

Tiny Loans, Big Questions:

Client Protection in Mobile Consumer Credit



Keeping clients first
in financial inclusion

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Responsible Mobile Credit: Contours, Not Yet Consensus

The mobile financial services ecosystem is vast, fast-growing, and ever-changing. Globally, there are more than 500 million registered and 174 million active mobile money accounts, and mobile money services are accessible in two-thirds of low- and middle-income countries.¹ The growth and potential of digital financial services for the underbanked has generated significant enthusiasm from financial sector stakeholders, including development economists. One study showed that access to mobile payments has lifted nearly 200,000 Kenyan households above the poverty line.²

While mobile financial services can bring important and widespread benefits, it is also important to examine the risks. In such a rapidly evolving sector, it is no surprise that there has so far been relatively little discussion or consensus-building on emerging consumer harms these new services and business models may create. However, this is beginning to change. There is growing recognition that mobile financial services can pose significant risks to clients. Instances of situation-specific consumer research document such risks, and interest is growing among financial service providers, investors, and policy makers to acknowledge risks and develop appropriate mitigation.

The Client Protection Principles

1. *Appropriate Product Design and Delivery*
2. *Prevention of Over-Indebtedness*
3. *Transparency*
4. *Responsible Pricing*
5. *Fair and Respectful Treatment*
6. *Privacy of Client Data*
7. *Mechanisms for Complaint Resolution*

The Smart Campaign is working with mobile financial services providers to examine emerging consumer risks. The Campaign is a global effort to embed principles and practices of consumer protection throughout the financial inclusion sector. The Client Protection Principles (CPPs, see box) have been the cornerstone of the Smart Campaign's work since it began with a focus on microfinance nearly 10 years ago. The Campaign defined good practices, operational standards, and regulatory language that applied the Principles to the risks identified in microfinance business models. It also led a process of consensus-building and adoption among sector participants, and today the Smart Campaign's standards are known and applied around the globe. As fintech providers are looking for concrete ways to evaluate and improve their practices to avoid consumer harm, the CPPs provide a useful framework to identify key consumer risks and possible mitigation strategies.³ As the Smart Campaign begins to focus more on digital financial services, in this Brief, we will examine a mobile product that has generated both significant scale and a certain amount of controversy: the very small instant consumer loans that have ballooned from 11 deployments in 2011, to 52 in 2016, with a particular concentration in East Africa.⁴ In just a few years, through models such as M-Shwari, M-Pawa, Tala and Airtel Money, tens of millions of people have borrowed tiny amounts over their phones. These services represent an enormous increase in financial inclusion. They address a fundamental consumer need previously unavailable to

lower income people from the formal financial system: the need for very short-term money management tools to cope with income and expense volatility. While these instant, small mobile consumer loans are in many ways a boon, they also contain, and in some cases heighten, risks for their users.

This Brief enumerates and discusses emerging consumer risks posed by these instant small mobile loan products, using the Client Protection Principles as an organizing framework. We hope and intend that this Brief will assist participants in the mobile financial sector to articulate and build a consensus about responsible practices, though this framework should not limit the discussion.

The Promise and Peril of Mobile Credit

The Smart Campaign is interested in small, instant mobile consumer lending models because of their rapid scaling and use by people at the base of the pyramid. In Kenya for instance, M-Shwari has issued more than 60 million loans; one in five Kenyans reported having borrowed via the service.^{5 6} And next door in Tanzania, M-Pawa reportedly made loans to nearly 5 million borrowers within its first two years of operations.⁷ Indeed, the Kenya FinAccess 2016 survey reported that respondents were much more likely to cite digital credit (40.9%) than traditional banks (6.7%) or microfinance (1.8%) as sources they use in times of need.⁸ This is an enormous achievement in a short time.

Table 1. Illustrative Deployments of Small Mobile Consumer Credit

| Product | Country | Model | Launched | Loan Size | Fees and/or Interest Rates | Typical Tenure |
|-----------------------|----------|---|----------|-------------------------------------|----------------------------|----------------|
| M-Shwari | Kenya | Commercial Bank of Africa and Safaricom | 2012 | Average US \$12 ^{ix} | 7.5% facilitation fee | 1 month |
| Tala | Kenya | Tala App | 2014 | Average US \$50 ^x | 11-15% fee | 1 month |
| M-PAWA | Tanzania | Commercial Bank of Africa through Vodacom | 2014 | Up to US \$50 | 9% facilitation fee | 1 month |
| Airtel Money Kutchova | Malawi | FDH Bank through Airtel | 2016 | From US \$0.7 to \$70 ^{xi} | 10% facilitation fee | 7 days |
| Airtel Money Bosea | Ghana | Fidelity Bank Ghana, Tiaxa through Airtel | 2016 | Average US \$50 ^{xii} | 10-20% monthly | 1 month |

The defining characteristics of the small mobile consumer lending model include:

- **Start to Finish Digitization:** Marketing, credit appraisal, disbursement, loan repayment, and customer support are done digitally. While a mobile lender often works with a mobile network operator (MNO) and its agent network, there is sparse direct interaction between the borrower and the lender.
- **Small Amounts That Grow:** Lenders start with loans as small as several dollars. With successful repayment, loans can increase to as much as several hundred dollars.
- **Short-Term:** Loan tenure is typically several weeks, 30 days; or up to 50 days.
- **Instant:** Algorithms allow for quick, automated decisions. Individuals can receive their loans almost instantaneously.

"At 17:46 on a Monday, a mobile money customer transfers Shs20,000 to a bank account known as MoKash. Two minutes later, the customer receives a message, that in part, reads "...You qualify for a MoKash loan Shs30,000." The customer goes ahead and applies for the loan and at 17:51 hours, the loan is approved."

*Groundbreaking: When the mobile phone became a bank
DailyMonitor 25 08/16/16*

- **Alternative Data Analytics:** These models operate in places where a vast swath of the population has a mobile phone but not a credit history. Lenders combine data from new sources to assess creditworthiness, including phone calls, texts, airtime top-ups, data use, mobile money transactions, utility payments, GPS data, social media use, Wi-Fi network use, mobile phone battery levels, contacts lists, and many other data points.⁹

There is much to like about small mobile consumer loans. As a tool for financial inclusion, mobile credit can unlock access for consumers who have no formal financial footprint, addressing a ubiquitous and important problem. These loans are intended to assist people to manage stress-inducing income and expense fluctuations common to poor households: an immediate, consumption-smoothing inflow is often helpful.¹⁰ While the products currently on the market appear fairly uniform, the startup ecosystem has ushered in new design methodologies that allow for rapid prototyping and have the potential for customer segmentation and customization.

The convenience and ease-of-access to mobile credit products is remarkable, especially when compared to other available products. The Smart Campaign found in Benin, for instance, that microcredit borrowers on average waited more than a month between applying for a loan and actually receiving it.¹¹ Mobile loans measure waiting time in minutes or even seconds.

Mobile loans are more private than other sources, something customers may appreciate. The public nature of traditional loans is often a drawback, and public shaming of microfinance clients behind on their payment, while relatively rare, is one of the most harmful behaviors clients have reported to the Smart Campaign.¹² With a fully digitized interface between borrower and lender, mobile credit may drastically reduce this risk.

With mobile credit, providers have at their disposal a low-cost, direct path for iterative engagement with clients, which they could use to confirm or build client understanding of the products, and offer behavioral nudges and new products.¹³ Companies, such as Juntos Finanzas, have been experimenting with behavioral economics through automated SMS responses based on algorithms to generate active communication with clients aimed at helping them achieve their goals. And recent research conducted by the Consultative Group to Assist the Poor (CGAP) shows the potential of thoughtful interactions with mobile borrowers to reduce default and increase repayment, among other ‘win-win’ outcomes.¹⁴

At the same time, consumer risks are present in various guises, and certain aspects of the business model may heighten specific client protection concerns. For example, when digital credit is delivered through partnerships, such as mobile lender leveraging an MNO network, or partnering with a separate data analytics firm, there is a heightened risk of confusion over responsibility for resolving consumer problems, as compared to traditional lending, where only one company is involved. The very speed and convenience of lending has been suggested as a concern, because it may prompt reckless borrowing by consumers. And aggressive marketing is surfacing broadly as one of the key consumer complaints about mobile-based models.

The next section of this Brief details and summarizes the state of evidence and knowledge around client protection for mobile credit, with recommendations for improvement. The evidence stems largely from three assessments conducted with the Smart Campaign of mobile lenders, as well as research conducted by CGAP, MicroSave and the International Telecommunications Union (ITU), among others. The Client Protection Principles are used as a Framework, and can be expanded as new risk areas emerge. While some client protection issues apply to both mobile and traditional forms of credit, the topics highlighted in this Brief are heightened or novel in mobile models.

Overall, the state of evidence is nascent and thus the concerns raised are not meant to suggest stifling the industry and its innovators. **Rather, we raise them to spur dialogue so that mobile credit can bring its greatest benefits while maintaining adequate standards of protection.**

Identification of Mobile Credit Risks

1. Appropriate Product Design and Delivery

Suitability and Aggressive Sales. We define product suitability as a provider’s duty to design products that are useful and relevant for target clients and to market them in a way that promotes healthy use. The tiny consumer loan product is appropriate for a very broad segment of the market, so the concerns in this area focus mainly on marketing.

Marketing practices should be truthful, accurate, transparent, and non-aggressive. Sometimes, in the digital credit space, products are often marketed forcefully to customers who lack an understanding of the price, terms, and the implications of default. In Kenya, MicroSave documented unsolicited SMS messages that surprise users with loan offers which, coupled with the ease of access, might lead to take-up of unnecessary and even detrimental loans.¹⁵ In consumer research from other regions, the Smart Campaign has documented complaints from microfinance clients who borrowed in response to push marketing even though they did not need – or even want – the loan, confirming that customers dislike aggressive marketing partly because they know they may succumb to its lures.¹⁶

The flip-side of the remarkable speed and convenience at which mobile loans can be approved and disbursed is that there is no cooling off period, that is, a time when the consumer can consider whether a loan is appropriate. FinAccess 2016 reported that many first-time users of M-Shwari tried it out for ‘no reason at all’.¹⁷ This is worrisome given that behavioral research suggests people think about digital credit more casually than traditional loans.¹⁸ Based on experiments conducted with providers, CGAP has advocated adding a small amount of friction, or additional time, into the loan process to allow customers to consider whether it is right for them.¹⁹

Summary and Recommendations: Some documentation of risks exists, though more thorough evidence is needed. Good practice guidance is not yet developed. There is no consensus around the spread of good practices among providers.

We would like to see more examples of providers that set policies regarding product suitability, and examples of providers that leverage their technology platforms to monitor, segment, and adjust their product offerings and incorporate feedback from clients into product design.

Advice From M-SHWARI for Fixing Erroneous Blacklisting

Recently I discovered that I was adversely listed for failure to pay for an M-SHWARI loan which I did not take. What can I do?

You need to write to the credit reference bureau that issued the report and inform them that the information contained in the report is disputed. The credit bureau is required to conduct an investigation within 21 days.... Upon completion of the investigation and it is found that the information is either erroneous or incorrect, the credit reference bureau will rectify the information. If after 21 days the bureau is yet to complete the investigation, then it is required to delete such negative information from its records.

2. Prevention of Over-Indebtedness

Under this Principle, we consider the credit approval process and whether it takes adequate care to prevent debt which could be harmful to consumers.

Algorithm Growing Pains and Portfolio Quality. Given the dearth of traditional data available for many potential borrowers, initial credit deployments are often made with imprecise algorithms that are meant to learn and improve over time. The experience generated by these early loans is used to hone the algorithm, and a relatively large number of defaults might even be expected at first. This process is considered to be a necessary part of the model's development. These lenders will, "make more loans, knowing that they will make more bad loans, in order to teach their algorithms how to distinguish good risks from bad ones. That is the tuition price for learning how to build and train new underwriting algorithms."²⁰

If loans are very small, the provider can write defaults off. Nevertheless, there can be real consequences if lenders report the defaults to credit bureaus. Sources claim that 2 million borrowers have been blacklisted in Kenya, many of them for loans of a few dollars.²¹ It takes time, resources, and effort to clear one's name from the credit bureau, as 'clearance' certificates can cost up to US\$20, which is a disproportionate amount considering the size of the loans.²² Refinement of the credit model should not be done at the expense of the consumer.

The Smart Campaign unequivocally supports credit bureaus as a piece of financial infrastructure that strengthens markets and leads to stronger client protection practices.²³ However, in this case rules could perhaps be developed to prevent adverse reporting to the credit bureau for clients that fail to repay tiny amounts, especially during early phases of a model.

Relatedly, expectations for appropriate levels of portfolio quality in digital lending are needed both because the viability of the lending models depends on successful maintenance of adequate portfolio quality *and* because high levels of delinquency are harmful to customers, whether they default (because consequences can be severe) or not (they pay the cost of delinquencies in higher fees or interest rates). And, as we've seen in the high-touch world of microfinance, reports of non-repayment can spread quickly among clients and escalate into a full-blown repayment crisis. There is a dearth of publicly available data on the portfolio quality of these models over time, but we would expect to see a responsible level achieved after the initial algorithm-sharpening process.

Summary and Recommendations:

Underwriting and its evolution in the digital lending business models need to be better understood, though proprietary algorithms have not been shared publicly. The industry should also begin discussing benchmarks for portfolio quality; we call on providers to share with trusted researchers portfolio quality and Non-Performing Loan (NPL) figures to help advance benchmarking, much as it evolved in the microfinance industry through the MixMarket and MFTransparency.

Capacity to Repay and Information Sharing. In traditional lending and in the Smart Campaign’s work with microfinance institutions, the bedrock of credit appraisal has been repayment capacity assessment, which is coupled with some assessment of willingness to pay. In contrast, algorithm-based scoring models use information such as mobile wallet transactions, airtime top-ups, etc. to score probability of default on a statistical basis. Mobile lenders may not have data on income or current debt burden, or if they do, they may “lack mechanisms to verify the veracity of information provided by the applicant.”²⁴ Finally, there appears to be little curiosity among providers to follow-up with mobile borrowers themselves on the implications the additional debt. As the Smart Campaign and others have found that even with clients who pay on time, the obligation can lead to stress and the selling of assets, skipping of meals, etc.²⁵

For very small loans, an exhaustive examination of repayment capacity is neither feasible nor necessary, but as the loan size escalates over time, the harms of default are amplified for both the borrower and the lender.

As in traditional credit, assessment of debt burden requires information sharing between providers. While some lenders report information to their local credit bureau, in many countries, credit bureau data is often incomplete and focused only on negative information that does not provide a view of current debt levels. Mobile lenders can be in the dark on how many loans their clients have.²⁶ The risk of multiple borrowing is enhanced when know your customer (KYC) regimes are not solid enough to prevent easy ‘document arbitrage’ that enable borrowers to open multiple mobile money accounts to access multiple loans.²⁷

Summary and Recommendations: Industry discussion is needed on best practices on the use of data on repayment capacity, by loan size. We would also like to see more glossaries that explain, in laymen’s terms, the universe of variables used in underwriting and why some are better than others (without revealing the secrets of any provider).²⁸ Research on developing a stress assessment component to underwriting algorithms would add value to the sector to ensure that the loan does not add undue stress to the client.²⁹

Digital lenders should also make real-time credit reporting and information-sharing a priority. This would catalyze a leapfrogging of traditional credit bureaus, which have been historically weak in many markets. Incentives (and regulation) would need to be aligned for such schemes to work.

3. Transparency

The Smart Campaign’s approach to transparency goes beyond disclosure and asserts that providers have a duty confirm in some way that clients actually understand the key terms and conditions of the product. Even in traditional microfinance, ours and other research has found that poor clients rarely understand fully the terms and conditions of their products, and are often ‘surprised,’ by a product feature after purchase.³⁰

A variety of research has documented lapses in effective communication of terms and conditions over the mobile interface. The ITU reviewed user agreements for mobile money services in nine African countries and found that the contracts were lengthy, did not include all relevant fees and charges, and were predominantly in English.³¹ MicroSave documented that the majority of mobile credit providers in Kenya send users to a web-based terms and conditions statement, which can be many pages long. Few mobile users access the site, much less take the time to read it.³² In the same project, very few customers understood the implications of non-repayment including fees, penalties, and reporting to the local credit bureau. Additionally, the Smart Campaign has encountered scenarios where pricing information was not fully conveyed because it did not include third-party charges, such as cash-out fees by an MNO.

Both MicroSave and CGAP have documented instances where providers only disclosed the cost of credit after completion of the purchase.^{33 34} This is an unequivocally harmful practice. Although regulators, such as the Competition Authority of Kenya, have established transparency and price disclosure requirements for digital financial service providers, such requirements do not appear to be followed strictly in practice.³⁵

Summary and Recommendations: The harms and risks have been articulated and documented. Work is needed to help providers figure out how to transparently convey the information they need over the mobile interface so that clients truly understand. Clients should also be able to store and save the terms and conditions, which is a challenge considering the limited memory of many feature phones. There is also great promise for building customers' financial capability using the mobile interface, though more work is needed.

4. Responsible Pricing

Responsible pricing encompasses the concepts of financial sustainability (for the institution) and affordability (for the client), but also the notion of profit levels and uses. It is not because a product is 'affordable' to clients that providers should charge the maximum they can. Responsible pricing implies a notion of shared benefits.

The understanding of what drives pricing for digital credit remains limited, as many of the companies are startups and there is widespread experimentation. It is generally conceded that high interest rates may be less problematic for consumers for short-term loans than for longer terms (provided the short-term loans are not routinely rolled over, effectively becoming longer term loans). We would also expect prices to decrease as customers build positive histories, algorithms become better predictors (reducing default costs), and growth allows businesses to distribute fixed costs across more customers. However, there is little evidence of decreasing pricing in practice.³⁶ Observed pricing is a combination of fees and interest rates that range wildly (see Table 2).

| Provider | Channel | Loan Range (Kshs)* | Fee or Nominal Interest Rate | Repayment Period | Annual Percentage Rate (APR) |
|-------------------------|--------------|--------------------|--|--------------------------------|------------------------------|
| Branch | App | 250 – 50,000 | 1 – 14% (as monthly rates) | 14 – 365 days | 12 – 170% |
| Equitel Eazzy Loan | SIM toolkit | 50 – 200,000 | 14.5% annual rate + 1% appraisal fee | 30 days | 27% |
| Equitel Eazzy Plus Loan | SIM toolkit | 1,000 – 3,000,000 | 14.5% annual rate + 2 – 3% appraisal fee | 2 – 6 months | 21 – 27% |
| Jumo/ Kopa Cash | USSD | 500 – 13,000 | 0.5% daily | 7 – 28 days | 183% |
| KCB-M-Pesa | SIM toolkit | 50 – 1,000,000 | 14% annual rate + 2.5% negotiation fee | 30 days 90 days 180 days | 73% 61% 49% |
| Kopa Chapaa | SIM toolkit | 500 – 10,000 | 8.5 – 17% | 10 days | 310 – 621% |
| M-Shwari | SIM toolkit | 100 – 20,000 | 7.5% | 30 days | 91% |
| Okoa Stima | SIM toolkit; | 100 – 1,000 | 10% | 7 days | 521% |
| Pesa na Pesa | App | 500 – 100,000 | 10% | 7 days | 521% |
| Pesa Pata | App | 2,000 – 20,000 | 30% | 30 days | 365% |
| Pesa Zetu | Website | Varies | 6 – 10% | 28 days | 85 – 130% |
| Saida | App | Up – 25,000 | 7.5% and up | 30 days | 91% and up |
| Tala | App | 500 – 50,000 | 5 – 20% | 30 days | 61 – 243% |
| Zindisha | Website | 100 – 1,000,000 | Initial membership fee of 5% of loan request, then 5% per loan | Varies | Varies by repayment period |

Table 2. Excerpt from CGAP Chart on Pricing for Digital Credit in Kenya³⁷

Summary and Recommendations: The client protection frontier is to understand pricing models and their evolution. This is crucial before beginning to think about benchmarks and acceptable ranges. Discussion is needed about affordability of high interest rates on short-term and very small loans.

5. Fair and Respectful Treatment

This principle is primarily concerned with treatment of customers during interactions with staff, including collections. It also addresses discriminatory behavior, including discrimination in loan approval and terms and conditions.

Appropriate Collections. Given that they occur electronically, collections of mobile loans occur in a vastly different context than traditional microfinance, where collections can become a flashpoint for intense pressure and client shaming. This is a potential benefit of the shift to digital delivery. Yet, other challenges have emerged in the digital lending space. For example, early research found that borrowers prioritized traditional lenders over digital lenders because of the personal touch, and pressure they experience with traditional loans. At the same time, these borrowers were unaware of the fees, cost of clearing their name, etc., that came with non-repayment of mobile loans. Borrowers also appear unclear that with certain providers, late payments are automatically deducted from their mobile wallet, air-time top-ups, or mobile savings account.³⁸ The obvious remedies for these problems involve information provision – at opportune times and in understandable language.

The repayment schedules of many of these loans are rigid with no opportunity for renegotiation. For initial loan sizes this may make sense, but as the loans begin to grow, flexibility should be built in.

Summary: Little examination on this topic to date but more needs to be done on information-provision and repayment flexibility, especially as loan sizes increase.

Non-Discrimination. Non-discrimination means treating all clients equally, regardless of their race, religion, ethnicity, political affiliation, disability, or gender. **Additionally,** the Smart Campaign maintains that credit offers for individuals may differ based on risk-based analysis, but that such differentiation should be consistently applied, stated in advance, and made with the goal of benefitting clients.³⁹ Attributes that are considered inappropriate bases for differentiation by society at large and often embedded in law, such as religion, language, gender, or ethnic origin, are particularly problematic.

The explosion of new data points used in mobile credit underwriting, and the way algorithms work, which obscures the influence of various data points on the ultimate score, raise a host of new questions.⁴⁰ There is concern simply because the algorithms are proprietary black boxes that are not available for scrutiny by consumers, regulators, or other stakeholders. Providers

themselves assert that they do not know which variables ultimately determine a customer's score because there are so many of them and they change through the machine learning process. Even if inputs do not discriminate unfairly, however, it is possible that results are discriminatory, because of correlations between the indicators used and those characteristics that are singled out as unfair bases for discrimination.⁴¹ If individuals are appraised based on their friends (social media), neighbors (geography), and those with similar interests, it could be highly correlated with sensitive and protected classes.

There is also a concern that customers cannot escape through good behavior or intent from the risk group the algorithm assigns them. An individual's final appraisal might not be fully based on her own merit, but on factors that she has in common with others that the model determines risky; a model, for instance, that penalizes a consumer with good credit history because she likes to shop at a low-end store.⁴² The non-transparency of the process reduces the possibility of appeal or persuasion. Customers are not likely to challenge their score, whether traditional or newer digital black box.⁴³ CGAP documented that clients in Kenya indeed do not understand why they are rejected for loans.⁴⁴

Summary and Recommendations: The industry needs a better understanding of what these algorithms include (personal attributes), and whether there is discrimination at the output level, even if not the input level. Legal frameworks surrounding discrimination were not written to address these new business models and it is not clear how they may be adapted.⁴⁵ Because providers consider their credit appraisal algorithms to be proprietary intellectual property, this is an extremely sensitive topic for discussion.

6. Data Privacy

Security and privacy of information are major concerns for digital credit, as for all mobile financial services. CFI Fellow Patrick Traynor, et al, reviewed 54 privacy policies of digital financial services, finding that, "almost half (over 44%) of these mobile money services do not have any privacy policy whatsoever." Of those that actually did provide privacy policies, "roughly one-third (33%) fail to provide them in either of the two most common languages of their market."⁴⁶ Given the much-expanded data sources used in credit appraisal, one wonders how well clients understand how much of their data is used in credit decisions.

CGAP has explored the question of how best to gain client consent. It found with First Access in Tanzania that consumers were more concerned about the way their information is used than with keeping information private, and researchers were able to build customer understanding of data privacy and credit scoring through an SMS-exchange.^{47 48}

Major data privacy issues also include data security, permissible uses of data, ownership rights and related questions. These questions are currently under intensive discussion; they are applicable to digital financial services generally, not only to mobile consumer lending, and indeed, they range beyond finance to many aspects of the digital age.

Summary: A hot topic. Lack of clarity around effective informed consent. Lack of willingness by many providers to restrict use or offer informed consent. Legal underpinnings unclear in many places. Security and data ownership under intense discussion.

7. Complaint Resolution

Digital borrowers, like users of any product or service, are bound to occasionally have reasons to complain or problems to resolve. Providers should offer timely and responsive mechanisms for problem resolution. The need for easily accessible problem solving resources is especially important for services that are delivered strictly digitally. If clients are confused by the lending interface, have questions, or experience an erroneous transaction, well-staffed call centers and other means of assisting with problem resolution are essential.

The appropriate focal points for problem resolution can be difficult to identify when multiple companies are involved in providing the service. For example, a mobile lender may leverage an MNO's agent network for cash-in and cash-out points. Borrowers are therefore interacting with an agent who is not a full-time employee, likely does not work for the lender, may offer a kaleidoscope of additional products, and is usually strapped for time. Although agents offer a human face, as cash transactions are their primary duty, they may have little ability to respond to questions regarding consumer loans.

Summary: The general availability and quality of complaints channels has not been documented. The risks of a complex value-chain for client protection accountability have been articulated, but little has been done to document good practices. This is a high-need, non-controversial area for further research and good practice development.

Fintech Protects: An Action Research and Consensus Building Process

There is increasing interest throughout the mobile financial services sector to identify and address emerging consumer risks. At the highest levels, the G20 articulated the need for responsible digital financial services in its Digital Financial Inclusion framework, “Principle 5: Establish Responsible Digital Financial Practices to Protect Consumers.”⁴⁹ A variety of organizations, including the Smart Campaign, GSMA, the Digital Credit Observatory at Center for Effective Global Action (CEGA), the International Telecommunications Union (ITU), the Better than Cash Alliance (BTCA), and MicroSave have contributed evidence and articulation of client protection risks in the digital financial space.⁵⁰ CGAP is particularly notable for its numerous research efforts in this area. While codes of conduct and principles have been articulated, most of these statements are at such a high level that they leave questions about actual practice unanswered.

Pointing out the risks and stating high-level principles is an important start. At this point, attention is turning from principles to practices. Providers are increasingly expressing interest in examining their models and establishing practice norms. To date, there have been relatively few consensus-building and best-practice oriented efforts. The Responsible Finance Forum, an annual event organized by a consortium of donors, has for several years focused its agenda on responsible digital finance, though as it is largely driven by public sector donors; providers have not been deeply engaged.⁵¹ One valuable initiative is GSMA’s code of conduct: GSMA is testing and implementing detailed operational standards to accompany its published code.

To contribute to this broad effort, the Smart Campaign is developing an action research and consensus-building process – Fintech Protects – modeled on its original, successful campaign and drawing on both the knowledge of how to conduct such a campaign and our existing technical base. The ultimate aim of Fintech Protects is to help ensure that digital financial services can bring their greatest benefits while maintaining adequate protections – in other words, for providers to be able to act responsibly within a secure ecosystem. Getting there requires a process of documenting the scope and prevalence of consumer risks, observing good and bad practices, developing tools that support good practices, and building consensus across the sector. The Campaign will carry out a range of activities, including developing Fintech Protects as a community of practice where providers can compare notes, researching good practices that address identified risks, and convening stakeholders in selected countries. As this Brief has suggested, small mobile consumer loans will be an initial area of focus. The Campaign is also working on good consumer protection practices for banking agents.

Building industry will and know-how to address emerging consumer risks will take involvement from many participants. We invite those interested in participating in Fintech Protects to join us. Visit www.smartcampaign.org and visit Fintech Protects to learn more.

Notes

- ¹ GSM Association (GSMA), State of the Industry Report on Mobile Money, Decade Edition: 2006–2016 (Executive Summary), GSMA, 2017, www.gsma.com/mobilefordevelopment/wp-content/uploads/2016/02/GSMA_Executive_Summary_PRINT-READY-VERSION.pdf.
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- ³ Alexandra Rizzi, “Building Trust and Growing Digital Financial Services: A Look at Jumo,” *Center for Financial Inclusion Blog*, October 25th 2016, <https://cfi-blog.org/2016/10/25/building-trust-and-growing-digital-financial-services-a-look-at-jumo>
- ⁴ GSM Association (GSMA), State of the Industry Report on Mobile Money, 22.
- ⁵ MicroSave, “Where Credit Is Due: Customer Experience of Digital Credit In Kenya,” (presentation). March 2017 http://www.microsave.net/files/pdf/Where_Credit_Is_Due_Customer_Experience_of_Digital_Credit_In_Kenya.pdf
- ⁶ Cook, Tamara and Claudia McKay, “How M-Shwari works: The story so far.” Consultative Group to Assist the Poor (CGAP), (2015).
- ⁷ John Aglionby, “Tanzania’s fintech and mobile money transform business practice,” *Financial Times*, July 12, 2016. <https://www.ft.com/content/0e8b56ee-41ca-11e6-9b66-0712b3873ae1>
- ⁸ FinAccess 2016 as cited in Blumenstock (2017).
- ⁹ Eilin Francis, Joshua Blumenstock and Jonathan Robinson, “Digital Credit: A Snapshot of the Current Landscape and Open Research Questions,” , BREAD Working Paper No. 516, July 2017. http://ibread.org/bread/system/files/bread_wpapers/516.pdf
- ¹⁰ Income volatility among the poor and underbanked has been well-documented in the Financial Diaries research series both in developing markets as well as the United States.
- ¹¹ Caitlin Sanford et al, “Client Voices Benin Country Report,” Smart Campaign, October 2015. http://smartcampaign.org/storage/documents/Client_Voices_Benin_Eng_FINAL.pdf
- ¹² Sushmita Meka et al, “My Turn to Speak: Voice of Microfinance Clients in Benin, Pakistan, Peru and Georgia,” February 2016. http://smartcampaign.org/storage/documents/Synthesis_Report_ENG_FINAL.pdf
- ¹³ For more on these types of innovations and emerging financial capability frameworks, see Julia Arnold and Elisabeth Rhyne’s, “A Change in Behavior: Innovations in Financial Capability,” <https://centerforfinancialinclusionblog.files.wordpress.com/2016/04/a-change-in-behavior-final.pdf>.
- ¹⁴ Rafe Mazerand Kate McKee, “Consumer Protection in Digital Credit,” *CGAP Focus Note 108*, August 2017. <http://www.cgap.org/publications/consumer-protection-digital-credit>
- ¹⁵ MicroSave, “Where Credit Is Due: Customer Experience of Digital Credit In Kenya.”
- ¹⁶ The Smart Campaign documented extremely aggressive sales in competitive, well-developed markets, specifically Georgia and Peru. Clients expressed fear of missing out on a good offer or opportunity, even when they didn’t need it. While these offers were not digital credit, we feel the same tactics are being applied, perhaps even more effectively. For more on this research see the Smart Campaign’s Client Voice reports from Peru and Georgia.
- ¹⁷ Central Bank of Kenya, Kenya National Bureau of Statistics & FSD Kenya. (2016). The 2016 FinAccess Household Survey on financial inclusion. Nairobi, Kenya: FSD Kenya.
- ¹⁸ CGAP has conducted demand-side work on borrower perceptions in East Africa to determine whether this is occurring and MicroSave has documented examples of this already.
- ¹⁹ Rafe Mazer and Kate McKee, “Consumer Protection in Digital Credit.”
- ²⁰ Jeremy Liew, “BankThink Future of Consumer Lending Belongs to PhDs, Risk-Takers,” , April 30th 2012. <https://www.americanbanker.com/opinion/future-of-consumer-lending-belongs-to-phds-risk-takers>
- ²¹ Eilin Francis, “Digital Credit: A Snapshot of the Current Landscape and Open Research Questions.”
- ²² George Ngigi, “Pain of Kenyans Blacklisted for Amounts as Small Sh100,” *Business Daily Africa*, September 8th 2016. <http://www.businessdailyafrica.com/economy/Pain-of-Kenyans-blacklisted-for-amounts-as-small-as-Sh100/3946234-3374120-r0r2bfz/index.html>
- ²³ The Smart Campaign conducted research on what happens to clients who default (See Solli et al 2015) which found that weak credit bureaus led to swifter and harsher collections practices.

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- ²⁴ MicroSave, “Where Credit Is Due: Customer Experience of Digital Credit In Kenya.”
- ²⁵ Jessica Schicks, “Over-Indebtedness of Microborrowers in Ghana,” *CFI Publication* 15. November 2011.
- ²⁶ Michelle Kaffenberger and Patrick Chege, “Digital Credit in Kenya: Time for Celebration or Concern?” CGAP (blog), October 3rd 2016. <http://www.cgap.org/blog/digital-credit-kenya-time-celebration-or-concern>
- ²⁷ Interview with representative from GSMA. July 20th 2017 as well as observed from earlier GSMA paper “Managing the Risk of Fraud in Mobile Money,” October 2012.
- ²⁸ The Digital Credit Observatory recently put out a call for proposals to, among other queries, help answer the question of “How...non-traditional credit-scoring algorithms...be designed to minimize default, over-indebtedness, leakage, fraud and other risks to consumers?” For more check out their website <http://www.digitalcreditobservatory.org>
- ²⁹ Microfinance Opportunity and Social Performance Solutions have proposed such an idea.
- ³⁰ Sushmita Meka et al, “My Turn to Speak: Voice of Microfinance Clients in Benin, Pakistan, Peru and Georgia,
- ³¹ Sarah Ombija, “Review of DFS User Agreements in Africa: A Consumer Protection Perspective New,” International Telecommunications Union, January 2017. http://www.itu.int/en/ITU-T/focusgroups/dfs/Documents/01_2017/ITU_FGDFS_Report-on-Review-of-DFS-User-Agreements-in-Africa.pdf
- ³² MicroSave, “Where Credit Is Due: Customer Experience of Digital Credit In Kenya.”
- ³³ Rafe Mazer, “Digital Credit Delivery & Consumer Protection,” presentation at SoFI Rwanda conference on 10/19/2016.
- ³⁴ MicroSave, “Where Credit Is Due: Customer Experience of Digital Credit In Kenya.”
- ³⁵ ITU Focus Group on Digital Financial Services, « Main Recommendations, », January 2017. http://www.itu.int/en/ITU-T/focusgroups/dfs/Documents/201703/ITU_FGDFS_Main-Recommendations.pdf
- ³⁶ Michelle Kaffenberger and Patrick Chege, “Digital Credit in Kenya: Time for Celebration or Concern?”
- ³⁷ Ibid. “
- ³⁸ Consumer Empowerment and Market Conduct (CEMC) Working Group “Digitally Delivered Credit Policy Guidance Note and Results from Regulators Survey,” Alliance for Financial Inclusion Guideline Note No. 17, September 2015. http://www.afi-global.org/sites/default/files/publications/guidelinenote-17_cemc_digitally_delivered.pdf ,
- ³⁹ For more on how the Smart Campaign incorporates these concepts into its current work, see the Client Protection Standards 2.0 available at http://smartcampaign.org/storage/documents/Standards_2.0_English_20150711.pdf
- ⁴⁰ Tala for example, states that they use 10,000 data points to make a credit decision. See Tala website, accessed July 2017. <https://tala.co/>
- ⁴¹ Of course discrimination has been documented in traditional lending and credit scoring as well, such as history of redlining.
- ⁴² Mikella Hurley and Julius Adebayo, “Credit Scoring in the Era of Big Data,” *Yale Journal of Law and Technology*: Vol. 18 : Iss. 1 , Article 5, Page. 183. July 2017.
- ⁴³ For example, in 2013 a study conducted by the Federal Trade Commission found that more than a quarter of consumers had errors in their traditional credit reports. Of these errors, 13 percent were relevant to their score and contributed to higher interest rates and possibly denials. If this is the case with traditional scoring, where there are far fewer data points, what does this mean for the new models? For more see the FTC as cited in Hurley and Adebayo.
- ⁴⁴ Michelle Kaffenberger and Patrick Chege, “Digital Credit in Kenya: Time for Celebration or Concern?”
- ⁴⁵ In the United States for example, the Fair Credit Reporting Act (FCRA) and the Equal Credit Opportunity Act were developed to ensure equity in consumer credit reporting and to protect consumer privacy in data usage and disclosure, and to prevent lenders from discriminating on basis of race, religion, nationality, sex, or marital status. But these laws were developed in the era of traditional scoring and face new loopholes and pitfalls in the era of alternative and big data.
- ⁴⁶ Jasmine Bowers, Bradley Reaves, Imani Sherman, Patrick Traynor and Kevin Butler. “Regulators, Mount Up! Analysis of Privacy Policies for Mobile Money Services,” Florida Institute for Cybersecurity (FICS) Research University of Florida Gainesville, Florida. Unpublished.

⁴⁷ Rafe Mazer (CGAP), Jessica Carta (First Access), and Michelle Kaffenberger, “Informed Consent How Do We Make It Work for Mobile Credit Scoring?” CGAP. August 2014. <http://www.cgap.org/sites/default/files/Working-Paper-Informed-Consent-in-Mobile-Credit-Scoring-Aug-2014.pdf>

⁴⁸ Ibid

⁴⁹ Global Partnership for Financial Inclusion, “G20 High-Level Principles for Digital Financial Inclusion,” July 2016.

⁵⁰ The BTCA has also published more specific Responsible Digital Finance Guidelines. For more see here <https://www.betterthancash.org/tools-research/case-studies/responsible-digital-payments-guidelines>

⁵¹ For more information see <https://responsiblefinanceforum.org/>

The Smart Campaign works globally to create an environment in which financial services are delivered safely and responsibly to low-income clients. As the world's first financial consumer protection standard, the Campaign maintains a rigorous certification program, elevates the client voice, and convenes partners to effect change at the national level. Nearly 100 financial institutions, collectively serving more than 41 million people, have been certified for adhering to the Campaign's consumer protection standards.

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in financial inclusion