Towards Responsible but "High-Cost" Digital Credit: Striking the Policy Balance in Developing Markets

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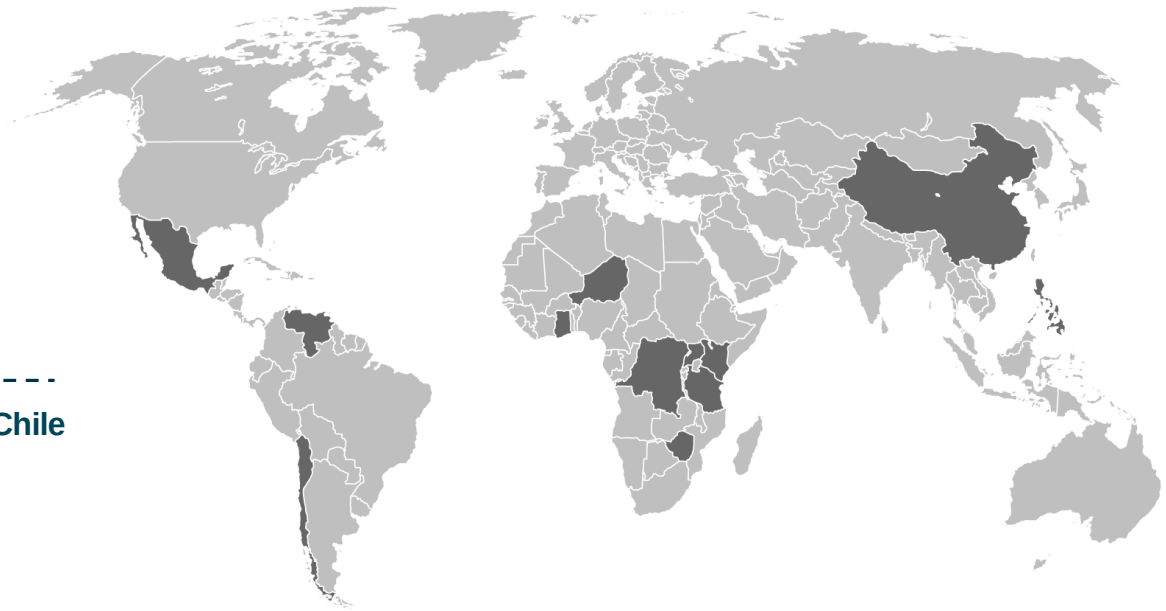
High-Cost Credit: The case of digital loans in Emerging Markets and Developing Economies

- Snapshot of developments
- What's different about digital?
- Key consumer risks
- Behavioral testing of solutions: pre-sale disclosure, post-sale communications, data usage awareness
- Implications for supervision in low-capacity environment

Digital Credit a Global Trend



Mexico

KONFÍO
kubo financiero

China

蚂蚁金服 ANT FINANCIAL
Tencent 腾讯

Venezuela and Chile

TIENDA PAGO

Philippines

Mynt A FRESH LOOK AT MONEY
AMP ADVANCED MERCHANT PAYMENTS

Kenya

M-Shwari
branch
KCB M-PESA ACCOUNT
KOPO KOPO
inVenture
Saida
Equitel

Tanzania

nimetimiza loans at your fingertips
cba m-pawa

Zimbabwe

ECOCASHLOAN$

DRC, Niger, Rwanda, Uganda

airtel

Ghana

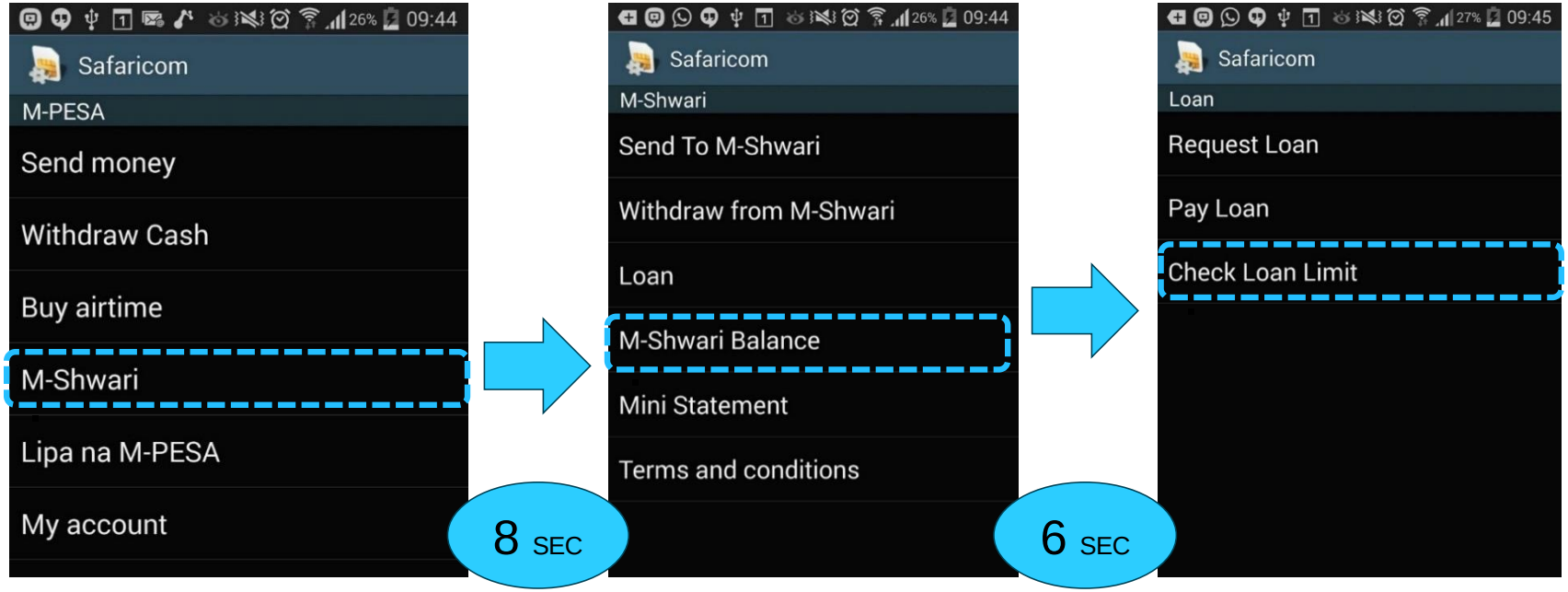
airtel

Key Attributes of Digital Credit

CONVENTIONAL CREDIT		DIGITAL CREDIT
Days	TIME TO MAKE DECISIONS	Instant
People's Judgment	RISK MANAGEMENT PROCESS	Automated
In Person	SENDING INFORMATION AND PAYMENTS	Remote

Example:

Providers	Safaricom, cba
Country/Launch	**Kenya** (2012)



Turn around time on account activation

Turn around time on transaction processing

Common features, diversity of models

Instant, Automated Remote plus …

- Very short-term
- High-cost (more commonly fees than “interest”)
- Roll-over feature
- Generally unsecured but asset-financing + …
- Bundled with deposits, insurance, non-fin svcs

Diversity:

- Segments (consumer, small biz, merchants)
- Models: banks, NBFIs, telcos, unregulated lenders, supply chain firms
- Lender + outsourced, JVs, crowdfunding platform

Digital Credit an Example of Cross-Jurisdictional Challenges

PRODUCT	LENDER	REGULATED BY A FINANCIAL SECTOR AUTHORITY?	OTHER PARTNERS
M-Pawa	Commercial Bank of Africa	YES	Vodacom Tanzania
Tigo Nivushe	Jumo	NO	Tigo Tanzania
Airtel Timiza	Jumo	NO	Airtel
Mkopo Rahisi	Inventure	NO	
L-pesa	L-Pesa Microfinance Tanzania	NO	None (but use e-money payment channels)
Branch	Branch	NO	None (but use e-money payment channels)
Get Bucks	Get Bucks Microfinance Limited	NO	None (but use e-money payment channels)

What's different about digital?

- Risks: new, higher/lower, incidence falls on different parties
- Product features: price, transparency, consequences
- New actors incl. beyond supervisory perimeter
- Recourse
- Credit risk: Algorithmic predictive power → transparency, debt stress, fairness (profiling)
- Data practices, credit information reporting, profile "portability"

Also …

- Can scale very fast
- Target segments may be more vulnerable
- Consumer behavior different and/or problematic

How does digital delivery of credit change consumer behavior and risks?

In a digital environment, do borrowers. . .

… **resist temptation** better/worse with unexpected SMS offer? **[take-up rate]**

… focus adequately on how they will repay? [**hyperbolic discounting**]

… **perceive turning down offer as a loss**, or feel "honored" to receive an offer that is "pre-approved"? **[push marketing]**

How does digital delivery of credit change consumer behavior and risks?

In a digital environment, do borrowers. . .

… change the amount of credit they take because of ability to check their loan limit on the handset, instead of independently requesting the loan amount? **[framing and default options]**

… "feel" loss or gain of digital money **differently than cash**?

We utilized behavioral design insights to test impact of different information disclosure + message content

COGNITIVE LOAD
Helps relate to the challenges of adopting the behavior and lower the perceived barriers

PRICE SALIENCE
Ensuring that value is clearly communicated and abstract benefits are made more tangible

LOSS AVERSION
Valuing losses more than equivalent gains

CALL TO ACTION
Driving immediate behavior to counter inevitable procrastination

SOCIAL NORMS
Being influenced by the decisions and actions of those around us

CONCRETE BENEFITS
Connecting the product with tangible, immediate economic benefits

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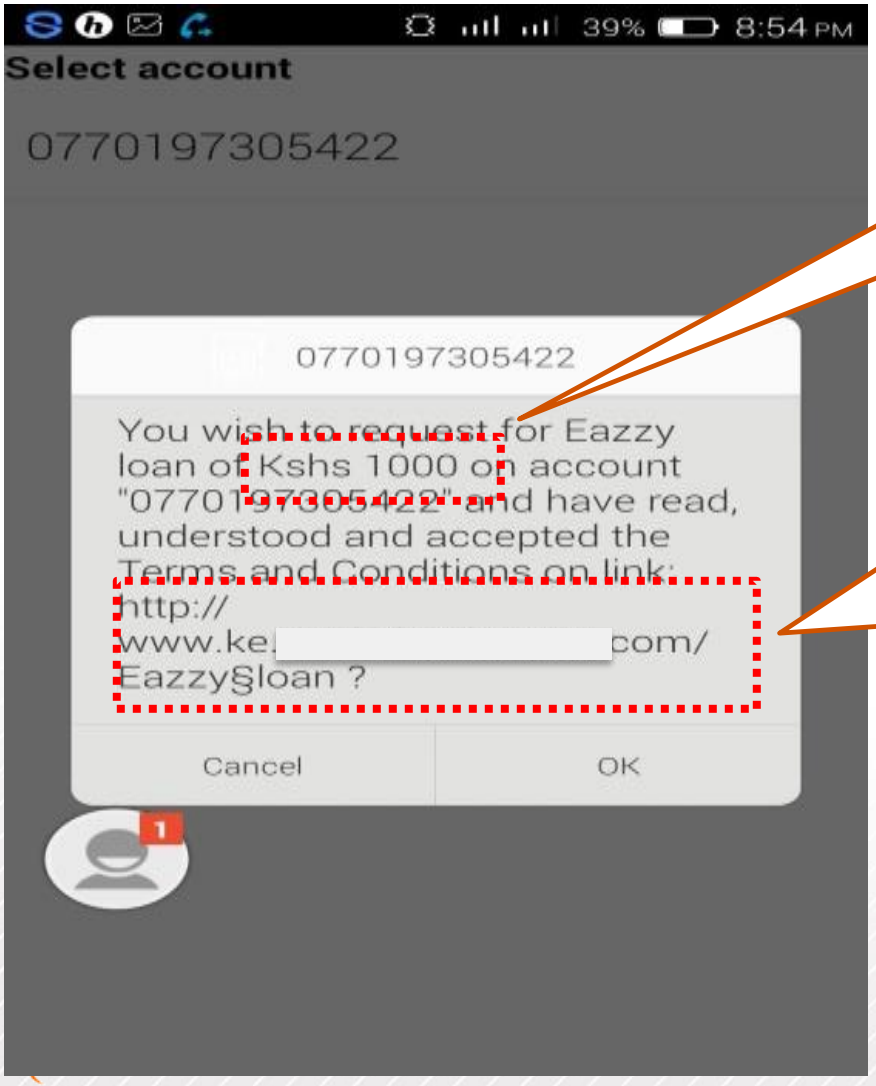
Poor disclosure in high cost consumer credit

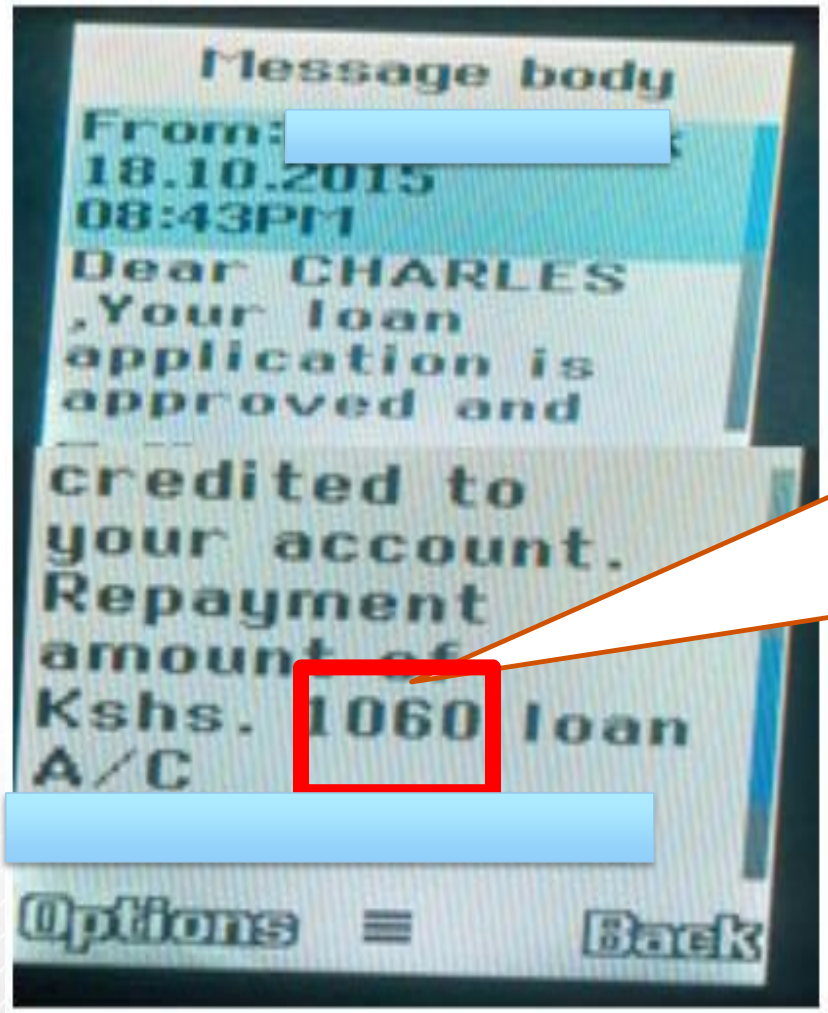


No fees mentioned (trust me, this loan is not 0% interest)

Open the URL to view the loan Terms and Conditions

-What about those with feature phones?
-Areas without internet connectivity?

Poor disclosure in high cost consumer credit



-Most borrowers thinks that the interest rate on this loan product is **2%** but varies between 2%-10%.

- In this case the interest rate is **6%**.

Information released post-purchase.

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Better disclosure can actually benefit providers' bottom line

Jumo: Digital lender active in Kenya and Tanzania

Challenge: How can CGAP use behavioral design to improve disclosure and consumer borrowing behaviors?

1. Lab Experiment

What? Decision-making games testing financial **product valuation and borrowing behavior**
Why? Understand **deep behaviors** of consumers such **as trust, time preference, risk appetite**

2. Field Experiment

What? **Airtel Money** Transfer to **large sample** of respondents in **Busia** region
Why? Test various **reminder messages** to identify shifts in **valuation** and **understanding** of **repayment** protocol

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Separating finance fees leads to better borrowing decisions

Choose your repayment plan:
1.Repay 228 in 45 sec
2.Repay 236 in 1min and 30sec
3.Repay 244 in 2min and 25sec

vs.

Choose your repayment plan:
1.Repay 200 + 28 in 45 sec
2.Repay 200 + 36 in 1min and 30sec
3.Repay 200 + 44 in 2min and 25sec

Clarifying interest rates led to a **reduction in default rates** on first loan cycles from **29.1% to 20%**

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Does digital credit really have to cost so much?

Yes!

- Relatively “thin file” consumers
- Short-term, unsecured loans are always expensive

No!

- 4 years in -- some providers still not doing risk-based pricing
- Loan origination costs are significantly lower
- Competition barriers hindering competitive pressures
    - Proprietary treatment of data
    - Network effects of existing voice and mobile money channels

M-Shwari loan charge not interest, CBA tells customers

MONDAY SEPTEMBER 19 2016

email print

A Commercial Bank of Africa (CBA) branch along Kirinyaga road on March 10, 2016. The Commercial Bank of Africa (CBA) says it will not reduce the facilitation fee it charges on M-Shwari. FILE PHOTO | SALATON NJAU

By VINCENT ACHUKA

"There is no interest levied on M-Shwari loans. What we have is a one off facilitation fee of 7.5 per cent charged at disbursement."

Active choice approach increases viewing of T&Cs and reduces delinquency rates

Welcome to TOPCASH:

1.Request a loan
2.About TOPCASH
3.View T&C's

→

Choose your loan amount:

1.KES 200
2.KES 400
3.Exit Loan

VS.

Welcome to TOPCASH:

1.Request a loan
2.About TOPCASH

→

Kindly take a minute to view Terms and Conditions of taking out a loan:

1. View Ts&Cs
2. Proceed to loan request

Terms and Conditions **viewing increased from 9.5% to 23.8%** by making it an active choice

Reading the Terms and Conditions led to a **7% absolute drop in delinquency rates**

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SMS Field Testing Experiment: Reminder Message Framing and Repayment Effects

Reminder messaging:

Respondents were recruited into a lending cycle where they were offered 100 KES on enrollment, but given 500 KES if they repaid that 100 KES in one week.

Reminder messages were adjusted to accommodate different behavioral themes.

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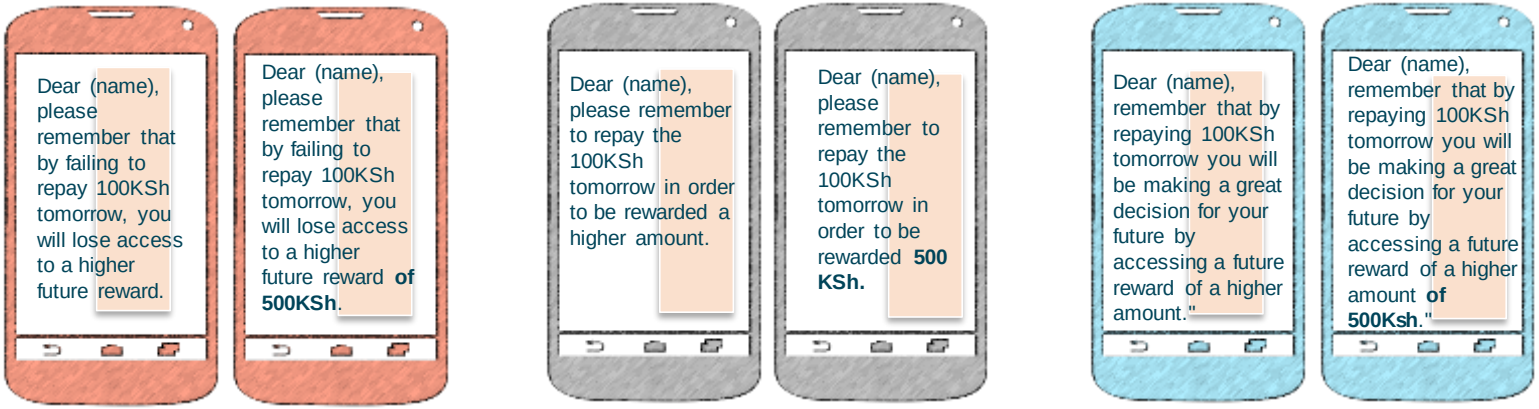
SMS Field Experiment: Results from First Round Testing



Timing and Planning

Respondents who received evening reminders were **8% more likely** to repay their loan than in the morning

Gender Effects

Treatments had a significant **positive** effect on men, but a significant **negative** effect on women.

Education and Age

Future goal had a positive (but not significant) effect, but this was significant among **the educated and older groups**

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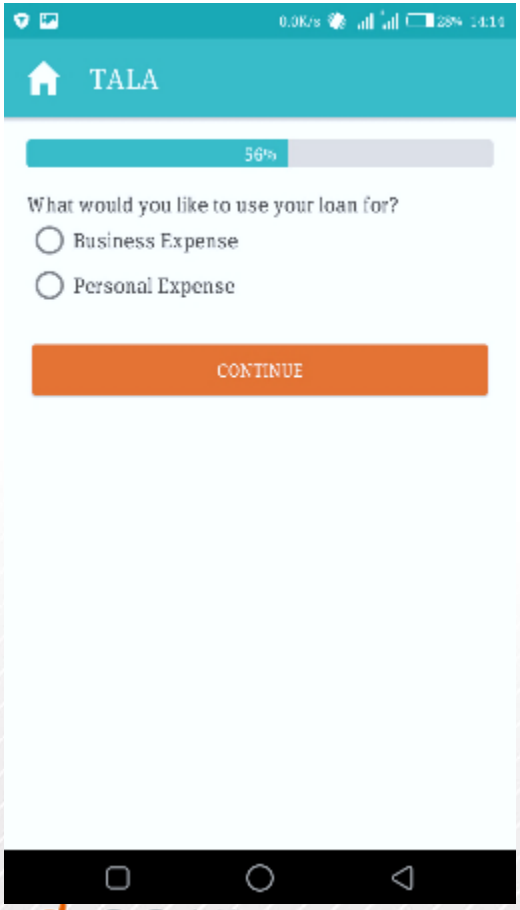
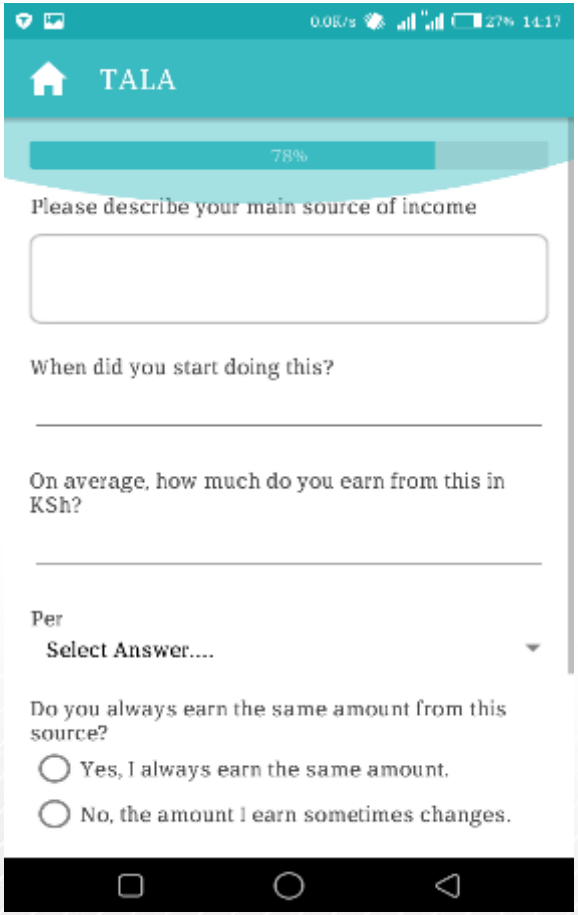
Could default settings be a simple solution to behavioral risks?

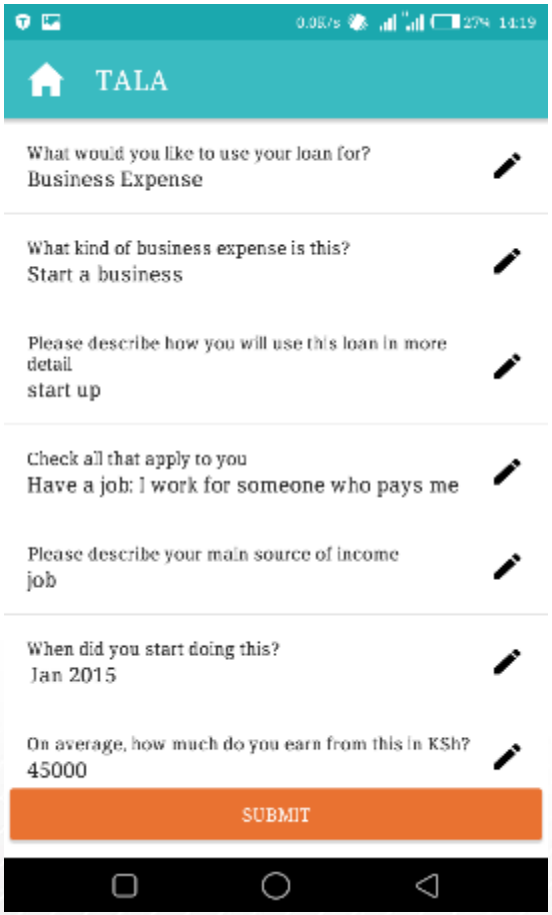
- Marketing: Opt-in to credit offers (or at least “1 and done” marketing)
- Loan amounts: Setting amount below maximum
  - Ordering in menu
  - Placement of sliders on apps
  - In-app/menu advice

Automated Suitability Assessment

Loan pre-qualification information and existing data trails could allow for increased segmentation and advice







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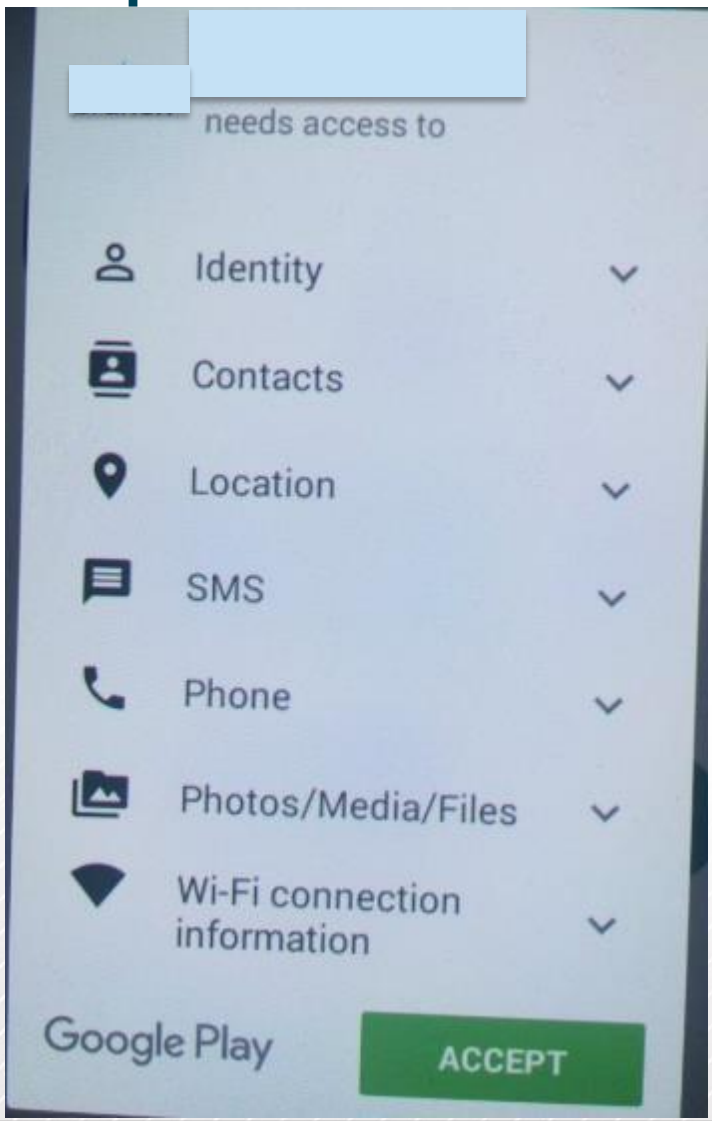
Data Usage & Ownership in Digital Credit

Accept Terms & Conditions



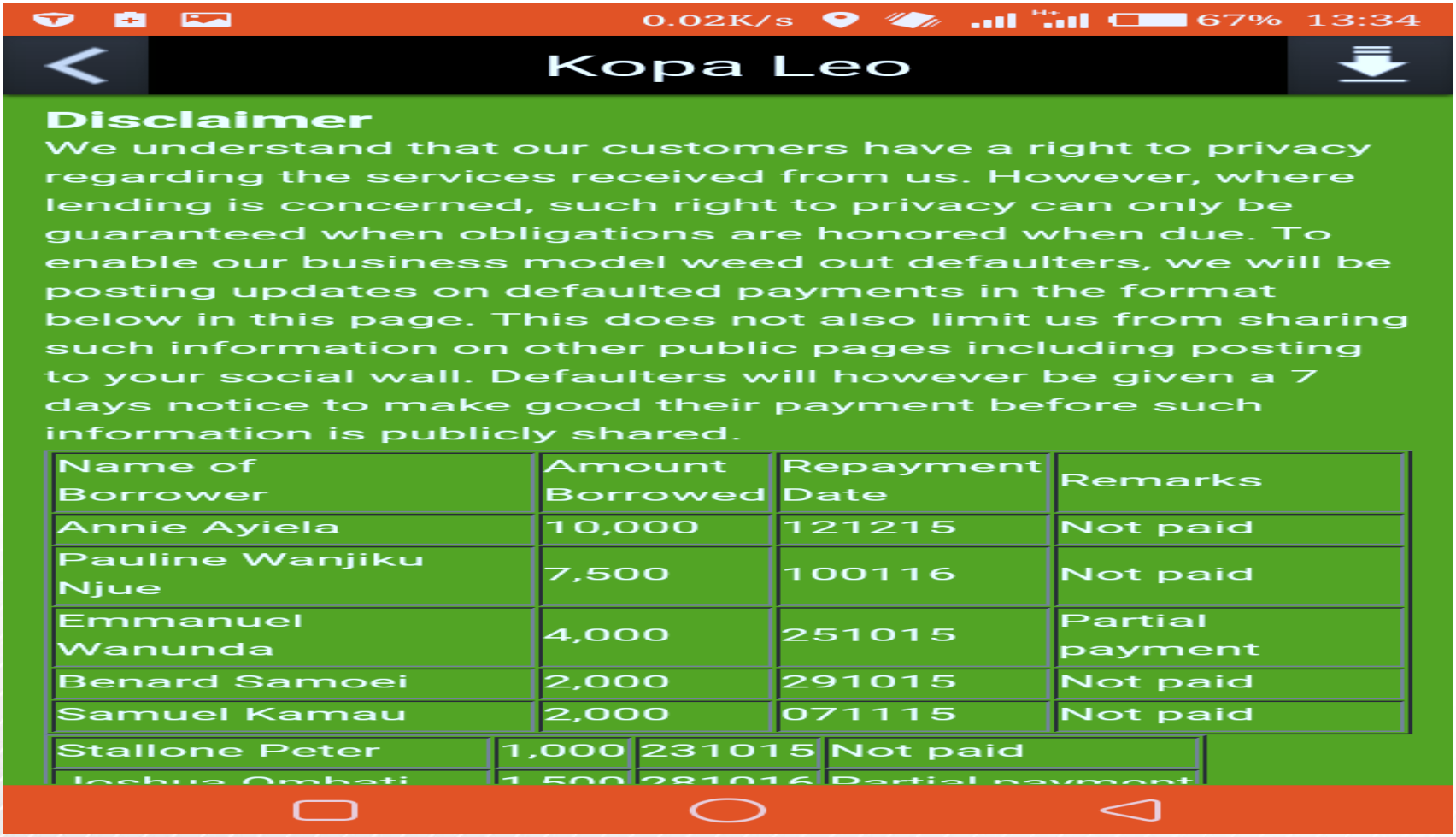
Standard Form Contract Data Usage Disclosure

"Each time you visit one of our sites or use one of our Apps we may collect the following information:

technical information, including the types of mobile device you use, unique device identifiers (for example, your Device's IMEI or serial number), information about the SIM card used by the Device…

information stored on your device, including contact lists, call logs, SMS logs, contact lists from other social media accounts, photos, videos or other digital content…"

Data Usage & Ownership in Digital Credit



Name of Borrower	Amount Borrowed	Repayment Date	Remarks
Annie Ayiela	10,000	121215	Not paid
Pauline Wanjiku Njue	7,500	100116	Not paid
Emmanuel Wanunda	4,000	251015	Partial payment
Benard Samoei	2,000	291015	Not paid
Samuel Kamau	2,000	071115	Not paid
Stallone Peter	1,000	231015	Not paid
Joshua Ombati	1,500	281016	Partial payment

Digital Credit Supervision (+ need for Supervisory Coordination)

- Reporting requirements and market monitoring
- Licensing/registration/partnerships
- Product approval or non-objection (sandboxing)
- Off-site and on-site examination
- RegTech/SuperTech?

"Must-haves" may require multiple authorities to act:

- Remove regulatory arbitrage issues (Competition authority) -- Kenya
- Reporting/monitoring via e-money channel (Central Bank) – Tanzania
- On-channel pre-purchase disclosure (Central Bank + telco authority) – Kenya
- Consumer consent, data usage and portability (Competition, Central Bank, telco authority)
- Rules on marketing/sales (Competition, Central Bank, telco authority)

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Advancing financial inclusion to improve the lives of the poor

Cooperazione Italiana Ministero degli Affari Esteri

Ministry of Foreign Affairs of the Netherlands

IFC International Finance Corporation

Foreign Affairs, Trade and Development Canada
Affaires étrangères, Commerce et Développement Canada

Bill & Melinda Gates foundation

Omidyar Network

Schweizerische Eidgenossenschaft
Confédération suisse
Confederazione Svizzera
Confederaziun svizra
Swiss Agency for Development and Cooperation SDC

MetLife Foundation
Ensuring Access. Empowering Communities.

Michael & Susan Dell Foundation

The Government of the Grand Duchy of Luxembourg

FMO Entrepreneurial Development Bank

Ministerio de Asuntos Exteriores y de Cooperación
aecid

UNDP

afd Agence Française de Développement

ILO

USAID From the American People

UKaid from the British people

giz

Federal Ministry for Economic Cooperation and Development

KFW Bank aus Verantwortung

Sida

Australian AID

citi

IFAD Investing in rural people

Ford Foundation

Norad

World Bank Group

UNCDF

The MasterCard Foundation

MIF Multilateral Investment Fund Member of the IDB Group

ADB

European Investment Bank

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