Insights on Uganda’s Digital Lending Landscape

Series II : Supply Side, Supporting Functions and the Regulatory Environment

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List of Acronyms

#	Abbreviation	Description
1	API	Application Programming Interface
2	ATS	Average Ticket Size
3	BoU	Bank of Uganda
4	CAGR	Cumulative Annual Growth Rate
5	CRB	Credit Reference Bureau
6	DFS	Digital Financial Services
7	eKYC	Electronic Know Your Customer
8	FIA	Financial Intelligence Authority
9	FinTech	Financial Technology
10	MFI	Microfinance Institution
11	MNO	Mobile Network Operator
12	n	Number of Respondents / Sample Size
13	NITA-U	National Information Technology Authority of Uganda
14	PMP	Potential Market Penetration
15	PSP(O)	Payment Service Provider / Operator
16	SAM	Serviceable Addressable Market
17	SIMPO	Security Interest in Movable Property Registry System
18	TAM	Total Addressable Market
19	UBA	Uganda Bankers Association
20	UMRA	Uganda Microfinance Regulatory Authority

1. Introduction

Article Series

Series 1: Demand - Customer and Product

Series II: Insights on Uganda's Digital Lending Landscape

- Supply Side,
- Supporting Functions and,
- the Regulatory Environment

Following the conclusion of Series I of the digital lending article series, our objective to foster productive discussion and debate on Uganda's Digital Lending continues in Series II. This series focuses on the digital credit providers, the essential supporting functions and the regulatory environment within Uganda's digital lending landscape. A total of 43 market system actors i.e., 20 digital lenders (both bank and non-bank), 19 supporting function actors, 3 regulatory bodies and 1 Umbrella Body were interviewed for this series.

In this instalment (Series II), we aim to provide a comprehensive understanding of the unique interplay between the different market system actors that are facilitating digital lending. By examining their operations, business models, pricing strategies, and product differentiation, we seek to uncover the unique factors propelling or inhibiting their success in an evolving digital ecosystem.

Simultaneously, we navigate the intricate regulatory landscape and essential supporting functions crucial for sustainable and profitable participation in the digital lending sector through the provision of valuable insights and actionable recommendations that will empower UBA Member Financial Institutions and other market system actors to navigate this transformative era of digital finance effectively.

We also address the fundamental questions, "Digital Credit for What? For Whom? and Why Digital Credit?" as we scrutinize the specific problems that digital credit solutions aim to solve and quantify their impact for all stakeholders. With Uganda's National Development Plan prioritizing economic growth, digital lending emerges as a pivotal tool, particularly in addressing the critical challenge of financial inclusion.

Through these efforts, we aim to instigate concrete, actionable measures that foster significant operational changes, inform policy decisions, and facilitate necessary amendments to cultivate an improved enabling environment for every participant in Uganda's digital lending ecosystem.

1. Introduction

Executive Summary

🌍 **Overview:** Series 2 of our digital lending article explores the dynamic landscape of Uganda's digital lending sector, uncovering the interplay between traditional financial institutions, fintech innovators, regulators, and supporting functions shaping the ecosystem.

📊 **Market Dynamics:** Uganda's digital lending sector is characterized by a dynamic competition between traditional banks, microfinance institutions and nimble fintech lenders navigating what in their opinion is a stringent and unclear regulatory environment. We note that, while banks benefit from established frameworks, fintech lenders are increasingly leveraging emerging technologies to innovate and disrupt credit provision.

📜 **Regulatory Environment:** 14 out of the 20 digital loan providers interviewed in the survey emphasized the significant challenges posed by regulatory ambiguity and fragmentation to the smooth integration of digital lending solutions. Nonetheless, ongoing collaborative efforts among regulators and industry stakeholders are aimed at streamlining processes, enhancing compliance, and creating a more conducive regulatory environment for digital lenders.

🔄 **Risk, Operational Hurdles and Fraud:** Operational efficiency in digital lending is hindered by integration hurdles and technical glitches, impacting the seamless delivery of financial services. Moreover, recent instances of fraud highlight the critical importance of robust fraud risk management systems. These incidents underscore the necessity for continuous improvement in validation / verification processes and heightened vigilance against fraudulent activities in the digital space. Implementing stringent fraud detection mechanisms and fostering a culture of compliance and transparency are essential for safeguarding the integrity of digital lending operations and maintaining trust with customers.

💡 **Opportunities:** Despite the highlighted challenges, Uganda's digital lending landscape presents ample opportunities for innovation and growth. Case in point is the 25 Million Ugandans striving under the Serviceable Addressable Market (SAM) projected to grow digital loan volumes to UGX 17.7 T by 2029.

🚀 **Future Outlook**: By addressing challenges head-on and leveraging untapped opportunities, Uganda can harness the transformative power of digital finance to drive prosperity and progress for individuals and communities across the nation. This series aims to provide actionable insights and recommendations to navigate the complexities of Uganda's digital lending ecosystem and pave the way for a brighter future.

1. Introduction: Market Potential

Global and Regional Context

Digital lending has emerged as a transformative force in both the global and African financial landscape, offering unprecedented access to credit and financial services. The growth trajectory of digital lending worldwide is remarkable, showcasing its potential to revolutionize traditional finance models and foster financial inclusion on an unprecedented scale.

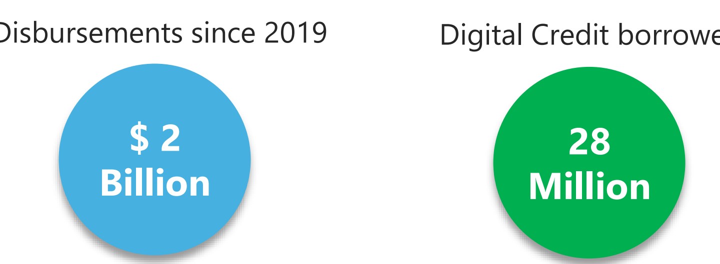
According to Mordor Intelligence, the Global Digital Lending Market size is projected to reach USD 795.34 billion by 2029, growing at a robust CAGR of 11.9% during the forecast period (2024-2029)[1]. This underscores the immense potential and lucrative opportunities within the digital lending landscape.

While the specifics can vary by region, the overall positive trend towards digital lending is clear in developed markets such as the United States and the United Kingdom where peer-to-peer lending platforms and digital banks have gained significant traction. Meanwhile, emerging economies like China, India and other Latin America Countries have seen a surge in digital lending activity.

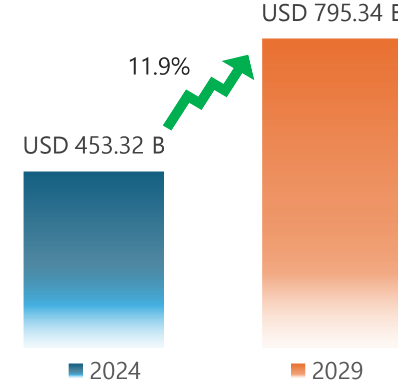
In India, the digital lending sector has seen extraordinary growth, going from a value of USD 9 B in 2012 to almost USD 150 B in 2020. Experts anticipate that the market will continue to grow, and it is predicted to reach a staggering value of USD 350 B[2] in the near future.

In Africa's case, countries like South Africa, Nigeria, and Kenya are leading the way in digital lending, each with unique market dynamics and growth potential fueled by the continent's rapidly evolving fintech ecosystem. Case in point is M-Pesa Fuliza that has been a game-changer in Kenya's financial landscape. By leveraging transaction data and mobile phone usage patterns, it can offer instant microloans to users, including those without a credit history[3].

M-Pesa Fuliza Digital Credit Performance[3]



Projected Global Market Size Growth



1. Digital Lending Market - Size & Report
2. https://www.statista.com/statistics/1202533/india-digital-lending-volume/
3. Vericash: The New Dynamics of Digital Lending

1. Introduction: Ugandan Market Potential

Local Context

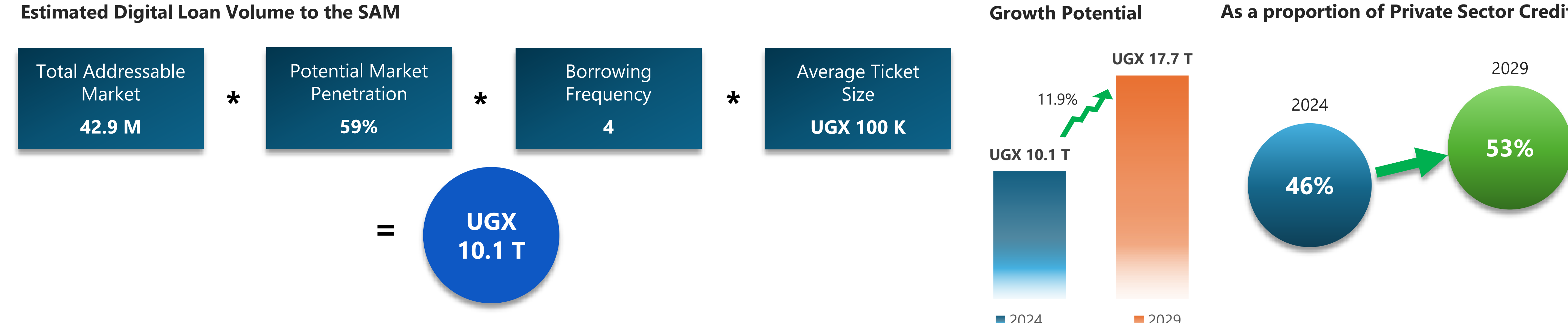
In the Ugandan Context

We project continued expansion of the digital lending market in Uganda, driven by factors such as increasing smartphone adoption, expanding access to financial services in rural areas, and the growing acceptance of digital payments. With supportive regulatory frameworks and ongoing investments in digital infrastructure, the digital lending market is poised for sustained growth, presenting lucrative opportunities for investors and stakeholders in the financial services industry.

Sizing Uganda's Digital Credit Market Opportunity

Assumptions and considerations

- Registered mobile money customers in Uganda were 42.9 Million as at the end of June 2023 – Total Addressable Market (TAM)[4].
- Potential Market Penetration of 59% (assuming its comparable to the proportion of respondents that indicated that they have taken out a digital loan in the past[5]. This results in a Serviceable Addressable Market (SAM) of 25.3 Million.
- Average ticket size: Digital loan amounts typically range from UGX 5 K to UGX 500 K, For our estimation, we consider the modal ticket in this range of UGX 100 K.
- On average a single customer takes 4 digital loans per year. This is based on the borrowing frequency from Series I.
- Private sector credit in Uganda that is UGX 21.5 Trillion as of Jan 2024[6] will maintain a CAGR of ~ 9.4% through the period 2024 to 2029. Comparable to the last 5 years leading up to 2024.
- The potential market can utmost grow at the global CAGR of 11.9%



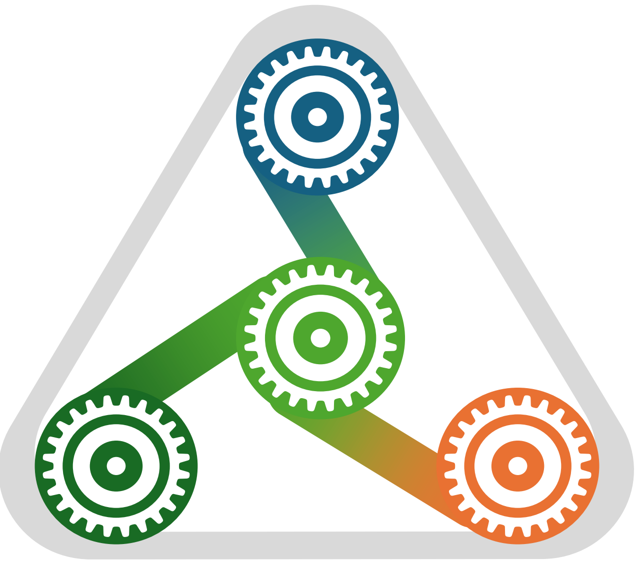
4. Number-of-registered-mobile-money-customers-in-uganda
5. Series I Digital Lending Article - Demand Side
6. https://mepd.finance.go.ug/reports.html

Disclaimer: The market opportunity represents both the tapped and untapped digital credit market and should not be misconstrued to mean the current value of digital credit disbursements in Uganda.

1. Introduction: Industry Insights and Trends

Regional, Local and Global Context

Financial Institutions around the world are making changes to their physical branch strategy as face-to-face customer traffic has fallen drastically. This puts increased pressure on industry players, with self-service options and interaction via customer care centers coming to the forefront. With more customers reaching out through mobile apps, using chat features and looking for an omnichannel digital experience, the pace at which customer expectations have changed has accelerated dramatically over the last two years.



Key take away:

As the trend towards automation continues to grow, proactive risk management and alignment with regulatory requirements becomes increasingly important since the automation of a non-compliant operation significantly increases the risk of systemic harm to the broader customer base.

Rise of Alternative Credit Scoring Models

Traditional credit scoring models rely heavily on credit history and collateral, often excluding individuals with limited credit history or unconventional income sources. As a result, alternative credit scoring models leveraging alternative data sources such as mobile phone usage, social media activity, utility payments and transaction history are gaining traction. These models enable lenders to assess creditworthiness more accurately, expanding access to credit for underserved populations.

Regulatory Scrutiny and Compliance

The digital lending industry is subject to regulatory scrutiny and evolving regulatory frameworks aimed at ensuring consumer protection, preventing predatory lending practices, and maintaining financial stability. Regulatory authorities like UMRA, NITA and BOU are focusing on issues such as potential interest rate caps, data privacy, transparency, and responsible lending practices. Compliance with regulatory requirements is essential for digital lenders to operate legally and sustainably in the market.

Expansion of Digital Platforms

Digital lending platforms continue to proliferate, offering a wide range of loan products and services tailored to diverse borrower needs. From peer-to-peer lending platforms to online marketplaces and mobile lending apps, digital platforms provide convenient access to credit, streamlined application processes, and faster loan disbursements. Additionally, some of these platforms leverage advanced technologies such as artificial intelligence, machine learning, and blockchain to enhance risk management, automate underwriting processes, and personalize loan offerings.

Increased Focus on Financial Inclusion

Digital lending plays a crucial role in promoting financial inclusion by providing access to credit for individuals and businesses that have been historically underserved by traditional financial institutions. Digital lenders are increasingly targeting underserved segments such as micro, small and medium enterprises (MSMEs), low-income households, and unbanked populations, offering tailored loan products, flexible repayment terms, and financial education to empower these segments and drive economic growth.

2. Segmentation and Profiling

Overview

Segmentation and profiling of digital credit providers, supporting function actors, and regulators is essential for gaining a comprehensive understanding of the digital credit market ecosystem. By segmenting and profiling these key stakeholders, we can unravel the intricate dynamics and interactions within the ecosystem, paving the way for informed decision-making and strategic planning for each of the market system actors. Below is how the digital lending market system actors are set up.

Regulators and Umbrella Bodies

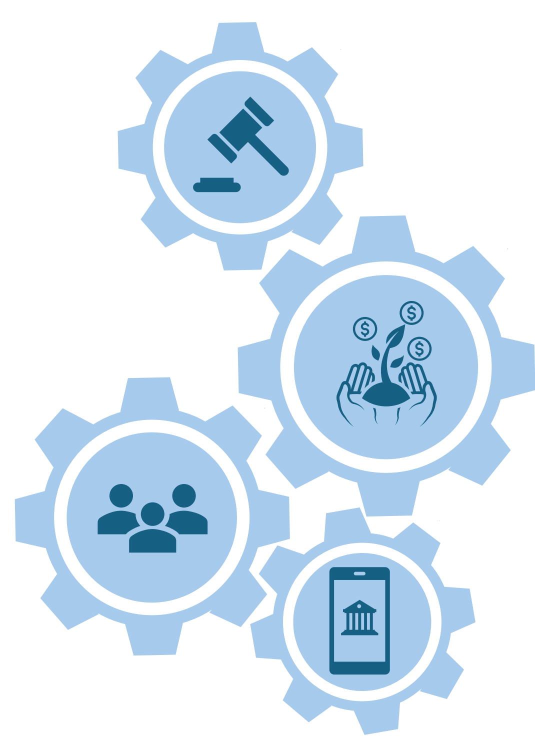
Digital lending in Uganda is primarily overseen by four authorities i.e., UMRA, BoU, NITA-U, and FIA. There are also umbrella bodies like Financial Technology Service Providers' Association (FITSPA) that play a pivotal role in organizing FinTechs in the Country.

NB: UMRA has drafted and launched new guidelines to regulate digital lending for Tier IV FIs. These guidelines aim to eliminate the unethical operations, provide clarity on licensing, branding, transparency and consumer protection in the digital lending space.

Digital Credit Customers

Digital credit customers are defined as individuals who acquire loans / credit through a digital channel such as a USSD code, mobile app or website with little to no human interaction. In Series I, digital loan customers were segmented as Formal Sector Players, Informal Sector Players and Students.

All these customer segments exhibited similar sentiments, attributes and preferences for digital loans.



Supporting Function Actors

These are entities providing essential services, resources, or infrastructure to support the functioning of digital credit provision. They play a crucial role that is not limited to, technology provision, risk assessment, credit scoring, and payments facilitation. In this article, they include, MNOs, CRBs, Online Merchants, eKYC Providers, PSPs, and PSOs.

The collaboration and seamless integration with these actors is paramount for enhancing the efficiency and accessibility of digital lending services, ultimately driving financial inclusion and economic empowerment.

Digital Credit Providers

These operate automated and remote lending procedures that rely on seamless smart technology for customer acquisition, credit assessment, loan approval, disbursement, recovery, and any other related customer support. These include:

- Banks
- Microfinance Institutions (MFIs)
- FinTech Lenders

Key takeaway: Exploring the interplay between these segments elucidates how they influence and are influenced by one another. The intricate web of relationships and dependencies underscores the interconnectedness of the ecosystem, highlighting the need for a holistic approach to understanding its dynamics.

2. Segmentation and Profiling

Market System Actors (Majority of these were interviewed)

Digital Credit Providers

Supporting Function Actors

Regulators and Umbrella Bodies

Disclaimer: This slide mainly showcases the actors that participated in the targeted survey. However, this is not an exhaustive list of all Uganda's digital lending market system actors and some of the listed digital credit providers are not yet licensed or regulated.

3. Business Model Description

Digital lending business models vary slightly among key digital loan providers, each employing 'fairly unique' approaches and strategies to carve out their niche and establish market presence. This section aims to compare and contrast the business models of Banks, MFIs and Fintech Lenders highlighting their service offerings and operational strategies.

Banks & MFIs

Key Partners

CRBs
MNOs
Technology providers
Insurance providers

Key Resources

Capital, Branches, software, apps, human resource talent

Key Activities

Lending, Investment

Value Proposition

Trust and credibility of a traditional institution. Access to a wide range of financial products and services and personalized customer service.

Channels

Multichannel approach encompassing physical branches, online banking platforms, USSD Codes, and mobile apps.

Customer Segments

They typically serve their already existing customer base, including individuals, small businesses, and corporations.

Customer Relations

Have established customer relationships and brand recognition, leveraging these assets to cross-sell digital loan products and foster trust and loyalty.

Cost Structure

They incur fixed costs associated with maintaining physical branches, regulatory compliance, and staff salaries.

Revenue Streams

They generate revenue through various sources, including interest income from loans, fees / charges, and cross-selling of other products.

Fintech Lenders

Key Partners

Payment processors
eKYC Providers
Marketing and distribution partners
Banks

Key Resources

Capital, End to end tech infrastructure, data providers

Key Activities

Lending, Marketing

Value Proposition

Provide quick and convenient access to credit through streamlined digital processes

Channels

Predominantly operate through mobile apps and web platforms.

Some also use referral programs and affiliate partnerships.

Customer Segments

Serve specific niche or underserved segments with limited credit history, using digital platforms and data analytics to reach them efficiently.

Customer Relations

Rely on digital channels and innovative marketing strategies to acquire and engage customers. Also carry out community engagement through social media.

Cost Structure

The predominant costs incurred by fintech lenders are the cost of capital, cost of tech, integration and customer acquisition.

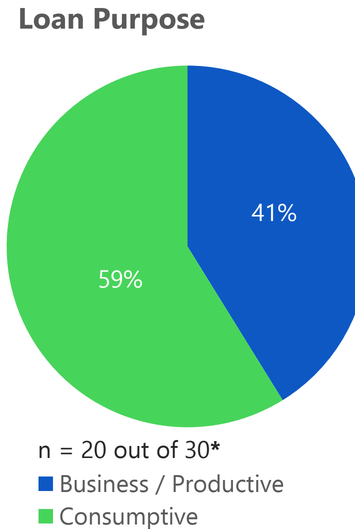
Revenue Streams

Fintech Lenders derive revenue from interest charges and fees associated with loan origination, servicing, and late payments / penalties.

Key take away: While Banks and MFIs in Uganda are only just beginning to focus more on digital lending, their models share similarities with fintech lenders. However, they possess distinct advantages that should not be overlooked. These include access to low-cost capital, an existing and loyal customer base, proprietary data on depositors that aids in identifying eligible borrowers with existing relationships, and established brand recognition. Unlike most Fintech Lenders! **Nevertheless, a move into this domain necessitates robust risk management and controls, as further emphasised in subsequent sections of this article.**

3. Business Model Description: Survey Findings

Credit on your Fingertips: Access Points, Loan Purpose and Target Markets



The widespread adoption of smartphones has opened new channels for lenders to connect with potential customers, making financial products more accessible than ever before. Our targeted survey highlights the evolving landscape of digital lending, driven by technological advancements and an impending shift towards personalized financial services tailored to individual needs and preferences.

Loan Purpose

The personalized nature of smartphone data usage has led to a preference for consumptive digital loan products, which cater to immediate consumption needs. This trend is further reinforced by the reliance on transactional data for credit assessment, which tends to favor consumptive loans over business digital loans.

Target Market

The majority of digital loan providers target both formal and informal sector players (65% from the survey conducted), reflecting a broad approach to serving diverse segments of the population.

Access Points

In series I, we noted that convenience and quick turnaround time are the major influencing factors for use of digital loans amongst customers ahead of pricing. The Series II survey, revealed that some digital lenders are capitalizing on this insight by offering digital loans through apps, USSD, WhatsApp and Web.

It was noted that digital loan access through a web platform has the longest TAT which is indicative of where digital loan providers should focus their efforts i.e., apps and USSD.

Key takeaway

Whereas banks and other digital lenders are innovating around web platforms, it's essential to recognize that these may not always be the most efficient means for digital credit provision.

Target Clientele

12%
24%
65%

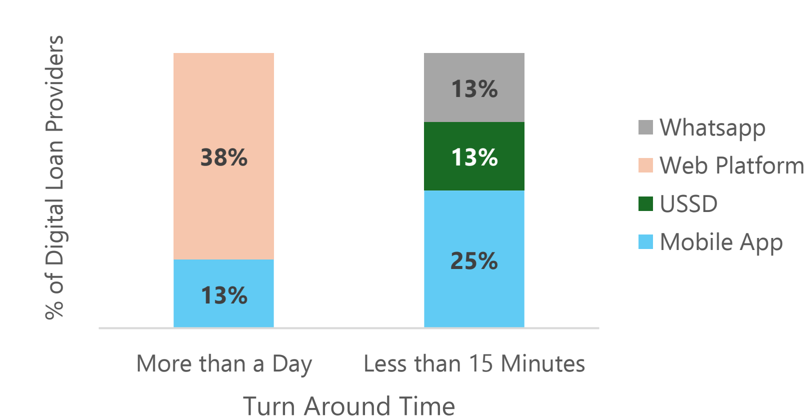
- Formal Sector Players
- Both Formal and Informal Sector Players
- Informal Sector Players

Demand Drivers (Series I)

Driver	%
Convenience	38%
Turnaround Time	25%
Affordability	17%
Other	20%

n = 246

Turn Around Time Vs Access Point

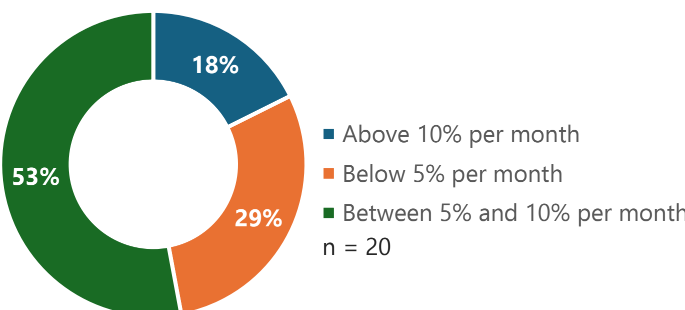


* 30 is the estimated number of licensed financial institutions that offer digital credit products in Uganda

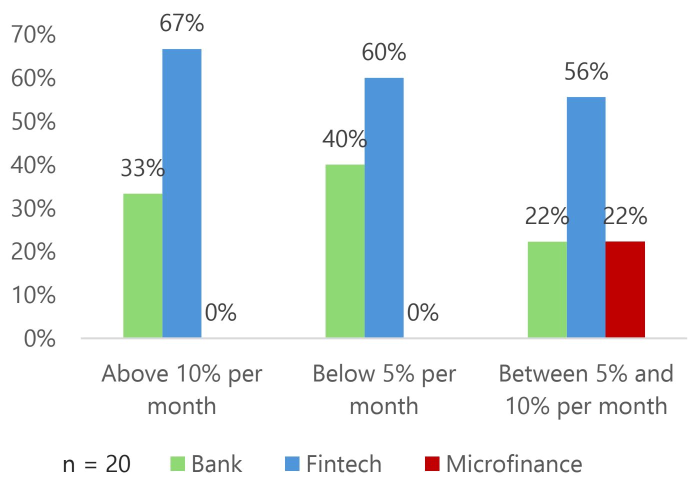
3. Business Model Description: Survey Findings

Decoding the Varied Pricing Landscape of Digital Loans

Interest Rates and Associated Fees



Pricing by the Different Digital Lenders



In Series I, feedback from digital loan customers underscored widespread dissatisfaction with existing products, primarily due to exorbitant fees and unfavorable repayment terms. Moreover, there appears to be a significant lack of transparency among fintech lenders regarding the pricing mechanisms associated with their digital loan offerings, a problem the new digital lending guidelines aims to resolve.

Under Section 90 of the Tier IV Microfinance Institutions and Money Lenders Act, the Minister of Finance, in collaboration with UMRA, has the authority to establish a maximum interest rate applicable to money lenders[7].

Given that fintech lenders are currently licensed as money lenders, a spotlight is increasingly being cast on this stipulation. Majority of digital lenders interviewed (11 out of 20) are charging loan fees between 5% and 10% per month on a flat rate basis, which is relatively high compared to the pricing on other credit products that averagely go for 2% per month on a reducing balance basis.

Particularly noteworthy is the revelation that a significant proportion of those charging above 10% per month are fintech lenders. These fintech firms **cited high costs of capital, steep customer acquisition expenses, and elevated borrower risk as primary factors** contributing to the comparatively high charges on their digital loan products.

It is evident that this presents a pricing barrier that deters some potential customers and impedes the widespread adoption of digital credit products. Furthermore, the current pricing structure hinders FinTechs from benefiting from economies of scale due to the resultant limited customer portfolio. Thus, it's imperative to explore strategies to mitigate these pricing challenges to foster greater accessibility and scalability within the digital lending ecosystem.

Key Takeaway

There is a pressing need for digital lenders in Uganda to adopt a more risk-based pricing approach. While these lenders predominantly offer non-collateralized loans, which inherently carry higher default risk, incorporating a broader range of data points can significantly enhance their ability to differentiate between low-risk and high-risk borrowers.

This approach would allow lenders to offer competitive interest rates to low-risk borrowers while accurately pricing loans for higher-risk borrowers based on their specific creditworthiness. Embracing a risk-based pricing approach represents a substantial shift in how digital lenders evaluate and price loan products.

For instance, in India[8], all banks have announced plans to price retail loans based on the relative riskiness of borrowers using consumer credit scores. This move has been primarily driven by aggressive competition from alternative lending startups and the anticipated growth of the retail banking opportunity to USD 3 trillion by 2026, according to Credit Suisse. Research has shown that lenders implementing differential loan pricing can compete more effectively by offering each customer risk segment the lowest price in line with the costs of providing them loans.

However, it's important to note that such risk-based pricing models have not yet gained significant traction in the East African region.

7. Tier 4 Microfinance Institutions and Money Lenders Act, 2016
8. Risk Based Pricing of Loans in India: An Overview - Enterslice

3. Business Model Description

How the models impact scale, customer engagement and risk management

Fintech Lender's Agility Vs Traditional FI's Scale

While fintech lenders and traditional financial institutions share some similarities in their digital lending approaches, there is a noticeable disparity in the scale and customer engagement achieved by traditional financial institutions, whether they are digitally focused or not.

Innovation Vs Risk Management

Fintech lenders, known for their agility and innovation, are leveraging cutting-edge technology to provide seamless user experiences, aiming to broaden their customer base. However, this rapid expansion entails inherent risks, including heightened levels of default and fraudulent activity. To address these risks, digital lenders often resort to charging high fees or implementing harsh collection methods to safeguard their operations.

To achieve scale FIs are leveraging their existing relationships

In contrast, banks and MFIs, equipped with their longstanding reputation, brand recognition, and extensive customer base, typically prioritize leveraging existing customer relationships to promote their digital loan offerings. This approach cultivates trust and loyalty among their customers, thereby increasing the likelihood of successful loan acquisition and repayment. Nevertheless, banks and MFIs may face challenges in scaling their digital lending operations due to the presence of legacy systems and bureaucratic procedures that impede agility and innovation.

This is partly why some of the Banks are partnering up with MNOs to tap into the unbanked adult population amounting to more than 16.5 Million Ugandans[9].

Other banks are using a phased approach of scrapping branches and moving majority of their services to their Mobile Application with the aim of conditioning the mindset or altering the conservative customer's preferences overtime.

Balancing Scale, Engagement and Risk Management

In navigating the complexities of the digital lending landscape, successful lenders must strike a delicate balance between fostering meaningful customer engagement, implementing robust risk management protocols, and ensuring scalability within their chosen business model.

Achieving this balance requires a nuanced approach that integrates

- Technological innovation with
- Prudent risk assessment practices especially around validation and verification of customers.

This proactive approach not only enables lenders to capitalize on emerging opportunities but also mitigates potential threats to their business operations, ensuring long-term sustainability and growth in the digital lending market.

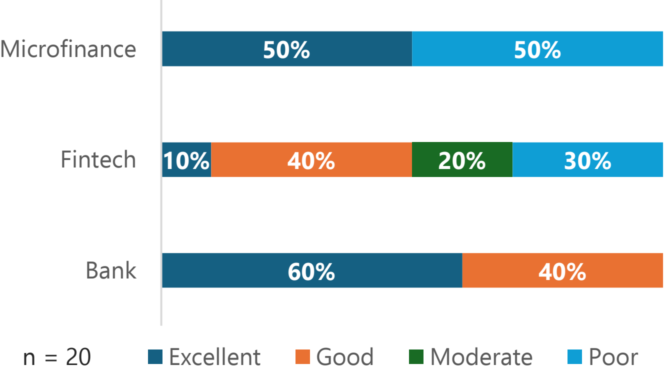
9. Report on banking and the status of financial inclusion: Finscope Survey 2018

3. Business Model Description: Survey Findings

Sentiment on Supporting Functions - The Hidden Hurdles

Supporting functions engaged include MNOs, CRBs, Online Merchants, eKYC Providers, PSP/Os.

General Rating of Supporting Function Actors



Digital lenders express dissatisfaction with the level of tech support from supporting functions emphasizing that lack of support hampers data-driven decision-making and operational effectiveness.

Some supporting functions are also still in the learning phase and may not fully grasp the intricacies of the different digital lending business models. This lack of understanding leads to misalignment and delays in addressing operational issues.

Sentiment on Digital Tech Providers and PSPs

Score Card 2/5

Supporting function actors play a crucial yet often underestimated role. However, beneath the surface lies a web of challenges and frustrations that digital loan providers must navigate. For instance, integration with key partners, such as eKYC providers and PSPs presents a significant hurdle, with cumbersome or sometimes incompatible processes and high costs hindering the smooth flow of digital credit and innovation. Operational inefficiencies on the part of some PSOs and PSPs further exacerbate the situation, with delays in funds remittances upon repayments, disrupting cash flow management and overall operational effectiveness.

Sentiment on Credit Referencing

Score Card 3/5

The absence of standardized credit scoring methodologies among CRBs poses a significant hurdle for digital lenders. While standardization could streamline credit assessment processes, it may inadvertently stifle competition and innovation in the market. However, exploring avenues for collaboration and harmonization among CRBs could lead to more consistent credit evaluations without compromising market dynamism.

Necessary Improvements (Priority Sequence)

1. Improved Access to Alternative Data: In the United States, regulatory changes such as the Fair Credit Reporting Act (FCRA) have paved the way for lenders to access alternative data sources[10] beyond traditional credit reports, enabling more comprehensive credit assessments and improved risk management. For instance, fintech lenders in the U.S. have successfully leveraged alternative data such as utility payments, rental history, and even social media data to assess creditworthiness and expand access to credit for underserved populations. Similarly, in India, regulatory initiatives like the Account Aggregator framework have facilitated the secure sharing of financial data across institutions, promoting financial inclusion and innovation in digital lending[11].

2. Enhanced Integration and Collaboration: More integration with partners like NITA with their UG Hub platform and the SIMPO Database which presents opportunities that strengthen KYC verification, and credit appraisal processes. For example, in India, digital lenders have successfully leveraged the Aadhaar biometric identification system, operated by the Unique Identification Authority of India (UIDAI), to streamline KYC verification processes and enhance risk management.[12] Similarly, in Kenya, the integration of mobile money platforms like M-Pesa with credit scoring systems has enabled lenders to make more informed lending decisions and expand financial inclusion[13].

3. Cost Reduction & Operational Efficiency: Fintech lenders push for lower transaction costs by negotiating reduced rates with supporting functions like PSPs. Additionally, improving issue resolution is crucial for enhancing the operational efficiency of digital lending.

10. Fair Credit Reporting Act
11. Business operations account aggregator
12. Unique Identification Authority of India
13. M-Pesa Safaricom

3. Business Model Description: Survey Findings

Sentiment on Regulators - Actor Perspectives

Sentiment from MFIs and Banks

Score Card 4/5

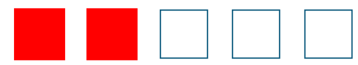
Many respondents highlighted the importance of regulatory compliance and obtaining necessary licenses for operating in the digital lending space. Regulatory bodies such as UMRA are instrumental in providing guidelines and licenses, ensuring that digital loan providers align with laws and regulations.

Regulators are perceived as flexible and willing to engage with market actors, in formulating suitable regulatory frameworks. This collaboration helps create an enabling environment for digital lending operations to thrive.

It is important to note that while UMRA has drafted and launched new digital lending guidelines for Tier IV FIs, it is imperative that UMRA promptly enforces and monitors the implementation of these guidelines to ensure responsible operation by digital and online lenders. This swift action is crucial for safeguarding consumer interests and fostering a transparent and accountable digital lending landscape in Uganda.

Sentiment from Fintech Lenders

Score Card 2/5



Fintech Lenders noted that the other prevalent issue is regulatory fragmentation, characterized by the presence of multiple regulators and stringent licensing requirements. This fragmentation leads to response fatigue and financial strain on digital lenders, with delays in license approvals hindering operational efficiency. Moreover, the high thresholds for licenses act as barriers to entry, limiting competition and innovation in the market.

The annual license renewal process is also perceived as a regulatory burden, consuming time and resources for majority of the fintech lenders. While compliance is acknowledged as necessary, players are advocating for more frequent inspections rather than yearly license applications, but this seems impractical given the resource constraints faced by UMRA.

Note: Despite these hurdles, there is recognition of the need for regulatory intervention, particularly regarding interest rate regulation to protect consumers from exorbitant rates.

Necessary improvements (Priority Sequence)

1. Bridge the skills gap: There is a recognized skills gap within regulatory bodies, highlighting the need for capacity building and skill development to effectively regulate the digital lending landscape.

2. Streamline the licensing procedures and requirements to reduce administrative burdens on industry players through centralized collaboration between UMRA, NITA, FIA and BoU (for some players). For example, in Singapore, the Monetary Authority of Singapore (MAS)[14] has implemented a streamlined licensing platform known as the "Sandbox Express" initiative where FinTechs can apply for all necessary licenses quickly and efficiently, enabling them to innovate within a regulated environment while minimizing administrative hurdles.

3. Continuous inspections and monitoring instead of annual licensing for fintech lenders. For instance, in the United Kingdom, the Financial Conduct Authority (FCA) employs a risk-based supervision approach for fintech firms[15]. This approach involves ongoing monitoring and inspections tailored to the risk profile of each firm, allowing regulators to promptly identify and address emerging risks or compliance issues.

4. Extend regulatory sandbox to cater for digital credit innovations. For example, in Kenya, the Central Bank of Kenya (CBK) has implemented a regulatory sandbox framework to facilitate the testing of new financial products and services, including digital lending solutions[16]. This approach has enabled Kenya to nurture a vibrant fintech ecosystem and expand access to digital credit services, providing a valuable precedent for Uganda to follow.

5. Increased awareness and sensitization: There is a consensus on the need for more informative conferences, workshops, and sensitization programs aimed at educating both the population and financial institutions about the benefits and potential of digital lending.

14. Monetary Authority of Singapore - Sandbox Express
15. Approach to Supervision: Financial Conduct Authority UK
16. Regulatory Sandbox Framework - CBK

3. Business Model Description

Challenges Faced and Barriers to Entry

Both banks and non-bank digital lenders encounter **various challenges** in the digital lending landscape.

Banks often struggle with legacy systems, regulatory constraints, and a risk-averse culture, hindering their agility and innovation in adopting digital lending solutions.

Limited access to affordable capital and undercapitalization hinder the growth and expansion of digital loan operations. Demand for loans exceeding supply indicates intense competition and the need for scaling up operations.

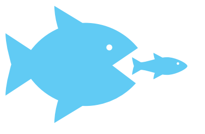
Fraud and Risk Management: Fraud risks, including customers borrowing with no intention to repay, pose significant challenges to financial sustainability and risk management.

Data quality issues, including misleading information from some data providers / customers and fraudulent activities, affect credit scoring accuracy and loan portfolio quality.

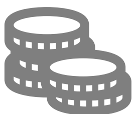
Limited internet coverage, poor network connectivity in rural areas, and low digital literacy levels hinder access and adoption of digital loan products. System integration challenges and reliability issues with core banking platforms affect the rollout and functionality of digital loan products in some instances.

Limited customer knowledge and awareness of digital platforms, along with false perceptions and skepticism (given some bad actors), affect adoption rates and market penetration.

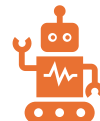
Entering the digital lending market presents **significant barriers** for both traditional banks and fintech lenders as shown below.



Competitive Pressures



Limited Access to Affordable Capital



Technological and Infrastructural limitations

Customer trust and perception

Regulatory compliance & complexities

Data privacy and Data protection concerns

Overall, navigating regulatory complexities poses a significant challenge for fintech lenders in the digital lending landscape, requiring substantial investments in compliance structure. Furthermore, intense competition, limited access to capital, and the need for robust technology infrastructure present additional hurdles for fintech lenders seeking to gain traction in the market.

Traditional banks, on the other hand, grapple with internal cultural resistance, technological limitations stemming from legacy systems and must work to overcome some negative perceptions associated with traditional banking models to succeed in the digital lending space.

To overcome these challenges and barriers, digital lenders must invest in modernizing their infrastructure, fostering a culture of innovation, and forging strategic partnerships to complement their strengths and mitigate for their weaknesses.

4. Deep Dive into Partnerships

Overview of the Collaborative Environment

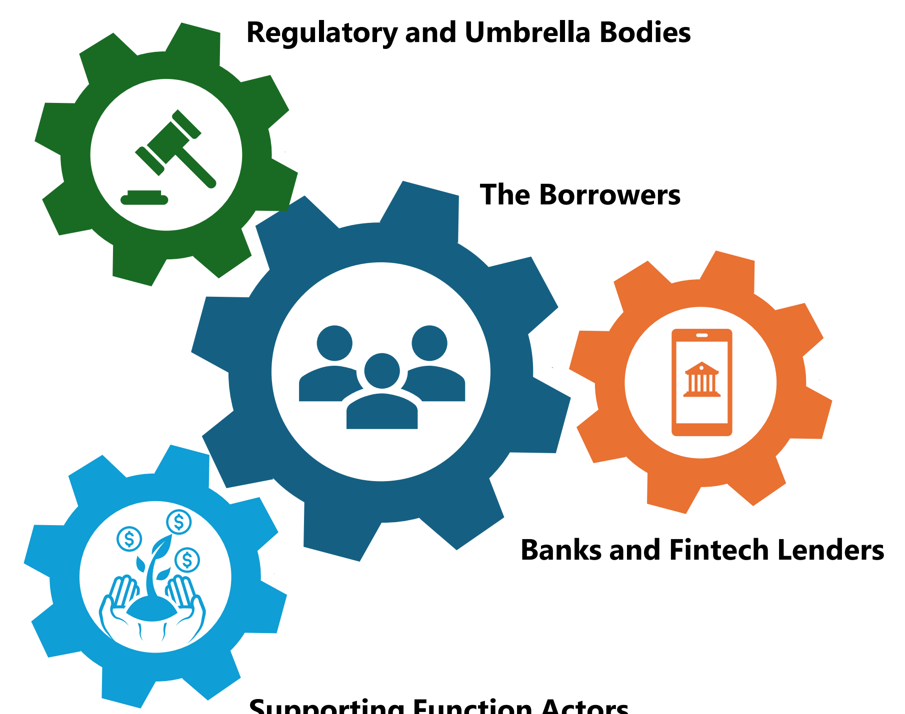
In Uganda's dynamic digital lending landscape, partnerships between various stakeholders are playing a pivotal role in shaping the industry's trajectory. These collaborations extend beyond traditional lender-borrower relationships, encompassing a diverse array of entities such as MNOs, Tech Providers, Regulators, Credit Reference Bureaus (CRB), online merchants, eKYC Providers, payment service providers (PSPs), Umbrella Bodies and more.

High Level Analysis of the Partnerships

Partnerships between the different market system actors are multifaceted, with each partner contributing unique expertise and resources to the ecosystem. FinTechs like Jumo Uganda, YABx and Craft Silicon, for instance, are providing the technological infrastructure and innovative solutions that enhance the efficiency and accessibility of digital loans in Uganda. CRB providers like gnuGrid, Credit Info and Metropole are playing a crucial role in assessing borrowers' creditworthiness, enabling lenders to make informed decisions on whether the prospective borrower has multiple borrowings elsewhere. Similarly, collaborations with online merchants and PSPs facilitate seamless integration of lending services into e-commerce and payment platforms, expanding the reach of digital loans to a broader customer base.

The unique interplay between the different market system actors

The interplay between these market system actors is characterized by collaboration, competition, and coexistence. Regulatory bodies collaborate with industry stakeholders to foster innovation while safeguarding consumer interests. Supporting function actors collaborate with MFIs, banks, and fintech lenders to enhance operational efficiency, mitigate risk, and deliver seamless customer experiences. Meanwhile banks, MFIs and fintech lenders compete for market share, driving innovation and pushing the boundaries of digital lending.

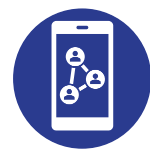


The interplay between the different actors forms the backbone of the ecosystem. Through mutual collaboration, innovation-driven competition, and adherence to regulatory standards, these entities collectively drive the growth, resilience, and sustainability of the digital lending industry.

Through strategic alliances with various stakeholders, FinTech lenders are tapping into broader networks and capabilities, enabling them to penetrate previously underserved markets and demographics. This concerted effort not only promotes financial inclusion but also encourages the adoption of digital lending among previously overlooked segments of society.

4. Deep Dive into Partnerships

Specific Partnership Types, and their role in Scaling Coverage and Adoption



01

Partnerships with MNOs

Collaborations with telecom companies like MTN and Airtel are instrumental in serving traditionally underbanked populations. These partnerships involve data sharing and API integrations to leverage their customer information and payment systems.

02

Technology Integration Alliances

Partnerships with technology firms like Craft Silicon, YABx and Laboremus enable access to electronic know your customer (eKYC) services, technology infrastructure, and advanced data analytics tools, facilitating better credit decision-making and risk assessment processes.

03

Value Chain Partnerships

Some providers are engaging entities along the value chain, such as distribution, manufacturing companies, together with embedded finance partnerships with ride hailing apps, online merchants and / or large supermarket chains to offer credit to their officers, suppliers, and customers. These partnerships often involve data sharing for credit scoring purposes and aim to expand access to credit to varied customer segments.

04

Other Collaborations

These include but are not limited to, Partnerships with PSPs enabling seamless loan disbursement and repayment through various channels, partnerships with insurance providers to offer credit loss coverage. Some other lenders are leveraging agent networks from the Agent Banking Company to reach customers in remote areas

Role of a collaborative environment in scaling coverage and adoption of digital loans

Access to Untapped Market Segments

Partnerships with entities like the MNOs and agent networks provide digital lenders with access to previously underserved or unserved markets. Leveraging the existing infrastructure and customer base of these partners allows lenders to penetrate deeper into rural areas and reach customers who may not have had access to formal financial services before.

4. Deep Dive into Partnerships

Role of Partnerships in Scaling Coverage and Adoption of Digital Loans

2	**Enhanced Data and Credit Scoring**	Partnerships with data providers, like eKYC providers and CRBs enable lenders to access comprehensive borrower data for credit scoring and risk assessment. By leveraging partner data, lenders can make more informed lending decisions, reduce default rates, and offer competitive loan terms to borrowers.
3	**Streamlined Disbursements and Repayments**	Payment service providers are facilitating seamless loan disbursement and repayment processes. Integration with mobile money platforms and digital payment channels allows borrowers to access funds quickly and conveniently. Moreover, partnerships with agent networks enable cash-in and cash-out services, further enhancing accessibility for borrowers.
4	**Product Innovation and Customization**	Partnerships with technology firms and fintech startups drive product innovation and customization in the digital lending space. Lenders are leveraging their expertise to develop tailored loan products that meet the unique needs of different customer segments. These innovative products not only attract new borrowers but also enhance the overall customer experience.
5	**De-risking the Environment**	Partnerships present significant opportunities from a risk-based perspective. As partnerships strengthen, they contribute to derisking the lending environment, enabling lenders to operate with greater confidence and extend loans more freely.

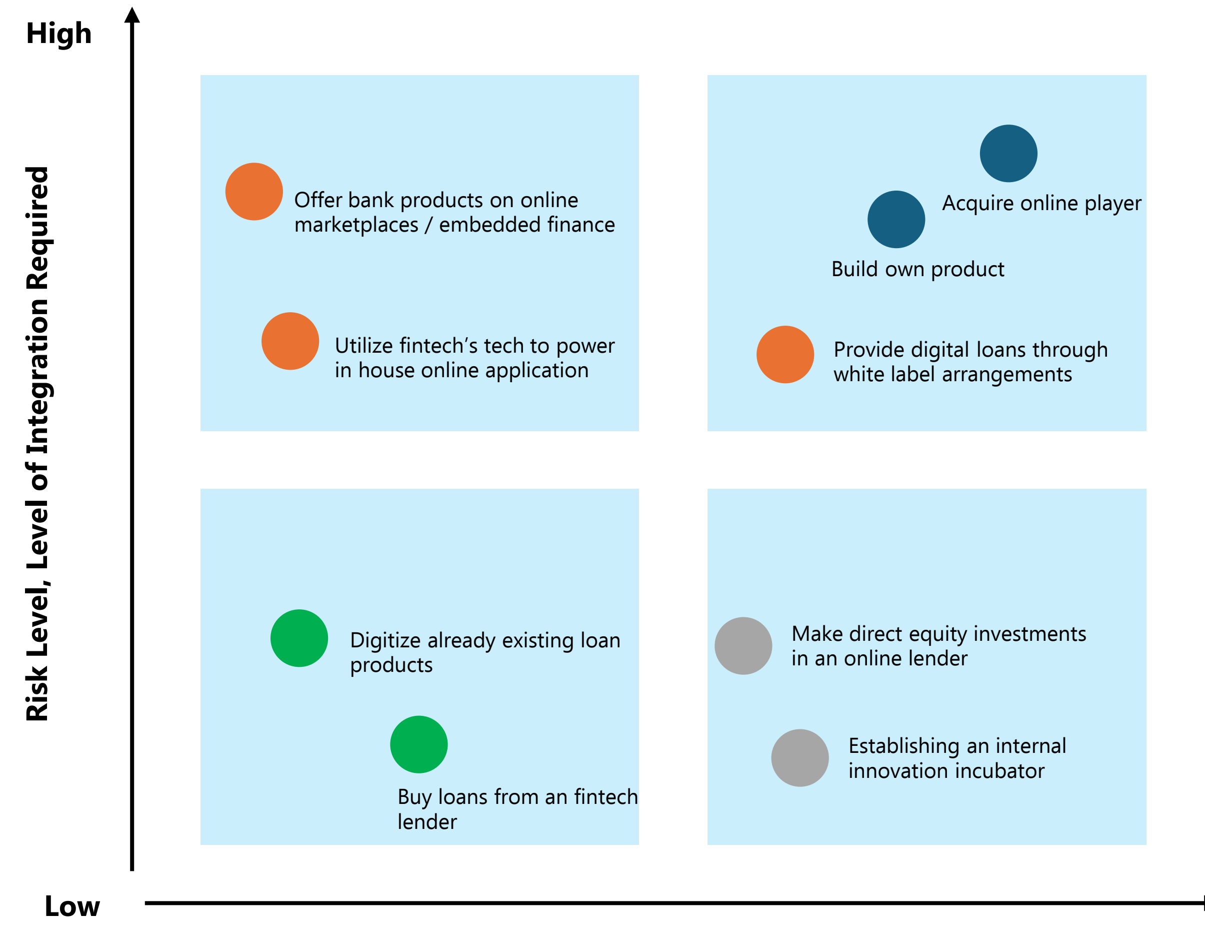
Although it is possible to roll out digital loan offerings without leveraging partnerships, it may not be easy. While Digital Financial Services (DFS) have expanded financial inclusion primarily through payments, the scope remains limited beyond that. Digital credit, especially in Uganda, primarily focuses on consumer lending and is still in its nascent stage. Challenges like over-indebtedness, unproductive consumer lending, high interest rates, and default rates are prevalent, acting as deterrents or areas requiring improvement to fully utilize DFS potential.

Moreover, as we delve into the subsequent sections, we'll explore various risks that need to managed proactively.

Therefore, while partnerships are not a necessity, they could potentially help navigate some or all of these challenges and catalyze the potential of digital credit in Uganda.

4. Deep Dive into Partnerships

How can Traditional FIs coexist / collaborate with Fintech Lenders?



The emergence of online lending startups in Uganda highlights the immense market potential and yet it comes with inherent risks, while traditional FIs possess advantages such as low-cost capital and a built-in customer base (implying lower customer acquisition costs than fintech lenders), they face the risk of becoming obsolete if they fail to embrace digital innovation and must embrace it to remain competitive as highlighted in the previous subsection.

Banks should also consider strategies that align their desired level of digital integration with how much time and money is required[17] while also assessing the risks associated. These strategies can be broadly categorized as.

- **Arm's Length:** This strategy involves banks contracting for new digital activities in arms-length agreements while keeping current operations relatively separate and pristine.
- **Partnership:** Here banks can choose partnership arrangements where new technologies are integrated into their loan application and decision-making apparatus.
- **Build or Acquire:** Banks may opt for a "build or acquire" strategy, where they make significant investments to develop their own digital front ends or acquire existing fintech companies to gain new digital capabilities.
- **Long game:** This would entail establishing an internal innovation incubator or pursue long-term corporate investments in separate emerging companies.

These strategies offer traditional FIs different approaches to navigate the evolving landscape of digital lending, allowing them to coexist or compete with emerging online players while leveraging their existing strengths and resources.

Other ecosystem actors also stand to benefit from any these arrangements through potential acquisitions or collaborations, creating a win-win situation for all stakeholders involved.

17. How Banks Can Compete Against an Army of Fintech Startups (hbr.org)

4. Deep Dive into Partnerships

Options on how to coexist / collaborate with Fintech Lenders

In order to create a win-win situation for all stakeholders in the digital lending ecosystem, the outlined recommendations ought to be ranked by risk level, along with a structured implementation timespan.

Arm's Length (Low Risk)

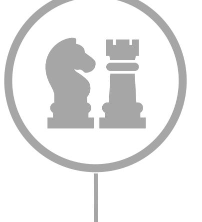
By maintaining a separation between current operations and digital ventures, banks can mitigate disruption to existing operations. However, this approach may limit access to cutting-edge technologies and innovations

Implementation can span 6 to 12 months

Partnership (Moderate Risk)

While partnerships offer access to innovative solutions and expertise, there are risks associated with dependence on external partners, conflicts of interest, and challenges in aligning strategic objectives.

Implementation may span 1 to 3 years



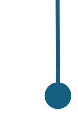
Long Game (Moderate to High Risk)

While it offers potential rewards in terms of innovation and market leadership, it requires patience, sustained investment, and acceptance of uncertainty regarding outcomes.

Implementation may span 2 to 4 years

Build or Acquire (High Risk)

It carries the highest risk due to the substantial financial commitment, uncertainties in technology development, and potential integration challenges (at acquisition).



Implementation may span 3 to 5 years

By prioritizing these strategies based on risk considerations and implementing them within appropriate timelines, traditional FIs can navigate the evolving landscape of digital lending effectively while leveraging their strengths and mitigating potential challenges.

Recommendations (Priority Sequence)

1. Arm's Length (Low Risk)
Initially, opt for arms-length agreements to explore digital lending opportunities without disrupting existing operations. Monitor market developments and internal readiness, gradually transitioning towards more integrated approaches as digital capabilities mature.

2. Partnership (Moderate Risk)
Forge strategic partnerships with fintech companies to leverage their expertise and innovative solutions. Conduct thorough due diligence and establish clear communication channels to align objectives and manage risks associated with dependency on external partners.

3. Long Game (Moderate to High Risk)
Establish internal innovation hubs or make strategic investments in emerging fintech firms. Foster a culture of innovation and patience, recognizing that returns may take time to materialize. Emphasize continuous evaluation and adaptation to mitigate uncertainties.

4. Build or Acquire (High Risk)
Consider investing in internal digital capabilities or acquiring fintech companies to enhance digital lending infrastructure. Prioritize due diligence and strategic alignment to mitigate risks associated with integration and technology development.

4. Deep Dive into Partnerships

The Possibilities and The Risks Involved

The Possibilities

Collaborative data sharing among industry players presents intriguing possibilities for enhancing the efficiency and effectiveness of digital lending processes.

By sharing anonymized transactional data and borrower information, stakeholders stand to gain deeper insights into risk-based pricing, credit risk assessment, fraud detection, and customer behavior. This collaborative approach has the potential to streamline operations, improve decision-making, and ultimately optimize the customer experience.

There is also need to leverage emerging technologies in advanced analytics like artificial intelligence, and machine learning algorithms for credit scoring and risk assessment.

The Risks Involved

However, partnerships in the digital lending space are not without risks. Some of the challenges highlighted by the study respondents include:

- Data privacy concerns
- Cyber security risk
- Systemic risks
- Regulatory compliance issues,
- The risk of overreliance on partner organizations (Third party risk)
- Mismatches in strategic objectives or operational capabilities between partners leading to conflicts or operational inefficiencies.

Therefore, it is essential for stakeholders to carefully evaluate and mitigate these risks through proactive risk management measures, robust governance frameworks, transparent communication, clear contractual agreements and goal congruence.

Conclusion

Although, collaboration with strategic partners is integral to the success of digital lending initiatives, it also introduces inherent risks. Market system actors must conduct thorough due diligence on potential partners and establish clear roles, responsibilities, and accountability mechanisms. Partnership agreements should delineate fault escalation paths, service availability, costs, and confidentiality agreements to mitigate the risk of unanticipated failures or compliance breaches.

Overall, the collaborative environment in Uganda's digital lending space holds immense potential for driving positive change, fostering innovation, and advancing financial inclusion.

By embracing collaboration and partnership, stakeholders can unlock new opportunities, address emerging challenges, and create a more inclusive and sustainable digital lending ecosystem.

5. Risk Management

Proactive Navigation of Risk = Safeguarding Success in Digital Lending

Risk management is a critical aspect of digital lending operations in ensuring the sustainability and resilience of financial institutions amidst evolving market dynamics and emerging threats.

Recent cases of digital lending fraud in the country serve as stark reminders of the necessity for heightened vigilance and proactive risk mitigation strategies. These incidents shed light on the vulnerability of digital lending platforms to both internal and external threats. They also underscore the urgency of addressing regulatory ambiguities and bolstering risk control mechanisms.

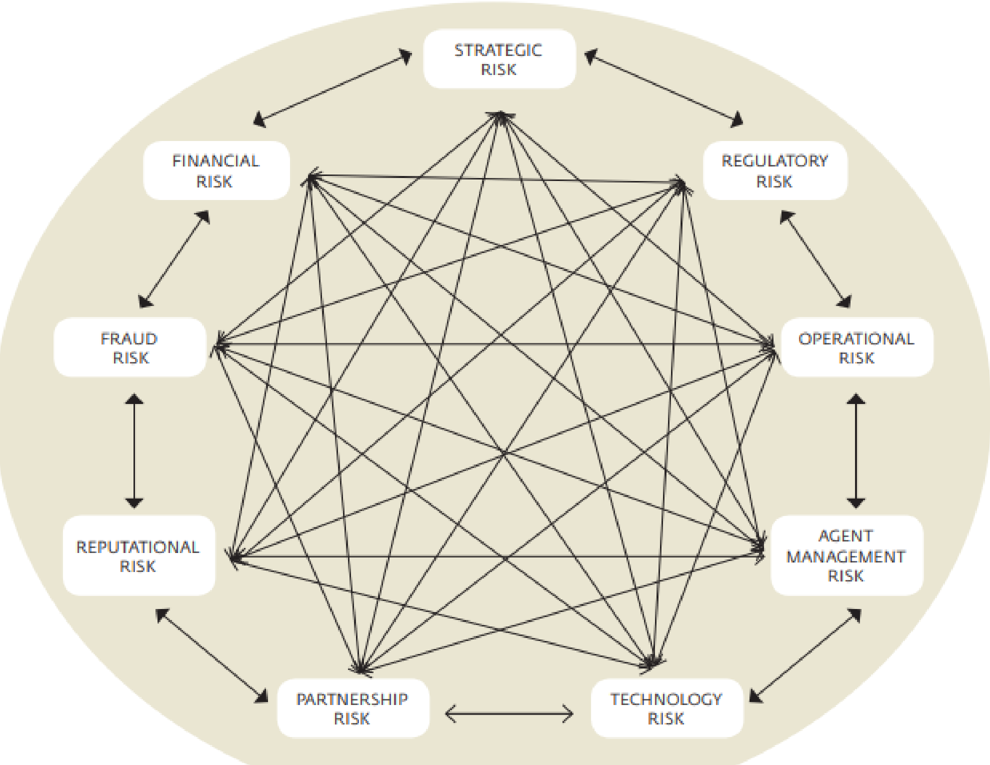
In this section, we highlight the importance of robust risk management frameworks and offer actionable insights for mitigating risks and enhancing the integrity of digital lending operations

Understanding the Evolving Risk Profile

Digital lending introduces a myriad of risks, from fraud and cybersecurity threats to regulatory ambiguities and strategic uncertainties. As digital loan offerings expand and customer adoption grows, all digital lenders must remain vigilant to emerging risks and adapt their risk management strategies accordingly. While some institutions have developed effective risk treatment strategies, many still lack a comprehensive approach, leaving them vulnerable to potential liabilities.

In this fast-evolving field, it has become apparent that what matters to one provider matters to all as large cases of fraud, for example, affect not just consumer trust in one provider but also in the entire market and in the promise of digital financial inclusion.

It is also important to note that, risks do not fall strictly in one category. If a risk situation arises in one area it can often create a risk situation in another area, and all risks must be considered together[18].



There is a growing need for more Comprehensive and more Proactive Risk Management Frameworks especially those that consider the varying stages at which providers are in their digital transformation journey.

It was also noted that risk registers are a common tool utilized by Digital Credit Providers, yet their efficacy remains questionable. Often limited to immediate financial risks such as fraud and technical issues, these registers fail to address broader risks such as strategic, reputational, and cyber risks. Furthermore, they are often treated as a mere compliance requirement rather than an integral component of ongoing risk mitigation efforts.

18. World Bank Document

5. Risk Management

Tailored Approaches for Each Digital Transformation Tide

Effective risk management is paramount for ensuring the sustainability and success of financial institutions. However, the approach to risk management must be tailored to the institution's position on the digital transformation journey.

Understanding the Digital Transformation Journey

Before delving into risk management strategies, it's essential to understand where institutions stand on their digital transformation journey. This journey encompasses several stages, including,

- digital infancy
- digital adoption
- digital transformation
- digital maturity

Each stage presents unique challenges and opportunities concerning risk management.

Faced with competitive pressures from fintech lenders, majority of the traditional financial institutions have embarked on this journey with the aim of transforming traditional credit processes into digital formats, reducing the "time to yes" to as little as five minutes and "time to cash" to less than 24 hours.[19]

It is also important to note that, Digitalization of credit processes means different things for different stakeholders at the different stages of their journey.

Most FIs in Uganda are at the digital adoption stage and below are some of their next immediate considerations.

1 Risk Management at Digital Infancy

During the digital infancy stage, financial institutions are just beginning to explore digital lending solutions. At this stage, the focus is often on establishing basic digital infrastructure and introducing rudimentary digital lending products. Risk management efforts primarily revolve around ensuring data security, compliance with regulatory requirements, and addressing operational risks associated with digital adoption.

2 Risk Management at Digital Adoption

As institutions progress to the digital adoption stage, they expand their digital footprint and offer more sophisticated lending products. Risk management efforts here must become more refined, with a focus on enhancing credit risk assessment methodologies, improving customer authentication/verification processes, strengthening internal controls to mitigate fraud and cybersecurity risks.

3 Risk Management at Digital Transformation

In the digital transformation phase, institutions must undergo a significant overhaul of their business processes, leveraging advanced technologies like artificial intelligence and machine learning to optimize lending operations. Here risk management strategies evolve to incorporate predictive analytics for early risk detection, automation of compliance procedures, and proactive monitoring of emerging risks.

4 Risk Management at Digital Transformation

Here institutions have fully embraced digital lending as a core component of their business model. Risk management practices are highly sophisticated, with an emphasis on continuous innovation and adaptation to stay ahead of evolving threats. Institutions at this stage must focus on leveraging data analytics for dynamic risk modeling, fostering a culture of risk awareness and accountability across the organization, and establishing robust crisis management protocols.

19. The-lending-revolution-vF.pdf (mckinsey.com)

5. Risk Management

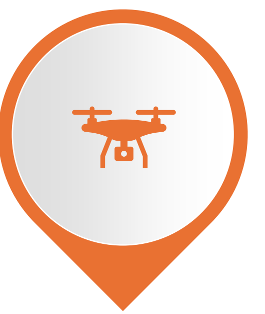
Lessons Learnt from Recent Fraud Incidents

Enhanced Due Diligence and Verification Processes:

Fraudulent actors often exploit weaknesses in the due diligence and verification processes of digital lending platforms to obtain loans using false identities or stolen personal information. As a result, digital lenders must strengthen their due diligence procedures by implementing more robust identity verification checks, comprehensive documentation reviews, and real-time validation of borrower information. Advanced technologies such as biometric authentication, facial recognition, and blockchain-based identity verification can enhance the accuracy and reliability of these processes, mitigating the risk of identity theft and fraudulent applications.

Collaborative Approach to Fraud Prevention:

Fraud prevention is a collective responsibility that requires collaboration among industry stakeholders, including lenders, regulators, law enforcement agencies, and consumer protection organizations. Digital lenders should actively engage with these stakeholders to share information, best practices, and intelligence on emerging fraud trends and tactics. Establishing industry-wide standards for fraud prevention, reporting mechanisms for suspicious activities, and coordinated response protocols can strengthen the overall resilience of the digital lending ecosystem and deter fraudulent actors from targeting vulnerable borrowers.



Proactive Monitoring and Detection Systems:

Fraudulent activities in digital lending often involve patterns or anomalies that can be detected through advanced monitoring and detection systems. Digital lenders should invest in sophisticated fraud detection tools and technologies that use machine learning algorithms, predictive analytics, and behavioral analysis to identify suspicious behavior or transactions in real-time. By proactively monitoring lending activities and detecting potential fraud indicators, lenders can take timely action to mitigate losses and protect both their businesses and their customers. Regular audits, product access tests, stress testing, and scenario analysis can also help identify vulnerabilities and strengthen resilience.

Continuous Improvement and Adaptation:

Fraudsters are constantly evolving their tactics and techniques to bypass security measures and exploit vulnerabilities in digital lending platforms. Therefore, digital lenders and supporting function actors must adopt a mindset of continuous improvement and adaptation to stay ahead of emerging threats. This involves regularly reviewing and updating fraud prevention strategies, investing in ongoing staff training and development, and leveraging technological innovations to enhance security and resilience. By remaining vigilant and responsive to evolving fraud risks, digital lenders can better protect their business and their customers from financial harm.

6. Call to Action

It's imperative to translate article insights into actionable steps for all stakeholders

Responsible Party	Actions
Digital Credit Providers	• Enhance eKYC mechanisms to strengthen credit appraisal for instance by utilizing of NITA's UG Hub platform and URSB's SIMPO Database • Conduct and establish customized risk management frameworks aligned with the institution's digital transformation journey and risk appetite. • Adopt risk-based pricing • Empower employees with the necessary skills, knowledge, and tools to effectively navigate the digital transformation journey • Outsource specialized professional services to guide your institution through every stage of the digital transformation journey. From assisting with the assessment of digital risks to implementing robust controls, deploying cutting-edge technologies, enhancing compliance measures, and fostering a culture of risk awareness, we provide tailored solutions to ensure your success in the digital era.
Regulatory Bodies	• UMRA should promptly enforce and monitor the implementation of these guidelines. • Implement a robust grievance redressal mechanism for handling digital lending complaints in Uganda. • Regulate interest rates across the credit sector but especially on digital lending platforms • Foster collaboration and information sharing among regulatory agencies to address cross-cutting issues such as data privacy, cybersecurity, and fraud prevention. • Implement robust oversight mechanisms to monitor digital lending activities and enforce compliance with regulatory requirements, including regular audits, inspections, and reporting obligations. Instead of just annual licensing. • NITA should fast track the development of a more inclusive consent framework to enhance access to alternative data in Uganda,
Umbrella Bodies	• Own and be responsible for the call to action and track progress on action points across the sector. • Advocate for Joint regulation and harmonization in the digital lending industry • Support capacity-building efforts for smaller financial institutions to enhance their risk management capabilities. • Advocate for the adoption of standardized risk management practices and regulatory frameworks across the industry. • Act as intermediaries to foster collaboration between digital credit providers and regulatory authorities, advocating for inclusive policies that support innovation while ensuring consumer protection.

6. Call to Action

It's imperative to translate article insights into actionable steps for all stakeholders

Responsible Party	Actions
Supporting Functions	**Mobile Network Operators (MNOs)** • Enhance collaboration with digital credit providers to streamline the customer authentication process and improve access to alternative data sources. • Invest in upgrading infrastructure to ensure seamless data and voice connectivity for uninterrupted digital lending transactions. • Explore partnerships with technology providers to leverage advanced authentication methods and enhance security measures for mobile-based lending services. **Credit Reference Bureaus (CRBs)** • Expand data sharing agreements with digital credit providers to include alternative data sources such as mobile phone usage patterns , social media activity and utility payments. **Online Merchants** • Incorporate digital lending options into checkout processes to provide customers with flexible payment solutions at the point of purchase. (Embedded Finance & Buy Now Pay Later Offerings) • Implement robust fraud detection measures to safeguard against unauthorized transactions and protect both merchants and customers. **eKYC Providers** • Enhance digital identity verification processes to streamline customer onboarding for digital credit applications. • Invest in technologies such as biometric authentication and facial recognition to improve the accuracy and security of identity verification. **Payment Service Providers (PSPs) & Payment System Operators (PSOs)** • Implement strong encryption protocols and multi-factor authentication mechanisms to secure payment transactions and protect customer data. • Enhance monitoring and surveillance capabilities to detect and prevent fraudulent activities and unauthorized transactions. • PSPs and PSOs are implored to reduce their rates to foster sustainable digital lending • Invest in upgrading infrastructure to ensure seamless data and voice connectivity for uninterrupted digital lending transactions.

6. Call to Action

It's imperative to translate article insights into actionable steps for all stakeholders

Responsible Party	Actions
Ministry of Finance, Planning and Economic Development (MoFPED)	• Increase budget allocation to UMRA to enhance the regulator's capacity to effectively regulate and supervise the digital lending sector, ensuring compliance and consumer protection. This could be done by securing additional funding for UMRA through the national budget. • Work with regulatory bodies like UMRA, NITA, FIA, and BoU to streamline regulations and reduce administrative burdens for industry players. • The ministry could invest in advanced regulatory technology (RegTech) solutions for the sector. This will also streamline regulatory processes, improve data collection and analysis, and enhance the efficiency of UMRA's supervisory activities. • Expand the regulatory sandbox framework to allow more digital lending innovations to be tested in a controlled environment. • Invest in digital infrastructure, including internet connectivity and mobile networks, especially in rural areas. • Encourage collaboration between the government, financial institutions, fintech companies, and other stakeholders to foster more innovation, sharing best practices, and a more supportive ecosystem for digital lending. • Create funding programs and incentives for digital lenders to access low-cost capital and .

7

Annexure

7. Annex

Detailed Proposed Interventions

1 Joint Regulation and Harmonization:

Joint regulation and harmonization in the digital lending industry presents an opportunity to optimize regulatory oversight by capitalizing on the strengths of various regulatory bodies while streamlining processes and minimizing duplication. By strengthening collaboration among regulators, such as BoU, UMRA, FIA, NITA, and possibly other relevant authorities, Uganda can establish a cohesive regulatory framework that ensures consistent standards and practices across the digital financial services sector.

This could entail harmonizing licensing procedures and fees to reduce administrative burdens on industry players while promoting fair competition and innovation. Furthermore, facilitating seamless information sharing among regulators through enhanced workflows and policy adjustments can improve regulatory efficiency and effectiveness, enabling timely responses to emerging challenges and promoting a more robust and resilient digital lending ecosystem.

2 Enhanced eKYC Mechanism:

The utilization of NITA's UG Hub platform and URSB's SIMPO Database presents a valuable opportunity for digital lenders to strengthen their credit appraisal processes and enhance risk management. By leveraging services like these and Laboremus' eKYC tech infrastructure, digital lenders can access vital databases including NIRA, URSB, and URA, enabling more comprehensive customer due diligence and verification procedures.

It is also key to note that, collaborating with NITA to develop a consent framework within the UG Hub platform is crucial to address regulatory constraints on information sharing and verification, particularly at an image level. This framework would facilitate secure and compliant access to essential data while ensuring adherence to privacy regulations. Additionally, tapping into the SIMPO Database for verification of collateral and assets can further bolster credit appraisal processes, enabling lenders to make more informed lending decisions and mitigate risks associated with defaults.

7. Annex

Detailed Proposed Interventions

3 Enhanced Grievance Redressal Mechanism:

Implement a robust grievance redressal mechanism for handling digital lending complaints in Uganda. Mandate digital lenders and their service providers to designate nodal grievance redressal officers, prominently showcasing their contact information on their platforms. This could be supplemented by empowering borrowers to escalate unresolved complaints to regulatory authorities for prompt action and resolution. This would help in the regulator's efforts to sieve out the predatory actors in the space and salvage the reputation of digital lending, which would in turn foster more trust within the ecosystem.

4 Risk Based Pricing

Implement a risk-based pricing model within the digital lending landscape to ensure fair and tailored lending practices while effectively managing risk. This intervention involves assessing borrowers' creditworthiness based on comprehensive data analysis, including alternative data sources such as mobile network operator data, fees payments, utility payments and or any other bill payments.

By incorporating enhanced risk assessments into pricing decisions, digital lenders can offer competitive interest rates that align with borrowers' risk profiles, thus promoting affordability and financial inclusion. Moreover, this approach incentivizes responsible borrowing behavior while safeguarding lenders against potential defaults, ultimately fostering a more sustainable and equitable digital lending ecosystem in Uganda.

7. Annex

Detailed Proposed Interventions

5 Cost Reduction

There is a consensus among providers that supporting functions, such as payment systems providers like MTN and Airtel, should reduce their rates to foster digital lending. High transaction costs and fees associated with payment systems hinder the profitability of digital lending operations and may discourage participation from both lenders and borrowers. Lower costs would enhance the viability of digital lending operations and encourage greater participation from innovative digital lenders and borrowers.

6 Interest Rate Regulation across the Sector

Concerns about high interest rates charged by online money / fintech lenders highlight the need for regulatory intervention to control predatory actors and protect consumers. Sensitizing the public and enforcing transparency measures can promote fair lending practices and mitigate risks associated with exorbitant interest rates

7 Customer Awareness and Adoption

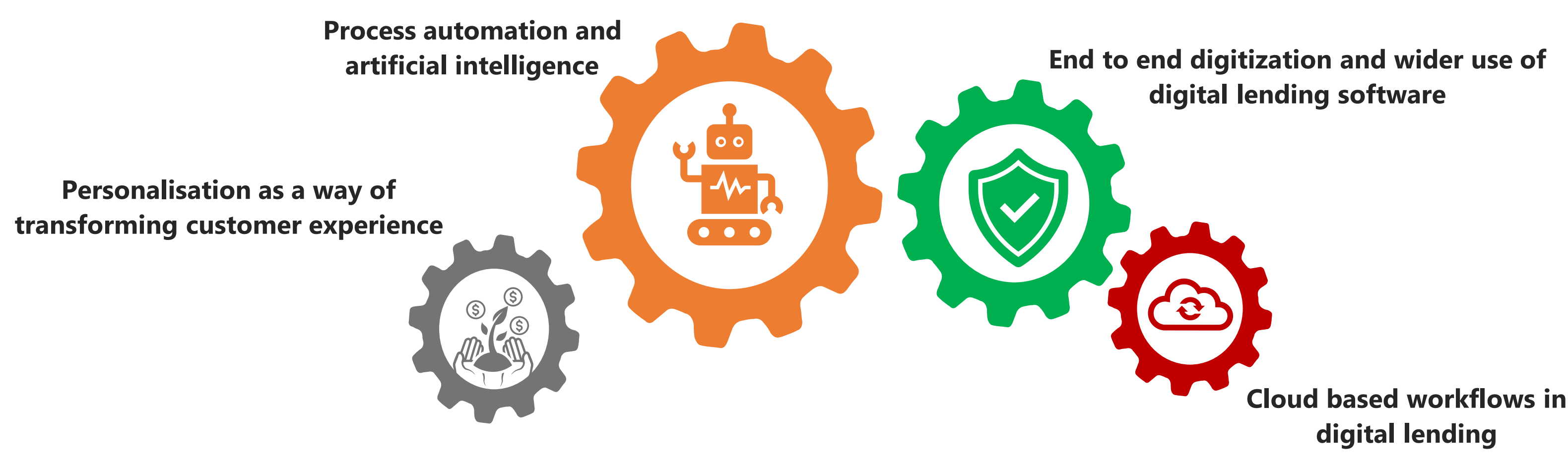
Limited customer knowledge and awareness of digital platforms, along with false perceptions and skepticism (given some bad actors), affect adoption rates and market penetration.
Collaboration between digital loan providers and regulatory bodies / umbrella bodies is essential in shaping regulatory frameworks that balance innovation with consumer protection, ultimately benefiting both borrowers and lenders in the digital lending ecosystem.

8 Advancements and Infrastructure Development:

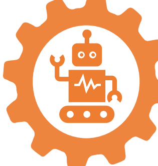
Investing in tech infrastructure development, such as expanding internet coverage and improving network connectivity in rural areas, is crucial to enhance access to digital lending services. Digital lenders should also prioritize the development of user-friendly mobile applications and digital platforms to cater to customers with varying levels of digital literacy.

More Trends

Amid the pandemic, most traditional financial institutions found themselves having to adopt and optimize technology much faster than ever before. Many banks that were just taking an incremental approach to digital were shocked into reality during 2020/21, and executives realized greater investment and faster transformation is needed to stay relevant. In terms of what lies ahead, there is consensus amongst industry experts that recent advances in artificial intelligence, machine learning, automation, and the cloud are set to redefine what's possible for borrowers and lenders.



As we proceed through 2024 and beyond, more trends will continue to transform the face of financial services. While lenders cannot predict that future, with the help of technology, they can put themselves in a strong position to adapt as quickly as possible



Process Automation and Artificial Intelligence (AI)

According to Blend[20], AI is set to improve profitability of businesses across 16 industries by 38% on average by 2035. Below is how it can be used in lender workflows.

- Quickly assess borrower information to make intelligent suggestions on products that are more likely to suit their needs
- Dynamically assess the solvency of a customer to reduce delinquency rates and minimize profit losses
- Answer the Frequently Asked Questions using AI-powered chatbots and guide applicants through the loan application process, reducing the burden on lending staff

The process automation can take the form of.

- Information already provided by the customer can be used to pre-fill a loan application
- Missing or inaccurate data can be flagged automatically, minimizing bottlenecks later.

This AI driven end to end automation delivers new efficiencies that are estimated to save major global banks up to USD 70 B by 2025

20. The latest digital lending trends impacting financial services | Blend

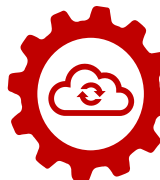
7. Annex

More Trends

End-to-End Digitization

The other lending technology trend is an increase in end-to-end digitization as more customers are looking for digital-first platforms. Financial institutions are increasingly prioritizing end-to-end digitization and omnichannel experiences to meet the growing demand for digital-first platforms[21]. Automation plays a key role in accelerating credit approval, loan servicing, and self-service options like advanced chatbots / WhatsApp banking for the likes of Centenary Bank and Emata. Additionally, the adoption of digital lending software, unified dashboards, analytics, and collaborative business models with fintech organizations are becoming prevalent. Amidst evolving customer expectations, institutions also face challenges like enhancing customer experience, managing staff attrition, reducing costs, and navigating regulatory changes.

This widespread use of digital lending software is facilitating faster and more convenient access to credit.



Cloud based workflows in digital lending

The trend of cloud-based workflows in digital lending represents a significant shift towards leveraging cloud computing technologies to enhance the efficiency and accessibility of lending processes.

This is making it easier to deliver services, manage documents, store information and process data online.
Specifically, it is enabling.

- Rapid roll out of the latest technologies like artificial intelligence and machine learning algorithms, into their lending processes. This is facilitating continuous innovation and is set to allow lenders to stay competitive in an evolving market.
- Easy, quick, convenient and consistent digital loan access experience essentially helping customers access loans whenever and from wherever.

Personalization as a way of transforming customer experience

The other significant trend is the emphasis on personalization to enhance the customer experience. This approach offers numerous benefits, such as delivering timely and relevant offers to customers in their preferred channels, anticipating their needs preemptively, and implementing risk-based pricing for tailored rates and credit terms. By leveraging personalized strategies and more alternative data, lenders can optimize interactions with customers, increase engagement, and improve overall satisfaction levels.

21. Finding-Lending-Diamonds-in-the-Rough_Cornerstone-Adv_Experian.pdf

7. Annex

Research Methodology

The research methodology employed to gain insights into the supply side, supporting functions, and regulatory environment comprised both primary data collection and secondary research.

Primary data collection involved a focused survey targeting 43 market system actors across various sectors: 20 digital lenders (both banks and non-bank institutions), 19 supporting function actors, and representatives from 3 regulatory bodies along with 1 umbrella body.

Additionally, secondary data collection involved a comprehensive literature review encompassing articles, accredited research papers, and relevant acts and regulations, as detailed in the reference list.

Limitations to the Findings

- The Team reached out to a total of 75 market system actors and was only able to secure 43 interviews across the supply side, the supporting function side and the regulatory environment and therefore may not fully capture the diversity of perspectives and experiences of all industry players.

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8. Next Steps

What to Expect in the Next Article Series

Article Series

Digital Lending

Series 1: Demand - Customer and Product

Series 2: Insights on Uganda's Digital Lending Landscape

Oil and Gas

In the upcoming article series, readers can expect a deep dive into how financial institutions can strategically position themselves to participate in Uganda's **Oil & Gas boom**, particularly now that the country has transitioned from exploration to the production phase.

Key topics to be covered include.

- Exploring safe, sustainable and profitable avenues for financial institutions to engage with the Oil & Gas sector,
- Leveraging insights from to inform banking strategies,
- Analysis of the oil and gas regulatory framework
- Understanding guarantee frameworks necessary for lending and addressing knowledge gaps in risk management specific to Oil & Gas operations.

Through comprehensive exploration of these topics, readers will gain valuable insights into the opportunities and challenges facing financial institutions in this burgeoning sector and how they can effectively navigate them to drive growth and sustainability.

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