



Linking financial services and social protection for resilience: lessons from Kenya

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This Policy Brief is based on research conducted under the BRACED programme and presented in Weingärtner et al. (2019a).

KEY POLICY MESSAGES

FINANCIAL SERVICES such as savings, loans or insurance can be complementary to social assistance, helping beneficiaries absorb and adapt to climate related shocks and stresses. However, they are not interchangeable, as beneficiaries might need the cushion provided by the safety net. Many social protection (SP) beneficiaries are classified as 'extreme poor' or belong to households that are not expected to graduate – owing to illness, age or disability – and might therefore not benefit equally from financial services.

THERE IS POTENTIAL TO BUILD ON THE STRUCTURES CREATED BY SP PROGRAMMES designed to enhance access to financial services, but those financial services on offer need to be adapted to better meet the needs of SP beneficiaries.

APART FROM ACCESS TO CASH AND FINANCIAL SERVICES, ADDITIONAL COMPLEMENTARY INTERVENTIONS ARE NEEDED, to help beneficiaries use financial resources to be better prepared for future shocks and stresses and to have positive long-term impact on their

BRACED aims to build the resilience of vulnerable people against climate extremes and disasters. It does so through NGO-consortia working across East Africa, the Sahel and Asia.

lives. These include business skills and financial literacy training, improved access to markets, and enhanced early warning systems.

INTRODUCTION

Climate-related shocks and stresses threaten people and communities around the world, compounding existing poverty and vulnerability and undermining long-term development. National and international actors are searching for new and better ways to help people deal with increasing climate risks and, in turn, support long-term resilience. One potential way of doing this is to facilitate access to, and use of, adequate financial services such as savings, loans and insurance in underserved communities. This allows people to prepare for, cope with and adapt to shocks and stresses (Moore et al., 2019). The role of social protection (SP) programmes in helping people anticipate and cope with climate-related shocks and stresses, such as droughts or floods, is also increasingly appreciated (Ulrichs and Slater, 2016; O'Brien et al., 2018; Costella et al., 2018; Weingärtner et al., 2019b).

This brief aims to inform policy by helping fill knowledge gaps on both the potential and the limitations of developing links between cash-based assistance and financial inclusion interventions for building the resilience of households to climate-related shocks and stresses. It is based on research conducted in Kenya assessing whether participation in SP programmes facilitates access to financial services

(Weingärtner et al., 2019a). The brief also aims to support policy discussions in Kenya, as well as in other countries, on integrated resilience interventions, financial inclusion, SP and graduation.

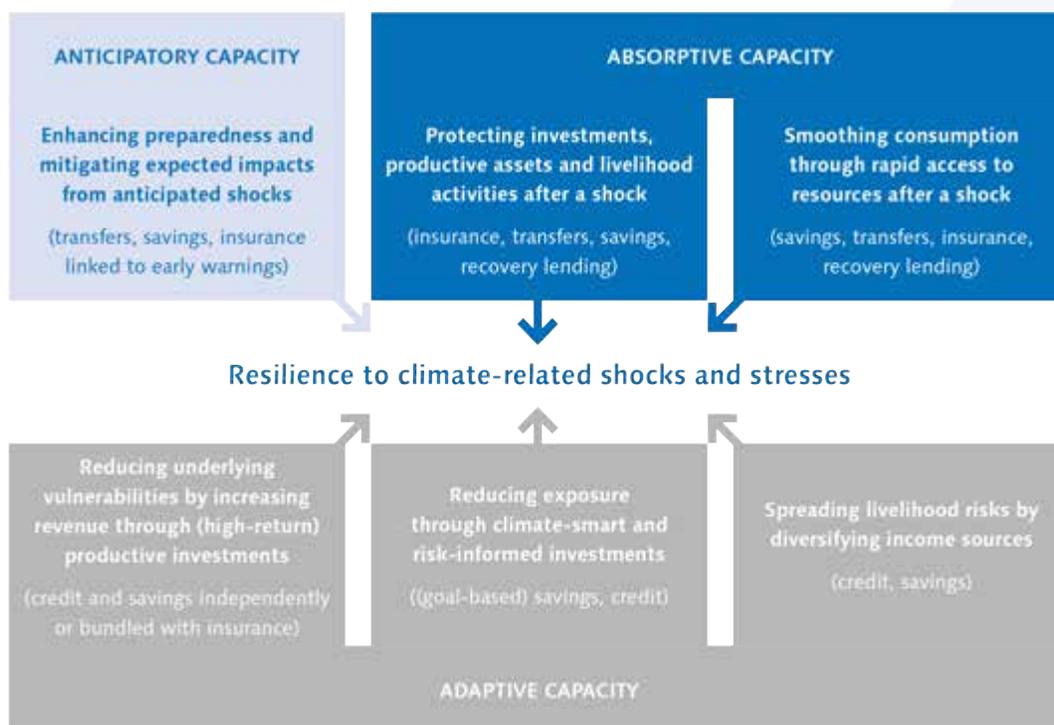
WHY LINK FINANCIAL SERVICES AND CASH TRANSFER PROGRAMMES?

Every year, financial services and SP programmes, such as cash transfers, are reaching greater numbers of people in low-income communities, who are exposed to climate-related risks. (Demirgüç-Kunt et al., 2017a; World Bank, 2018). Well-designed financial services (e.g. savings accounts) have been effective in helping people prepare for and cope with idiosyncratic shocks such as a household member falling ill.¹ However, there are limitations to the role these instruments can play in strengthening resilience, especially when they are used as standalone approaches.² For instance, the impact of financial services in addressing larger, covariate climate-related shocks and stresses in such communities is less established (Moore et al., 2019).

¹ 'Idiosyncratic shocks affect individual households or household members, for example job loss or the death of a breadwinner... Covariate shocks affect large numbers of people and/or communities at once. Such shocks are often concurrent. Covariate shocks may be natural, economic or political' (O'Brien et al., 2018)

² See Figure 1 for an overview of the resilience concept and capacities under the BRACED programme.

Figure 1: The role of cash transfers through SP programmes and other financial services in strengthening resilience to climate related shocks and stresses



Financial services do not necessarily work in the same way for people with varying socioeconomic backgrounds, while formal financial services often remain out of reach, unattractive or less effective for the poorest people (Hammill et al., 2008). Meanwhile, cash transfers through SP programmes can contribute to building the ability to anticipate and absorb shocks, but their role in building long-term, adaptive capacity is less evident (Ulrichs and Slater, 2016).

A common approach to linking social assistance with other types of support is the simultaneous provision of social assistance and complementary interventions to the same group of beneficiaries. This approach is sometimes used by programmes that aim to support participants to 'graduate' from poverty, by combining a basic income or transfer (cash or asset) with financial services (often savings and/or credit). It is reported that this graduation model, most commonly implemented at relatively limited scale and through a

project approach, has led to increased investments in productive assets, rising incomes and diversification of livelihoods (Hashemi and Umaira, 2011; Sabates-Wheeler and Devereux, 2015). However, whether these impacts materialise and are sustainable in the long term may depend on specific project design and context.

Alongside the simultaneous provision of cash transfers and financial services to the same beneficiaries, other policies and interventions pursue an approach that is layered along different target groups, mostly defined through income or asset levels. This means various types of public or commercial financial services are directed towards different beneficiaries. Access to financial services is seen as a type of support that social assistance beneficiaries can move into, once they have managed to stabilise and increase their asset base and income-generating capacity, and no longer need to rely on consumption support. Evidence of such a move is low, which indicates that SP

benefits alone might not be enough for beneficiaries to be able to 'graduate into' different types of support.

KEY FINDINGS FROM KENYA

The Kenyan government has recognised the importance of financial services for strengthening development and enhancing resilience. It has also engaged in efforts to increase the adaptiveness of its large-scale SP cash transfer programmes. One of these, the Hunger Safety Net Programme (HSNP), currently operates in four northern drought-prone counties, including Wajir, and aims to help vulnerable households deal with climate shocks. Social assistance cash transfer programmes in the country have already moved from delivering physical cash to funds via cards to funds via full bank accounts. The HSNP now uses the e-payment system, in which all beneficiaries have bank accounts through which they receive their transfers, with personal ATM cards linked to these accounts. This means, by nature, the HSNP increases the share

of the population with formal account ownership while also providing ID cards for the first time. In parallel, the Mercy Corps-led PROGRESS project, which is part of the Building Resilience and Adaptation to Climate Extremes and Disasters (BRACED) programme, operates in Kenya's Wajir county, where it provides pastoralist communities with access to Sharia-compliant financial services through:

- a savings and credit cooperative – Crescent Takaful Savings and Credit Cooperative SACCO (CTS)
- support for Village Savings and Loans Associations.

The research underpinning this policy brief has shown that the financial infrastructure (accounts and IDs) developed through SP programmes has helped beneficiaries' confidence in managing cash. However, it has also indicated that their use of formal bank accounts for any services beyond receiving the government cash transfer is very low. The majority have not branched out to use other financial services, such as taking out loans and insurance products offered by banks or other financial institutions. Just over 20% of HSNP beneficiaries in Wajir study sites manage to put aside savings, but only 8% of all people in the programme use their formal accounts to do so.

However, there appears to be high demand for financial services that are tailored to context and local needs, as demonstrated by early experiences of CTS in Wajir. Financial services can potentially contribute to graduation from SP programmes. They can also support some beneficiaries' resilience to climate related shocks and stresses, helping currently underserved people to make use of savings products, loans or insurance. Building on the financial infrastructure established through the HSNP is a critical entry point to deepen financial inclusion, though changes to the system are required to facilitate meaningful use of services by beneficiaries.

ENTRY POINTS AND WAYS FORWARD IN KENYA

Below, we review some of the key entry points that this research has highlighted as crucial for improving such linkages in the Kenyan context.

The role of trust and literacy

In Wajir, people have a high level of mistrust in financial institutions, as well as in government and its associated services, such as bank accounts provided through SP programmes. Low levels of financial literacy further contribute to this mistrust and to fears of inability to repay and losing collateral. These are major obstacles to CTS clients and HSNP beneficiaries in accessing financial services.

For this reason, it is important to build on existing local structures to establish trust and deliver numeracy and literacy training. Implementing organisations, such as Equity Bank's Wings to Fly programme, that provide services targeted at SP beneficiaries via financial inclusion or graduation programmes should work with local CSOs and community leaders to establish initial relationships and build trust. In the BRACED/PROGRESS project in Wajir, working through religious authorities has:

- helped transmit information on the products offered
- provided clarity on their conformity with local norms
- increased buy in.

At the same time, programmes working with such institutions need to be conscious of local power structures, to ensure that people outside of predominant community groups are not further excluded and marginalised. Engaging with the agencies and systems that implement SP, to identify those with highest potential to benefit, might be key to achieving this. Working through existing beneficiary welfare committees is crucial to delivering adult numeracy and literacy training.

Understanding social protection beneficiaries' profiles

SP beneficiaries have low levels of income and assets, which means that operational costs per client are relatively high for private financial service providers. Larger formal financial institutions lack an understanding of local contexts, client needs and market potential; coupled with a backdrop of highly informal economies, this leads those institutions to hesitate to expand into new areas. Finally, there is a lack of infrastructure linking cash transfer systems and financial institutions in order to provide adequate services at scale, particularly in more remote and rural areas. Through its expansion into North-eastern Kenya, which has been facilitated by the HSNP, Equity Bank has filled a gap in the local banking landscape. However, an opening remains in Sharia-compliant microfinance. New, smaller and less formal institutions such as CTS are slowly moving into this space, but capital is constrained, competition is low and the range of products on offer remains limited.

It is key to incentivise financial institutions to expand and engage with SP clientele by assessing the business case, demonstrating potential return on investment and conducting market research. One aspect of this is to establish the business case for expansion and facilitate localised market research that helps financial inclusions assess general demand and specific product need in particular. Initiatives dedicated to financial inclusion agendas such as Financial Sector Deepening Kenya (FSD Kenya) have a critical role to play in this regard. Challenge funds and grant programmes, such as those operated by the Mastercard Foundation or FSD Kenya (funded by the Gates Foundation and supported by Boston Consulting), are a starting point for supporting the development of products and services reaching 'last mile' costumers. These will need to demonstrate the economic viability of such investments so as to attract interest and more substantive, longer-term investment from mainstream banks. The recent addition of Cooperative Bank, Kenya Commercial Bank (KCB) and

Postbank to Equity Bank as HSNP cash transfer service providers might be a first step towards increasing competition in this market.

It will also be important to further incentivise financial institutions to expand and engage with SP clientele through de-risking. De-risking private investments through government or international development support in the form of public private partnerships can create an important lever to facilitate expansion. Those that include national or county government, local CSOs, grassroots financial service providers and larger financial institutions can help bring contextual knowledge into the development of new financial products and services, thus driving innovation and enhancing the adequacy of products. Past experiences from the Equity Bank expansion under the HSNP, as well as from the partnership between Mercy Corps and CTS under BRACED, provide valuable lessons of both the potential of such endeavours and their challenges. Care should be taken to address information asymmetries between different types of actors and to ensure accountability in such initiatives in order to avoid public subsidies of private investments that would have happened regardless of public involvement, based on commercial interest. Technical assistance to enhance the capacity in government departments and non-governmental organisations could help different actors better understand dynamics in the private sector, to assess and make use of them.

Another important aspect will be to explore options for including smaller, less formal financial service providers and informal groups in the delivery of cash transfers through SP programmes. BRACED experience shows potential for Savings and Credit Cooperatives such as CTS to cater specifically to the needs and financial capacities of HSNP beneficiaries in Wajir, because they offer group lending, Sharia-compliant products, lower administrative fees than banks and manageable loan amounts. At the same time, smaller and younger financial institutions are constrained in terms of the numbers and values of loans they can give out based on the availability of capital and, in the case of CTS, unable to

service the much higher existing demand. Partnerships with SP systems and the larger banks involved could help bring smaller financial institutions on board to scale up such existing services that are already responding to local needs.

Finally, it is important to re-think incentives and fee structures related to existing cash transfer delivery and financial services. Regular bank accounts in Kenya incur fees for different services such as withdrawals or transfers. Bank account holders under the HSNP are allowed a limited number of free withdrawals. This means they can access their allocations without additional charges but are also encouraged to withdraw larger shares at once rather than saving up money on their account and only withdrawing smaller sums as and when needed, because this would be more costly. Under the agent-based model used to deliver government cash transfers, agents only pay out cash, but do not administer other types of services. Whether they eventually could or should do so is questionable and would at least require very close monitoring and a feasible fee structure. Emergency transfer or subsidised insurance systems that are set up to pay out too often could also create moral hazard issues and result in maladaptive outcomes. Such potential adverse effects should be addressed in product design and provision. Developing financial services and processes that take the seasonality of livelihood risks into account should be another priority. More flexible and remotely usable mobile money services may be a way to address some of these challenges, though previous experience from the HSNP and FSD Kenya in exploring this option also shows that mobile money is not an easy solution to all problems. This is due to limited mobile network and mobile money agent coverage as well as difficulties in ensuring the security of cash transfers through the platform. However, this may change in the future, as both mobile network and mobile money agent coverage are expanding further.

The importance of regulation

Many people in North-eastern Kenya avoid interest-charging products and financial institutions on religious grounds. However, regulation on Sharia-compliant

banking and microfinance is lagging behind in Kenya compared to financial regulation more broadly. This further increases the level of uncertainty for financial service providers to engage in this space, as well as for clients.

A key area of focus should be to strengthen regulation and consumer protection. Sharia-compliant microfinance institutions and banks should work with regulating authorities to enhance regulation and provide adequate complaint mechanisms for clients, to enhance consumer protection. Regulators seem to understand Sharia-compliant financial services to some extent, but bringing regulation up to the speed of practical development is required to provide a safer space to financial service providers who want to become active in this area.

Complementary policy and programme interventions

Cash transfer programmes or financial services alone will not build resilience. Financial resources accumulated and accessed through these channels have an important role to play, but they need to be complemented with a wider range of policy changes, services and capacity building measures to strengthen anticipatory, absorptive and adaptive resilience capacities more comprehensively.

It is important to integrate financial service provision to SP beneficiaries into a package of wider support with an exit strategy. Complementary services requested by beneficiaries include

- financial literacy and business skills training
- enhanced access to markets and business opportunities
- increased access to climate and weather information that would help people make more informed investments.

Importantly, social programmes work at scale, while the provision of appropriate financial services might only reach a fraction of those enrolled in such systems. Not all SP beneficiaries will be able to

gain from complementary approaches, such as graduation programmes, and this might not be financially feasible. Systems such as the single/social registry could help target those who might benefit from different types of interventions. Responsibility for implementing and carrying the costs of such complementary activities needs to be clarified from the outset. Given decentralised structures in Kenya, the county governments could play a role and would arguably have a responsibility to help SP beneficiaries graduate from poverty.

GLOBAL LESSONS AND THE WAY FORWARD

Building on lessons from Kenya, the following paragraphs outline more widely applicable lessons and ways forward in linking financial services and SP globally.

Financial services are not a replacement for social assistance, but they can be complementary in strengthening resilience to climate related shocks and stresses.

Social protection programmes, including cash-based social assistance, are an important means for beneficiaries in arid and semi-arid areas to stabilise consumption over time and to absorb some of the impacts from climate-related shocks and stresses, such as floods or droughts. However, cash transfers are not enough for people to make meaningful investments in longer-term sustainable livelihood strategies, which would be needed to increase their ability to shift livelihoods when under stress and to adapt to a changing environment. Financial services such as savings, loans or insurance can be a relevant addition for some beneficiaries, helping them absorb and adapt to climate related shocks and stresses. However, many SP beneficiaries are classified as 'extreme poor' or belong to households not expected to graduate, owing to illness, age or disability. This means financial services do not benefit everyone equally and should therefore be treated as complementary for some, rather than a replacement for all social assistance.

There is potential to build on the structures created by social protection programmes to enhance access to financial services, but the services on offer need to be adapted to better meet the needs of social protection beneficiaries.

While signing people up for bank accounts through SP programmes ensures they will receive government cash transfers, it does not mean that beneficiaries will automatically use other financial services that could improve their ability to manage risk and build their resilience over the long-term (such as saving, or taking out loans or insurance). Low levels of financial service infrastructure, compounded by high interest rates and fears of penalties charged by financial institutions, constrain customer engagement. Despite these challenges, there appears to be high demand for financial services that are tailored to context and local needs. The following opportunities for financial service development have been identified:

- Develop microfinance markets by raising investment in the design and provision of adequate products, thereby increasing competition and addressing regulation gaps.
- Build on existing local structures to establish trust and deliver numeracy and literacy training.
- Explore options for including smaller and less formal financial service providers – such as savings and credit cooperatives and informal groups – in the delivery of SP programmes.
- Re-think incentives and fee structures related to existing cash transfer delivery and financial services.

Additional complementary interventions to social protection and financial services are needed to ensure climate resilience, including for extremely poor households.

Apart from access to cash and financial services, additional tools and interventions are needed to help beneficiaries use financial resources in a way that contributes to their resilience

and has a positive long-term impact on their lives. These include:

- business skills and financial literacy training
- improved access to markets
- more resilient market infrastructure and value chains
- enhanced early warning systems, allowing people to be better prepared for future shocks and stresses.

Such support can be delivered through graduation modules, resilience programmes or financial inclusion initiatives. Coordinating public and private investment and joint engagement of different stakeholders, as well as strategies for longer term funding of activities, is critical. In turn, ensuring that interventions are layered in a way that addresses different types of risks and constraints is key.

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to strengthen resilience to climate extremes and disasters, and initiates and supports processes to ensure that evidence is put into use in policy and programmes. The Knowledge Manager also fosters partnerships to amplify the impact of new evidence and learning, in order to significantly improve levels of resilience in poor and vulnerable countries and communities around the world.

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