



THE STATE OF FINANCIAL HEALTH IN KENYA: TRENDS, DRIVERS, AND IMPLICATIONS

EVIDENCE FROM FINACCESS

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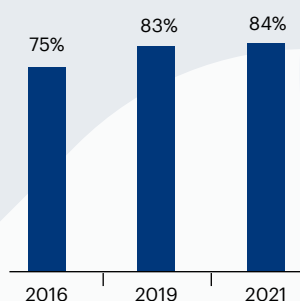
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Introduction

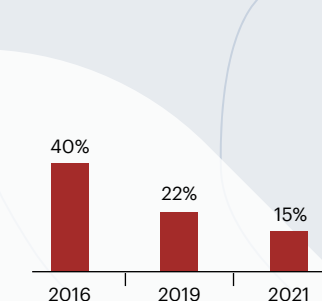
The financial health of Kenyans has declined rapidly since 2016, despite rising levels of financial inclusion. In 2021, 4 out of 5 adults owned a formal account but less than 1 in 5 demonstrated an ability to secure basic daily needs, cope with the costs of unexpected shocks and invest in their livelihoods and future¹.

Figure 1:

(A) Financial Access, 2016 - 2021 (% adults 18+)



(B) Financial Health, 2016 - 2021 (% adults 18+)



Source: Author's calculations from FinAccess surveys.

This paper suggests **4 key drivers of declining financial health: inflation, income, declining opportunities and demographic change.**

The financial health index

Manage day to day:

- Never went without food during the last year
- No trouble making ends meet between income cycles
- Has a plan for allocating income and expenses

Ability to cope with risks:

- Could raise lump sum in 3 days
- Regularly kept money aside for emergencies
- Never went without medicine in the last year

Ability to invest in the future:

- Using savings or credit to invest in productive assets
- Education or old age; is using/ plans to use savings
- Pension or investment income to make ends meet in old age; has been regularly putting aside money for the future.

¹ There are slight differences in the computation of the financial health index due to changes in the questionnaire over time. This has led to slight variations in the metric for 2021, with estimates ranging from 15% to 19%. Going forward, the Central Bank, Kenya National Bureau of Statistics and FSD Kenya are convening to standardise and improve the measure of financial health for Kenya.

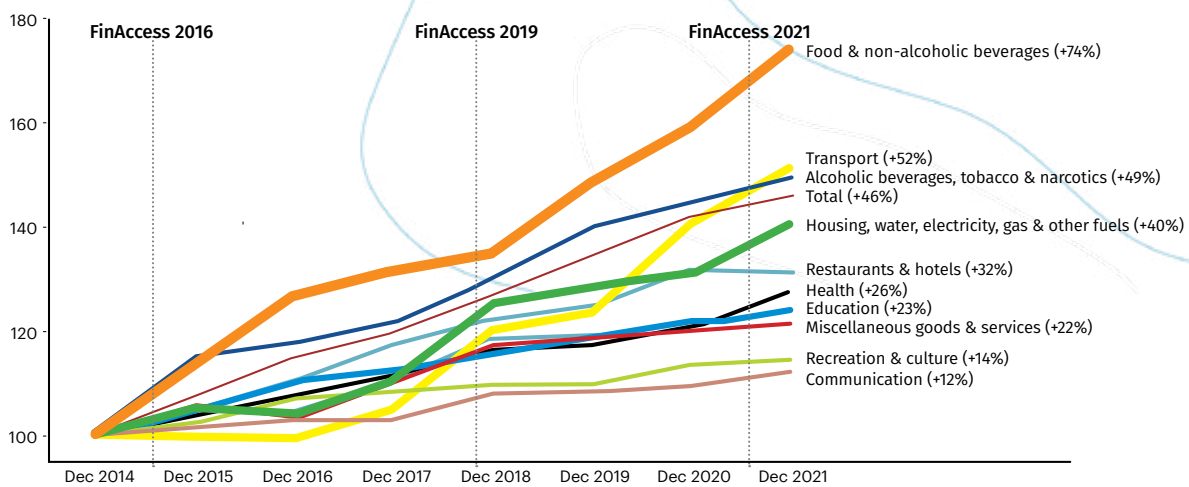
Drivers of declining financial health



1. Inflation

Food prices increased cumulatively by 74 percent, between December 2014 and December 2021 (Figure 2). The cost of food has major implications for household finances since food spending comprises over half of typical monthly household spending in Kenya, and even more for low-income households².

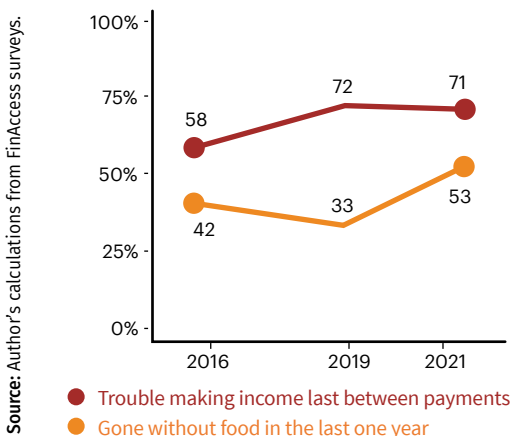
Figure 2:
Aggregate food prices increased by a cumulative 74 percent between Dec 2014 and Dec 2021
Cumulative changes in consumer prices by commodity groups (Price index, Dec 2014=100)



Source: Kenya National Bureau of Statistics, monthly CPI publications. Notes: The thickness of the lines are in proportion to the weight of each commodity in the CPI. The mid-point of data collection for each round of FinAccess is shown as vertical lines. Only commodity groups with a weight greater than 5 are shown.

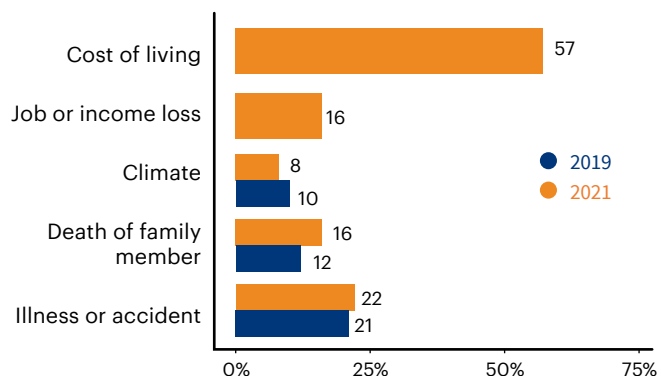
Rising cost of living was the most frequently cited shock with a large impact on household finances (Figure 3). Adults say they have adjusted to price shocks mostly by cutting back on expenses or getting help from friends and family.

Figure 3:
Adults are facing greater challenges managing day to day... % of adults (18+)



... rising prices are a big factor; cost of living was most common shock reported by adults in 2021...

Shocks faced by adults (% 18+) in the past year



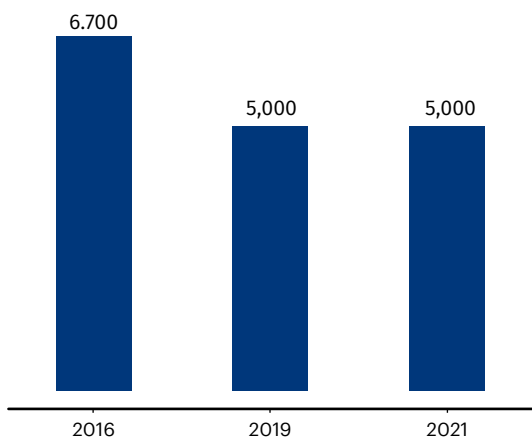
² Estimate based on consumption data (2015/16 Kenya Integrated Household Budget Survey).



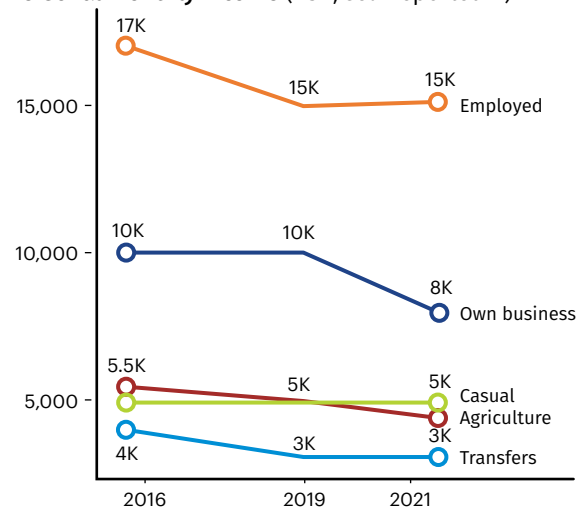
2. Income

Median monthly income reported by adults in FinAccess fell from Ksh 6,700 in 2016 to Ksh 5,000 in 2019 and remained at that level through 2021. While our ability to draw precise inferences about income from these data points is limited, they do suggest that personal monthly income has not kept up with the rise in consumer prices³ putting pressure on household budgets.

Figure 4:
Median income (KSh, self reported)



Personal monthly income (KSh, self-reported**)



Median incomes have either stagnated or declined across the population and for different livelihoods

Sources: *Source: Author's calculations from FinAccess surveys. **Notes:** Monthly income data is based on question: Including all your sources of income, how much money would you say you get on average in a MONTH?



Median monthly income fell from Ksh 6,700 in 2016 to Ksh 5,000 in 2019 and remained at that level through 2021.

³ It is important to acknowledge that there are a host of issues in using self-reported income data. Monthly income estimates from FinAccess are based on people's responses to a single survey question and rely on their ability to recall and aggregate income streams, oftentimes from a more than one source. Average income from agriculture or running a business may be particularly hard to compute mentally, given that income inflows may be infrequent and seasonal (in the case of farming) and costs associated with generating revenues should be netted out.

3. Opportunities



Since 2016, formal employment and business ownership, two important pathways for upward mobility, declined. The drop in business earnings being most pronounced in Nairobi and among adults in the top wealth quintile. During the pandemic, casual work and transfers displaced farming and business ownership as the top two most important income sources for adults (**Figure 5**). In 2021, 36% of adults depended on casual work and 32% depended on transfers, with casual work and transfers also being the largest source of income for the majority of these individuals. The share of men dependent on transfers for most of their income more than doubled between 2019 and 2021.

4. Demographics and social security

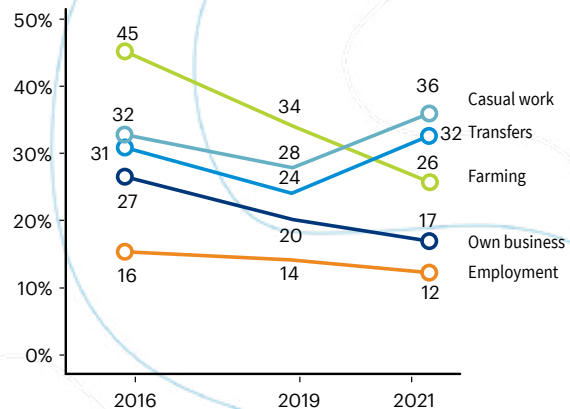


For every adult of prime working age (25-64) in Kenya, there are nearly 2 other people either under the age of 25 or over the age of 64⁴. In a context of limited government spending on social security, health and education, the finances of working adults caring for children or elderly relatives are increasingly strained.

Kenyans are increasingly committing financial resources for education, reflecting growing enrollment in secondary schools and the out-of-pocket costs required to pay school fees⁵. The share of adults using savings or loans to finance education rose from 28 percent in 2016 to 36 percent in 2021, outstripping investment in productive livelihoods (**Figure 6**). In 2021, over half of all prime working age adults struggled to keep up with school fees and as a result had a child sent home from school.

In the pandemic years between 2019 and 2021, there was also a substantial decline in those able to obtain needed medical care. Other data suggests that the main reason for this was inability to afford medicine and health care⁶. During the pandemic individuals absorbed the costs of health shocks mostly with the financial support of friends and family and by selling assets, which could reflect the high costs of hospitalization in relation to available savings, ability to borrow or gaps in insurance coverage.

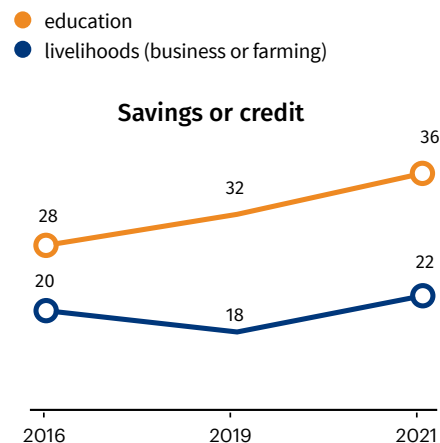
Figure 5:
All Sources of livelihood (% adults 18+)



As income from farming, business and employment becomes less common, income from transfers and casual work became more common

Source: Author's calculations from FinAccess surveys.

Figure 6:
Uses of savings and credit (% adults 18+)



Between 2016 and 2021, the share of adults using money from savings or loans to finance education increased from 28 to 36 percent. Savings are the predominant source of funds for education, but loans are increasingly used for this purpose.

Source: Author's calculations from FinAccess surveys.

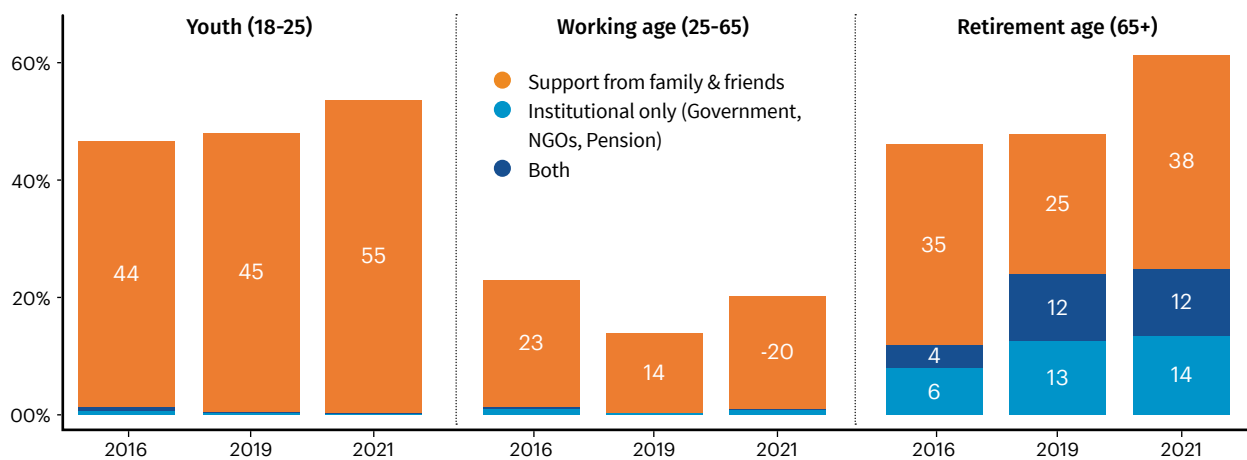
4 Based on United Nations World Population Prospects population estimates for 2020. In 2020, there were an estimated 20.4 million Kenyans between the age of 25 and 64, compared to 33.3 million either over the age of 64 or under the age of 25.
5 Between 2016 and 2020, while enrollment in primary school dropped slightly from 10.2 to 10.1 million, enrollment in secondary schools rose from 2.7 to 3.5 million and the primary to secondary transition rate increased from 81 to 91 percent (2021 Economic Survey, KNBS)
6 FSD Kenya Household Tracker; Finances, Health and Coping in Kenya (2021 Q3)



In a context of limited government spending on social security and education, the finances of working adults caring for children or elderly relatives are increasingly strained.

During the pandemic, the share of youth and retirement age individuals receiving transfers from family or friends increased by over 10 percentage points (**Figure 7**). The share of adults over the age of 65 receiving institutional transfers (from government or NGOs) doubled between 2016 and 2019 - reflecting the expansion of Kenya's Older Person's Cash Transfer program (OPCT). But during the pandemic, it was informal social networks that scaled to provide a lifeline of support to older adults (and youth) in need.

Figure 7:
Social transfers (% adults 18+)



Social and institutional cash transfers directed to youth and adults over the age of 65 increased substantially between 2019 and 2021.

Source: Author's calculations from FinAccess surveys.



Financial health and financial inclusion

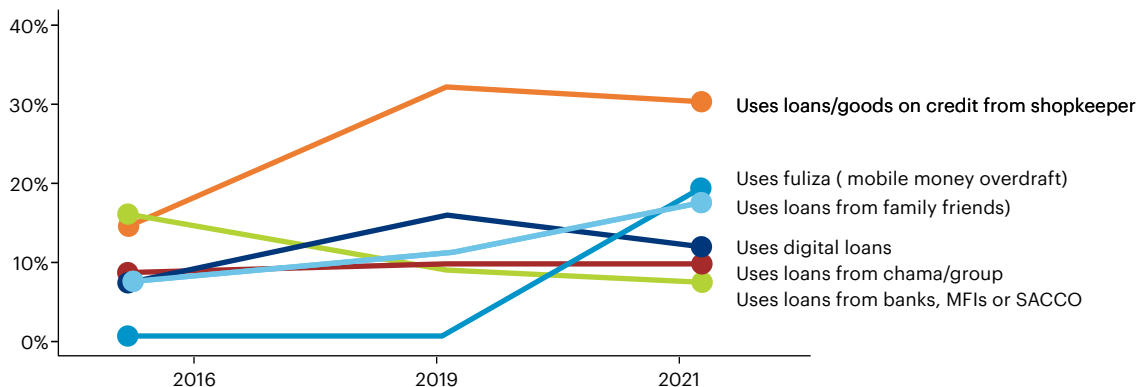
Between 2006 and 2021 formal financial inclusion more than tripled, rising from 27 to 84 percent with a formal account. But the pace of financial inclusion has been slowing. Between 2019 and 2021, the share of adults with a formal account only increased by 0.5 percentage points per year compared to increases of 2.7 percentage points per year between 2013 and 2019. Although not the sole reason, declining financial health has likely contributed to the slow-down in the adoption of formal accounts.

Those who said they did not have a bank account because they had no money to save increased by 21 percentage points between 2019 and 2021, from 35 to 56 percent. Those citing having “no job or regular income” as the primary reason rose from 22 to 35 percent and those citing that they “could not afford to maintain an account” rose from 19 to 23 percent.

Since 2016, fewer adults used informal and formal instruments to save and more adults channeled savings into mobile money accounts. While the pandemic likely incentivized substitution away from other instruments, these shifts may also relate to the drawing down of funds from relatively higher-cost, less liquid instruments (such as bank accounts or savings groups) to cope with rising costs, job losses or declines in income.

Similarly, **as financial conditions tightened, the demand for quick, low-value and flexible credit also rose rapidly.** Between 2016 and 2021, use of shopkeeper credit increased from 13 to 28 percent and use of “*Fuliza*” (a mobile money overdraft facility launched in 2019 by *M-Pesa*), reached 18 percent in 2021 (**Figure 8**). Meanwhile, the share of adults using loans to help them meet day to day needs more than doubled from 17 to 40 percent (**Figure 9**); and use of loans for coping with emergencies also rose significantly from 4 to 12 percent.

Figure 8:
% of adults (18+) using a savings instrument by type



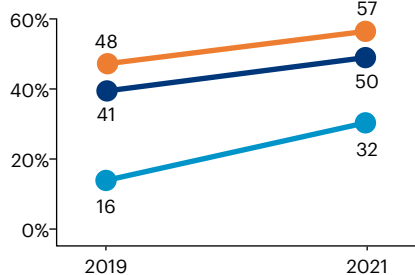
Between 2019 and 2021, usage of loans from family and friends, and shopkeeper credit more than doubled. In 2021, Fuliza, a mobile money overdraft facility - became the most common type of credit in use by Kenyans in the top wealth quintile.

Source: Author's calculations from FinAccess surveys.

The net result of these dynamics is that more adults are in debt, and more are having some trouble paying back loans. It is worth noting that between 2015 and 2021, the quality of the banking sector's loan portfolio also deteriorated: the value of non-performing loans as a share of total gross-loans increased steadily from 6 to 13.1 percent⁷.

Figure 9:
Adults (% 18+) that:

- currently have outstanding debt on one or more loans
- in past year, borrowed, sold assets or reduced food expenditure to repay loans
- in the past year, defaulted on one or more loans



Between 2019 and 2021, the share of adults holding some debt and who had trouble repaying loans increased.

Source: Author's calculations from FinAccess surveys.



⁷ Bank non-performing loans to total gross loans for Kenya were sourced from the World Bank World Development Indicators (Indicator ID: FB.AST.NPER.ZS).

Discussion

The sustained decline in financial health in Kenya from mid-2015 through mid-2021 documented in this paper occurs against a backdrop of economic growth during all but one of the intervening years alongside the consolidation and diversification of digital financial services that today, are nearly universally available. Nonetheless, individuals and families faced increased pressure on multiple fronts.


Compounding climate, price and employment shocks hitting a country with few formal safety nets; high inequality in the distribution of the opportunities generated by economic growth; and a demographic bulge of youth passing through secondary school-age and into the workforce are headwinds that have eroded the financial health of Kenyans. This is concerning because although the Kenyan economy has rebounded substantially since it contracted in 2020⁸, with food prices accelerating due to drought and the war in Ukraine, Kenyan households will continue to face financial pressures with a diminished ability to cope with additional shocks. Many of the strategies that Kenyans rely on for raising emergency funds – such as liquid savings, remittances and loans from friends and family or selling livestock - may be depleted or increasingly difficult to access.


Establishing a more robust foundation for broad-based financial health will require creating the conditions that boost the purchasing power of Kenyan households, freeing up income for greater savings and investment while boosting domestic demand for goods and services to support greater production and


diversification. Having made huge strides in providing widespread access to financial services, Kenya's financial sector also has an opportunity to align its efforts more deliberately with the financial wellbeing outcomes of its customers. The analysis in this paper suggests five policy directions to underpin positive financial outcomes for Kenyan households and more inclusive growth in the economy more broadly.

1. **Lower the cost of staple foods through improved productivity of Kenyan farmers and enhanced market efficiency.**
2. **Catalyze the growth of quality jobs, including investing in MSE growth.**
3. **Shift more of the burden of social protection from working adults to tax and donor funded social security programmes which enhance welfare and provide a foundation for inclusive growth.**
4. **Provide solutions to help families afford secondary school fees and invest in interventions that improve student learning outcomes.**
5. **Establish the regulatory framework, infrastructure and industry norms and capabilities that support the development of a financial services ecosystem that delivers positive financial health outcomes for retail customers and MSMEs.**

⁸ In 2020, Kenya's GDP declined by 0.3 percent and in 2021, Kenya's GDP increased by 7.5 percent (World Bank World Development Indicators, GDP Growth (Annual %), ID: NY.GDP.MKTP.KD.ZG)

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