Session Title: Digitizing Finance: Opportunities and Risks
Date: February 21, 2018
Time: 9 a.m. India Standard Time
Speakers: Bindu Ananth, *Dvara Trust*; Greta Bull, *CGAP*; Graham Wright, *MicroSave*; Prasad GR, *Capital Float*; Buhle Goslar, *JUMO*

- Bindu Ananth started the plenary by highlighting the number of newer risks or amplification of existing risks that arise with the digitization of finance, such as discrimination, denial of sale, or inadequate grievance redressal. She went on to recognize the high promise of digital financial service providers (FSPs), such as expanding to new markets or providing customized services and a reduction of cost of delivering these services. She asked the panelists to address whether these benefits are worth the associated risks they bring along and how a traditional FSP should adapt to these new digital technologies.
- Greta Bull started by saying that the world of finance is seeing a lot of exciting changes with new technologies and new business models. She highlighted the continued importance of traditional institutions but said there is a need for these institutions to adapt to the changing times.
    - The service provider should have a clear idea for using digital technologies along with an associated business plan. The use of technology without a clear idea/business plan is the biggest risk of new technology for any provider.
    - She also highlighted the risk associated with large number of outreach agents. Some mobile money operators spend more than half of their revenues on agent commissions. She suggested FSPs start small and focus on actual usage of their services rather than simply wide reach.
    - She emphasized that traditional institutions should invest in their IT infrastructure and do so wisely with an eye on the future, as IT infrastructure is far more difficult and costly to change. This infrastructure should be flexible to grow fast and must enable interaction within the institution.
    - She also emphasized the importance of existing customer data that many traditional institutions possess rather than using unstructured third-party data. While recognizing difficulties associated with digitization of paper records, she emphasized the need for financial service providers should start collecting data digitally.
    - She also highlighted the importance of putting the customer at the center and understanding them better in the transition to digital finance.
    - She said it is well worth it to think about suitable partnerships, especially with digital technology players. It is imperative that FSPs educate themselves about the larger finance ecosystem and associated changes.
    - Greta concluded by saying while there are many risks of digitizing for FSPs, such as operational risks, reputational risks, and the challenge of changing mindsets from thinking about individuals rather than groups, FSPs must enter the digital age as the world is changing.
- Graham Wright started his presentation by saying that digital financial service providers are the future and are targeting the customer segments of FSPs. FSPs must also take this opportunity and incorporate digital services sooner rather than later.
    - He also highlighted the fact that digital credit is not a homogenous product; it differs across a spectrum from small value consumer credit to credit for SME.
    - He gave the example of Kenya as the ‘cradle’ of digital consumer credit with 5 million users, which is mainly used for household consumption purposes.
    - Graham then highlighted 3 ‘personas’ of consumer digital credit users.

    - Repayer: They regularly repay their debts but are not rewarded for this. At best, they are given more credit.
    - Juggler: They have multiple loans from many sources and often repay their digital credit providers last.
    - Defaulter: They experiment with digital credit often for frivolous purposes due to its easy accessibility.
  - Graham highlighted the fact that a third of first-time digital borrowers default, which has had adverse impact on the credit rating of many Kenyans.
  - He said digital consumer credit can be a case of thin file lending, as such lending often depends on light digital footprints for credit underwriting. Currently, they almost exclusively depend on credit histories and mobile usage. There is an opportunity to use a variety of other data, such as transaction histories, payments, or sales data. But access to such data requires infrastructure like digital IDs and digital lockers. Here, Graham highlighted the case of India as an important one to study in contrast to the kind of data that is available with Silicon Valley giants.
  - Graham then talked about the other end of digital credit as SME credit, where digital footprints are much larger and allow for more effective use of digital services at lower risks. Graham concluded by saying that in-between small value consumer credit and SME credit is where the opportunity for FSPs lies in the space of digital credit. FSPs can also help manage digital credit providers manage their micro loans better.
- Question from Bindu to panelists: Give an example of a digital credit product that excites you.
  - Buhle Goslar highlighted the case of Musoni in Kenya, which is maturing the case for digital services in the agriculture sector.
  - Prasad GR gave the example of LazyPay due to its highly customer centric product.
  - Graham highlighted the case of Equity Bank in Kenya, which has an intuitive app that can be used for saving towards a goal. Equity Bank has also been able to transition to agent-based transactions as the primary form of interacting with the bank.
  - Greta said digital payments as a whole are very exciting as it is the primary use of any bank account and helps build digital trails for its users.
  - Bindu gave the example of Even in USA, which is money management service that helps smooth out uneven earnings flow for its users.
- Prasad provided an overview of Capital Float, which provides digital credit to SMEs in India.
  - He said Capital Float serves digital credit to the underserved SME segment using a "ecosystem" approach by tying up with platforms like payments, remittances, etc. It then extends credit to merchants who operate on these platforms. The primary data to understand and underwrite these consumers is provided by the platform, and a specific product is created to suit the borrower. They use Aadhaar, components of India stack, and e-contracts to deliver the credit.
  - The process starts with partnering with a platform, which provides pre-qualified leads. Its algorithm decides the sanction, volume of credit, period of repayment, etc. The field executive visits the client to explain the product and also uses digital services of Aadhaar to confirm identity; an e-contract is signed digitally. The credit amount is generally provided via the platform to ensure the final use case.
  - The major non-digital component remaining is collection. This is its major growth constraint.
- Buhle highlighted that JUMO has recently started a micro-savings product pilot in Tanzania and Uganda.
  - Customers saw a lot of value in such a product as they see savings and credit together in the context of their goals. She also highlighted that women tend to use micro-savings

  products more than digital credit products. Customers said it is important that micro savings accounts are a reliable store of value that is not eroded by numerous fees. Customers give less importance to interest on their savings but do link them to future credit availability.
  - She highlighted three important aspects for micro-savings products: predictability, simple structure and transparency. Thus, the reliability of digital services, including those provided by any partners, is of very high importance.
- Question from Bindu to panelists: What are the new forms of harms that are due to this adoption of digital credit/savings products?
  - Greta emphasized that it is important with this transition to digital services to continue to give the customer a sense of control. She also highlighted the risks posed by large scale data aggregators/harvesters, especially related to the privacy and security of this data.
  - Graham agreed with Greta, providing the example that today, even if a customer agreed to pay for services, there was no opting out of the data collection. He also highlighted the risks associated with "frictionless service" combined with aggressive push marketing. This combination has led to high levels of delinquency associated with digital credit.
- Question form Bindu to panelists: What is the importance of appropriate privacy policies and about human-touch – especially related to grievance redressal – with digital services?
  - Buhle said that JUMO customers "own" their digital footprints, but JUMO provides adequate security to this footprint. She also highlighted that many players do not provide adequate security. With customer grievance, the contact center of the associated partner is the first point of contact; upon escalation JUMO contact centers are involved.
  - Prasad said that Capital Float does not share personal data even with internal employees unless necessary. They employ high standards of anonymization and data localization to maintain security. With its services, field executives act more like relationship managers, maintaining contact post-loan disbursal and addressing grievances. They also have email- or call center-based support.
- Question from the audience (Beth Rhyne, CFI): Please comment on the various harms that have affected customers of digital credit regarding their data privacy.
  - Greta said that currently fraud related to individual transactions is rare, but fraud at central levels does occur. She said that there may be a lot of client harm occurring which we do not know about, such as profiling. It is difficult to prove such harm and the potential for it; there is no real solution for it currently.
- Question from the audience (Tanaya, CGAP): Is it valuable to introduce some friction in digital transactions in developing countries?
  - Buhle said that the value depends on the customers' mental models. For example, today there is often a higher volume of calls related to marketing rather than grievance redressal, but she expects this to no longer be a point of friction in future.
  - Graham emphasized that there needs to be a balance, and he said that service providers must look towards a "customer-defined friction," which will require creative thinking on the part of the service providers.
- Question from the audience: What are your views on the security of public digital infrastructure like digital IDs? What about authentication failures linked to such infrastructure and its impact on business and subsequent loss of benefit to customers?
  - Prasad said there are continuous changes to public infrastructure that lead to increased costs, but there are fewer authentication failures and higher overall reliability due to improvements. He also highlighted that tighter regulations also contribute to higher cost for the business.

  - Graham added that authentication failure is more of a problem in rural areas, and in many cases it's due to cheaper bio-metric devices. But he felt that the overall higher risk premium with current digital credit service is what is stealing the benefits of consumers.
- Question from the audience: What are the risks associated with FSPs partnering with digital service providers, especially associated with data privacy?
  - Greta said there is no single answer to this, as it depends on the market and the negotiating power of the parties in the conversation. She also highlighted that currently FSPs don't know how to negotiate well with digital service providers, which is a risk.
- Question from audience: How can you address customer education related to the use of digital services?
  - Buhle said JUMO looks at how customers use the information provided. JUMO has also tried to understand customer-agent interactions. It often rolls out agent products before direct-use products as agents provide a lot of feedback. Sometimes JUMO also uses direct campaigns or skits in market areas for customer education. She highlighted that peer-to-peer communication among customers remains the most important part of education and that providers must constantly experiment in this field.
  - Prasad said Capital Float provides help to its customers on using its app, which it has designed to provide a specific value proposition that benefits its customers.