Digital Credit: Pricing and pricing transparency

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CDC-SPTF FinTech Webinar Series

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Part 1: Digital Credit – Something(s) old, something(s) new

- Some of the conversations around price in digital credit echo debates from microfinance in the 1990s and early 2000s
- But the digital delivery/collection channels and new data sources also make possible product and pricing innovations not feasible with traditional in-person microfinance
Wow, the interest rates on these loans are high! Why are these loans so expensive?

<table>
<thead>
<tr>
<th>Provider</th>
<th>Loan Range (Ksh)</th>
<th>APR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equitel Eazzy Loan</td>
<td>250 – 50,000</td>
<td>12-170%</td>
</tr>
<tr>
<td>KCB M-Pesa</td>
<td>50 – 1,000,000</td>
<td>49 – 73%</td>
</tr>
<tr>
<td>M-Shwari</td>
<td>100 – 20,000</td>
<td>91%</td>
</tr>
<tr>
<td>Saida</td>
<td>Up to 25,000</td>
<td>91% and up</td>
</tr>
<tr>
<td>Tala</td>
<td>500 – 50,000</td>
<td>61 – 243%</td>
</tr>
</tbody>
</table>

Source: http://www.cgap.org/blog/digital-credit-kenya-time-celebration-or-concern
Digital Credit: Something old

Do consumers even understand what they are signing up for? How do we make prices transparent and meaningful?


- Survey of Kenyan consumers before and after improvements in pricing disclosure in DFS enforce by Competition Authority of Kenya.
- High usage of digital credit in sample: 72% of baseline respondents, 79% of endline respondents
- Dramatic increase in M-Shwari borrowers correctly remembering cost of loan from baseline to endline for Ksh200, Ksh500 and Ksh1000 (See Table)
- Given high cost of digital credit in Kenya, this finding has significant implications for responsible borrowing and supporting price competition

Source: http://www.cgap.org/blog/kenya%E2%80%99s-rules-mobile-money-price-transparency-are-paying

### Consumer Estimates of Cost of their last M-Shwari Loan, Baseline vs. Endline

<table>
<thead>
<tr>
<th>Loan Amount</th>
<th>Baseline</th>
<th>Endline</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ksh200 Loan</td>
<td>52%</td>
<td>80%</td>
</tr>
<tr>
<td>Ksh500 Loan</td>
<td>0%</td>
<td>38%</td>
</tr>
<tr>
<td>Ksh1,000 Loan</td>
<td>0%</td>
<td>56%</td>
</tr>
</tbody>
</table>

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Digital Credit: Something old

Are these loans helping the poor and underserved?

Tanzania Digital Credit Survey (CGAP, 2017)

- 21% of Tanzanian phone owners have taken a digital loan
- Borrowers are more likely to be male, younger, and urban, and 3x more likely to have a bank account
- 33% report using the loan for business purposes, 37% for ordinary household needs and 36% for airtime
- 31% of borrowers have defaulted in past, and 56% have paid late
- 27% of borrowers report paying fees they didn’t expect, didn’t understand, or had money directly withdrawn from mobile wallet
- 9% report having reduced food purchases to repay a loan

Source: http://www.cgap.org/blog/helping-or-hurting-10-facts-about-digital-credit-tanzania
Digital Credit: Something old

Who is monitoring all these new providers and product types?

- Mix of regulated banks and MNOs and unregulated lenders offering digital credit
- In some African markets where they have scaled consumer protection regulation and supervision is limited

<table>
<thead>
<tr>
<th>PRODUCT</th>
<th>LENDER</th>
<th>REGULATED BY FINANCIAL SECTOR AUTHORITY?</th>
<th>OTHER PARTNERS</th>
</tr>
</thead>
<tbody>
<tr>
<td>M-Pawa</td>
<td>Commercial Bank of Africa</td>
<td>YES</td>
<td>Vodacom Tanzania</td>
</tr>
<tr>
<td>Tigo Nivushe</td>
<td>Jumo</td>
<td>NO</td>
<td>Tigo Tanzania</td>
</tr>
<tr>
<td>Airtel Timiza</td>
<td>Jumo</td>
<td>NO</td>
<td>Airtel</td>
</tr>
<tr>
<td>Tala</td>
<td>Inventure</td>
<td>NO</td>
<td></td>
</tr>
<tr>
<td>L-pesa</td>
<td>L-Pesa Microfinance Tanzania</td>
<td>NO</td>
<td>None (but use e-money payment channels)</td>
</tr>
<tr>
<td>Branch</td>
<td>Branch</td>
<td>NO</td>
<td>None (but use e-money payment channels)</td>
</tr>
<tr>
<td>Get Bucks</td>
<td>Get Bucks Microfinance Limited</td>
<td>NO</td>
<td>None (but use e-money payment channels)</td>
</tr>
</tbody>
</table>
Loan tenure can be more flexible

- Kopo offers merchant loans with no fixed tenor—the repayment is made as a percentage of each merchant payment transaction. So loan repayment happens on pace with business activity.
- Similar models could be developed to reflect seasonality in various sectors of economy.
Loan terms can be adapted to include new repayment and penalty structures

- Jumo offering pay-as-you-use daily interest rates
- Easy to apply declining balance interest
- Branch not charging penalty fees
- Small-value repayments economically viable
We can more easily test and measure efforts to improve consumer understanding

M-Pawa Interactive SMS Experiment in Tanzania:

- Increased savings balances by Tsh4,447
- First loan payments Tsh1,730 larger
- Repaid loans 5 days sooner

Digital Credit: Something(s) new

*We can more easily test and measure efforts to improve consumer understanding*

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

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

Separating finance charges from principal in a lab experiment reduced default rates from 29% to 20%

Digital Credit: Something(s) new

*We can more easily test and measure efforts to improve consumer understanding*

By making it an active choice, viewing the T&Cs increased from 10% to 24%

Delinquency rates for borrowers who read the T&Cs were 7% lower

Digital Credit: Something(s) new

We can find new ways to gather data and apply customer segmentation

Let’s now hear from our two digital credit providers on their thoughts regarding pricing and price transparency in digital credit
Part 2: Digital Credit – Can we improve pricing?

Question 1: The cost of lending

▪ Is there more space to drive down costs not related to risk (e.g. capital, disbursement, collection)?

▪ What are the most promising ways to reduce risk further—and in turn reduce cost?
Part 2: Digital Credit – Can we improve pricing?

Question 2: Digital data and lending

▪ What do you think are the most meaningful types of data for digital credit?

▪ Do you think we are sufficiently addressing issues of data privacy and protection in digital credit? If not, what more can be done?
Part 2: Digital Credit – Can we improve pricing?

Question 3: Increasing competition

▪ How do we increase competition, choice and product diversity in digital credit?

▪ Do we need any policy reforms—existing or new—to achieve the potential of digital credit?
Questions from the audience?