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Local Counsel's Perspective on Fintech Trends, Challenges and Developments in Kenya, South Africa and Nigeria

Leila Belcarz interviews Henry Omino of Walker Kontos Kenya, Kate Beretta of Bowman Gilfillan South Africa and Yinka Edu and Tolulope Osindero of Udo Udoma & Belo-Osagie Nigeria in December 2016

Payments is a key fintech area in Kenya, South Africa and Nigeria, and banks are increasingly partnering with mobile payment providers to move into the space. South Africa has seen a marked rise in fintech start-ups/joint ventures, with a number of funders launching "incubators" and "accelerators". Nigeria is also seeing a rise in fully digital/online banks (e.g. Lidya) and mobile lending offerings. There has been an increase in Kenyan payments regulation (e.g. requirements for central bank licensing and ring fencing of customer funds), with a data protection regulation likely to be passed in the near future. These requirements are not especially onerous in light of the significant role played by the payments industry in Kenya, and has reinforced Kenya's role as a payments market leader and increased user confidence. South Africa's regulation of fintech is, in contrast, more reactive, having fallen behind technologies, presenting a challenge for fintech disrupters, but also increasing the opportunity for innovation. The Central Bank of Nigeria has encouraged use of mobile payments, and has introduced a cashless policy to discourage cash payments over certain limits, however, there is still a long way to go with getting Nigerian consumers comfortable with the security of mobile payments, and related data protection issues. In the near future, Kenya and South Africa are likely to see an increasing formal regulatory environment, with key mobile payments players in Kenya (e.g. M-Pesa) given a "designated firm" status, where they would have increased scrutiny and regulation. South Africa is also set to see the Financial Sector Regulation Bill enacted, which should ease the transition into adequate regulation of technological and innovative solutions in South Africa. With Nigeria's government and start-up incubators increasingly rolling out initiatives to increase the young population's technological literacy, and the rolling out of 4G mobile networks, these will drive innovation and demand for fintech products in Nigeria. Henry Omino, Kate Beretta, Yinka Edu and Tolulope Osindero give their perspectives on fintech trends, challenges and developments in Kenya, South Africa and Nigeria.

1 What trends or success stories have you seen recently in fintech deals/the fintech industry more generally?

Henry (Kenya): Mobile payments is a huge deal in Kenya, with the Kenyan Central Bank's September 2016 statistics showing that KES 283 billion were transferred via mobile payments. Increasingly, more and more major players are entering the space, such as Visa, which launched its mVisa app, as its Kenyan mobile payments offering in September 2016. Banks are also increasingly partnering with mobile service providers to have a mobile payments offering. Kenya's Equity Bank went even further recently, and went down the route of launching its own sim-card, to enable its subscribers to access its services.

Kate (South Africa): South Africa's fintech industry is growing rapidly, but in relatively early stages of development. The number of unbanked South Africans presents a significant opportunity, and payments is a key focus area. New payment players in South Africa include BitX (a digital wallet facilitating Bitcoin transactions), and Yoco and iKhokha (which provide simplified hardware and software to facilitate mobile payments). Direct investment into, and joint ventures with, fintech start-ups is also generally on the rise. Examples include Standard Bank's investment into SnapScan (a QR code based mobile payments app), Investec's investment in WiGroup (South Africa's first mobile wallet and mobile transaction services facilitator), and Old Mutual's investment in 22Seven (a personal financial management services application). Many South African funders have also launched "incubators" and "accelerators"[1] for fintech start-ups (such as Rand Merchant Bank's incubator division, the Foundery; the Barclays Rise accelerator program; Rand Merchant Insurance Holdings' AlphaCode; the Grindstone Accelerator by Knife Capital; and Standard Bank Incubator and Ignitor).

Yinka/Tolulope (Nigeria): Fully digital banks and mobile lending offerings are increasing in Nigeria, with Nigeria's first digital bank, Lidya, recently launching, and SunTrust Bank, Nigeria's first financial technology commercial bank, launching in August. Paylater recently entered the mobile lending space, providing uncollateralized loans to individuals on their mobiles. Mobile payments continues to play a key role, with the Central Bank of Nigeria (CBN) estimating that the average transaction value of mobile payments has risen from US$5 million in 2011 to US$142.8 million in 2016. Paystack (backed by US venture capital firm YCombinator) launched a payment platform earlier this year (it has now partnered with over 1,300 merchants), competing with the likes of Quick teller and Pagatech, who have been in the payments space for some time now.

2 How have policy decisions/regulatory changes helped to bolster the trends, if at all?

Henry (Kenya): There has been increased regulation in Kenya - when M-Pesa entered the market, the mobile payments space was essentially unregulated. However, the National Payment System Act 2011 and National Payments Systems Regulations 2014 have introduced an oversight, risk management, reporting and consumer protection framework. For example, mobile payment providers also need a licence from Kenya's Central Bank, which will consider the financial condition/history of the applicant, on a case by case basis (there are no thresholds, so there is room for manoeuvre for start-ups). Funds passing through the mobile payments system must be held in a trust fund in a "strong rated bank" (amounts must be split across different banks when certain thresholds are exceeded, to protect against the risk of banks collapsing). Payment providers must now have a customer care platform (customer complaints must be resolved within 30 days, and users have a right of appeal to the Kenyan Central Bank). Although there is now more regulation, it cannot really be described as especially onerous (there was extensive stakeholder consultation previously), taking into account the sensitivities of payment systems to the Kenyan economy, and the billions pushed through each month. Ultimately, these regulations are important, to provide clarity, ensure that Kenya remains a market leader in mobile payments and to increase user confidence. It also creates more of a level playing field for start-ups, as they know exactly what is expected of them. Consequently, the Kenyan market has generally accepted and embraced the increased regulation, and it could be said to have helped the mobile payments industry grow.

Kate (South Africa): The opposite is probably true, as the South African Reserve Bank has taken a relatively reactive approach to regulating the fintech industry, instead of a proactive one. This has possibly hindered new entrants, as the existing legislation and regulations (generally limited to regulating outdated technologies) have fallen behind technology. For fintech start-ups, in particular, this can create an initial cost barrier because it is often unclear how the existing framework applies to their new technologies (if at all), and how they should comply. However, this policy/regulatory lag has also increased opportunity for innovation. Because many fintechs fall outside of the regulatory landscape, there have been and will continue to be tremendous advancements and developments in the South African fintech space.

Yinka/Tolulope (Nigeria): The CBN's policies encourage use of mobile payments systems, which has aided sector growth. In 2012, it introduced a cashless policy to discourage cash payments over certain limits. This has triggered innovations in our payments system, with most banks having banking and payment apps, and other third parties offering mobile/internet payment solutions. Additionally, the Nigerian government, in collaboration with the World Bank, has proposed the introduction of "information communication hubs" across the 6 geopolitical zones in Nigeria, which will generally boost the fintech sector.

[1] Accelerators focus on accelerating business development through programmes providing startups with access to corporate infrastructure, services and mentorship for a set timeframe, while incubators focus on innovation and developing disruptive ideas with the hope of possibly building a business model (often with no set timeframe attached).

3 What challenges does the fintech industry face?

Henry (Kenya): Data protection laws are likely to be enacted, as currently there is no separate framework in Kenya (there is only limited protection in the Kenyan Information Communications Act, but the scope is limited). Various data protection bills have been proposed at times, with a 2015 bill currently being considered. While this will augment the regulatory framework, service providers already encrypt data, and so it is unlikely the data protection law will require them to do anything that they are not already doing.

Kate (South Africa): Fintech disruptors face major challenges in making sense of the South African regulatory landscape (which is geared towards traditional financial services players), and how it applies to them and their innovations. However, despite the rise in fintech start-ups, a major challenge for fintech start-ups is a lack of capital, because South Africa's investment culture is generally still geared towards private equity (rather than venture/angel funding). This attitude will clearly need to shift to facilitate increased fintech start-up innovation and disruption. Another challenge more broadly is a lack of education and training, both at a corporate integration and skills development level.

Yinka/Tolulope (Nigeria): 39.5% of Nigeria's population is financially excluded and only 36.3% of adults are banked (Enhancing Financial Innovation & Access's 2014 survey). While this is a huge opportunity for fintech to provide access to finance, low internet penetration due to poor technological infrastructure in Nigeria hinders this potential. Importantly, a significant percentage of the banked population do not trust the technology system because of cybercrime activities and inadequate data protection. These issues have to be addressed so that more consumers can get comfortable using fintech solutions. Fintech service providers also need to create more awareness on their security protocol and the safety of their platforms.

4 What new developments/key issues are likely to affect the fintech industry in the near future?

Henry (Kenya): Given the intrinsic importance of mobile payments in Kenya, there are reports that the government could officially identify key/important players in the mobile payments industry as "designated firms" (the Kenyan Treasury has identified M-Pesa as a crucial part of the economy, but has not yet given it a designated firm status), given they have become so hugely engrained in the economy, that if they failed/shut down, we would be in trouble. Designated firms would be subject to increased scrutiny from the Kenyan Central Bank and treasury department, and not just industry-wide regulation. This is a developing story, as we have not seen detailed views on this, so we will need to wait and see what this proposed scrutiny will look like. Whilst this is unlikely to be the same level of scrutiny applicable to banks, things will be more onerous. Eventually, other providers that are relatively small and in existence now or enter the market in the future, could also be identified as designated firms, as the size of their operations grow (e.g. the value and frequency of amounts). In the long run, this will all create an increased formal environment, but given how huge mobile payments has become in Kenya, this can only be expected over time.

Kate (South Africa): The Financial Sector Regulation Bill will soon be enacted, which should ease the transition into adequate regulation of technological and innovative solutions in South Africa. The key is that the prudential and market conduct standards that may be promulgated thereunder must not stifle, but rather support, technology-based growth. At a broader level, there is a lot of interest and excitement in the industry around blockchain, and the potential impact this will have on South Africa's financial services.

Yinka/Tolulope (Nigeria): Generally, Nigeria has a fast growing tech savvy young population, evident by increased numbers of mobile phones and social media use. The government is very committed to growing this even further, with computer programing being added to the curriculum of public schools by 2017, and the Lagos state government's "Code Lagos" computer programming initiative for students. Start-up incubators are increasingly being used to educate youths on technology generally as well. These initiatives will further drive innovation and demand for fintech products in Nigeria. More importantly, network service providers are starting to make 4G network available to consumers. With the faster internet speed that comes with 4G networks, more Nigerians will be encouraged to adopt fintech solutions for payments and other banking solutions.