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**Issue No.7**

# Topical Note

**March 2019**

**Fuliza**

**"Fuliza in numbers"**

## Table of Contents

Executive Summary .....	2
Introduction – Evolution of mobile credit .....	3
Safaricom's revolutionary service "Fuliza" .....	4
How does "Fuliza" work? .....	4
"Fuliza" so similar yet so different" .....	5
The business opportunity .....	5
"Fuliza" in numbers - The impact on revenue .....	6
Is "Fuliza" exposed to the same risks as mobile lending? .....	10
Disclosures: .....	11

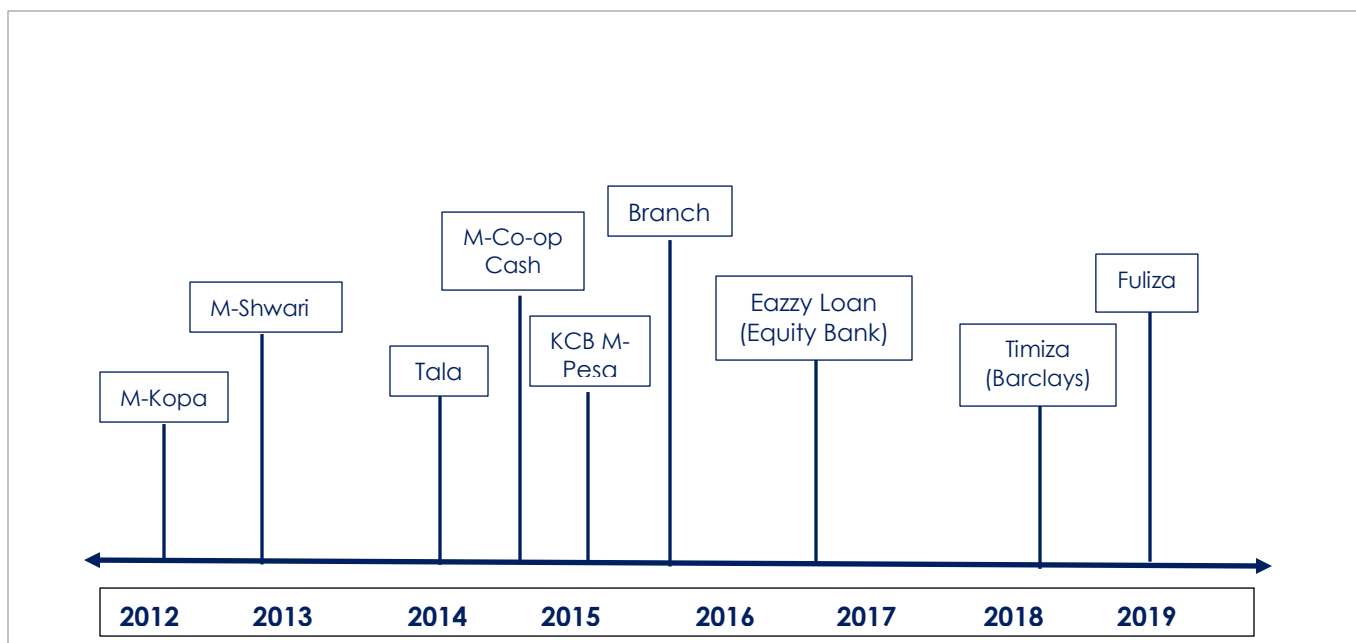
## Executive Summary

- Our 7<sup>th</sup> topical note titled “Fuliza” **“Fuliza in numbers?”** analyses Safaricom’s revolutionary service “Fuliza”.
- The report begins by giving a brief background of mobile credit and introduces Safaricom Plc’s new product “Fuliza”
- We hold the view that “Fuliza” will have a considerable impact on M-Pesa revenues and subscriber loyalty and this is also covered in the report.
- With regards to revenue, we estimate that “Fuliza” will increase total M-Pesa revenues by 2.6% FY2019/20 to KES.82.27Bn.
- This will see M-Pesa’s contribution to total service revenues increase to approximately 32% FY 2019/20 compared to 28% FY 2017/18.
- In terms of risk exposure, we see a near zero default rate for “Fuliza” thus underlying the viability of this product.
- “Fuliza” is a game changer in mobile financial services supporting our view of Safaricom’s competitive advantage in innovation and mobile money services.
- With “Fuliza” Safaricom makes a case for value added services as opposed to trying to compete with its main rivals on pricing.

## Introduction – Evolution of mobile credit

- Commercial banks in partnership with telecommunication companies were the first to offer digital loans followed by a number of fintech start-ups offering credit “loans” through mobile applications “mobile apps” emerging thereafter.
- Currently, there are more than 20 digital credit solutions in Kenya with the main ones being M-Shwari, KCB M-Pesa, M-Coop Cash, Equity Bank’s Eazzy Loan, Timiza (Barclays Bank) and Fuliza in partnership with Commercial Bank of Africa (CBA) and KCB Group (Fig.1).
- The digital credit ecosystem also includes several non-bank, credit-only operators such as Tala, Branch, OKash, Okolea, Haraka, Stawika, Uberpesa amongst others.
- In January 2019 “Fuliza” joined the growing list of digital lending platforms that seek to take advantage of both high mobile phone penetration and customer demand for small, quick and easily accessible credit.
- Mobile loan lenders mostly offer short-term credit with typical loan terms ranging from a few days to a month.
- Kenyans previously locked out of the short term credit market due to lack of regular income, credit histories or collateral amongst other requirements can now access credit.
- Mobile lending platforms use predictive analytics like mobile money data, call logs, social media data, text messages and contact lists to arrive at a credit worthiness score and limit.

**Fig.1: Evolution of mobile credit & mobile money related services**



Source: Sterling Capital Research

## Safaricom's revolutionary service "Fuliza"

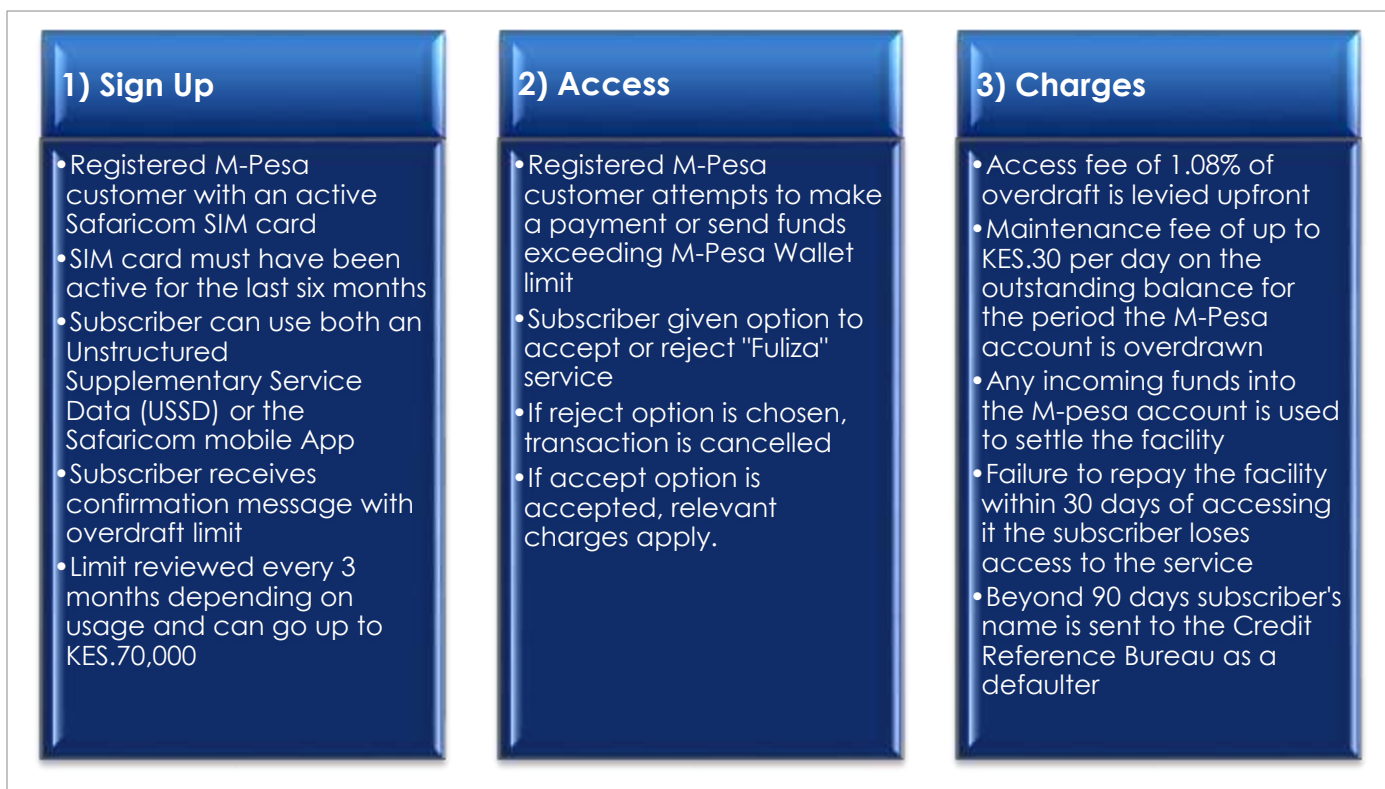
"Fuliza" is a short-term overdraft facility available to M-Pesa subscribers.

- **"Fuliza" is a short-term overdraft facility available to M-PESA subscribers that allows them to complete both money transfer and payment (Lipa Na M-Pesa transactions, i.e. Paybill) transactions when they have insufficient funds in their M-Pesa account.**
- The facility is offered in partnership with CBA and KCB Group who provide the lending facility.
- CBA and KCB have leveraged on the M-Pesa platform and are using algorithms based on historical M-Pesa transactions to set a limit on amount which can be accessed by individual customers.
- A registered customer can use "Fuliza" as many times as long as he/she remains within the allocated Fuliza M-Pesa limit.

### How does "Fuliza" work?

- "Fuliza" works in 3 simple steps making the service easy to register and access (Fig.2)

**Fig.2: Fuliza at work**



Source: Sterling Capital Research

## “Fuliza” so similar yet so different”

“Fuliza” is not a loan product but an overdraft facility.

1) **“Fuliza” is not a loan product:** It is a revolving overdraft service that allows an M-Pesa subscriber to transfer funds or make payments when they have insufficient funds in their M-Pesa accounts.

2) **Fuliza is only available for transactions done through M-Pesa** unlike M-Shwari and KCB M-Pesa where a client is free to withdraw the funds and spend as they please.

3) **Fuliza automatically deducts funds deposited in a client’s M-Pesa account to settle outstanding amounts** while M-Shwari and KCB M-Pesa allows a user to repay the loan at a time of their discretion.

- Some of its features make it very similar to other mobile credit products.

- 1) Subscribers accessing the facility are required to settle the outstanding balance within 30 days from the access date.

- 2) Defaulters (subscribers who fail to settle the facility) suffer a penalty and are listed with a Credit Reference Bureau (CRB).

- 3) Similar to M-Shwari and KCB M-Pesa loan limits, the overdraft facility's limit is based on a user's transactions profile.

- 4) These above named products require subscribers to repay their loans in time to maintain access to the service.

## The business opportunity

- “Fuliza” will have a positive impact on M-Pesa transactional volumes, revenues, customer acquisition as well as retention.

- We also see it changing the competitive landscape with regards to mobile and digital payments.

### 1) Fees and commission income

- Fuliza will drive M-Pesa revenues through the facility interest earnings and standard M-Pesa charges.

- **We see a 14.5% growth in M-Pesa revenues FY2018/19 to KES.72Bn and KES.82.3Bn FY2019/20 driven by growth in customer money transfer transactions, payments and fees and commissions from strategic business partnerships such as KCB M-Pesa, M-Shwari and Fuliza.**

## “Fuliza” in numbers - The impact on revenue

58% of all daily M-Pesa transactions fail due to insufficient funds.

- According to Safaricom, 58% of all daily M-Pesa transactions fail due to insufficient funds.
- Majority of the failed transactions would be completed within 2 days according to company sources.
- The high volume of incomplete transactions illustrated an *“un-met need where we could come in and help our customers complete their transactions, even if they lacked funds at the time.”* - Bob Collymore.
- We attempt to determine potential revenue from “Fuliza” using assumptions based on numbers provided by Safaricom one month after inception of the product (Table 1):

Estimate a 6% annual growth rate for total Safaricom and M-Pesa subscribers driven by the need to have the Fuliza service.

### 1) Subscriber estimates

- Estimated number of Safaricom and total registered M-Pesa subscribers with an annual growth rate of 6%.
- Estimated number of 30 day active M-Pesa subscribers with an estimated growth rates of 7.2%.
- Estimate a 10% monthly growth rate in the number of Fuliza customers, with 4.2Mn customers registered in the first month of inception.

### 2) Safaricom estimates an average overdraft settlement period of 2 days

- We estimate that 80%, 10% and 10% would repay the overdraft in 2, 5 and within 10 days respectively.

### 3) Overdraft advanced

- 10% monthly growth rate in overdraft advances with KES.6.2Bn advanced in the first month of inception.

### 4) Revenue Share allotment

- Revenue share split between Safaricom, Commercial Bank of Africa (CBA) and KCB Group at 40%, 40% and 20% respectively.
- Here we assume that both the access and maintenance fees will be shared in the same proportion.

**Table.1: Impact of Fuliza on M-Pesa revenues**

<b>Estimated Revenues Generated from Fuliza (Jan 2019 - March 2020)</b>			
<b>Period</b>	<b>Sep-2018</b>	<b>Jan-2019</b>	<b>Mar-2020</b>
Total Safaricom subscribers (Mn)	29.9	30.1	32.3
Total M-Pesa subscribers (Mn)	24.2	24.3	26.1
30-Day active M-Pesa subscribers (Mn)	21.0	21.1	23
Total Fuliza customers (Mn)		4.2	13.8
Total Amount advanced (KES. Bn)		6.2	201.5
Fuliza Access fees (1.08%) KES. Bn		0.07	2.2
Maintenance fees 0.5% per day - 80% pays within 2days (KES. Bn)		0.05	1.6
Maintenance fees 0.5% per day - 10% pays within 5days (KES. Bn)		0.02	0.5
Maintenance fees 0.5% per day - 10% pays within 10days (KES. Bn)		0.03	1.0
<b>Safaricom revenue share - 40% (KES. Bn)</b>		<b>0.07</b>	<b>2.1</b>
<b>CBA revenue share - 40% (KES. Bn)</b>		<b>0.07</b>	<b>2.1</b>
<b>KCB revenue share - 20% (KES. Bn)</b>		<b>0.03</b>	<b>1.1</b>
<b>Total estimated revenue generated from Fuliza (KES. Bn)</b>		<b>0.16</b>	<b>5.3</b>

Source: Safaricom & Sterling Capital Research

\*For illustration purposes only.

KES.2.2Bn would be generated in revenue through the 1.08% access fee and KES.3.1Bn through maintenance fees.

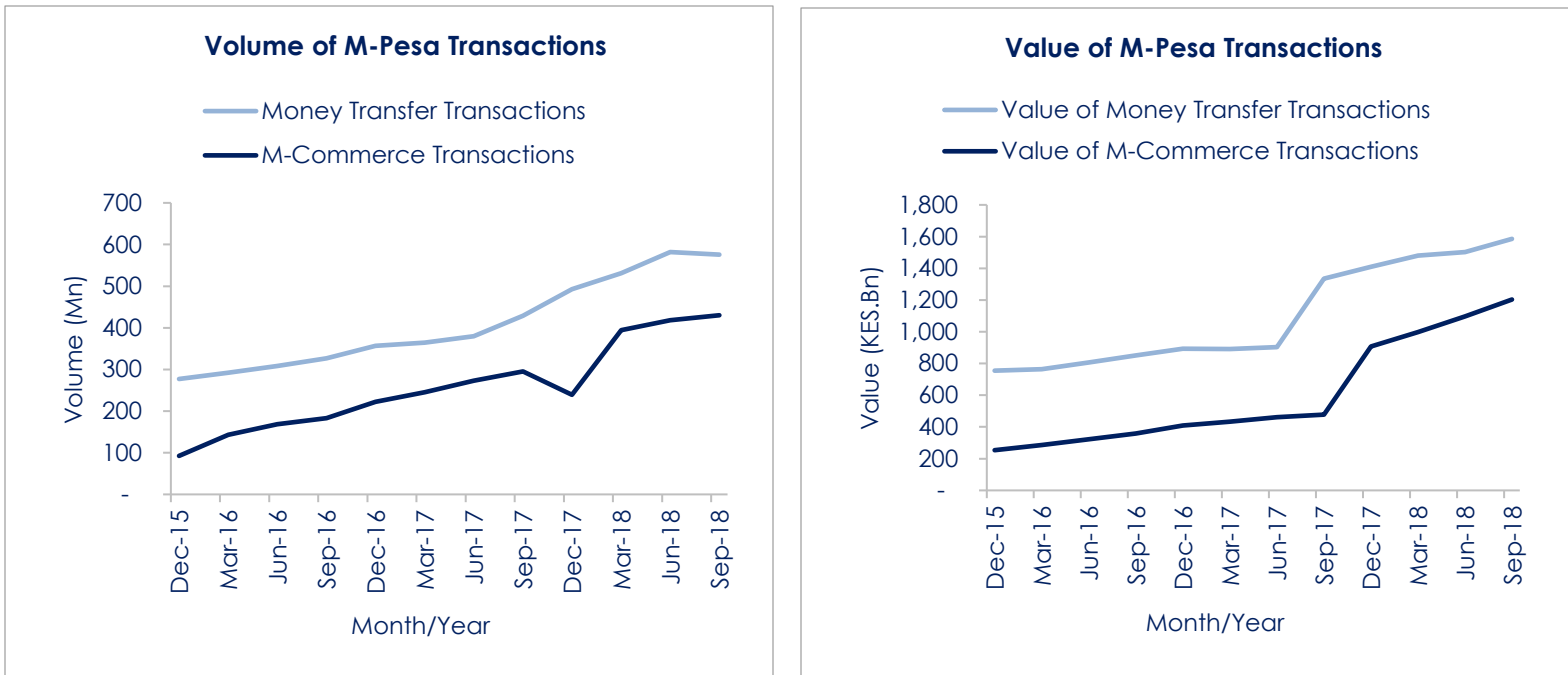
- We estimate that KES.2.2Bn would be generated in revenue through the 1.08% access fee and KES.3.1Bn through maintenance fees.
- We further estimate that KES.2.12Bn would be allocated to Safaricom as its 40% share of total revenue.
- Fuliza revenues would increase total M-Pesa revenues by 2.6% FY2019/20 thus increasing M-Pesa's contribution to approximately 32% of total service revenue.
- As already mentioned, Fuliza will also increase customer loyalty and therefore revenues generated by other services and therefore the overall impact on total service revenues is much more than would have been the case without the service.

## 2) Increase in transactional volumes

- The value and volume of M-Pesa transactions have increased rapidly since the roll-out of the service.
- We expect to see an increase in transactional volumes on the basis of a decline in failed transactions.
- We estimate a 15% increase in the number of total transactions (both money transfer and mobile payments).



**Fig.3: M-Pesa money transfer and payment transactions have exhibited rapid growth in recent years**



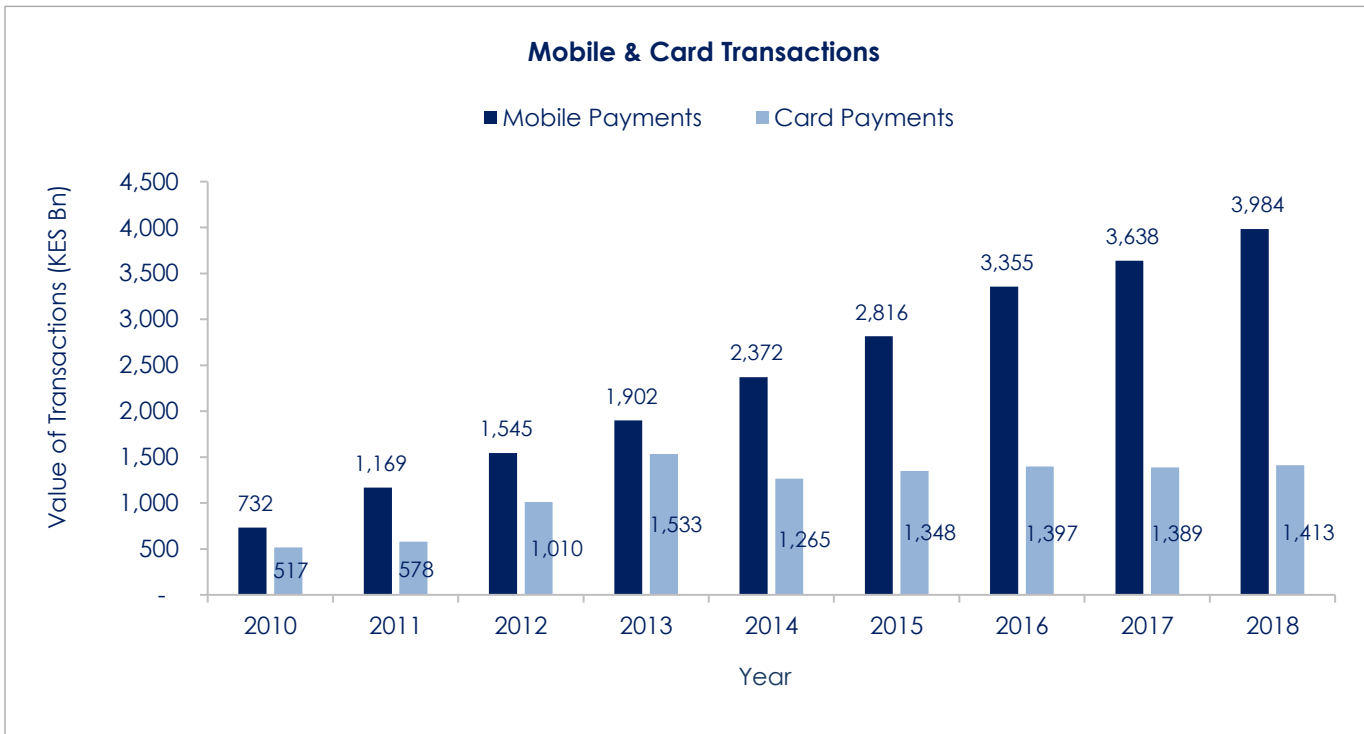
Source: Communications Authority

### 3) Competitive intensity of digital payments and mobile credit expected to increase

Mobile money payments growing at a faster rate than card payments. Fuliza is expected to further increase the volume of mobile payment transactions.

- Fuliza will offer stiff competition to mobile lending services on the basis of greater convenience, cost differentials and ease of repayment.
- We also look at “Fuliza” as a medium to long term competitor of other payment methods such as credit or debit cards.
- According to the Central Bank of Kenya (CBK), a total of KES.4Tn was transacted via mobile payments in 2018 compared to KES.1.4Tn transacted through card payments.
- Mobile money transactions in 2018 was an equivalent to 44% of Kenya's estimated Gross Domestic Product (GDP) for the year.
- The International Monetary Fund (IMF) had projected Kenya's 2018 GDP at KES.9.1Tn.
- Mobile money payment driven by M-Pesa has grown at 67.9% driven by the last 5 years compared to 11.7% for plastic cards during the same period.

**Fig.4: Mobile payments have grown at a faster rate than card transactions**



Source: Central Bank of Kenya

**4) Fuliza will support Safaricom's subscriber acquisition and retention strategy**

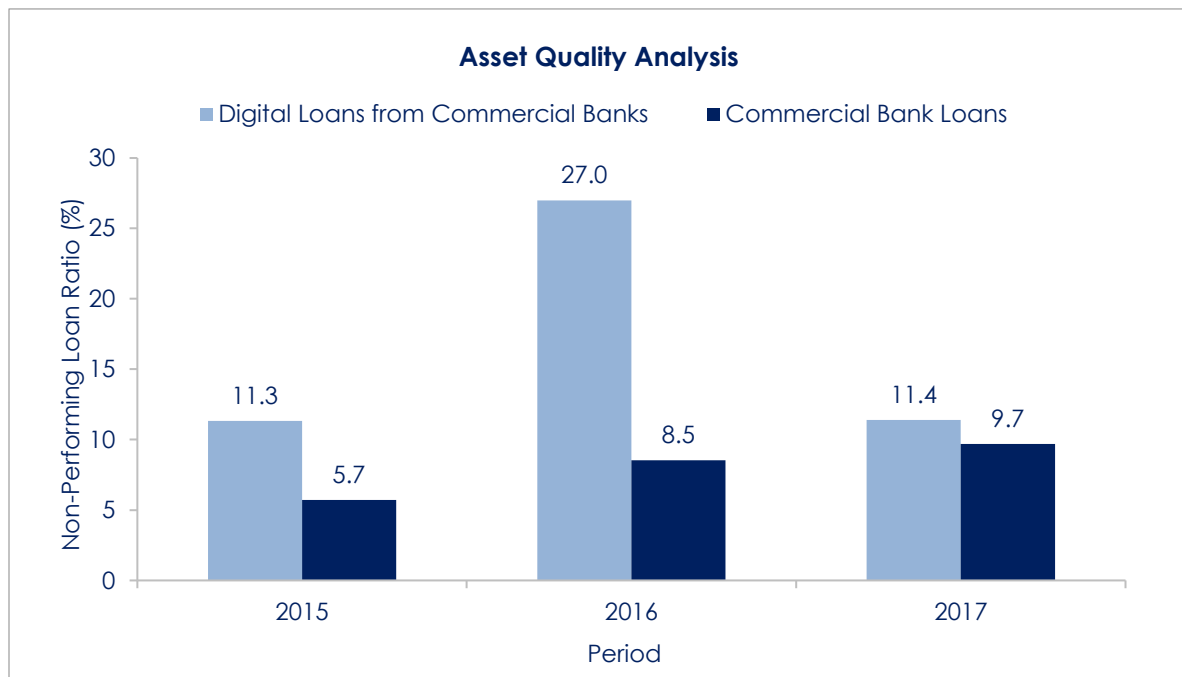
- Safaricom has been gradually losing subscriber market share to Airtel and Telkom largely due price competition in voice calls and mobile data.
- Just as is the case with M-Pesa, the introduction of Fuliza will have a positive impact on both customer acquisition and retention.
- In addition, it will reduce any relevance of a new mobile money service that the planned Airtel-Telkom merger will come up with.

## Is “Fuliza” exposed to the same risks as mobile lending?

Fuliza will have a near zero default risk

- Mobile loans are usually short term with comparatively higher interest rates than commercial loans especially when compounded yearly.
- Data provided by the CBK in its Financial Sector Stability Report 2017 indicate a higher Non-Performing Loans (NPL) ratio for digital loans extended by banks than that for the entire bank loan portfolio (Fig.4).
- In 2017, the NPL ratio for digital loans stood at 11.4% compared to 9.7% for traditional bank loans.
- However, unlike other forms of mobile credit, we anticipate “Fuliza” to have a near zero default rates due to the auto-collection when a customer deposits or receives money in their M-Pesa wallet.
- There has been talk of regulation of mobile lending rates because of the high interest rates levied on borrowers.
- Although it is too soon to take a position on the possibility of implementation, we believe that Fuliza could be exempted from such regulation on the basis of it technically being an overdraft facility and not a loan product.

**Fig.5: Digital loans’ comparatively poor asset quality**



Source: Central Bank of Kenya

- In conclusion, we believe that Fuliza is a well thought-out product both from a revenue generation aspect but also customer acquisition and retention.
- It will go a long way in warding off the impact of stiff price competition as a growing subscriber base begins to appreciate value added services as more important than price differentials on services such as voice calls and mobile data.

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