Segmentation of the financially under-served in Kenya and guidance for policymakers

Workshop | 5 September 2019

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Please note:

This presentation was delivered to Kenyan stakeholders for their input at "Inclusive Finance: tapping the potential of the unmet financial needs of Kenyans" workshop held on the 5th of September at the Serena Hotel, Nairobi.

These should be considered as the initial findings from Cenfri and 71point4. All inputs received from stakeholders will be incorporated into the final report to be published within the next two months

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Presentation structure

- Study background
- Financial needs of Kenyans and key segments
- Unmet needs and their drivers

Study background

Needs-based approach

Improving welfare by placing customer needs at the centre and targeting the underserved

Need: A collection of use cases that can be fulfilled by financial services

Transfer of value

Send money or digital value from one person to another

Meeting goals

Achieve life objectives or obligations that require funding across multiple income cycles

Liquidity

The need to meet expenses in a single income cycle

Resilience

The ability to deal with unexpected shocks that have a financial impact

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Optimising the financial sector: Understanding financial needs

This research aims to:

- Identify key population segments with unmet financial needs
- Understand drivers of unmet needs
- Develop recommendations for policymakers, regulators and FSPs

Usage analysis

Assess gaps in financial services supply by looking at unmet needs

Identify opportunities

Enable the financial sector to provide for the individual and policy goals set out

Research methodology: Combination of demand-side analysis (cluster segmentation analysis of the FinAccess 2019 survey) and supply-side analysis (desktop research and stakeholder interviews).

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The financial sector is integral for the Big Four Agenda

Vision 2030: "Transform Kenya into a newly industrialising middle-income country"

Third medium-term plan for the implementation of Vision 2030: **Big Four Agenda**

Food security

Manufacturing

Affordable housing

Universal health care

The financial sector and Big Four Agenda

- Enable **deeper financial markets**
- Ensure **greater access** to **financial services**
- **Capacitate individuals** and **businesses** with **useful financial tools**

Source: National Treasury and Planning (2018)

Financial needs of Kenyans and key segments

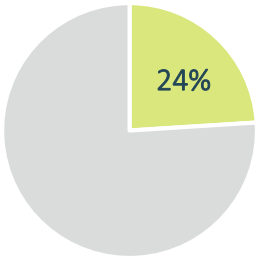
Kenyans experience a range of needs, to different extents

Survey measurement

Transfer of value

Made no payment via an account in the past 12 months

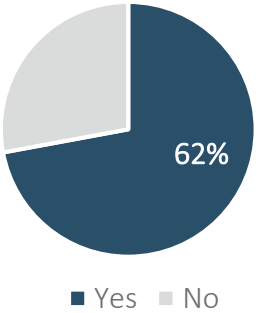
6.02 million adults



Liquidity

Could not meet regular spending needs in the past 12 months

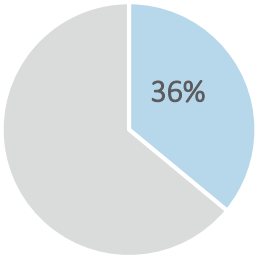
15.6 million adults



Resilience

Experienced a large financial shock in the past 12 months

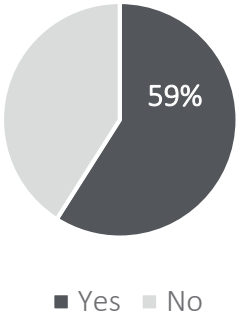
9.1 million adults



Goals

Currently trying to achieve a specific goal that requires a lot of money

14.85 million adults



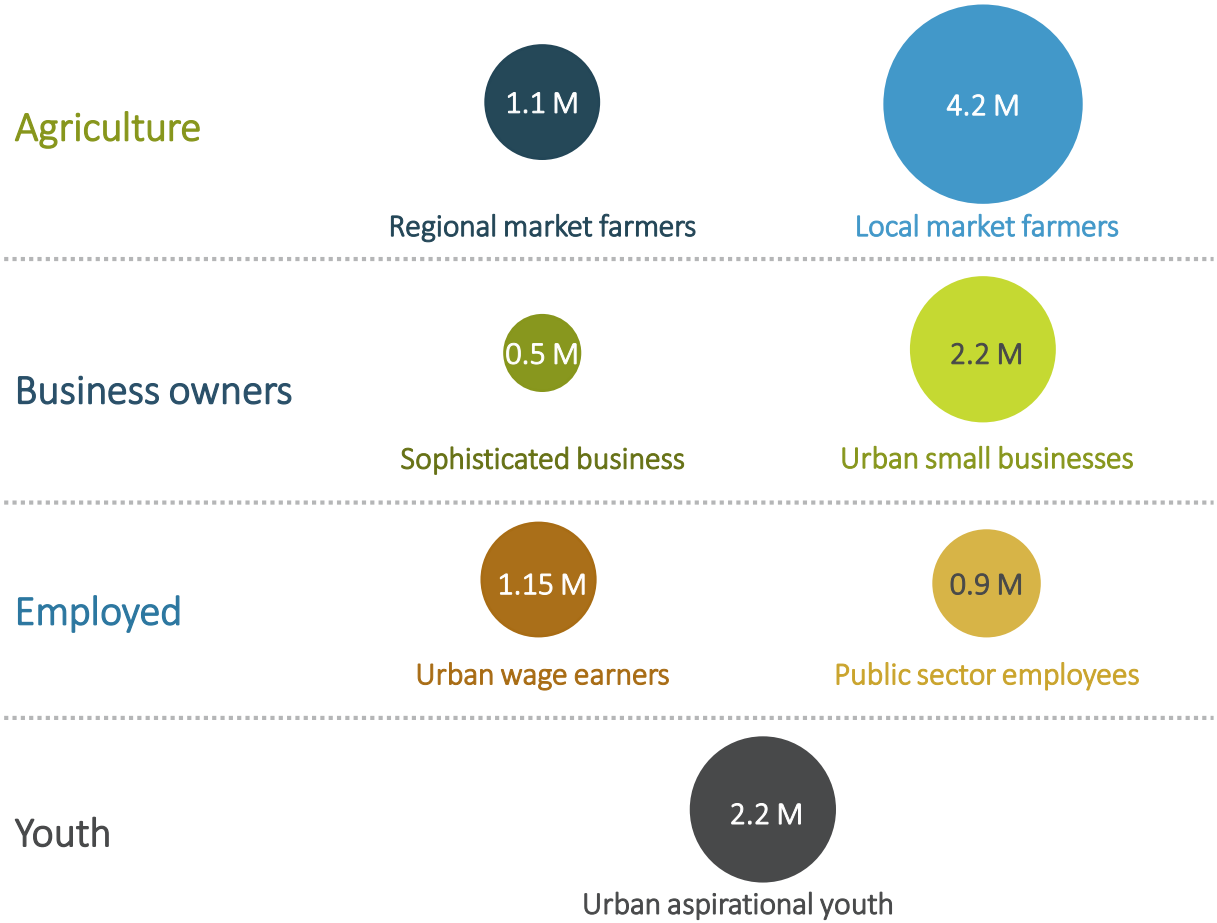
Source: FinAccess Survey 2019

A segmentation based on livelihood identified 16 distinct segments

Segment prioritisation criteria

1. Displays **unmet financial need**
2. Presents **viable business case** for FSPs
3. Strategically important for **policy objectives** and **economic growth**

Seven segments have been prioritised

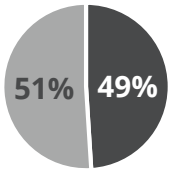


Source: FinAccess Survey 2019

Urban aspirational youth are between 18 and 25 years old, they have completed secondary school and are looking to either further their education or start a business

Urban aspirational youth

1.2 million



- Male
- Female

100% Aged between 18 - 25

100% Have completed secondary school

Most likely to be found in **Nairobi, Kiambu, Kajiado** and **Uasin Gishu**

TRANSFER OF VALUE

Most have made or received a digital payment (driven by remittances)

- **88%** have received a digital payment
- **94%** have made a digital payment

LIQUIDITY

HALF have experienced liquidity distress

- **50%** Could not meet their regular spending needs at some point over the past 12 months

RESILIENCE

LEAST LIKELY segment to have experienced a shock

- **24%** experienced a resilience shock in past year, mostly health-related and farm-related shocks

GOALS

MOST are currently trying to achieve a goal

- **75%** are CURRENTLY trying to achieve a key goal, either to further their education or to start a business

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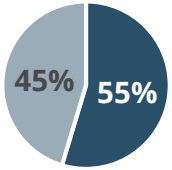
Regional market farmers sell mostly cash crops to cooperatives, factories and companies

Regional market farmers

1.1 Million



- Male
- Female

54% Aged 50 or more

59% Have not done any secondary schooling

Most likely to be found in **Kirinyaga, Nyamira, Kericho** and **Muranga**

Transfer of value

Farm-related payments are starting to BECOME DIGITISED

- **58%** have received a farm-related payment into their account
- **44%** have made a farm-related digital payment

Liquidity

MOST LIKELY segment to have experienced liquidity distress

- **57%** Could not meet their regular spending needs at some point over the past 12 months

Resilience

MOST LIKELY segment to have experienced a shock

- **46%** experienced a resilience shock in the past year, mostly health-related and farm-related shocks

Goals

Main goals are EDUCATION for their children and expanding their FARMS

- **58%** are CURRENTLY trying to achieve a key goal

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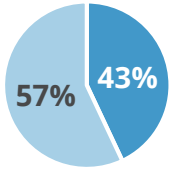
Local market farmers sell food crops at local markets, to local traders or to neighbours

Local market farmers

4.2 million



43% Aged 50 or more

78% Have not done any secondary schooling

Most likely to be found in Nyandarua, Embu, Narok and Homa Bay

TRANSFER OF VALUE

Farm-related payments are only cash based

- **5%** have received a farm-related payment into their account
- **5%** have made a farm-related payment digital payment

LIQUIDITY

MOST LIKELY segment to have experienced liquidity distress

- **57%** could not meet their regular spending needs at some point over the past 12 months

RESILIENCE

SECOND MOST LIKELY segment to have experienced a shock

- **40%** experienced a resilience shock in the past year, mostly health-related and farm-related shocks

GOALS

Main goals are EDUCATION for their children and expanding their FARMS

- **48%** are CURRENTLY trying to achieve a key goal

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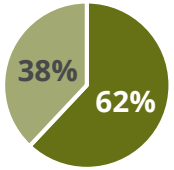
Sophisticated businesses are registered businesses that have access to business-specific financial devices

Sophisticated businesses

490,000



- Male
- Female

50% Aged 35 or less

47% Have at least some tertiary education

Most likely to be found in **Kiambu** and **Nairobi**

Transfer of value

MOST businesses in this segment accept digital payments

- **70%** received a digital payment linked to business activities
- **52%** made any business-related digital payment

Liquidity

LEAST LIKELY segment to have experienced liquidity distress

- **36%** could not meet their regular spending needs at some point over the past 12 months

Resilience

MAIN shocks include health-related shocks and death of a family member

- **37%** experienced a resilience shock in the past year

Goals

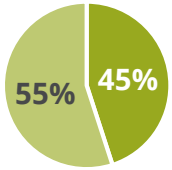
SECOND MOST LIKELY to be CURRENTLY trying to achieve a goal

- **79%** are CURRENTLY trying to achieve a goal, mostly related to expanding their businesses and housing-related goals

Urban small businesses are unregistered and mostly consist of a single person. Business owners likely mix personal and business finances.

Urban small businesses

2.2 million



- Male
- Female

54% aged 35 or less

(one-third of the segment are women 18 to 35)

Most likely to be found in Nairobi and Mombasa

Transfer of value

Businesses in this segment are almost entirely CASH based

- 19% received a digital payment linked to business activities
- 9% have made a business-related digital payment

Liquidity

HIGH levels of liquidity distress

- 56% could not meet their regular spending needs at some point over the past 12 months

Resilience

MAIN shocks include health-related shocks and death of a family member

- 35% experienced a resilience shock in the past year

Goals

Main goals are expanding BUSINESS and EDUCATION

- 76% are CURRENTLY trying to achieve a key goal

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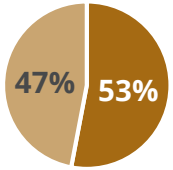
This segment works in the public sector (many in education). It has the highest credit usage and is the most likely to be overindebted.

Public sector employees

900,000



- Male
- Female

42% aged 35 or less

70% have at least some tertiary education

Most likely to be found in Uasin Gishu, Nyamira and Kiambu

Transfer of value

Receive salary into an account, ALL have made digital payments

- **93%** receive salary directly into an account
- **99%** have made a digital payment in the past year

Liquidity

HIGH liquidity distress given relatively high, stable income

- **48%** could not meet their regular spending needs in the past year
- High levels of over-indebtedness may contribute to this (31% say: more than half of their salary goes to debt repayments)

Resilience

MAIN shocks include health-related shocks and death of a family member

- **38%** experienced a resilience shock in past year

Goals

Main goals are EDUCATION for their children and PURCHASING LAND

- **65%** are CURRENTLY trying to achieve a key goal

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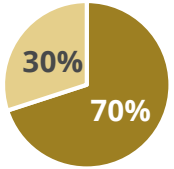
Urban wage earners work in manufacturing, private households and the retail trade

Urban wage earners

1.1 million



- Male
- Female

65% aged 35 or less

82% have completed secondary school

Most likely to be found in Nairobi, Mombasa and Kiambu

Transfer of value

Mostly paid directly into an account, everyone in the segment has made a digital payment

- **88%** have received salary/wage into an account
- **100%** have made a digital payment in the past 12 months

Liquidity

Just under half have experienced liquidity distress

- **46%** could not meet their regular spending needs at some point over the past 12 months

Resilience

MAIN shocks include health-related shocks and death of a family member

- **34%** experienced a resilience shock in past year

Goals

MOST LIKELY segment to be trying to meet a housing related goal

- **84%** are CURRENTLY trying to achieve a key goal. Just under half say their MAIN goal is housing-related

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Digitisation is happening in some segments and for certain use cases, however, many remain almost exclusively cash-based

TRANSFER OF VALUE	Aspirational urban youth	Regional market farmers	Local market farmers	Sophisticated businesses	Urban small businesses	Public sector employees
Income from ***main income source*** received into an account	46%	58%	5%	70%	19%	93%
Make **farm/ business related payments** via an account		44%	5%	52%	9%	

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Digitisation is happening in some segments and for certain use cases, however, many remain almost exclusively cash-based

TRANSFER OF VALUE	Aspirational urban youth	Regional market farmers	Local market farmers	Sophisticated businesses	Urban small businesses	Public sector employees
Income from ***main income source*** received into an account	46%	58%	5%	70%	19%	93%
Make **farm/ business related payments** via an account		44%	5%	52%	9%	
Receive **any payment** (incl. remittances) into an account	88%	84%	60%	98%	81%	99%
Make **any payments** (incl. remittance payments) via an account	94%	84%	69%	97%	92%	99%

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The segments deal with their liquidity distress using various devices

Liquidity	Aspirational urban youth	Regional market farmers	Local market farmers	Urban small businesses	Public sector employees	Urban wage earners
Experienced liquidity distress past 12 months	50%	57%	57%	56%	48%	46%

Source: FinAccess Survey 2019

The segments deal with their liquidity distress using various devices

Liquidity	Aspirational urban youth	Regional market farmers	Local market farmers	Urban small businesses	Public sector employees	Urban wage earners
Experienced liquidity distress past 12 months	50%	57%	57%	56%	48%	46%
Formal credit	6%	5%	1%	2%	21%	9%
Informal credit	2%	14%	11%	9%	6%	5%
Borrowed from friends/family	11%	5%	6%	7%	6%	7%
Formal savings	10%	12%	6%	11%	20%	33%
Informal savings	1%	3%	2%	5%	1%	2%
Savings with friend/ family/ secret place	8%	6%	3%	5%	7%	4%
Sold asset/crops/ livestock	1%	7%	14%	3%	0%	0%
Assistance from family/friends	33%	23%	24%	22%	9%	17%
Changed behaviour	13%	16%	20%	25%	18%	20%
Did nothing	3%	9%	13%	10%	9%	3%

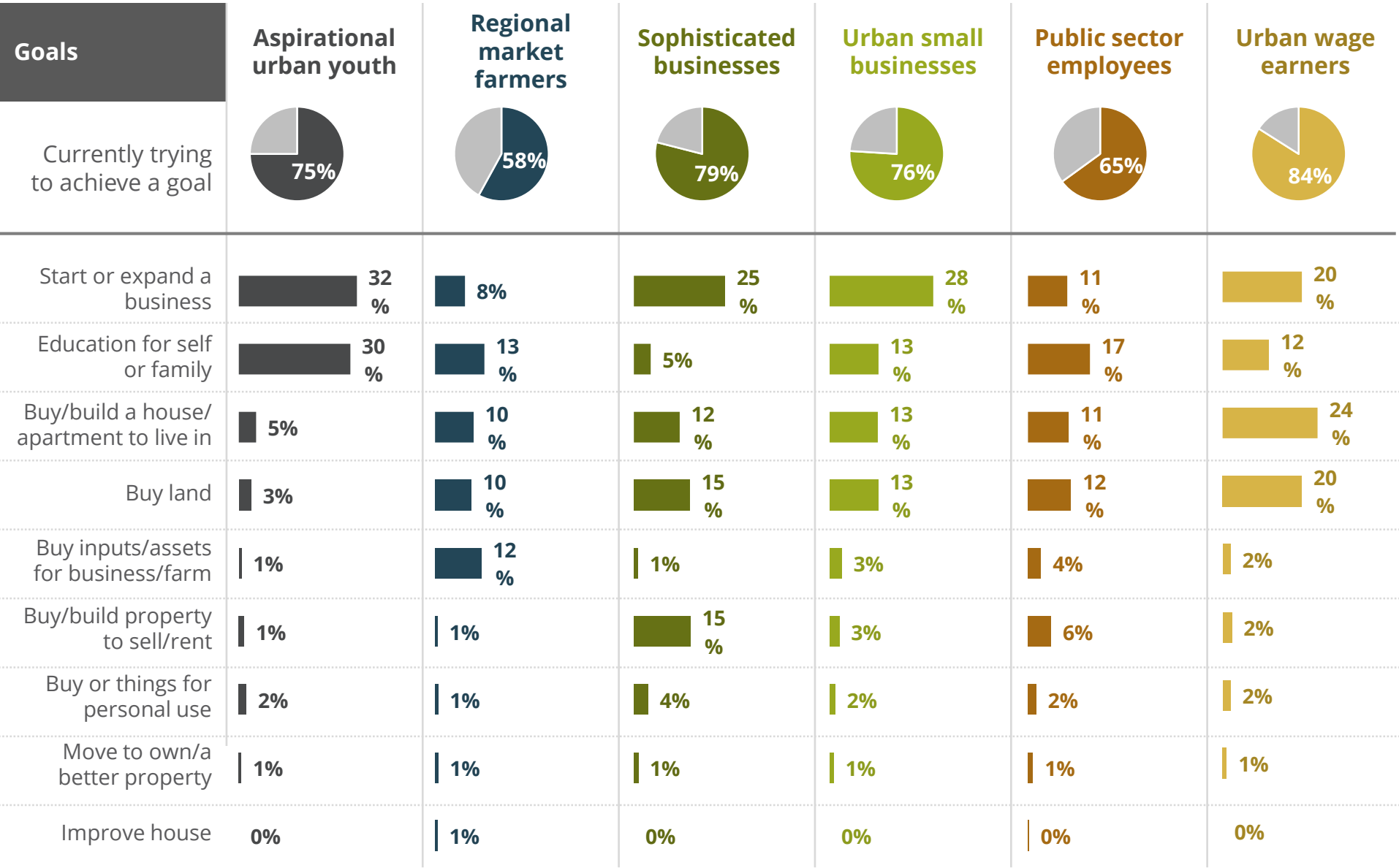
Source: FinAccess Survey 2019

Agricultural segments are the most likely to have suffered a shock in the past year. The most common shock across ALL segments is a major sickness/ health problem/ accident or injury

Resilience	Regional market farmers	Local market farmers	Sophisticated businesses	Urban small businesses	Public sector employees	Urban wage earners
Experienced big cost from managing resilience shock	46%	40%	37%	35%	38%	34%
Formal credit	6%	0%	5%	3%	12%	6%
Informal credit	2%	4%	1%	3%	1%	2%
Borrowed from friends/family	2%	5%	4%	7%	2%	2%
Formal savings	29%	9%	50%	23%	37%	29%
Informal savings	3%	3%	3%	3%	3%	3%
Savings with friend/ family/ secret place	6%	4%	5%	5%	0%	6%
Insurance	4%	3%	10%	2%	11%	4%
Sold asset/ crops/ livestock	10%	17%	0%	4%	1%	10%
Assistance from family/ friends	27%	39%	16%	40%	23%	27%
Changed behaviour	6%	8%	6%	6%	6%	6%
Did nothing	3%	7%	0%	1%	2%	3%

Source: FinAccess Survey 2019 I 18

The MAIN goals of those CURRENTLY trying to achieve a goal differ across segments. Urban aspirational youth are either trying to start a business or study further, whereas a significant portion of urban wage earners have housing-related* goals



Source: FinAccess Survey 2019 I 19. Note* Housing related goals includes: buy/ build a house/ apartment to live in, buy land, buy/build property to sell/ rent, Move to own or better property, and Improve a house

Wealthier segments use formal savings and credit devices to try meet their main goals. Many segments rely on non-financial devices to meet these goals

Goals	Aspirational urban youth	Regional market farmers	Sophisticated businesses	Urban small businesses	Public sector employees	Urban wage earners
Currently trying to achieve a goal	75%	58%	79%	76%	65%	84%
Formal credit	9%	19%	20%	10%	33%	18%
Informal credit	0%	4%	4%	5%	3%	3%
Borrowed from friends/family	6%	3%	0%	1%	2%	0%
Borrowed from Gov/NGO	1%	0%	0%	0%	0%	0%
Formal savings	23%	23%	46%	24%	31%	41%
Informal savings	2%	7%	2%	8%	9%	3%
Savings with friend/ family/ secret place	6%	3%	4%	6%	4%	5%
Sold asset/crops/ livestock	0%	5%	0%	0%	1%	1%
Assistance from family/ friends	10%	4%	0%	2%	1%	1%
Changed behaviour	27%	19%	22%	36%	11%	23%
Did nothing	3%	1%	0%	1%	3%	2%

Source: FinAccess Survey 2019 I 20

Several key needs cut across the target segments

Liquidity management



Business and climate resilience




Business expansion


Health risk resilience


Housing


Digital transfer of value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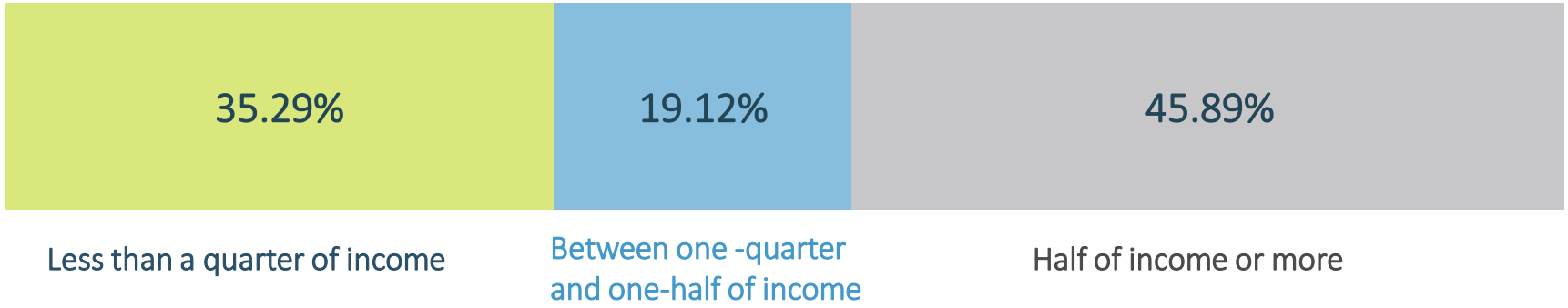
Unmet needs and their underlying drivers

Growing debt undermines future liquidity management

High levels of liquidity distress amongst wealthiest segments, leading to overreliance on credit

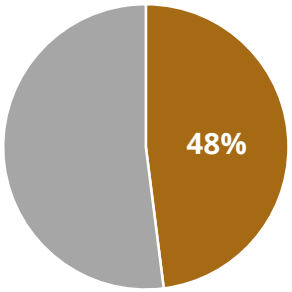
Indebtedness among public sector workers

Public sector workers who have taken out a loan (27% have no credit)
Proportion of monthly income contributed to debt repayments:

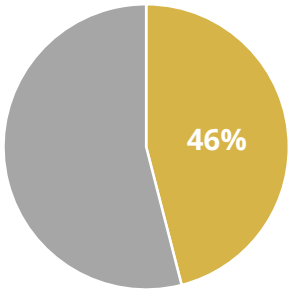


Experienced liquidity distress in the past 12 months

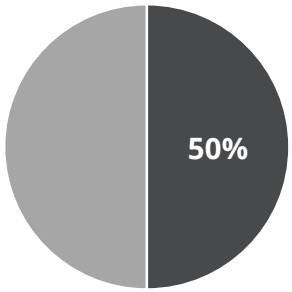
Public sector workers



Urban wage earners



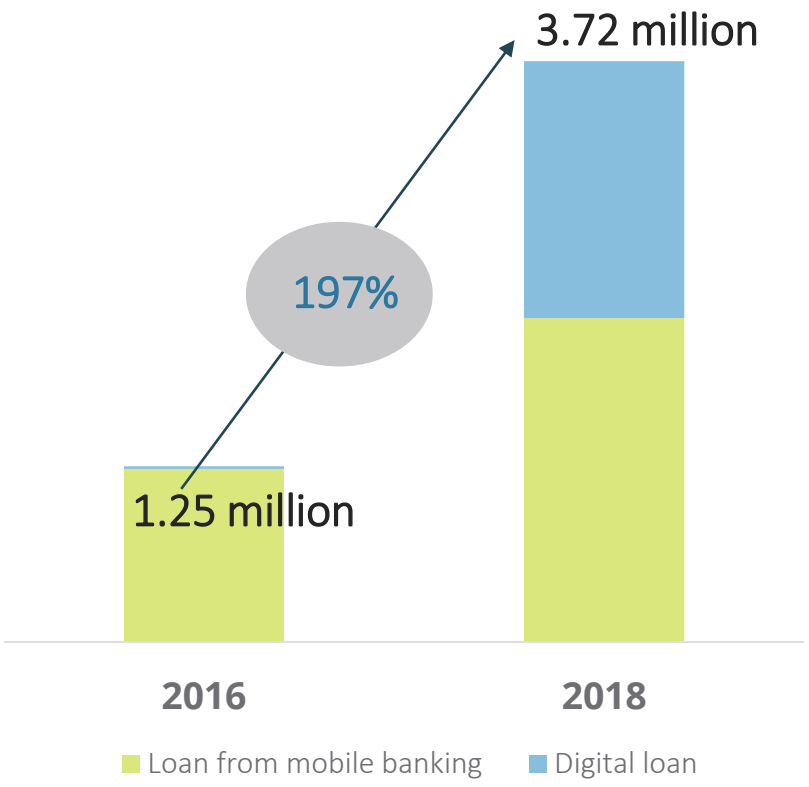
Aspirational urban youth



Source: FinAccess Survey 2019

And this is a rapidly growing trend

Growth of number of digital loans and loans from mobile banking

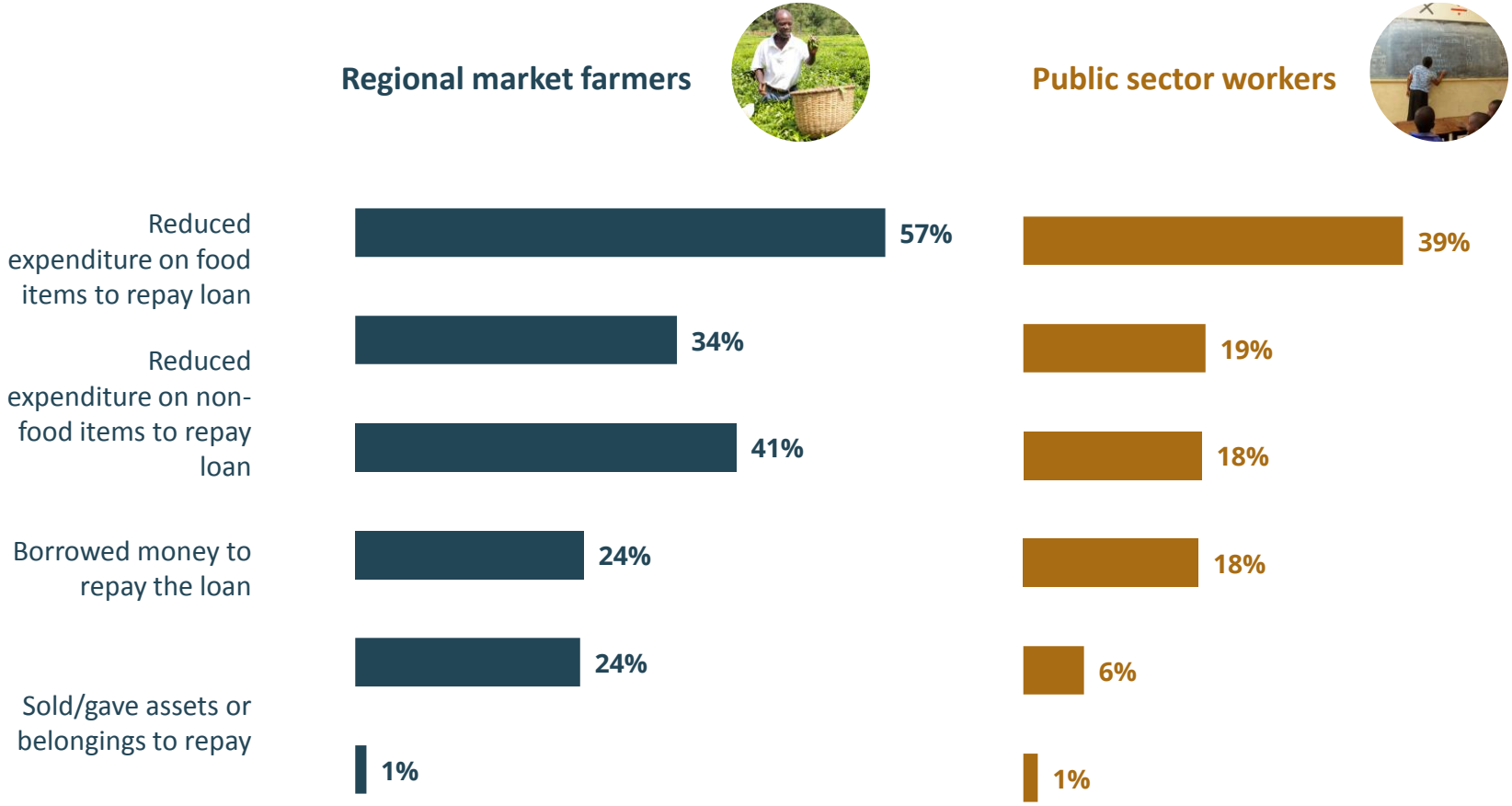


Negative consequences

- **47%** have repaid a digital loan **late** and **12%** have **default**
- **2.7 million negative reports** on digital loans

Sources: Kaffenberger et al. 2018, Mwangi, 2018, FSDK 2017, Gubbins and Totoloe 2018, FinAccess Survey 2019

So Kenyans fall back on welfare-reducing strategies to repay their debt



Source: FinAccess Survey 2019

Imbalance in regulatory approach has allowed innovation but left consumers vulnerable

Coordination

Challenge:

- **Lack of coordination** within and between regulators

Positive outcomes for consumers

Challenges:

- **Loan stacking** trends
- Rising **negative listing**
- Use of **welfare-reducing strategies** for **debt repayment**

Information flows and feedback loops

Challenges:

- **Weak coordination** mechanisms
- **Asymmetric information** as a result of infrequent coordination

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Redressing the balance important for sustainable development of the sector

Coordination

Opportunity:

- Improve coordination mechanisms

Positive outcomes for consumers

Opportunities:

- Credit Act for assessment of traditional and digital credit
- Financial market regulation designed for positive consumer outcomes

Information flows and feedback loops

Opportunities:

- Promote wider information-sharing between FSPs and non-FSPs
- Improve collection of credit information (including positive listing)

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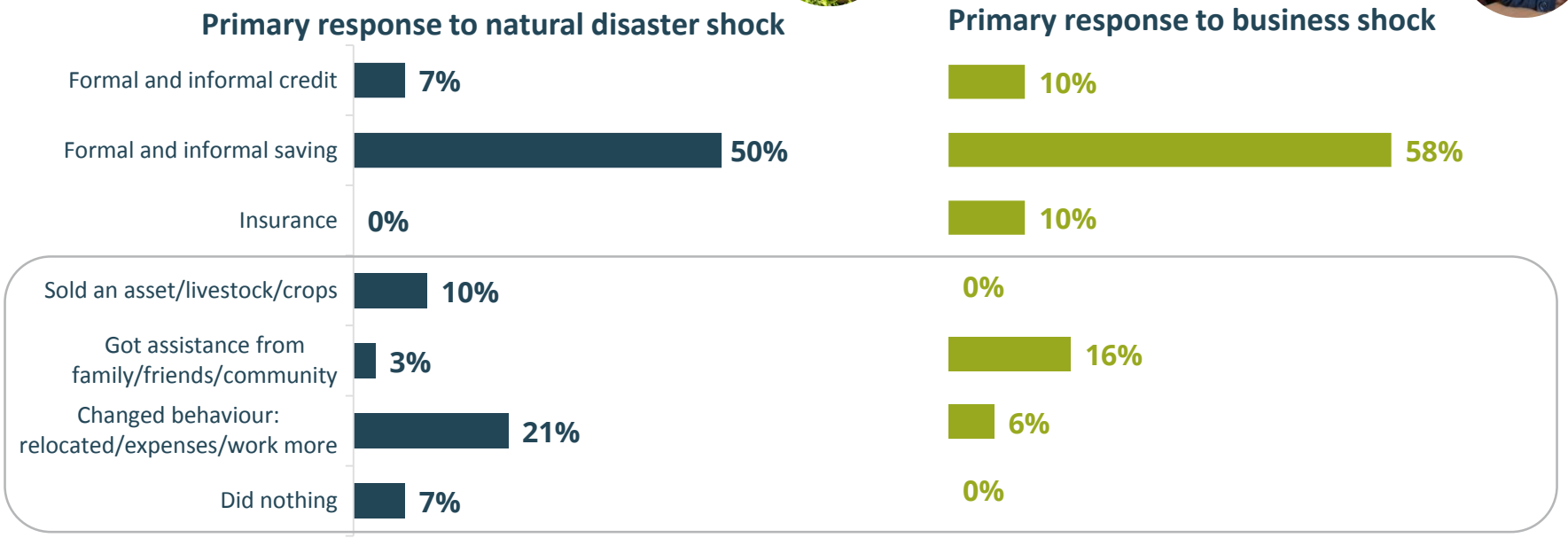
Farmers’ and SMEs’ resilience and access to growth finance undermined by challenging FSP business case

Farmers and SMEs frequently forced to rely on unsustainable livelihood resilience strategies

Regional market farmers

Sophisticated businesses



25% of sophisticated businesses want to expand their businesses, **15%** want to by a house to rent and **15%** want to buy land but only **20% of them use formal credit.**

Source: FinAccess Survey 2019

But they constitute a tough business case for FSPs

Value chain finance analysis prioritises the financial needs within the context of specific upgrades of a value chain if it is to take advantage of end-market opportunities.

FSPs are not meeting SMEs' and farmers' financial needs along most value chains

Challenges

Marginal business case	• Heterogeneous groups • Segments disadvantaged by fragmented value chains • Systemic nature of climate risks
Asymmetric information	• Heterogeneous groups • Distribution challenges
Marginal business case	• Heterogeneous groups • Segments disadvantaged by fragmented value chains • Systemic nature of climate risks

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However, there are ways to coordinate value chains effectively

VCs can be integrated horizontally, vertically or in both dimensions

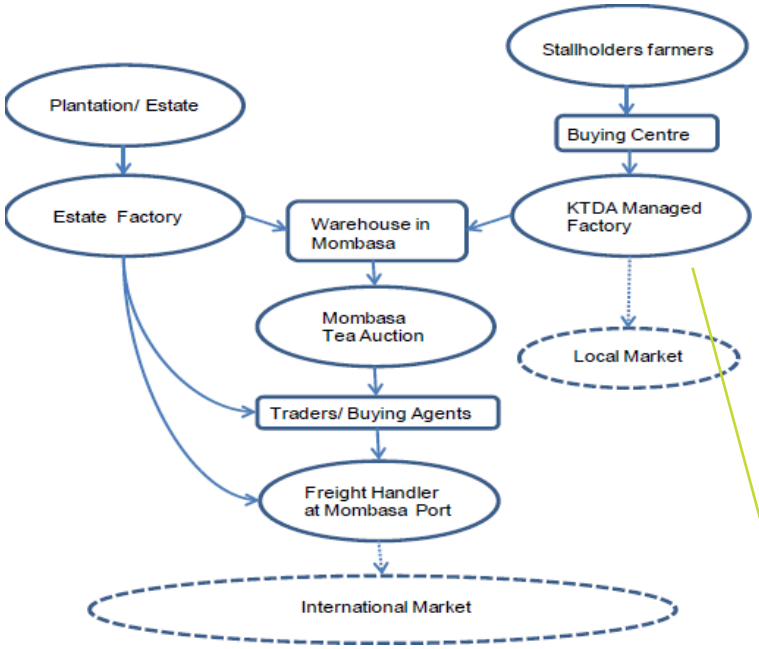
Model	Driver of organisation	Rationale	Instruments
Producer-driven	• Small-scale producers • Large-scale farmers	• Access new markets • Obtain higher market price • Stabilise and secure market position	• Alignment, coordination and accountability • Revenue collection • R&D and services • Market management and promotion
Buyer-driven	• Processors • Exporters • Retailers • Traders and wholesalers	• Assure supply • Increase supply volumes • Supply more discerning customers • Meet market niches	
Facilitator-driven	• NGOs and other support agencies • National and local governments	• Make markets work for the poor • Regional and local development	

Sources: FAO 2010, Vroegindeway 2015, IIED 2017

And comparing tea and maize illustrates the importance of an effective coordinating function

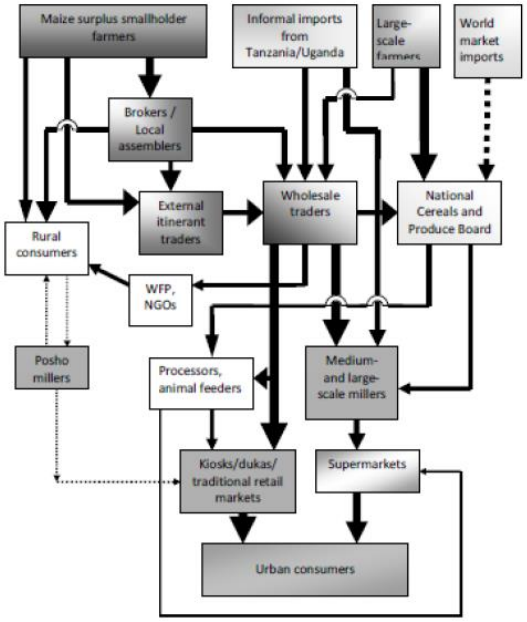
Tea value chain: contributes to **1.7%** of **GDP**

Highly integrated and efficiently operating value chain



Maize value chain: contributes to **0.1%** of **GDP**

Complex and unorganised system resulting in food security issues



Kenya Tea Development Agency plays central coordination role for smallholder farmers

Sources: MAFAP 2013, ODI 2015, KNBS 2018 I 35

KTDA illustrates how an effectively coordinated value chain can overcome many of these challenges

	Challenges
Asymmetric information	• Heterogeneous groups • Distribution challenges
Lack of consumer knowledge	Lack of knowledge about: • Needs and opportunities within VC • Delivery channels • Repayment channels
Marginal business case	• Heterogeneous groups • Segments disadvantaged by fragmented VCs • Systemic nature of climate risks

Instruments applied by KTDA

- Alignment, coordination and accountability
  Accountable to the smallholder farmers
- Revenue collection
  Levy and annual bonus to farmers
- R&D and services
  - Extension services
  - Research and training facilities
  - Loans
- Market management and promotion
  - Manages all sales for producers
  - Negotiates with buyers on producer's behalf
  - Sales promotion of teas

FSPs should consider to play or support a coordinative role in VCs to address challenges in serving SMEs and farmers.

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Sources: MAFAP 2013, IFC 2014, IIED 2017 I 36

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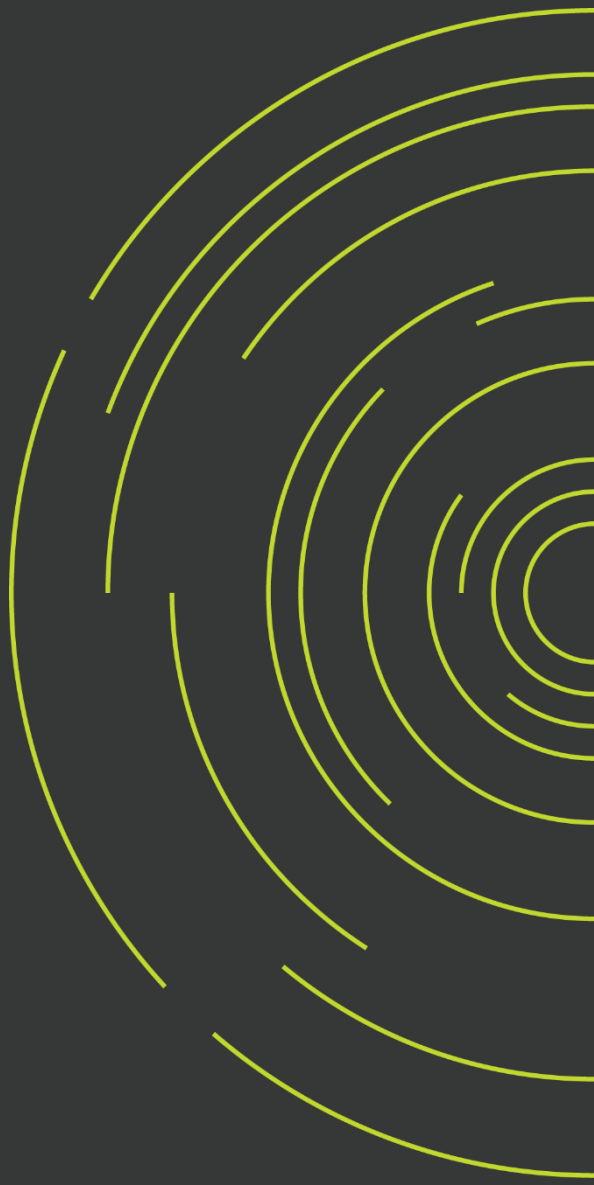
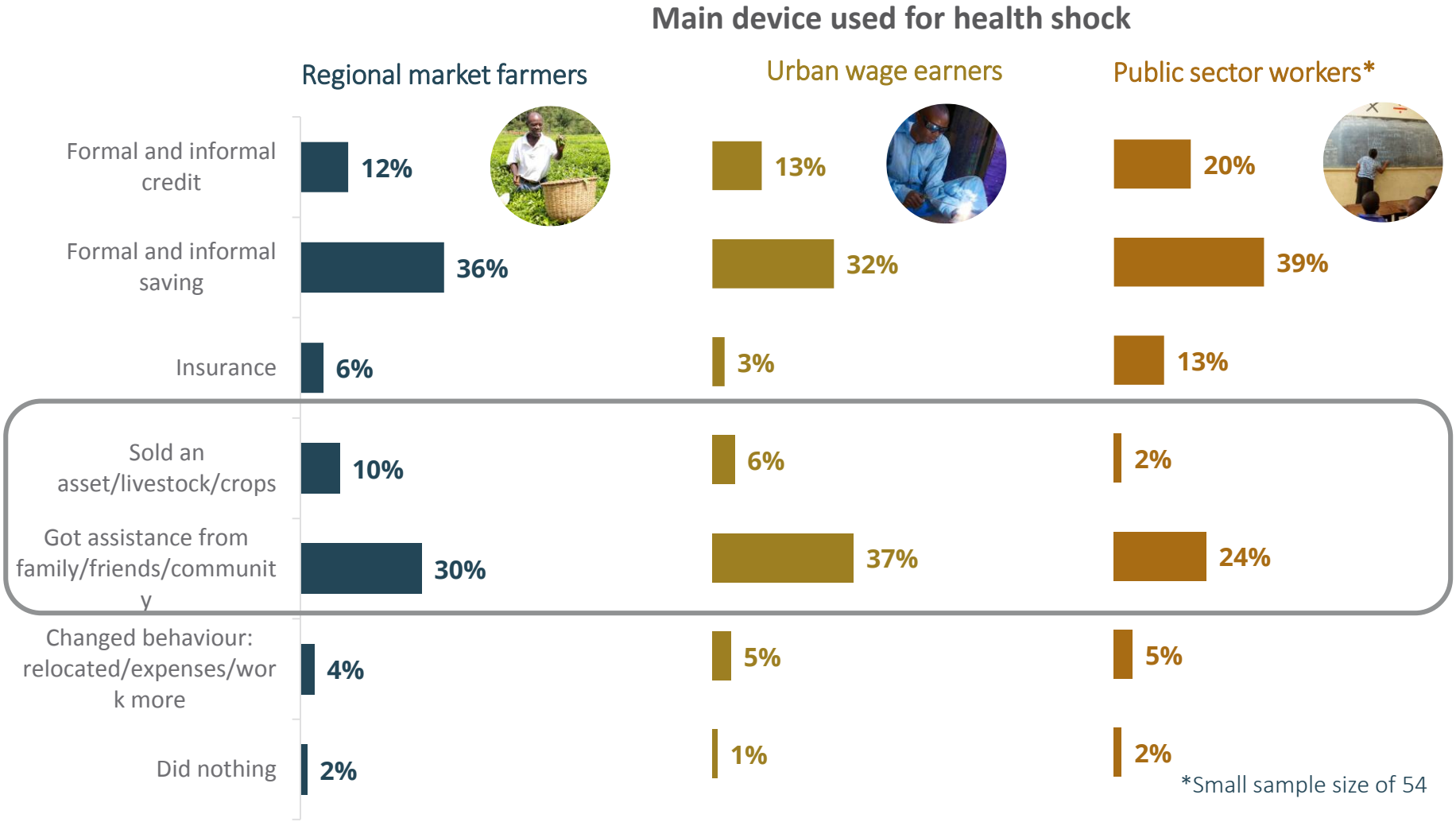
Inadequate health financing options to manage risk



Social solutions underpin health resilience in Kenya

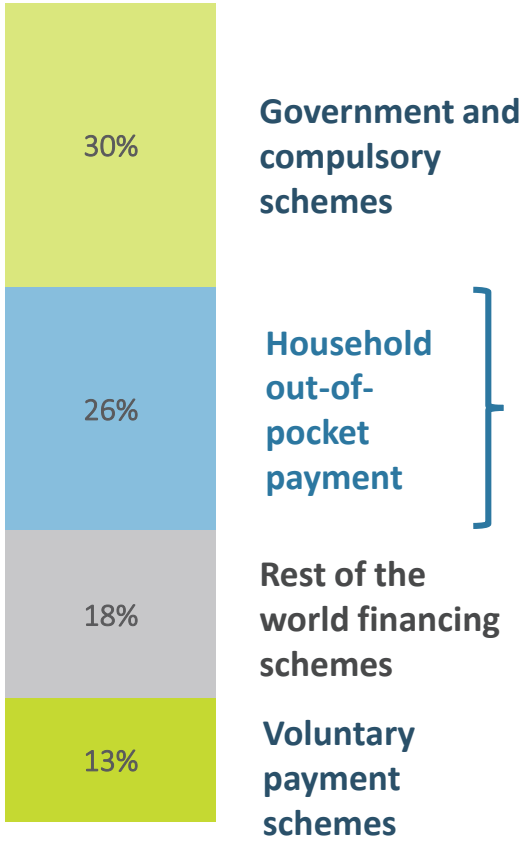
Unsustainable when risk are systemic, ongoing and prevalent for a longer time



Source: FinAccess Survey 2019

Inadequate health financing options inhibits health resilience

Financing scheme as % of total health expenditure (2015/16)



NHIF constrained to offer consumer-centric value

- Communication and information sharing
- Administrative obstacles
- Inflexible, high cost payment plans
- Delayed claim approval

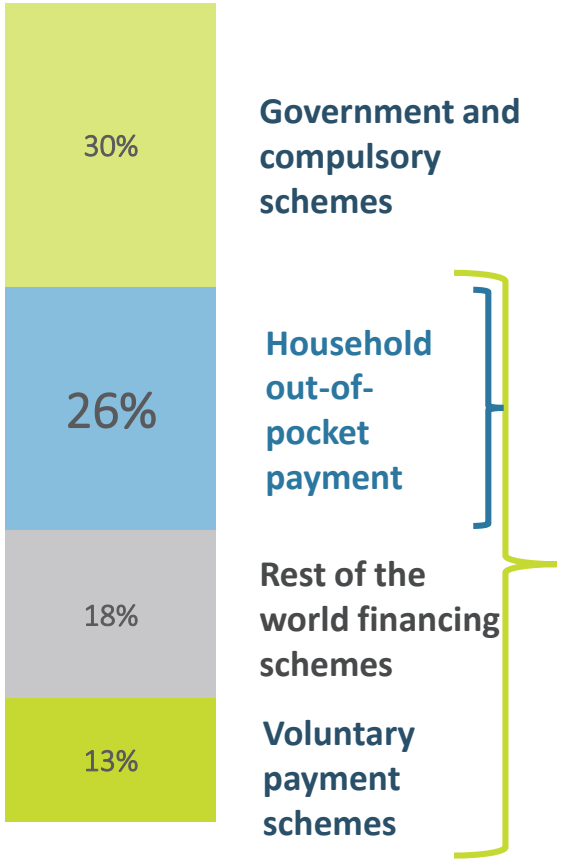
Lack of private sector top-up options

- Perceived weak business case
- Private sector crowded out
- Insufficient innovation incentives

Sources: Ministry of Health (2017), Barasa et al. 2018 I 39

Opportunity exists for complementary private-public solutions to boost uptake and profit

Financing scheme as % of total health expenditure (2015/16)



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Opportunities for private sector

- Capture **complementarity** between **NHIF** and **private solutions**
- **Foster digital platforms** for on-demand health support and finance

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Sources: Ministry of Health (2017), Barasa et al. 2018 I 40

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Unavailability of affordable housing and financing options

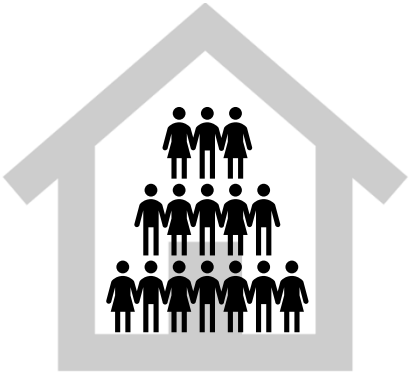
Affordable quality housing is a problem among even the wealthiest

Urban wage earners

26% [0.28m] live in inadequate dwellings

Public sector workers

30% [0.3m] live in inadequate dwellings

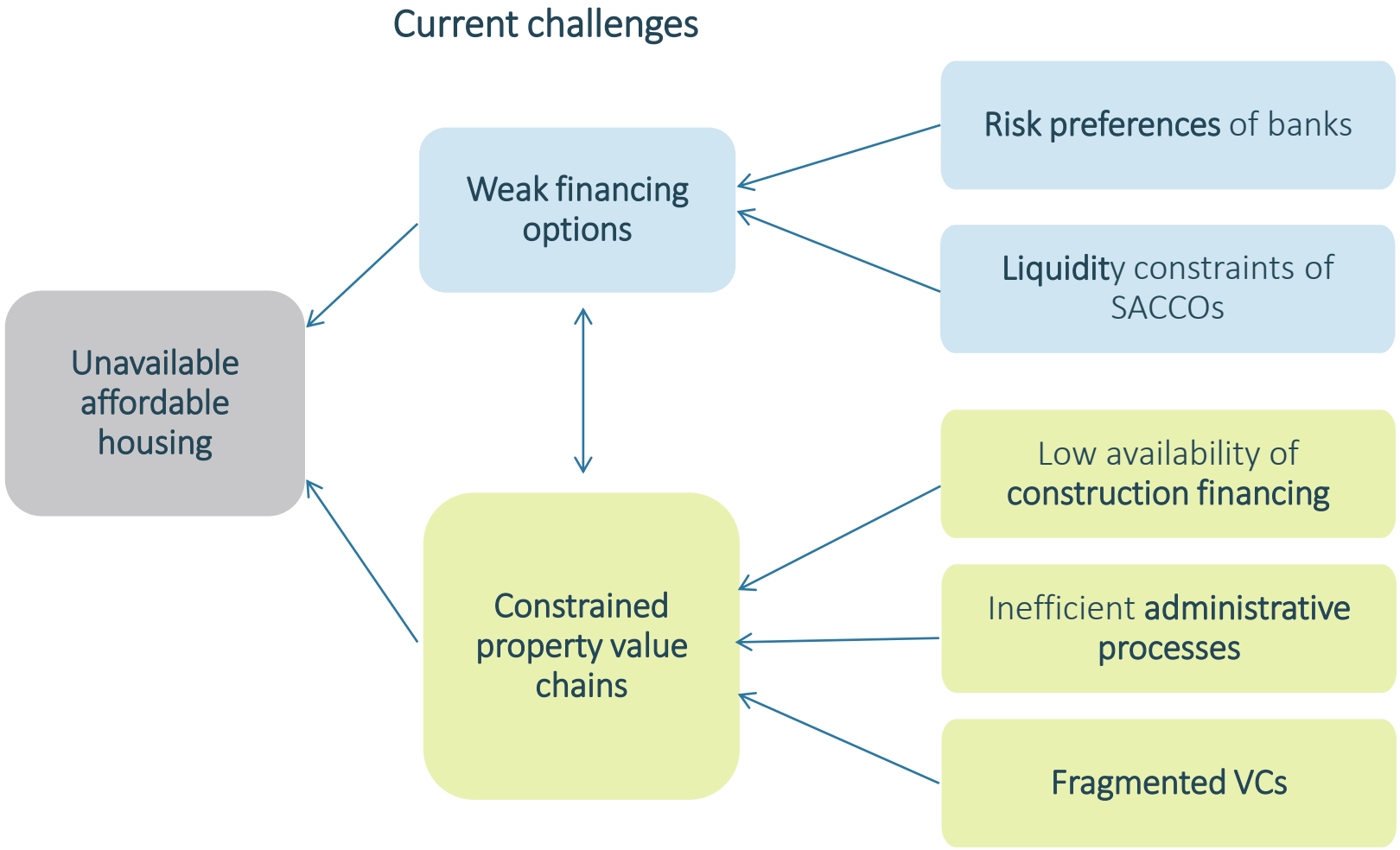


What constitutes inadequate housing?

- Semi-permanent
- Temporary
- Traditional
- Inadequate toilet
- Overcrowded

Source: FinAccess Survey 2019

Affordable housing constrained by weak financing and constrained value chains



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Greater efficiencies and opportunities can still be tapped

Current challenges

Unavailable affordable housing

Weak financing options

- **Risk preferences** of banks
- **Liquidity** constraints of SACCOs

Constrained property value chains

- Low availability of **construction financing**
- Inefficient **administrative processes**
- **Fragmented VCs**

Opportunities

- **Liquidity facilities** and innovation
- Greater **regulatory guidance** dual entity model
- Improve **regulatory framework**
- **Streamline** inefficient **land titling** and **transfer** processes
- **Sector coordination** and **defragmentation** of VCs

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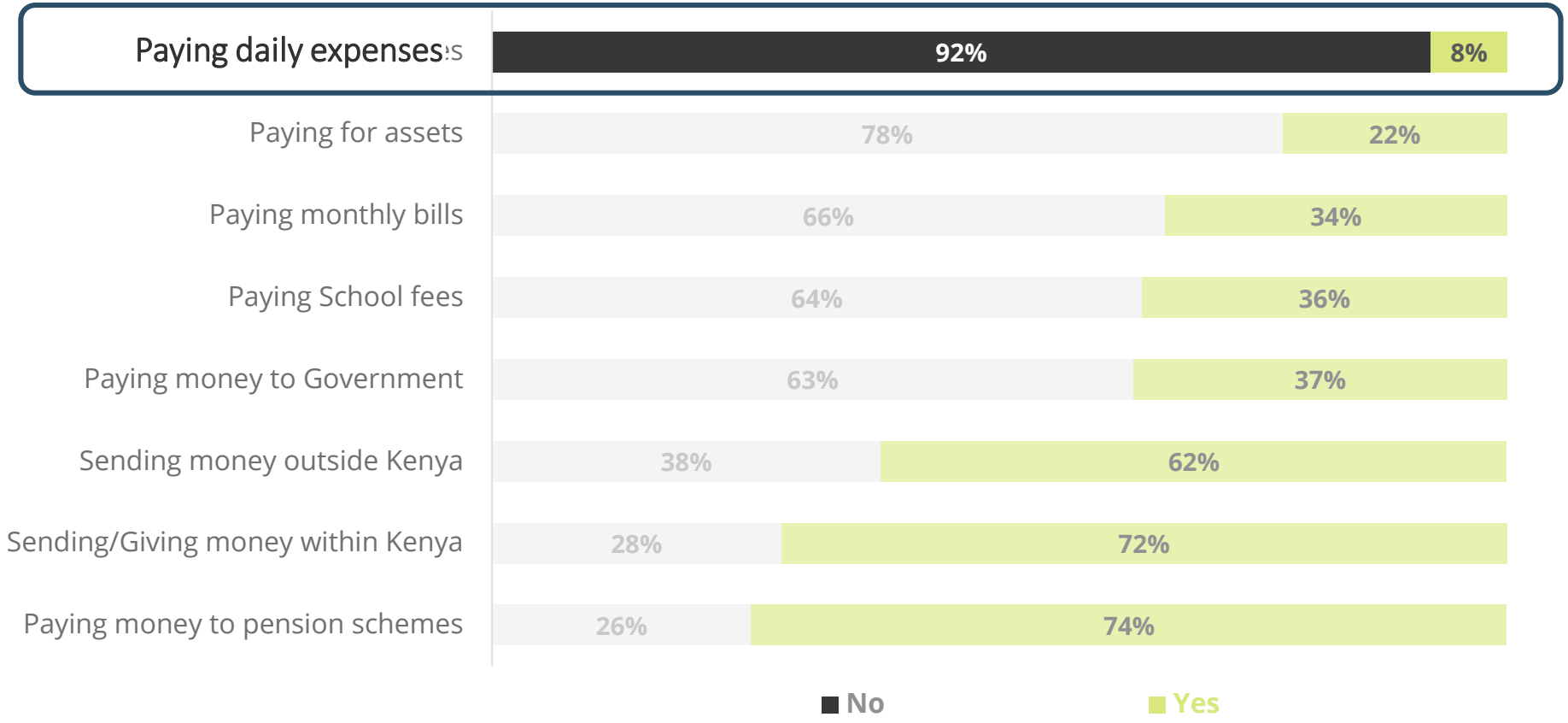
Weak digitisation of merchant payments

Over 90% of adults still rely on cash for daily expenses

HAVE MADE AT LEAST ONE PAYMENT VIA ACCOUNT FOR THE USE CASE IN THE PAST 12 MONTHS

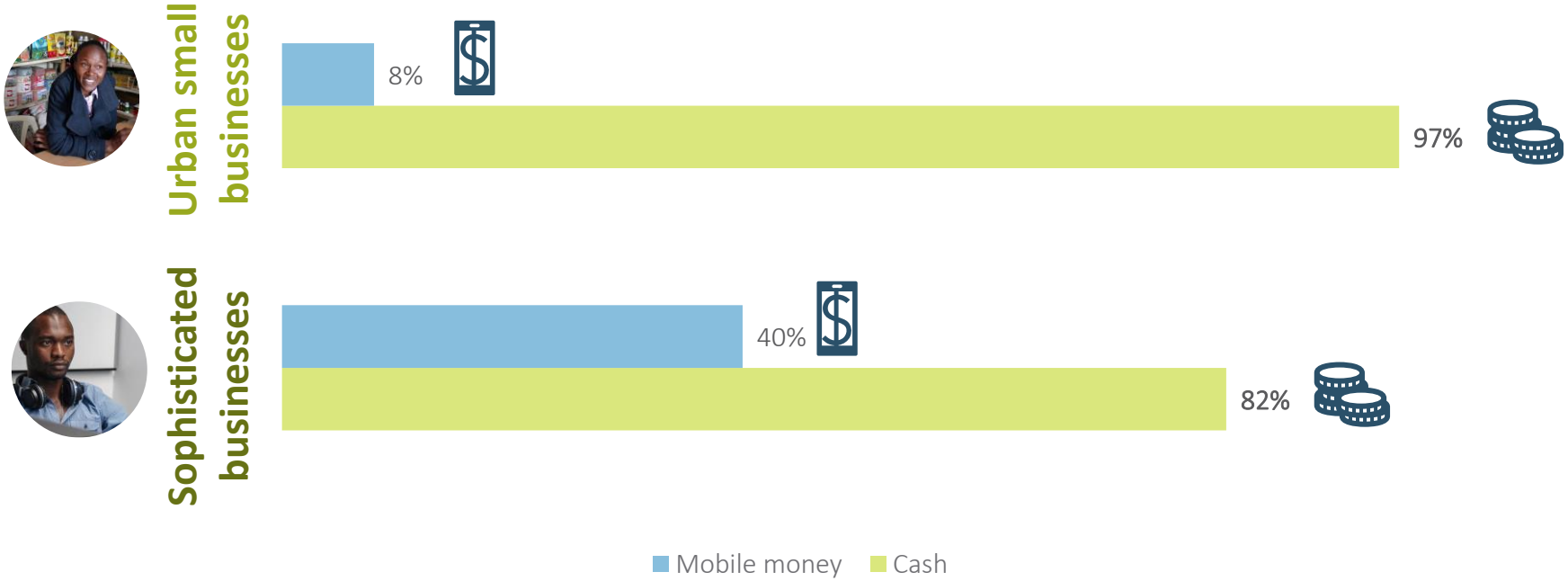


Source: FinAccess Survey 2019

Merchant use of digital similarly low relative to cash

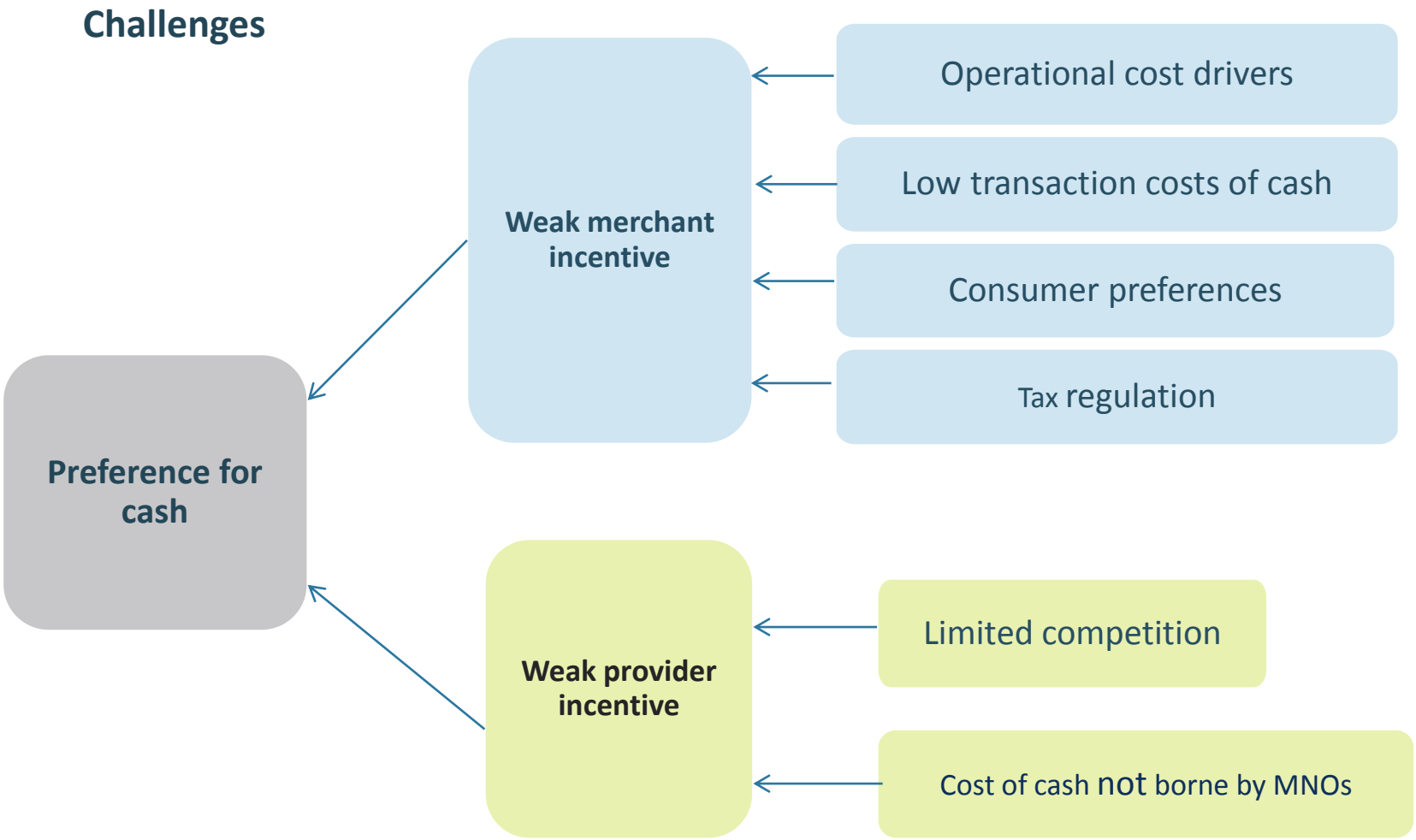
Cash payments raise merchant cost and undermine business expansion goals

Methods of payment for *business expenses* in the past 12 months



Source: FinAccess Survey 2019 I 47

Weak merchant and provider incentives enable cash preferences



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New value-driven approach needed towards merchant digitisation

Challenges

Preference for cash

Weak merchant incentives

- Operational cost drivers
- Perceived costlessness of cash
- Consumer preferences
- Tax regulation

Weak provider incentives

- Limited competition
- Cost of cash not borne by MNOs

Opportunities

Research **digitisation barriers** of merchants

Investigate and address **structural inefficiencies**

Promote innovation (e.g. QR codes, open APIs)

Research **true costs of cash** in relation to **MNOs**

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Summary

	Cross-cutting need	Unmet need	Drivers
	Liquidity management	Unsustainable liquidity management	Imbalanced regulation
	Business and climate resilience and business expansion	Sub-optimal strategies for resilient livelihoods	Fragmented value chains
	Health risk resilience	Inadequate healthcare financing options	Lack of private sector top-up solutions and constrained NHI
	Housing	Poor access to affordable housing	Low availability of housing finance and inefficiencies housing sector
	Digital transfer of value and business expansion	High reliance on cash	Weak digitisation incentives for merchants and providers

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Thank you

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Structure of breakout sessions

Structure of breakout discussions

- Split group into 4 breakout discussion tables – each one with a different topic (see box)
- Three breakout sessions – each lasts 15 minutes
  - **Session 1:** 11:00 – 11:15
  - **Session 2:** 11:20 – 11:35
  - **Session 3:** 11:40 – 11:55
- After each breakout session, **participants are free** to either **stay at their table** or to **rotate to the next table**

Breakout discussion topics

- Striking the balance in regulating for the digital age
- Strengthening agricultural livelihoods
- Enhancing affordable housing
- Enabling digitisation of merchant payments

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