taking micro-finance institution (DTM). Congratulations to KWFT DTM, which now joins Faulu Kenya DTM as the first of the new financial intermediaries under this new regulatory framework. FSD was privileged to be able to work with both institutions through their transformation. Strategically important to the institutions themselves, from the perspective of financial inclusion and contribution to poverty reduction, the arrival of two new providers of micro-savings services is perhaps the most important achievement. Evidence continues to mount that giving poor people access to reliable, safe and accessible savings has the more reliably positive impact on livelihoods. While credit and other services can have a potentially transformative role for many, studies show that not everyone will necessarily benefit from such services. By contrast there is a universal need to be able to save to manage the day-to-day ebbs and flows of income and expenditure, to meet the costs of unexpected emergencies and major life events and to take advantage of investment opportunities.

Two other former NGO MFIs also provide savings as full commercial banks: K-Rep Bank was the first to transform over ten years ago, while in March this year approval was given by the CBK for Jamii Bora to create a new micro-finance bank in a reverse takeover of City Finance Bank. Alongside these institutions, the major players in the micro-savings market are other commercial banks with a strong focus on reaching the mass market. It is notable that all these micro-savings providers are relatively large with at least 150,000 clients. Both Faulu and KWFT found the process of transformation challenging and had to invest heavily in people, systems and infrastructure. Some conclude that this shows the regulatory framework is simply too demanding. An alternative view is simply that scale is a prerequisite to efficiently and safely offer savings services in a mass market. If this is right then perhaps rather than looking for changes in regulation, smaller MFIs need to think about alternative strategies for achieving scale, including mergers or outsourcing costly back-office functions.

David Ferrand
Director

NEWS AND VIEWS

Treasury Permanent Secretary Joseph Kinyua, displays the Costs of Collateral reports at the launch ceremony in Nairobi.

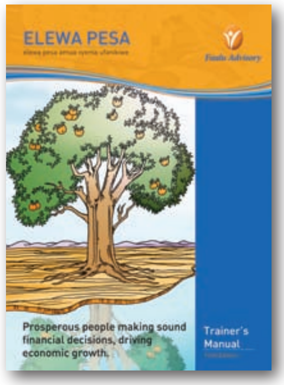
Cost of Collateral study launched

A well attended breakfast launch at the Intercontinental Hotel on the 24th March 2010 was the culmination of efforts by the Central Bank of Kenya and the Kenya Bankers Association to raise the profile of systemic rigidities that affect the cost and accessibility of credit. Attended by key stakeholders from both the public and private sector, there was widespread agreement with the findings of the study and an enthusiasm for implementing the recommendations. Among the key findings were that lack of a unifying legal framework regarding the creation, perfection and enforcement of security interests and the numerous, disconnected and manual registries add significantly to the overall cost of credit. This acts as a major constraint to increased access, especially for smaller enterprises.

Both the Minister of Finance (represented at the launch by the Permanent Secretary) and the Governor of the Central Bank were in favour of establishing a stakeholder task force to drive reforms to the collateral system. Recommendations for reform include digitisation and interconnection of the many registries, consolidation of numerous and sometimes contradictory laws and reworking of the Stamp Duty Act which is a major constraint. FSD is committed to these reforms and is ready to support the proposed task force in its efforts to increase access to credit.

The EasySave project

A recent initiative of Mobile Commerce Ventures (MCV), EasySave is an effort to develop new financial management products designed to meet the needs of underserved low-income customers across Kenya. This will be tackled through leveraging the established mobile payments and mobile wallet technology to deliver low-cost and flexible micro-loan and micro-saving products. The piloting phase will learn about how customers interact with the product, customer uptake, default rate, frequency of repayment, savings withdrawal rate. MCV is working with FSD and CGAP to develop insights into both the viability of this business model and low income customer borrowing and saving preferences. The customer pilot went live in February 2010. The first batch of 150 customers are actively using both micro-savings and have received a micro-loan.



Financial education pilots take off

The Financial Education and Protection Partnership (FEPP) is supporting Faulu Kenya to undertake a financial education programme. One of the first outputs is a trainers manual branded *Elewa Pesa* (Understand your finances). The manual, adapted from the Global Financial Education Program (GFEP), has 3 modules on savings, budgeting and debt management. Tailored to the Kenyan context, the manual was developed based on issues established after a baseline survey. With a target to reach 75,000 consumers, Faulu has developed three in-house master trainers, 12 financial education champions and 113 staff members in the target branches. 180 community based trainers have also been developed. The team has reached 1,322 clients so far in Bungoma, Coast and Kitale regions.

Benjamin Baraza, a field officer in Bungoma says - *"Some of the clients were very pessimistic about it and they thought it was a waste of time. I explained the relevance of the trainings to their businesses. Of the 140 clients who attended the training at Ogallo, there was remarkable improvement in savings deposits - Umoja self help group members in Indangalasia made it mandatory to make deposits every week. Issues of debt management in the area have greatly improved."*

INDEX-BASED WEATHER INSURANCE PILOT PROJECT

Adverse weather conditions from drought to excessive rainfall pose a major threat to the incomes of farmers. Weather perils lead to reduced agricultural productivity and, occasionally, serious famines. The secondary effect is decreased investment in the agricultural sector, further threatening food security and livelihoods. In Kenya during the prolonged droughts of 2008-09 some financial institutions either downsized their agricultural portfolios or stopped sector lending due to the increased production risks. In 2008 agriculture accounted for an estimated 25% of the economy as measured by gross domestic product; meanwhile lending to the sector represented only 3.6% of total commercial bank lending. Since then credit to the agricultural sector has bounced back with a growth of 26% over the year but still only represents 5.1% of total lending.[1]

A staff member of the Kenya Meteorological Department installs an automated weather station provided by the project at a farm in Menengai, Nakuru district. On the right is a complete installation.

Traditional insurance products have had limited success in tackling the risks which constrain investment and credit for agriculture. It has proven especially difficult to develop cost-effective products to reach the large number of relatively small producers who form a critical part of the agriculture sector in Kenya. Validating claims involves visiting individual farms, a time-consuming and costly process. Furthermore there is a risk that farmers will not tend insured crops diligently relying instead on a payout from the policy (so called 'moral hazard') or that those who know they are most likely to claim (because of difficult to measure factors such as poor soil, micro-climatic effects etc) are more likely to buy policies (the 'adverse selection' problem).

An approach using indexes constructed from weather data offers a powerful new way to mitigate these problems. Rather than seeking to cover each individual farm against losses, index-based weather insurance (IBWI) is premised simply on insuring against the occurrence of adverse weather conditions in a given area. For each crop covered a weather index is developed which aims to match as closely as possible the likely level of losses which a farmer will experience according to specific weather conditions such as drought. This dramatically reduces the costs of the product since it obviates the need for farm visits and eliminates the moral hazard and adverse selection problems as claims are based solely on independently recorded weather data. A farmer could be paid, for instance, whenever factors such as rainfall or temperature are either so high or so low that it is likely to cause significantly decreased crop yields.

FSD Kenya, the Rockefeller Foundation and the World Bank are working together to test the prospects for using IBWI in Kenya. Partnering with key players in the industry, the project is supporting the piloting of a number of IBWI products encompassing both crops and livestock. Partners include financial institutions, insurance companies, reinsurers, input suppliers and the Kenya Meteorological Department (KMD). While the aim is to develop sustainable products delivered by the private sector, success depends strongly on support from the KMD, which has an invaluable historical record of climate data in Kenya and operates an extensive system of weather monitoring. The project is working closely with KMD to put in place the infrastructure needed to provide reliable weather data for the pilots.

In advance of the 'long-rains' growing season this year, Equity Bank and APA Insurance developed pilot products for insuring maize in Embu and Nakuru districts. The products were bought by 515 farmers covering 787 acres of maize. This initial phase covered the cost of agricultural inputs against losses resulting from drought. The next phase is planned to give farmers an opportunity to protect against losses of expected yield income caused by drought or excess rainfall.

In Marsabit district, the International Livestock Research Institute (ILRI) is working with the initiative (including additional support from the UK's Department for International Development (DFID), to pilot index-based products for livestock as a complement to the Hunger Safety Net Programme. The first pilot was launched by Equity Bank and UAP Insurance Company earlier this year. In contrast to the crop pilots, the indexes are based on satellite imagery of available grazing in the areas covered. A payout will occur where the index of available grazing falls below the defined threshold. The aim is to build the resilience of pastoralist communities in the district enabling them to restock rapidly when droughts occur. The pilot product was bought by 2,000 pastoralists covering 3,467 cattle, 17,514 goats and 278 camels.

Preparations are underway for further pilots targeting the 'short-rains' season later this year. Crops targeted are wheat, sorghum, banana and tea in various locations while the livestock product will be rolled out further in Marsabit to cover the coming season. The project is also researching the potential to develop products for other significant sectors such as dairy, cotton, pyrethrum and coffee.

1 Central Bank of Kenya, Quarterly Statistical Bulletin, December 2009.

EVENTS CALENDAR

18 - 20 May	**Lighting Africa 2010 - International Business Conference & Trade Fair,** Nairobi - Kenya. For information: www.lightingafricaconference.org
20 - 21 May	**Africa Banking Forum 2nd edition,** Marrakech - Morocco Email Khadija Ennahdi: kennahdi@sp.ma For registration: www.i-conferences.org/abf
21 May	**infoDev's Climate Technology Innovation Center Workshop,** Nairobi - Kenya Email: ngangaj@gmail.com
19 July - 6 August	**16th Boulder Microfinance Training Programme,** Turin - Italy Email: boulder@euacpmicrofinance.org For information: www.mfw4a.org/events/