



E-BANKING WITH THE POOR:

Opportunities and implications for microfinance providers

ISSN 1834-9900

No.1, July 2007

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Summary

Increasingly, microfinance practitioners see ICT innovation as a key strategy in taking the microfinance sector to the next level in terms of outreach and sustainability. We are already seeing innovations such as correspondent banking, card services and mobile phone banking. However, the roll-out of ICT-enabled microfinance is likely to change the business models and methodologies that have been core to the microfinance enterprise, and MFIs will need to respond accordingly. Furthermore, e-banking will also enable commercial banks to do microfinance more profitably, especially in serving the upper strata of the typical microfinance client-group, and this may put significant pressure on the financial viability of specialist MFIs.

Introduction

Over the last three decades, banks in developed economies have transformed their business management and service delivery from paper-based systems to integrated ICT-enabled systems. Consequently, e-commerce has become so ubiquitous that cash is now almost superfluous. Cash is used for only the smallest transactions and even this is poised to be replaced by a micropayments service, where people pay for small items through their mobile phone, or through a value-carrying smart card.

Might the same evolution occur in less developed economies? Increasingly, microfinance practitioners see ICT innovation as a key strategy in taking microfinance to the next level in terms of outreach and sustainability. However, the roll-out of ICT-enabled microfinance is likely to change the methodologies that have been core to the microfinance enterprise, and microfinance institutions (MFIs) will need to respond accordingly. Furthermore, e-banking will enable commercial banks to do microfinance more profitably, especially in serving the upper strata of the typical microfinance client-group, and this may put significant pressure on the financial viability of specialist MFIs.

Microfinance

Microfinance is the provision of relevant and affordable financial services to poor households. The 'micro' prefix refers to the size of the financial transactions; it does not imply that the MFIs themselves are small. Microfinance is primarily concerned with credit and savings although, in recent times, allied services such as insurance, leasing, payment transfers and remittances are being introduced to the mix. In the early days, microfinance was focused on providing working capital to people who generate income for themselves in very small business activities. While this emphasis remains, the sector has broadened its objectives to *the delivery of financial services to poor households so that they can manage their financial resources more effectively.*

Microfinance and ICT innovation

Management information systems

A suitably functional, computerised MIS is prerequisite for a MFI to monitor the quality, sustainability and efficiency of its loan portfolio, to measure development impact, and to manage administration tasks. It is difficult for a MFI to upscale significantly and maintain the accuracy and transparency of its loan portfolio without an MIS that can grow with the institution. These MIS are the most fundamental aspect of a MFI's hi-tech infrastructure. Indeed, ICT innovation for the *delivery* of microfinance services is not possible without an appropriate back-office MIS.

Mobile computing

While the back-office MIS enables the MFI to monitor its loan portfolio, this functionality is undermined if the data analysed by the MIS is not up-to-date or accurate. With dispersed branch offices, paper-based transaction records and manual data entry, there can be a data delay of days or even weeks, and the possibility of introducing errors during the data entry process is high.

A recent innovation that serves to overcome these issues is mobile computing applications – palmtop computers that loan officers take to the field so that transactions can be recorded directly into the MIS, negating the need for intermediary data entry at the branch office. The data entered into the palmtop computers is typically uploaded to the MIS at the end of the day, either directly in the branch office or via a remote communications link. Furthermore, the roll-out of wireless broadband infrastructure will enable these systems to be always online', resulting in true real-time data collection and monitoring of the loan portfolio at branch and institutional levels.

These mobile computing solutions do not alter the operational methodologies employed by the MFI. Therefore, while bringing immediate efficiency and accuracy benefits, they can be implemented with little disruption to on-going operations.

Correspondent banking

Providing services to clients in remote locales is a key challenge for MFIs. These locales include rural areas where the population density is low, the market is smaller and service provision is more expensive. One approach to meeting this challenge is through 'correspondent banking', where a bank links with third-party merchants located in remote areas. Correspondents manage transactions on behalf of the partner institution and are remunerated on a fee-for-service basis.

The key qualities needed of Bank Correspondents are that they are long-term businesses, respected and trusted in their communities. They also need to be 'ICT-enabled'; they will generally be equipped with technology such as an EFTPOS device, barcode readers and/or keypads, a personal computer, etc. They will be linked to the partner institution's servers using a telephone line, cable or satellite link. Typical correspondents include post offices, supermarkets, general stores, gas stations, etc. An example of correspondent banking in Australia is the 'Bank@Post' services offered by Australia Post.

With respect to the regulatory environment, Bank Correspondents must be legally empowered to provide a full range of services for customers, while not neglecting risks of fraud, theft and money laundering. An innovative approach to banking policy and regulation is needed if Bank Correspondents are to achieve their full potential for delivering inclusive financial services.

Card services, EFTPOS and ATMs

There are a number of similarities between microcredit services and consumer credit cards. Like microfinance methodologies, credit cards were introduced to reduce the costs associated with small transaction lending. Common characteristics include unsecured credit, small transactions, and pre-defined credit limits. Other salient features of credit cards, which many microfinance clients would like their providers to duplicate, include on-demand borrowing, a re-draw facility, and repayment flexibility within pre-defined guidelines. We know that microfinance clients desire these features because they continue to utilise local moneylenders for these very services where they are not provided by their MFI.

Given the similarities between credit cards and microcredit services, the concept of a 'microcredit card' arises as a likely innovation. The introduction of card-based services also requires the roll-out of either EFTPOS functionality with third-party merchants and/or Automatic Teller Machines (ATMs).

The delivery of card-based microfinance offers even more opportunities. MFIs can implement microfinance-tuned credit-scoring algorithms, allowing clients who have proven their creditworthiness over time through successful repeat business to have their borrowing limit automatically increased, be given access to additional MFIs can also consider smart card technology as part of their 'microcredit card' solution. Smart cards have an embedded computer chip that can store client and transaction data, as well as process information. Smart cards function as electronic passbooks, thereby reducing reliance on printed receipts. Because all relevant client data is stored on the card, MFIs can utilise EFTPOS systems and ATMs that do not need to be always on-line. This is a significant advantage in areas where telecommunication services are unreliable and/or expensive. Finally, smart cards can be used in conjunction with biometric technologies (such as fingerprint scanners) to enhance the process of client identification, thereby enhancing privacy and data security.

Internet banking

Internet Banking provides clients with real-time information about their accounts, and the ability to transfer funds between their accounts. It is an empowering tool because it gives bank clients the flexibility to manage their financial resources at their own leisure, without having to visit a bank office during opening hours. In particular, it is a vital accompaniment to card-based services, allowing clients to keep track of numerous small electronic transactions.

The main constraint to MFIs implementing Internet Banking is their clients' minimal access to the Internet. In some areas, this constraint is being overcome somewhat with the roll-out of rural telecentre networks.

Mobile phone banking

GSM cellular phones are becoming increasingly accessible and affordable for the poor. The World GSM Association reports that during the years 2003-2006, more than 800 million mobile phones were sold in developing countries. Mobile phones are now not only the preferred means of telecommunication but, in many cases, the only option. Furthermore, the World GSM Association reports that the mobile phone is the first and only communications technology to have more users in developing countries than in developed ones.

GSM phones can become 'mobile wallets' by facilitating electronic payments in exchange for goods and services. This development in m-commerce has been applied to facilitate savings deposits, loan repayments and other funds transfers. For the cost of sending an SMS message, the phone user / microfinance client uses an application stored on his mobile phone to initiate a transfer from his mobile phone account to his bank account. Examples include 'WIZZIT Bank' (www.wizzit.co.za).

Conclusion

Most of the above examples of ICT innovation in microfinance are being trialled or implemented in various MFIs or banks around the world. However, they are yet to become widespread. There is much to learn and more experimentation to take place. Nevertheless, the microfinance sector stands at a junction point, where its business models and processes are going to be challenged by these innovations.

There are many constraints to the roll-out of ICT-enabled microfinance. First, all of the usual digital divide issues apply: ICT regulatory regimes that hinder rather than enable innovation, non-existent or unreliable ICT infrastructure, and the lack of human capacities needed to fully engage with the ICT applications. Second, there are challenges from the microfinance perspective as well: financial sector regulation that restricts innovation in e-banking and m-commerce, technical capacities of MFIs to manage the roll-out of ICT systems, and managerial capacities of MFIs to manage the necessary changes in business processes that will accompany the ICT innovations.

One cautionary observation is that some ICT-enabled services, especially card-based services, tend to individualise the banking process and isolate the client from his/her peers. This conflicts with those group-based methodologies that are held up as the key reason for the high-repayment rates that are typical in the microfinance business. This concern cannot stop the transition to electronic services, but it is something that will need to be monitored.

Some people will say 'it cannot be done in microfinance, electronic banking with the poor will not work'. To this attitude, we can reply with two salient points. First, it *has* to work, because economies and enterprises that have embraced electronic banking and commerce will find it increasingly difficult to do business with those that have not, leaving the latter at a continuing disadvantage. Second, we do well to remember that more than 20 years ago when microfinance was in its infancy, there were many who said 'the poor cannot repay, the poor will not repay, the poor cannot save'. On all counts they have been proven wrong. Perhaps the same will be the case with e-microfinance.