How can Microfinance Institutions Effectively Implement Mobile Financial Services?

Insights from IFC Research

The results below are from research that IFC conducted with four MFI institutions globally. This summary was prepared with input from Margarete Biallas, Leila Search, Scott Stefanski, Vanessa Vizcarra and Minakshi Ramji.
Introduction

In the last two decades, microfinance institutions have democratized access to finance for large swathes of low-income, under-banked, and unbanked households. Yet, further expansion is constrained by their inability to build and maintain branch infrastructure. In recent years, mobile phone technology has shown that it has the power to transform banking and dramatically reduce costs for serving poor households who transact in small amounts. Microfinance institutions are experimenting with this transformative technology to expand beyond the limits of traditional branch-based banking. If successful, a mass market banking upheaval could lead to financial inclusion for millions/billions.

Clear trends in banking are seen: the role of brick and mortar is being reinvented while technological disruption races ahead of institutional ability to absorb. Yet, with very few lead microfinance institutions in MFS implementation, what makes for success?

Looking at four microfinance institutions’ mobile financial services solutions—Caja Sullana in Peru, Musoni in Kenya, mBank in the Philippines and Tameer Bank in Pakistan—IFC sought to understand how Microfinance institutions can achieve profitable growth in this channel, and extracted insights and lessons along the way to help in future microfinance m-banking designs.

FOCUS ON STRATEGY

To achieve success, an MFI must first clearly understand and define what they want to accomplish with MFS and how the market, environment, and other factors can facilitate or hinder their implementation. Secondly, the branchless banking initiative must perform and reduce traditional branch dependence, and thus decrease transaction costs.

Mobile strategies must recognize that it is about much more than simply offering a ubiquitous window into account information and payments integration. While these are critical first steps, a comprehensive strategy should address solutions across the MFIs activities such as customer acquisition and maintenance, transaction support, marketing and engagement, accounting, and collections.

Lowering set up costs (including the cost of technology, agent implementation, and cost of set up and maintenance of the network) and improving internal efficiencies bring an MFI closer to a positive cost-benefit ratio. Increasing revenue by launching the most valued set of products and appropriate pricing, and new products supporting microfinance institutions commercial activities also help achieve profitable success.

In the cases we examine, microfinance institutions, particularly first movers in this space, have taken opportunistic approaches to their MFS strategies. Microfinance institutions have introduced solutions that only improve consumer access and convenience, and reduce costs. However, most of them do not have a comprehensive MFS strategy putting them at a disadvantage to financial institutions such as banks that are entering the market, pursuing the same clients, in a much more strategic manner.
INCREASING REACH—FACT OR FICTION?

Undoubtedly, for most microfinance institutions, MFS represents an opportunity to dramatically increase their reach. Extending their network through physical branches is expensive, time consuming, and requires a relatively large number of employees. An agent network offers the opportunity to increase outreach at a lower cost.

Growth in access points does not guarantee growth in number of clients nor does it translate to growth of the value of clients. But, microfinance institutions have made headway establishing agent networks and consumers have responded through uptake. The research finds that microfinance institutions focus on and are able to dramatically increase supply points through an agent network. This is particularly true when the agent network is outsourced to a third party or when the agent network already exists through another arm in the institution. When microfinance institutions try to build an agent network themselves, growth in access is slower, but still higher growth than through traditional branch expansion.

While increased access points may not guarantee growth, microfinance institutions are finding promise with a combination of increased reach, ease of entry with gateway products and high demand-based products (introducing bill payment, airtime purchase, and remittances) that can help drive initial take-up.

AND AT WHAT COST?

Setting up and maintaining an agent network costs less than a traditional branch network but does not necessarily imply increased revenues when measuring the channel alone. Agent network setup and maintenance costs are lower than the cost of a traditional branch network and the cost of a digital transaction can be 88 percent less than a branch transaction. Such significant cost differences imply huge savings for organizations implementing MFS.

However, reduced costs do not necessarily result in immediate higher revenue on the channel alone. And, MFIs need to be sensitive to seeking higher overall revenues in the short term at the expense of reduced revenue per client due to reduced contact. Importantly, for some microfinance institutions, higher income may not necessarily be the immediate goal. In this research, only one microfinance institution operating in a highly populous country and focusing on remittance transactions was able to generate high revenues equivalent to 21 percent of its overall revenue. Even in this instance, almost all the revenue from the channel is diverted into paying out commissions for the channel. For Caja Sullana, MFS represented a key pillar of their alternate delivery channel strategy and was critical to reduce branch dependence. Their benefits were calculated via cost savings through the MFS channel since all the e-enabled transactions would have otherwise happened at a bank branch. Using this calculation, they estimate that their savings through MFS is about five percent of the institution’s net profit for 2012. For some microfinance institutions, mobile is simply a delivery channel and they expect to earn revenues from their products and services. Pricing of products and services on the channel vary across institutions and depends upon their strategy. Institutions using mobile to offer an additional delivery channel may choose not to charge for transactions, and must account for the commissions on these transactions.

If microfinance institutions look to mobile only as a means of offloading transactions from branches, they should expect that revenues earned from the channel will likely be put back into the channel as commissions. MFIs need to construct a mobile channel strategy that is not divorced from its overall operations but rather as a way to more fully engage with clients to both reduce costs and guide client growth. This mentality instead positions agent networks as the first line of client engagement to identify and better serve needs which will ultimately result in higher income from increased sales of more products and services. These considerations must be considered when assessing costs and revenues particularly break even, for this channel.
NEW & IMPROVED PORTFOLIO, PRODUCTIVITY GAINS

In one case, the microfinance institution experienced notable declining trends in portfolio at risk, because consumers were able to make timely and more frequent repayments. For example, Musoni found that 42 percent of loan repayments were made at nearby agents outside normal banking hours. The mobile channel can also increase timeliness and convenience for clients when they can make more frequent smaller payments conducive to limited cash flow.

Musoni also found that they can make headway with adoption in traditional lending groups by reducing by 50 percent the time required to conduct group lending tasks, opening time for more valuable educational and new applicant activities. In addition to increased adoption by consumers, loan officer productivity is higher as a result.

MFS presents microfinance institutions more than the opportunity to extend current portfolio to more customers effectively. By introducing mobile, microfinance institutions can cater to markets unavailable during branch hours and design specialized products that otherwise would not be supportable. Caja Sullana was able to introduce a product directly at shops with a 52 percent profitability compared with overall credit portfolio profitability of 7.5 percent.

EVOLVING MOBILE FINANCIAL SOLUTIONS

Microfinance institutions must analyze and assess how to best integrate a digital channel for their customers. Under a comprehensive strategy, they must focus on appropriate products and fuller client engagement. As the case studies show, institutions will make revenue on the digital solution through the additional sales of financial products and services, not through the channel itself.

In this study, the microfinance institutions have shown MFIs can harness mobile to create greater access through agent channels, both proprietary and outsourced networks. In the case where an MFI has sought to attract greater client engagement by offering remittances and bill payments, results have not yet justified the approach as these transactions constitute only 10% of overall transactions and done at a loss to the MFI. As MNOs with the benefit of scale further penetrate these opportunities, the case for MFIs to compete here will only be more difficult.

Where there is promise is where MFIs draw upon their knowledge of client needs to introduce tailored financial products that could unlock the potential of mobile-assisted accounts. For instance, mobilizing savings through this channel holds the promise of lowering cost of funds, which could be a huge benefit for these microfinance institutions, particularly those operating in countries where financing for microfinance institutions is hard to come by.

Banks and some greenfield microfinance institutions are approaching MFS comprehensively, entering as competition that has the strategy to scale cost effectively from the beginning. This will create strong barriers difficult for microfinance institutions to overcome if they don’t move now to shore up their customer relationships. MFIs should comprehensively look at how they can deploy mobile channels and data strategies to scale operations, expand services, and ultimately better serve shareholders, whether those are investors, donors, or the customer base.