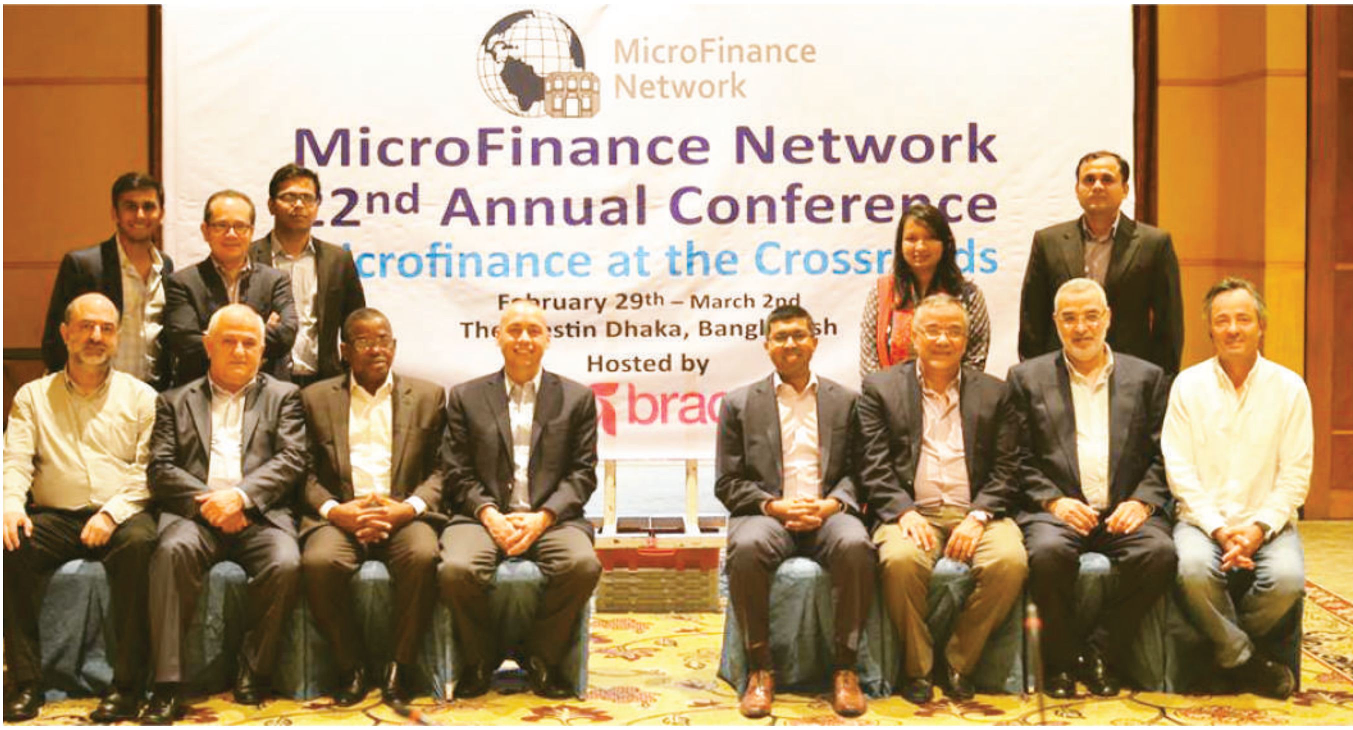
MFN Annual Conference 2016

Dhaka, Bangladesh

MicroFinance Network



About the MicroFinance Network

The MicroFinance Network was founded in 1993, and has since been a leading global network of 25 MicroFinance institutions from five continents that share the common belief that an MFI can serve more clients by establishing a sustainable and profitable institution.

Traditionally, members meet annually to discuss relevant issues and developments, and the core of the Network is knowledge sharing and learning. In the past, conferences have focused on issues ranging from scaling up the microfinance business model to better understanding clients and their needs. In recent years, the focus has expanded to discovering new business models, serving the client's needs more fully, and using technology to radically transform the dynamics of our current offerings. The membership has always been a forward thinking group, and the challenges that traditional MFIs face in combination with opportunities that exist for financial inclusion drive the Network to keep building a better future for our clients.

You can find more information about the Network at our website, **www.microfinancenetwork.org.**

Abstract

This Year's Annual Conference of the MFN was an intensely gratifying experience for the participants; we can't wait for next year's. The discussion sessions we had among CEOs, with their depth, rich content, and powerful insights that were based on open communication, sharing and trust, assured us that the Network is living its mission. Furthermore, we left Dhaka reassured of the immense opportunities the MFIs have not only to maintain their relevance but also to lead the financial inclusion space in years to come. In synthesis this is what we achieved:

First, we have developed as a group a systematic process to analyze the external context of the MFIs which has shaped our understanding of the worldwide trends that affect them. This analytic process now allows us to track the evolution of the external environment rigorously year by year. This dynamic has allowed the participants to develop a worldwide view of the most significant trends in the MFIs relevant context. Furthermore, we have developed

a strong support group for each participant member to help put to the test and debate their response strategies to most critical challenges. Second, we developed an overall understanding of the emerging financial technologies, by mapping the fintech's ecosystem onto the financial value chain and analyzing them systematically. We are now less anxious about how to approach technological innovation. Third, we immersed ourselves into bKash's history and BRAC's mission driven innovation strategy and processes. BRAC, the largest NGO in the world, serving 126 million people with a wide diversity of programs, is the best example that even large MFIs can innovate tremendously if they understand that innovation is a culture, what it entails, how it is led, and if they develop a strong commitment to innovation. Additionally, the discussions led us to the possibility of not only innovating as individual MFIs but also to sharing innovation approaches among members. Fourth, by having a young social entrepreneur CEO as our guest speaker we were able to engage in a discussion of introspection and reflection that left us tremendously encouraged about the opportunities to lead the industry in the next decade if we are able to find and integrate these technologies and entrepreneurs into our innovation strategy. In a one on one setting unrelated to the MFN, such a discussion could not have taken place, as each organization would have seen Artoo only as one of many suppliers. Fifth, we learned how the shape of this industry's life cycle signals to a level of maturity but not to market saturation. Therefore, there are still ample opportunities to reach more customers and offer more solutions with our traditional business model. However, the challenge of the CEO is to balance the benefit of this pursuit with the risk of not being proactive in developing and implementing an innovation strategy. Finally, we concluded that the largest challenge, perhaps, is for the CEO. Being the leader of an MFI into the next decade will demand extended role and capabilities: the renewal of their entrepreneurial spirit.

We thank the participants for their contributions during the annual meeting, and eagerly look forward to exploring in even more depth some of these topics in 2017 with all the MFN members!

Agenda of the Yearly Meeting in Dhaka

After 17 years the Microfinance Network Annual Meeting returned to the birthplace of microfinance: Bangladesh. The agenda was designed to have a deep immersion in the topics that are expected to have most impact on the MFNs organizations in the next few years, first with an emphasis on those factors most currently relevant to its members and then on the long term effect factors namely technological innovation.

Therefore, the first day of the conference started with a PESTEL analysis[1], scenario building, and strategic responses to critical factors; then, we focused on technology-based innovation, the main theme of this year´s conference.
During the second day we focused on the details of mobile money. We went to the field, saw firsthand the bKash operations and tried it on the spot. Then we met with bKash´s CEO, and learned the story, challenges, and success factors behind their business model. In the latter half of the day, we met with the leaders of BRAC´s social innovation lab, an initiative sponsored by the Gates Foundation, where new mobile money applications are being developed. The third day sessions focused not only on what technological initiatives are relevant but also on gaining an understanding of how these technologies are identified, evaluated, chosen and implemented. In order to get an entrepreneur´s perspective, we invited Sameer Segal, CEO and founder of Artoo, to describe how their CRM platform is empowering MFIs in India. Finally, our closing session focused on the MFI´s innovation path going forward and on the scope and challenges of an innovation strategy.

[1]PESTEL or STEEP analysis refers to a framework used to analyze and monitor the macro-environmental (external environment) factors (Political, Economic, Social, Technological, Environmental, Legal) that have an impact on an organization. The result of which can be used to generate scenarios, identify threats and weaknesses, and develop mitigation strategies.

Environmental Scanning

What external factors are having the most influence on the MFIs?

MFIs are facing a wide variety of factors that affect their organizations. Some of these external factors have the potential to radically affect their business models, are highly dynamic, and are taking a toll on some MFIs around the world. Building on the discussions that took place in Alexandria in 2015, the question raised for MFI members in 2016 was how can we improve our analytic processes to clearly identify these factors, their trends, and their implications so that we can develop appropriate responses and capabilities to mitigate a risk or to capture an opportunity?

Members from several countries shared how political factors are disrupting their MFI´s. They are experiencing how MFIs are highly visible political targets and are more vulnerable in those countries with low levels of institutionalization of their financial system. The participants described in detail how political interventions have interrupted, disturbed day-to-day operations, or eliminated product and service opportunities. These interventions have ranged from regulatory, such as interest rate caps, to direct intervention such as organizational takeovers. How can MFIs respond? We concluded that MFIs face high risks if their mode of responding to external threats is only reactive. Therefore, active engagement with the external context is necessary, there is no more “flying under the radar”. Building political influence becomes strategic in order to prudently navigate these political waters and protect the viability and long-term profitability of the organization.

The participants shared their experiences of how their institutions are responding to such political situations, and members collectively brainstormed and debated solutions for each other. Not only does such a rich and open discussion allow for developing benchmarks but also facilitates the development of strategies particular to each MFI context.

Industry Analysis

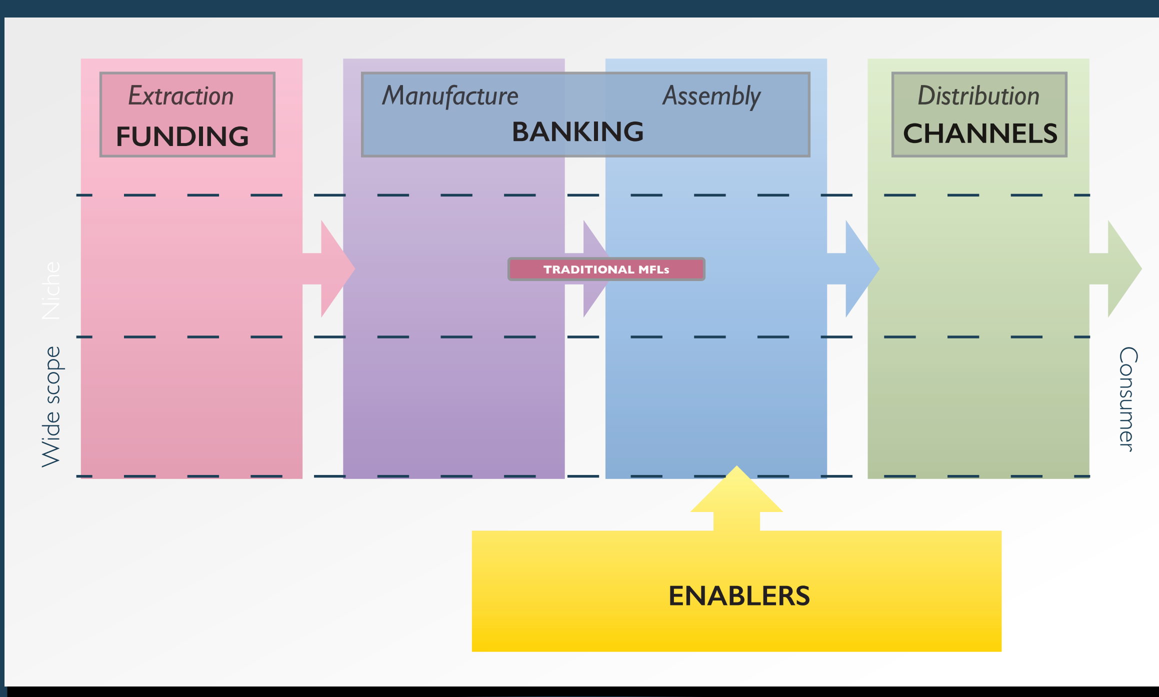
How do we make sense of the new technologies and business models?

A significant number of new players, primarily known as “fintechs”, are rapidly populating the financial space. At first glance, it is difficult to identify which of these emerging organizations present opportunities to enhance our business models, which pose competitive threats at an early untested stage, and which are becoming increasingly viable. How can we understand and distinguish among these players, and develop a strategy to interact with them? To do that we developed and analyzed responses to four sets of questions:

How are fintechs altering the financial industry value chain? Where are they positioning themselves? How do fintechs and their business models compare?

First, the financial industry is experiencing a phase of large emergence of technologies and business models. Second, these organizations are not only focused downstream but also spread throughout the different stages of the value chain. And third, some models that are becoming successful are being implemented in different market segments than those relevant for the MFIs, usually at higher income brackets, that eventually might trickle down to our market segments.

These characteristics represent a situation of great complexity, where the identification and differentiations between facilitators, potential allies and new competitors is an important strategic task, combined with predicting which new solutions to other market segments would allow new competitors to enter the MFI´s segments.

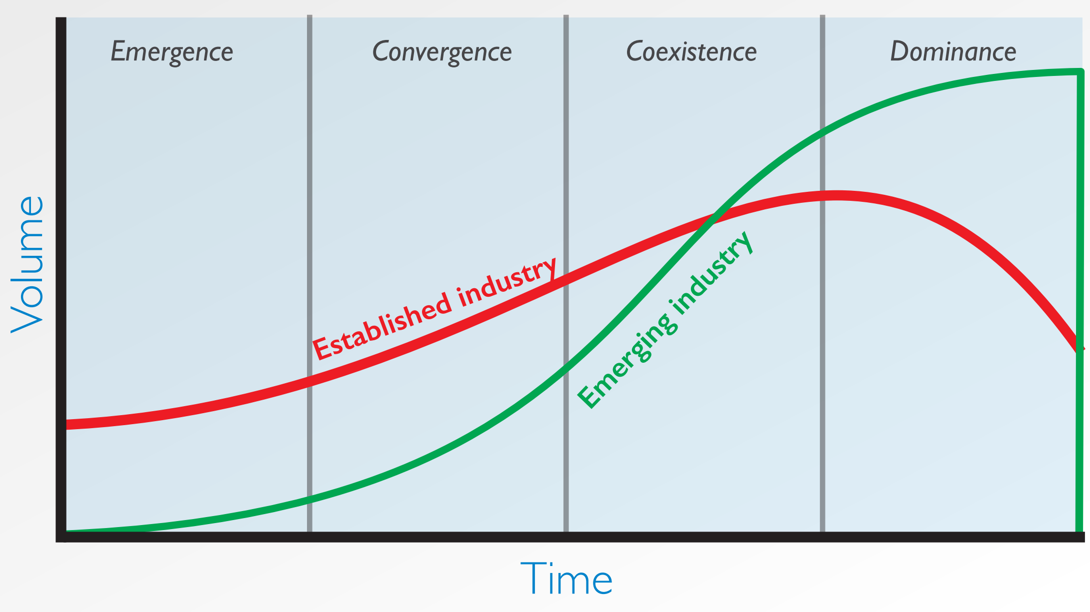


Industry Analysis

Where are these fintechs and technologies in their life cycle? How mature are they?

During the session we discussed how uncertainty impacts the potential of new solutions and business models and observed how fintechs are positioned along the life cycle, therefore how they vary in their impact uncertainty. Some of them have not yet passed the test of standardization and widespread adoption, such as in the case of Robinhood or Kreditech, while others have already achieved significant scale and have successfully lowered transaction costs, such as mobile money (M-pesa, bKash).

We agreed on the importance of having a systematic evaluation of these technologies and business models in the strategic agenda of the CEO. By doing so, the MFIs may be able to strike a balance between high potential technologies and not yet proven technologies, thus dedicating resources to the best opportunities and generating strategies to mitigate the threat of obsolescence of assets, activities or business models.



(Anita M. McGahan, 2004)

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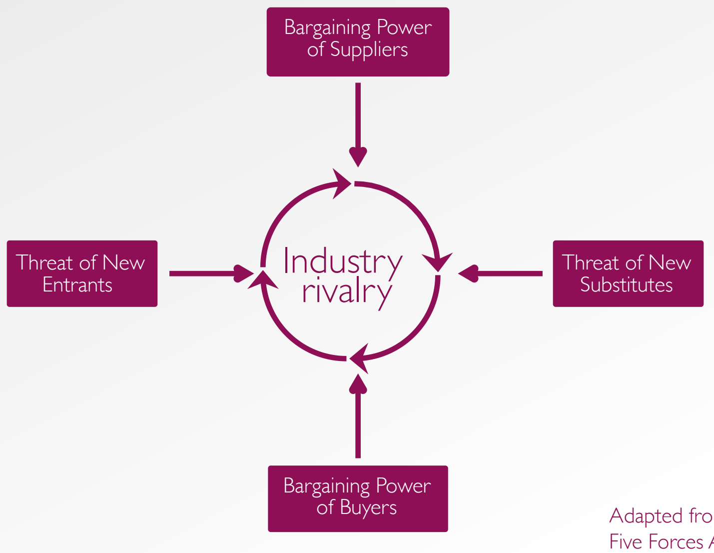
Industry Analysis

How does each new business model affect industry configuration and dynamics and the MFI positioning?

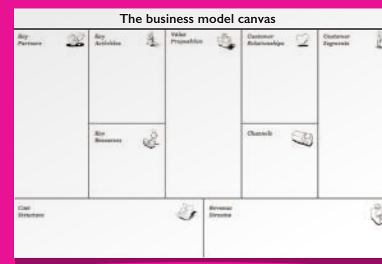
The proliferation of business models and technologies suggest that in the upcoming years the industry will have a more competitive dynamic. We analyzed the potential impact of these solutions on the different forces that configure industry positioning and profitability. Although we found that the emergence of fintechs is already making inroads in the traditional banking landscape, in some segments of the financial inclusion space the effects are not yet highly perceivable. Our analysis found that: First, technological adoption by customers can weaken the relationships with customers by lowering their switching costs, although we observe that technological adoption in our segments is still a major challenge. Other technology providers, such as Credit Karma are generating additional knowledge via big data applications that can provide more granular market segmentation, and a few such as Kabbage or Prosper are providing alternative delivery channels. The opportunity and challenge for the MFIs to lead the integration of these kinds of technologies in their CRM processes is evident. Second, many emerging solutions appear to potentially insert themselves in activities that are part of the MFIs value chain. As such, those who understand them and have the ability to integrate them will have a potential to achieve significant reductions in transaction costs, a critical strategic value driver of the MFIs. Thus, a set of those emerging models, such as Square, which allow merchants to more efficiently process transactions, can be strong complements in the financial inclusion space. Third, some of the models lower barriers to entry by providing efficient standalone solutions to market segments, with their own technology infrastructure; such as in the case of Kreditech, which aims at challenging the traditional lending model. Finally, technology based models that allow developing more customized solutions delivered through alternative channels seem to provide more efficient substitute products to the market.

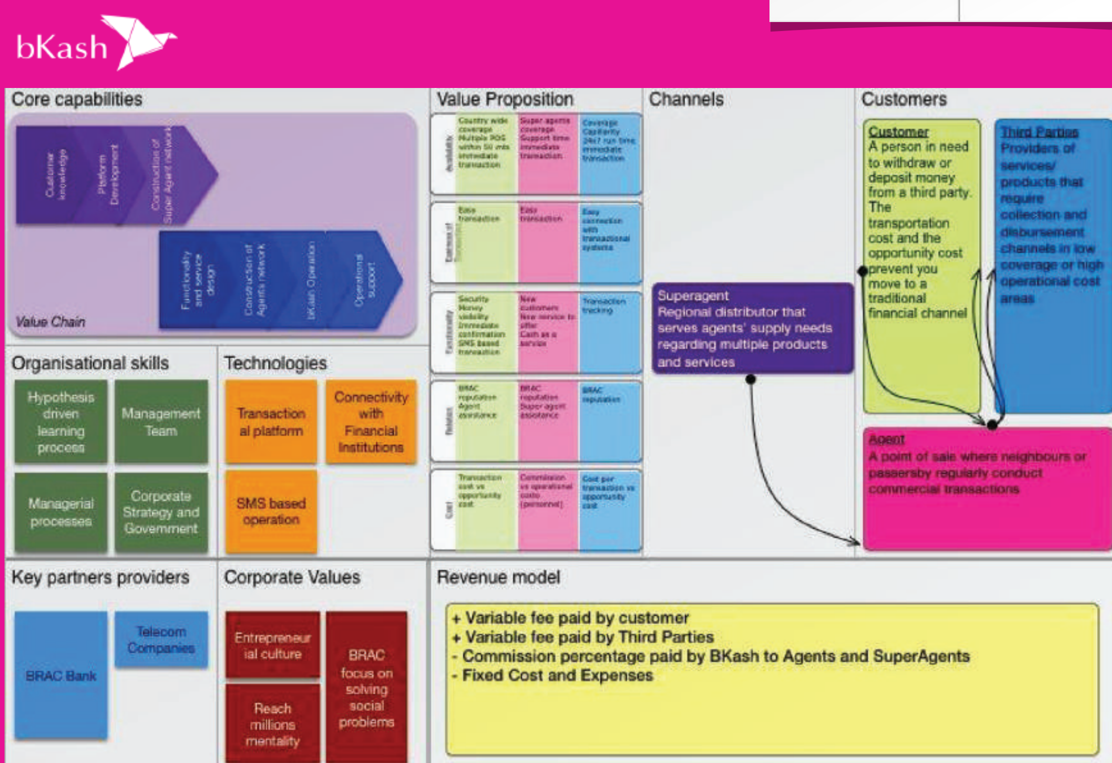


Adapted from Porter´s Five Forces Analysis

Industry Analysis

What is the business model of these Fintechs? What area or element of the MFI business model does the Fintech affect? Is it a complementor, a supplier or a competitor?





To fine tune the analysis, evaluate the impact on our MFIs, and map an appropriate strategy, the emerging technologies and their business models have to be compared and analyzed against our own business models. We found that the impact of each solution can be diverse: the cannibalization of clients, the ability to capture more information about the client, better assess risks, complement our value proposition, and reduce transaction costs to name a few. Therefore, we agreed that constant monitoring of our business models, as well as those of new players, is essential to our strategic analysis to evaluate prudently their impacts, set a path going forward and generate the implementation initiatives to march forward in our mission.

An example of the above analysis is the business model canvas of bKash. We learned in the session on bKash, that the mobile money initiative has converted into a profitable and relevant operation for BRAC, still faces adoption challenges, and has the potential to generate synergies and opportunities for other programs, such as those related with microcredit, education, and health.

BRAC, bKash, and the Innovation Fund

How do you go from 0 to 25 million customers in 4 years?

In recent years, one of the hottest topics in the financial inclusion space has been mobile money. Many analysts consider it will be a pervasive technology in the future. Mobile money is one of the fastest growing business models in the fintech landscape. As of 2015, mobile money was already available in 93 countries, and mobile money providers across the globe are processing an average of 33 million transactions a day.

The number of registered accounts has grown by 31% in 2015 to a total of over 400 million at the end of December of that year . However, dozens of organizations that have tried to develop mobile money have failed. In Bangladesh, for example, about twenty companies had already obtained approval for doing mobile money in 2008 when BRAC started to look at this opportunity. bKash was launched in 2011 and in four years it achieved a dominant position in the market with 25 million customers, and with such an impact that today to do mobile money in Bangladesh it is said “to bkash”, it has become a verb. Consequently, the participants could not wait to get into the details of the success factors of this technological implementation by one of the member MFIs.

We started our day by visiting the bKash operations in the field. The high density of bKash agents amazed us. There were 8 agents located within a 100 square meter radius of each other! We also saw a typical transaction, where a rickshaw puller sent money to his son in a rural village, facilitated by the agent, and it was immediately evident the strength of the value proposition to the customer: wide availability, speed of delivery, ease and safety of transaction, trust relationship between customer and agents, and high value/cost for the service.

After the field visit, bKash´s CEO graciously spent the rest of the morning with us sharing the entrepreneurial story of bKash. In the early days, it was characterized by its austerity, focus on learning, and time spent in the field. The rapid and iterative manner in which it has achieved scale, penetration in the market and financial viability highlighted carefully thought decisions regarding governance, organizational structure, people and systems that led this disruptive initiative to flourish. The management team has been able to maintain an aligned organization, transitioning from and informal team to a more formal traditional organizational structure as it has grown, they have been able to attract top talent with the required knowledge and experience from other industries, and assembled a strong management team. A board was formed since day one, with members that had industry specific knowledge. The board set clear objectives and revised them constantly—“solve the problem with the cash disposable”.

> The approach of the Board has been “let’s solve this together” by developing a high level of trust and confidence between ownership and management.

There is a need to constantly change while not halting the current operation. It is like changing the engine of an airplane while flying, or the tires on a car while driving.

Kamal Quadir
Founder of Bkash

A complementary role of BRAC has been to support the initiative by providing capabilities and resources that would complement what bKash was requiring on an as needed basis. This strategy has been the key to avoid smothering the initiative by the day-to-day operations and formal systems of the traditional BRAC organization.
In the next phase bKash will face a new challenge, which is that of connecting the new venture with the rest of BRAC to achieve synergies and efficiencies in better serving clients.

How does BRAC innovate?

As the day went by and we immersed ourselves in the details of this initiative it became evident that there was an institutional approach behind innovation at bKash. In the next meeting BRAC opened the door for us to learn about their innovation culture. The leaders of BRAC´s Innovation Fund for Mobile Money spent the afternoon with us and shared details about their philosophy, innovation processes, and values. This fund, supported by the Gates foundation, is set up to accelerate the switch from cash to mobile money.

During the first round of the Innovation Fund Challenge six projects were selected. In 2015 they did the second round and added more projects. These projects are not only for BRAC microfinance, they extend to the other BRAC initiatives, companies and programs ranging from solutions for paying primary school teachers through mobile money, to paying health workers their monthly stipend through bKash. At its core, the program is trying to see whether the ultra-poor borrowers in remote areas who receive a weekly stipend from BRAC see value in receiving their payments through mobile money.

BRAC applies an explicit process for each initiative, the same they used since the first program: solving the problem of children dying of dehydration. It is a five-step process: innovate, implement, measure, learn, adapt. The impact of their first program was just amazing: reducing the child mortality rate in Bangladesh rate from 250 deaths per 1,000 births to 40. A few maxims reflect BRAC's values which are simple but profoundly effective and important: "Small is beautiful but large is necessary", "Learn as you go", "Use what is there", "Get it done", "Nothing is ever perfect", and "Programs must be first effective, then efficient".

The fund leaders highlighted how innovation is risky, expensive, and time consuming. Thus, achieving balance between scale and innovation is a must. To prioritize initiatives each is evaluated and mapped in a 2 by 2 matrix in which one variable is the assessment of the level of commitment and interest of the people in charge of implementation, and the other variable is scalability, which at BRAC means the ability to reach millions. Furthermore, their programs depend on achieving cultural change; therefore, BRAC understands the intricacies of adoption and implementation of programs that incorporate not only the solution and its technical characteristics but also behavioral change.

> The streamlined approach followed by BRAC demonstrated that the success of the bKash initiative couldn't be explained only by an isolated innovation effort. Very quickly we learned that the breadth of success in BRAC implementing a wide range of initiatives stems from a strong institutionalized innovation culture.

Having an innovation model that is simple, repeatable, known by the whole organization, and applied to all initiatives has yielded tremendous success not only to bKash but also to other initiatives within BRAC. Consequently, if the traditional MFIs have technological innovations goals in their agenda, a necessary condition will be to develop an innovation strategy and culture.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I want programs to first be
effective, then efficient.
Fazle Hazan Abed
Founder of Brac

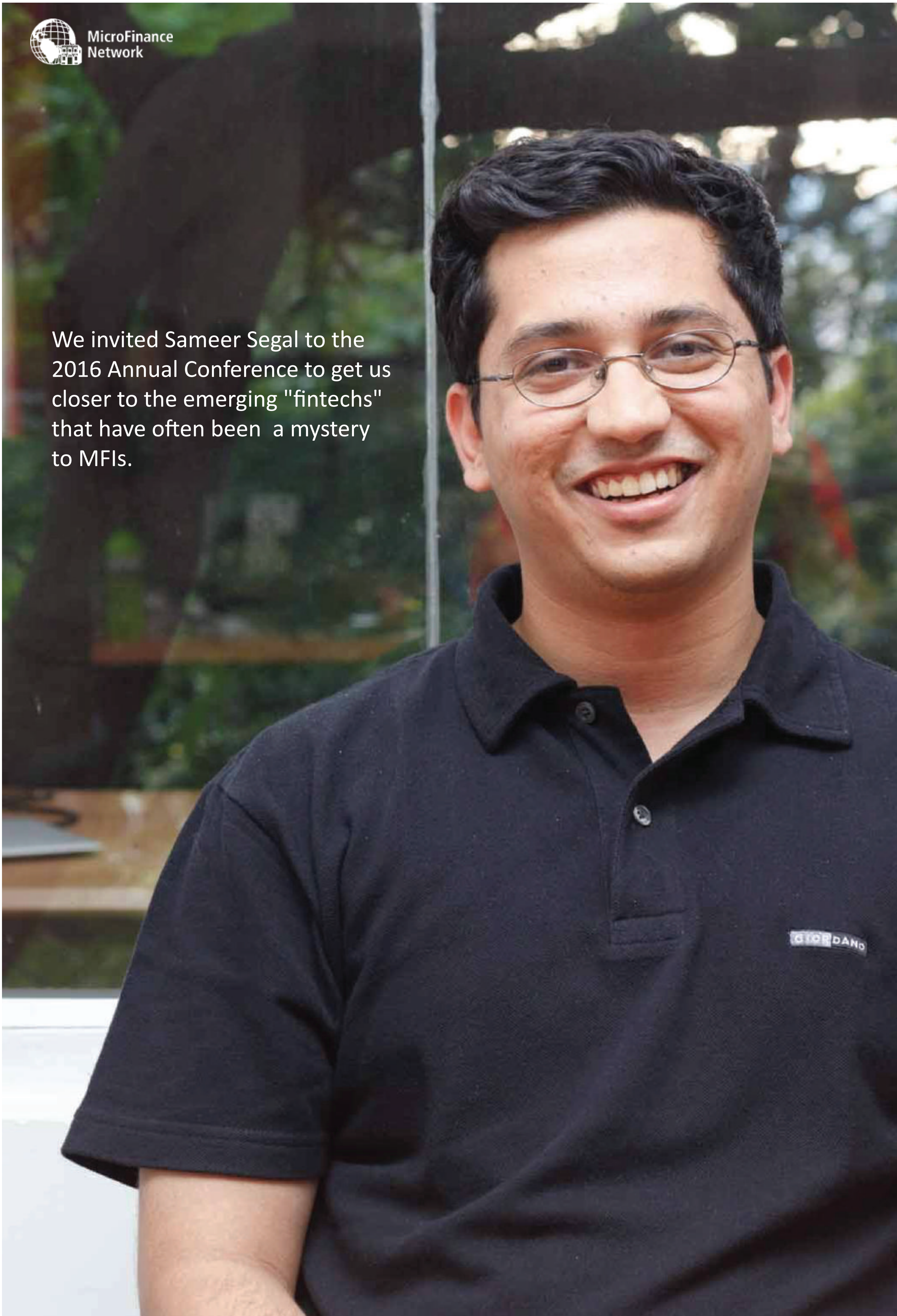
technology to the rescue

Keynote Conference by Sameer Segal

We invited Sameer Segal to the 2016 Annual Conference to get us closer to the emerging "fintechs" that are often a mystery to the MFIs. Sameer is the founder and CEO of Artoo, a Bangalore, India based startup that complements the MFIs by using inclusive technology to empower loan officers, improve end-to-end processes, and increase customer satisfaction. At its core, Artoo is a financial customer relationship management platform ("CRM") that allows MFIs to manage the entire customer lifecycle from loan sourcing to post-disbursement servicing, all on a single platform. To date, Ujjivan, India´s third largest MFI, is successfully using Artoo´s technology. Sameer, the 29 year old CEO and founder of Artoo, shared his experience launching and developing this technological solution. The participants were left wondering how someone who knew little about the MF industry five years ago could come in and develop relevant solutions that serve our clients' needs within a short period of time.

Artoo was born out of a summer internship Sameer did with Ujjivan, where he wondered why the world´s most intuitive technologies could not be applied to the bottom of the pyramid. His fresh entrepreneurial spirit allowed him not only to understand the problem and identify the opportunity to reengineer the end-to-end customer relationship process but also to come up with a valuable solution. He observed how established companies tend to automate existing processes and noted that many companies make the mistake of simply digitizing everything that is on paper and moving it to a tablet, but not enough companies spend sufficient time on thinking how a process should be redesigned once technology is involved (re-ordering steps, eliminating steps, inserting new steps etc.)

As for the process of developing Artoo, Sameer highlighted the importance of iterative learning on building an impactful business. For example, he explained how the initial designs of the Artoo software for tablets demonstrated that it was not possible to please everyone, thus their design decision-making processes were focused on tradeoffs between the size of the device (male loan officers wanted larger displays while female loan officers cared about the weight of the device and wanted it to fit in their handbags), battery life (management wanted 8 – 10 hours) and features (customers wanted videos on the device to provide more information).



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Sameer also talked about the challenge of building an entrepreneurial team, integrating people with specialized and complementary skills, and how entrepreneurs need to have skin in the game, for example, he stopped drawing his salary when in the initial phases Artoo only had 6 months of money in the bank.

Sameer is highly optimistic about the future. He is open to taking Artoo in various directions depending on how opportunities present, but at the same time he has it very clear that the company needs some strategic anchors around which it should grow. He calls these Artoo´s "north stars and guiding lights", and defines them as three simple principles:

- *How do we make field staff happy?*
- *How do we dramatically change economics of this model and its business results?*
- *How do you radically improve the experience of the borrower?*

This was a session in which we could radically contrast the speed and frugality with which an entrepreneur operates, versus the abundance of resources and slowness of mature MFIs entrepreneurial processes. We were quickly reminded of the early days of microfinance, when we were entrepreneurs finding a new business model to serve our clients. The session left us with a sense of urgency to rekindle our entrepreneurial spirit. We were also reminded that we are not alone in this pursuit, if we open our eyes to the world of financial inclusion around us there are great opportunities. We can get the best of both worlds if we are apt to find suitable partners with whom we could ally to build the solutions of the future.

The world is not binary. The future of microfinance will not be all agents based, nor will it be all self-service. There is a space where technology can coexist with, and even enhance, human interaction.

Innovation Strategy and Process

Why is an innovation strategy important for the MFIs?

There is wide consensus that the radical changes in the business models of players in the financial inclusion space will come from the application of technological innovations. As we found in previous sessions, these innovations will generate deeper knowledge of customer segments, change the product delivery channels, fine tune value propositions, and provide significant increases in operational efficiencies. We did have a harder time agreeing amoung us on how many years these changes will take, and we expect that this timing will vary by the characteristics of the geographical location and by the context of each MFI. However, keeping up or leading change is complicated by the fact that developing and integrating new technologies requires capabilities that take years to develop, as the discussions and the experiences shared in previous sessions demonstrate. Therefore, the decisions regarding the focus of MFIs technological development and the resource allocations to those projects will have a long-term impact in their organizations. Consequently, MFN members agreed that having an innovation strategy is a must if they want develop or maintain a leadership position in the industry. Furthermore, the lack of a deep understanding on what innovation and innovation strategy is has generated flawed approaches by many organizations not only due to flawed implementation but also to a lack of a sound strategy.

> An [Innovation] strategy is nothing more than a commitment to a set of coherent, mutually reinforcing policies or behaviors aimed at achieving a specific competitive goal. Good strategies promote alignment among diverse groups within an organization, clarify objectives and priorities, and help focus efforts around them.
>
> *(Gary Pisano, HBS)*

What is our current approach to technological innovation?

The construction of competitive advantage depends on creating differentiation in our business models. To incorporate technological innovations in our MFIs we explored how members are approaching it and we found significant variance. On one hand some are trying to pioneer these experimental changes, while others are scanning the environment and implementing changes that have been successfully implemented elsewhere. In asking ourselves what factors place or don´t place innovation in the forefront of our business strategy, we found that day-to-day operations, other short-term external threats, governance rules, inertia, and organizational culture are some of the obstacles to a stronger approach to innovation. We went deeper into our analysis and found that although we are in a mature stage in the industry, the market is not yet saturated and we have not served all of our client needs therefore we also wondered if the residual growth of the MFIs and past success lower the emphasis on innovation. Some members proposed that purpose and vision should lead our innovation strategy and, through deeper customer knowledge, innovate to deliver integrated personalized solutions at lower cost and through alternative channels. With that in mind we analyzed and discussed a set of frameworks that facilitate navigating and choosing among different kinds of innovation strategies.

Finally, we closed the Yearly Meeting with shared remarks at the amazing learning that happened in the three days of the Yearly Meeting, the group highlighted how the trust, the dynamics and the openness to sharing within the MFN was an example of how it could allow us to learn and innovate faster and more efficiently not only institutionally but also as a sector.

Conclusion

MFN members have been leading actors building the MF industry in the world. As a network we have been witnesses and catalysts of this industry evolution: how it was born, how microfinance business models in different contexts became feasible, how MFIs have been able to grow and transform into large scale financial institutions, how they deal with increasing competition, how they live and prosper in a regulated environment, and how they have transcended from microfinance to financial inclusion.

However, as we look towards the future, the external context presents significant changes that generate great opportunities and challenges for the MFIs that wish to adapt and continue in the lead of this industry. We are trending towards a more connected, digital, and agile world. We believe technology will play a key role in shaping a new paradigm that will determine the new improved solutions that we will offer to our clients. Therefore, MFI´s leaders must balance between pursuing the opportunities still present in the traditional business model with understanding, embracing, and implementing technologies that multiply the impact on our clients at the base of the pyramid.

Moreover, in this more connected and dynamic landscape, there is a constant need to share experiences and develop a worldwide perspective on the critical matters of our industry. As part of the Meeting, members addressed among themselves their challenges in current diverse social and political situations, and in the process appreciated the MFN as a platform that helps them navigate this rapidly changing environment. The overall experience during the three days of sessions made us rediscover the value and uniqueness of this group of leaders that we call the MFN, inspiring us to reassert the commitment that has brought us together since 1993: to solve the financial needs of the people at the bottom of the pyramid. With so much value to create, we look forward to having all members join us next year and share our pursuit in shaping the future of financial inclusion.

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