The Innovation Village

FUTURE LAB
By The Innovation Village

THE ROLE OF

FINANCIAL HEALTH

IN BUILDING RESILIENT MSMEs

SOLOMON KITUMBA

Founder of Swipe2Pay

Swipe2Pay is a fintech company which enables SMEs to accept both card and mobile money as a mode of payment and to also make sense of their sales data to inform them about how they are running their business. The solution goes beyond payment processing and includes a free point-of-sale app and a free business intelligence portal, enabling business owners to monitor their store performance.

JOEL MUHUMUZA

Country Manager, Uganda at Jumo

Jumo is a full technology stack for building and running financial services, providing access to savings, lending & insurance products to startups/SMEs in emerging markets. Jumo is currently established in six (6) locations in Africa and three (3) in Asia namely: Uganda, Tanzania, Kenya, Ghana, Zambia, South Africa, Pakistan, Singapore,and India.

STEPHEN WAISWA

Digital Financial Services and ValueChain Consultant working with UNCDF under the Mobile Money for the Poor Project (MM4P)

The United Nations Capital Development Fund (UNCDF) mission has since evolved from financial inclusion to building a digital economy towards inclusion and leaving no one behind. Stephen is tasked to deliver competitive dynamics and market insights to support the digitization efforts in both the Maize and Dairy Value Chain in Uganda. Additionally, he is accountable for assessing the competitive landscape and helps foster financial Inclusion by positioning and unlocking the potential within the Agricultural Value Chain where most of the bottom of the Pyramid participate.

KENNETH LEGESI

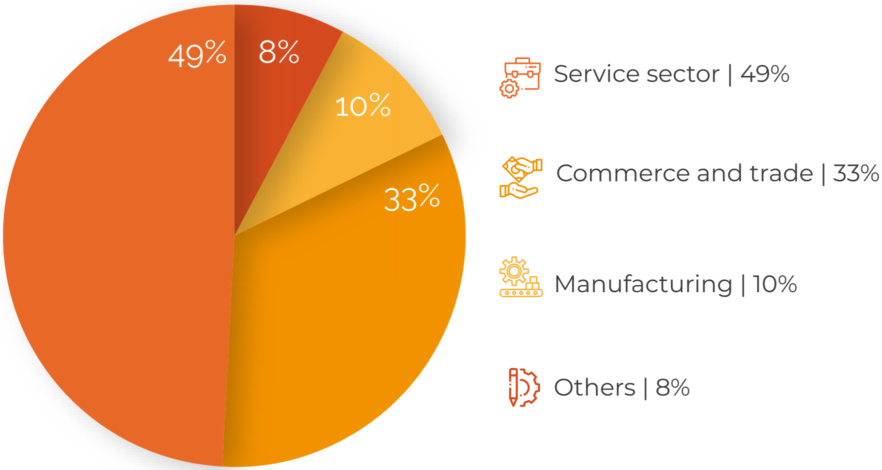
Partner and Chief Investment Officer at Ortus Africa

Currently managing The 97Fund for early stage funding and investing in startups. Formerly worked at Deloitte Uganda and United Kingdom as a Corporate Finance and Infrastructure and has vast experience in sectors such as Tech, Ecommerce, Energy Infrastructure.

According to the Ministry of Trade, Industry and Cooperatives 2017 report, Micro, Small and Medium Enterprises (MSMEs) are the anchor engines of economic growth, job creation and innovation in Uganda accounting for approximately 90% of the entire private sector, generating over 80% of manufactured output that contributes 20% of the gross domestic product (GDP) spanning across all sectors. MSMEs are also the highest informal sector employer with over one million enterprises; Micro 93.5%, Small 4.1% and Medium 2.4% employing over 3.5 million people[1].

Furthermore, MSMEs are marred by inadequate technical, business and managerial skills; lack access to affordable finance and credit; low adoption of technology tools and limited access to quality assurance services without which they cannot compete, grow and scale.

These challenges have been further exacerbated by the recent COVID-19 pandemic as businesses have closed due to the lockdown and cash flow challenges, they have had to dramatically cut costs especially employee wages and daily operations that are crucial for the wellbeing of the business.



What is financial health?

Financial health is one's ability to earn income; monitor their spending patterns including their ability to save and have residual to spend. This information can be evaluated and enable them to not only borrow or access credit for a particular need in future but also to pay back.

From a market systems perspective, a key initiative at UNCDF, it begins with an in depth market assessment using different principles using Human Centred Design (HCD) tools to understand the capabilities of the people in the community e.g. the cash mapping exercise to comprehend spending habits, incomes earned, etc.

[1] http://mtic.go.ug/2016/index.php?/doc_download/303-msme-policy-booklet/

What are the indicators in the local Ugandan Context?

In the local Ugandan context, the indicators can be categorized into these factors;

Income:

One should be selling products and/ services to generate some form of income.

Expenses:

One should know what is bleeding their cash e.g. taxation, Capital expenditure (CAPEX).

Full visibility of the accounts (AR and AP):

a. Accounts Receivable (AR):

Selling on credit and being able to balance the AR with the suppliers.

b. Accounts Payable:

Money owed by a business to its suppliers shown as a liability on a company's balance sheet. Examples include: accounting services, legal services, supplies, and utilities, to mention but a few.

Essentially, in order for MSMEs to be "financially healthy", they must be able to balance out these factors by being able to;

- Withstand certain extreme conditions or rigours
- Spend less than you bring in
- Survive for the next 5 months without income from customers in a worst case scenario
- Handle debt
- Plan in time

However, the current nature of MSMEs here is that they are very personalized to founders/owners which does not make them financially healthy. MSMEs are typically cash based and very informal, with the pandemic posing an even greater threat to their existence. Measures such as (extended) lockdowns have crippled businesses and social distancing which is a new normal will affect the "personal nature" of these businesses.

What are some use cases that we can draw from startups?

Fortunately, in the pre COVID era, a number of startups have stepped up to address these challenges (even before the global crisis). It would be worth sharing lessons learned to inspire the development of their solutions.

Swipe2pay have been doing credit scoring for MSMEs to enable them access credit from banks and other financial institutions since they have no formal records or no financial history. By streamlining business processes in real time, they have built a payment layer outside cash i.e. cashless via mobile money, MPESA and recently Interswitch. They use business performance data to determine business creditworthiness navigating the shortcoming of lack of financial history. Swipe2pay helps MSMEs with digital migration onto the digital marketplace.

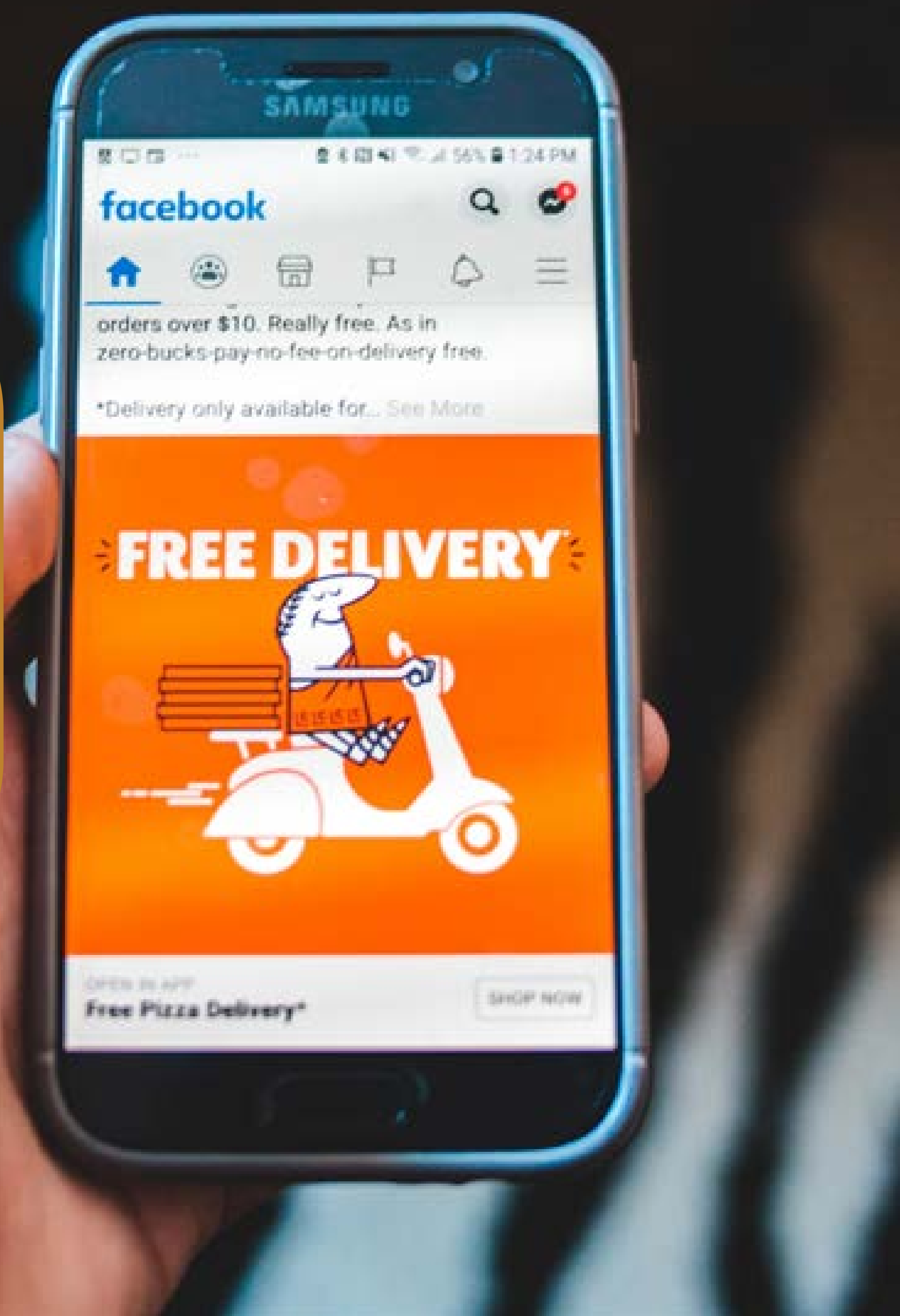
Jumo's goal is to recognize that capital is available and that MSMEs can access this capital. However, the largest share of these businesses are unknown. Jumo has been able to gain some form of visibility through mobile money, as remittances are sent from one phone to another and is leveraging Mobile Network Operators (MNOs) to obtain data for credit scoring. The businesses that pay on time are able to borrow more.

However, the biggest hurdle is that beyond digitizing how one receives credit as there is no visibility of what and how MSMEs run their operations. Additionally, the way capital is deployed is another shortcoming. Banks have money but the current mechanisms to lend money to MSMEs has limited impact.

In this COVID-19 era, how many businesses can be digitized? There is a need for **creative destruction** to change the fundamentals of how to link MSMEs to their customers. There has to be a better enabling environment to enable this transition for MSMEs and their robustness.

What opportunity spaces has COVID-19 paved for industry and business?

There is a need to improve the loan appraisal process in credit scoring, and there are alternative sources of data to inform this such as Savings and Cooperatives (SACCOs) transactional data. Additionally, startups can take up numerous distribution models and scale up delivery mechanisms to capture data of last mile customers for instance across the agriculture value chain.



Women's economic empowerment - Closing the gender gap

Zooming in on the composition of most MSMEs, one could argue that they are primarily driven by women. The Mastercard Index of Women Entrepreneurs ranked Uganda with the highest percentages of women-owned businesses across the 58 markets evaluated around the world. 38.2% of businesses are women-owned implying women entrepreneurs are powerful engines of economic growth and wellbeing of the society[2].

However, this pandemic undermines the work done towards addressing the age-old gender inequality and reinforcing the vicious cycle of poverty. In the midst of this crisis, what innovative pathways e.g. what new financial products can be developed or what business models can be adopted?

Access to financial instruments

The disparity between men and women's access to financial services has always been an issue - more of societal one than economics. According to UN Women, there are four reinforcing barriers to gender equality namely; deeply patriarchal socio-cultural norms regarding ownership of property and education; discriminatory laws and insufficient legal protections of women's rights; gender gaps in unpaid household and care work; and unequal access to digital, financial and property assets[3].

For instance, businesses such as cross border trade where women dealing in agriculture products or artisans will be some of the most affected. This is due to the fact that the need for cash is high and also a lot of exchange of cash takes place.

Historically, Village Savings and Lending Associations (VSLAs) have always been a great resource for how banking started as groups pooled their resources together. This is also an area where women have outpaced men as they are more likely to pay back loans. There is a need to create better structures and build stronger networks to allow co-rallying of resources that exist within than bringing in external resources. Asia presents use cases for the impact of VSLAs in the different markets - credit is the fuel for growth.

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[2] https://newsroom.mastercard.com/wp-content/uploads/2019/11/Mastercard-Index-of-Women-Entrepreneurs-2019.pdf
[3] http://hlp-wee.unwomen.org/en

Laying digital rails for financial inclusion

The 2013 Finscope reported that 25% of women are likely to own a mobile phone yet alone be active users of mobile money compared to men at 38% and a significant gender disparity as 40% of men were more likely to save at banks compared to women[4]. Today, there are still certain areas that do not permit women to own or access phones.

There is a dire need for innovative device campaigns to improve phone ownership as the digital trend becomes a mainstay in transactions. This will become an enabler in business especially in the rural areas especially targeting women in the agriculture sector who account for 70% labour participation. How might we build digital rails to create a springboard to allow digitalization and drive financial inclusion? How might we target phone penetration in the rural areas and last mile customers?

In the event of an extended lockdown, what should MSMEs prioritize to ensure business continuity?

MSMEs at the moment should appreciate "the new normal of business unusual", be more agile and adopt to new trends with practical resilient techniques such as;

- Protect your staff from exposure to the pandemic[5]
- Pivot their business to create new products and services to what is in demand e.g. alcohol and spirits manufacturers converting ethanol to hand sanitizers to fight the pandemic
- Seek better access to finance especially short term working capital, capital to go the long haul, unlock innovative financing e.g. community crowdsourcing, convert cash reserve for cash flow as you plan for the unforeseen future (worst case scenario)
- Cut your overhead costs
- Retaining their existing customers by engaging them to determine if their needs are the same or otherwise.
- Review your human capital and explore new ways to upskill them to thrive.

[4] https://www.bou.or.ug/opencms/bou/bou-downloads/Financial_Inclusion/Finscope-Report-2013.pdf
[5] https://www.monitor.co.ug/News/National/Government-manufacturers-ethanol-hand-sanitizers-Covid-19/688334-5501390-r8lgrb/index.html

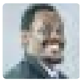
What capabilities and resources should be incorporated in the recovery and resilience action plans?

We need to "normalize the new normal". It is undeniable that the circumstances have driven and new tools have been adopted as well.

- The pandemic has shown that globally everything is debt financed, therefore **financial discipline** is important e.g. creating cash reserves
- **Digitization:** Explore opportunities to migrate to cashless
- **Diversification:** As more digital tools become available, how can you move beyond your initial customer base.
- **Adaptability:** analyse your value proposition and critique if your business models. Is it still relevant to your customers? And if not, what do they require?
- **Work From Home (WFH)** is becoming more conventional for the workplace. What will your business need to consider traditional methods over remote working?
- Workforce needs to be **upskilled** to allow them be multiskilled so they are relevant to the business
- **Policy frameworks and enabling environments:** How will the government fastrack and turnaround policies? Currently, the cost of digital devices is high thus prohibitive to the growth of the digital economy. Developing tax holidays for specialized devices will enable us to achieve the end game.

In conclusion, Ben Roberts Group CTIO of Liquid Telecom, recently stated that COVID-19 might have kickstarted the digital economy[6] and therefore;

Every SME should at least have some online strategy fitted into how they operate – online payments and online transactions



The more independent we have become, the more interdependent we have become.

Let's not reinvent the wheel – learn from other countries and adopt for Uganda (Centre for Finance Inclusion)

This has shown us as a nation that we have to be building systems that address such shocks – enable digital solutions (marketplaces or platforms)

[6] https://medium.com/african-innovations-liquid-telecom/did-corona-just-kick-start-the-digital-economy-2d6df96c03ce

04 | Audience Q&A

How easy is it going to be for MSMEs to attract funding?

These times are unconventional and so conventional sources are not available. Alternatives and blended funds such as government response funds, guarantee funds, tax breaks, breaks on paying NSSF and government buying local products/services will support MSMEs instead of Venture Capital.

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