

IBM GLOBAL BUSINESS SERVICES

IBM Microfinance Initiatives

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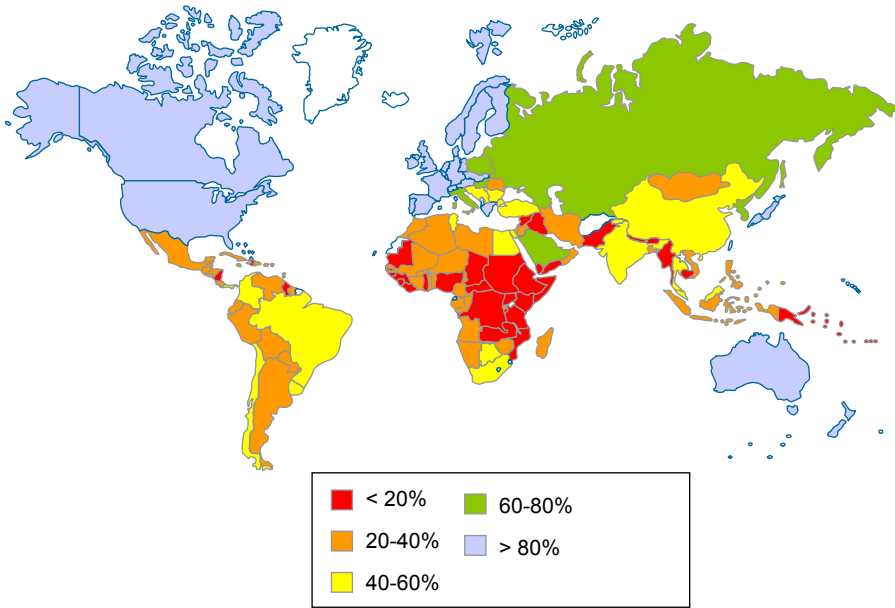
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DISCUSSION DOCUMENT



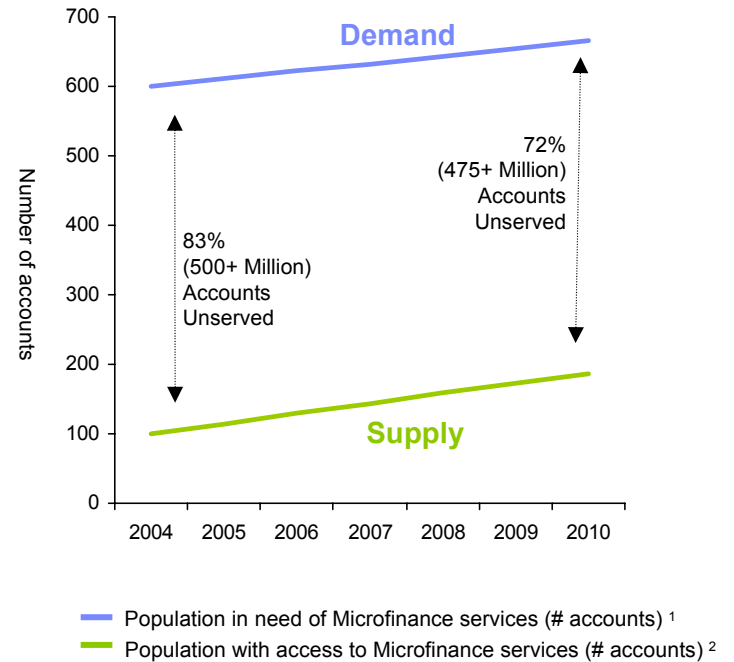
Over 3 billion people live on less than two dollars a day and only 17% of them have access to formal financial services

Households with at least one bank account
2007



Source: Demirguc-Kunt, Beck and Honohan, 2007, Policy Research Report on Access to Finance, World Bank

Supply and demand of Microfinance
Number of accounts, millions



Notes: ¹ Based on CGAP data and population growth rates from the UN Population Division
² Current and forecasted numbers based on Microcredit Summit Campaign data, 2005
 Assumption that 1 Account = 1 Family = 5 People

The traditional financial services business model face several hurdles in serving the “unbanked” segment

Challenges for Traditional Banks

Description

Costs of Distribution

- Low customer profitability does not support cost of traditional banking channels
- High costs of distributing the services to remote locations with low volume

Credit Uncertainty

- The lack of formal credit history of individuals in these markets makes risk assessment difficult; lenders must rely on more qualitative factors and often charge higher interest rates to offset this additional risk

Literacy

- Low literacy rates make traditional tools such as loan applications and bank statements less relevant
- There is a higher burden at the point-of-sale to educate consumers verbally on the various banking products

Physical Security

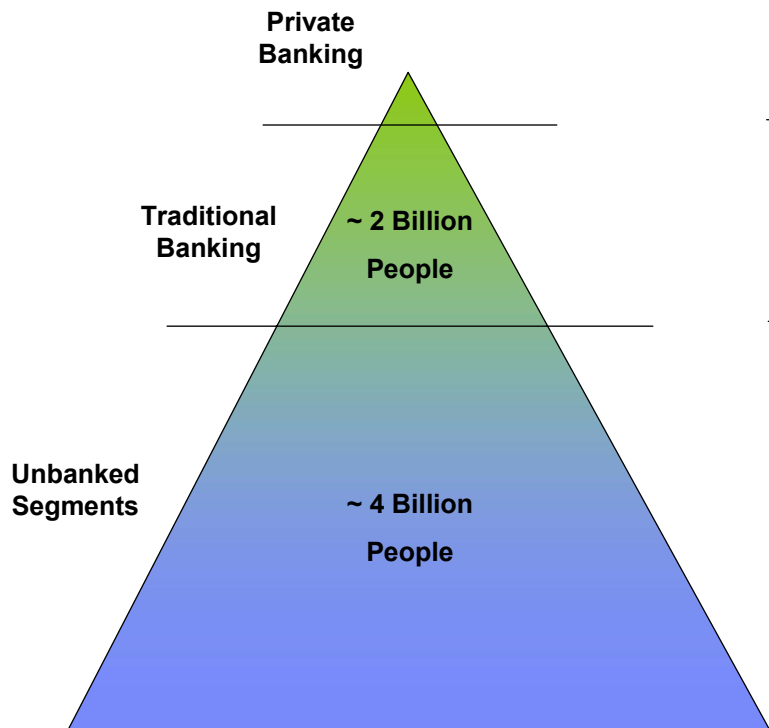
- Remote cash terminals (ATMs, microbranches, etc.) are subject to security issues in certain markets. Successful MFIs business models have established partnerships with ‘safe’ distribution networks

Transparency

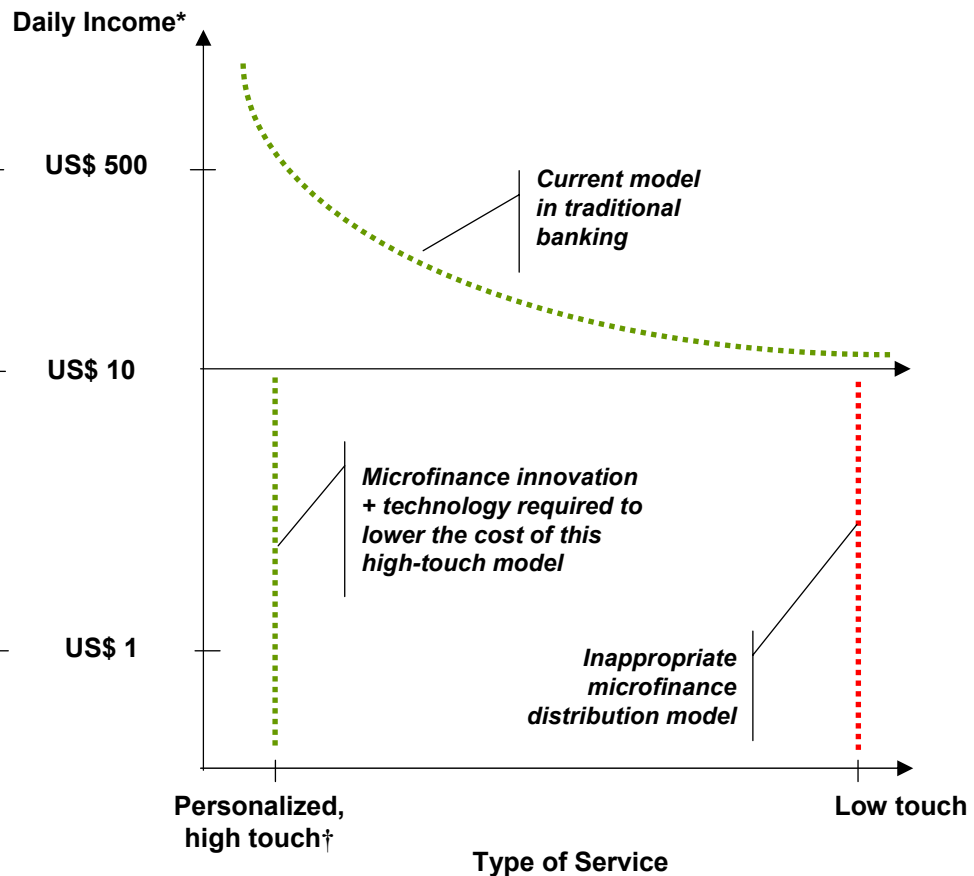
- Lack of transparency into operations of MFIs discourages established financial institutions from using them as distribution channels or limiting the amount of capital they commit to the MFIs

Traditional retail banking models are often inappropriate for efficient microfinance operations

Global Banking Pyramid



Type of Service vs. Daily Income

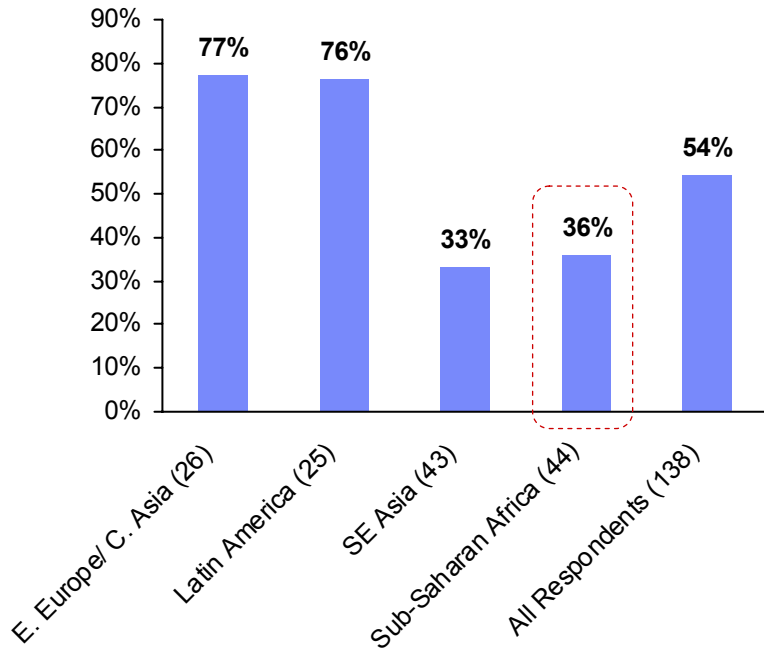


* Log Scale

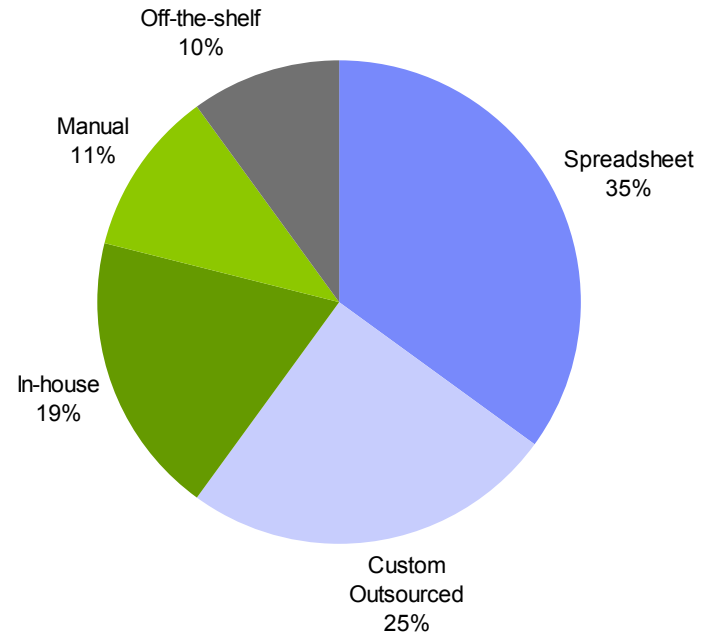
† Service includes origination, management and collection

In the past, the vast majority of microfinance institutions did not have access to appropriate back-office technology

Use of Information Management Systems by Region



Type of Information Management System



Source: CGAP

One reason MFIs have had difficulty finding & using suitable banking software is that their functionality requirements are very different from those of traditional banks

Microfinance Functionality

- Group lending & savings
- Basic life / funeral insurance
- Collection sheets
- Bulk entry of collection sheets
- Custom schedules for loan repayments
- Partner-agency model
- Microfinance reports, surveys, and PPI
- Back dating of transactions
- Enable loan officers to “go to the customer”
- Joint liability rules & enforcement
- Offline capability
- Simple customer communications
- Easy application maintenance via management console

Traditional Retail Banking Functionality

- Individual savings & lending
- Configurable products
- Flexible organization hierarchy
- Role-based user admin
- Loan rescheduling workflows
- Custom fees & interest calculations
- Securities
- Mutual funds
- Trade finance
- Foreign exchange
- General ledger
- 360 customer view & cross sell
- Guarantees
- Leasing
- Syndicated loans
- Bill pay
- Contact log
- ATM / POS
- Credit cards
- High-volume transaction processing capability
- Brokerage
- Custody
- Market positions
- Cash management
- Mortgages
- Order book
- Settlement
- Product catalog
- Capital markets
- Money market
- Swaps
- Futures / options
- Bonds
- Application integration



Our analysis indicates that leading core banking ISV solutions may not effectively address key functional and technical needs of the microfinance industry

In summary, today's established banks often find it difficult to efficiently reach the poor, while MFIs often have challenges in scaling up and reducing costs with volume

Established Banks

- Expensive network of branches, ATMs, and call centers
- Internet banking not easily used by the unbanked
- Cannot serve illiterate customers
- Inflexible and expensive IT systems
- Rigid credit management & collection philosophies don't leverage group / social lending practices
- Traditional scoring systems depend on quantitative credit history

Underbanked/Rural Segment

Established Banks

- Inflexible back office (45% of MFIs using paper or spreadsheets)
- Larger MFIs use traditional applications that are expensive and lack full support for key microfinance functionality
- Banking regulations very challenging

Microfinance Institutions




Innovative distribution including mobile branches and group lending

Underbanked/Rural Segment





The Microfinance Processing Hub provides a shared technology platform for MFIs that helps reduce costs, scale rapidly, and get access to reliable and secure banking software

CURRENT SITUATION




MFIs with no MIS 46%

	Loan officers
	Pen/paper or spreadsheet loan tracking
	Managers & analysts trying to manually calculate reports & performance data

MFIs with in-house or custom MIS 44%

	Loan officers
	Branch workstations
	Networking Servers, databases IT Staff
	Software developers

MFIs with off-the-shelf / package MIS 10%

	Loan officers
	Branch workstations
	Networking Servers, databases IT Staff




\$ for license + maintenance →  Software developers *Local software shop*

MICROFINANCE PROCESSING HUB





All banking functions are available via web browser on a basic PC

Outsourced MIS

	Loan officers
	Branch workstations
	Internet access to data center

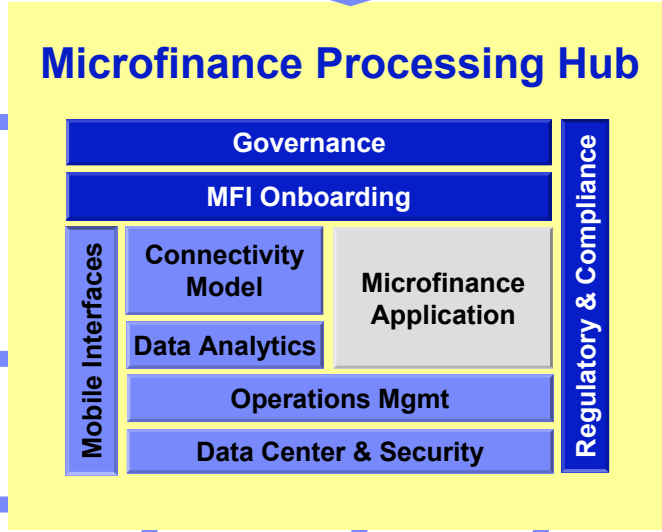
\$ for services used → Processing Hub data center (serves 100s of MFIs)

	Software developers
	IT staff

- Pay-per-use arrangement, with low startup costs and easy scale-up as MFI grows
- Easier reporting & compliance
- Robust technology and security
- Ready access to rich features and new products

Finally, the Processing Hub helps MFIs electronically link with other key players from across the financial industry to drive a more efficient and vibrant economy

Microfinance Institutions



Int'l Payment Networks
 IBM can negotiate cost-effective deals with payment or ATM networks, giving MFIs global payments capabilities

Regulators
 The Hub delivers automated, accurate, and transparent regulatory reporting & compliance

Smartcard / POS Vendors
 ATM or debit cards, payment terminals, and transaction routing

Credit Bureaus
 The Hub can read from, and provide data back to, credit bureaus. This helps end customers establish an identity and get larger and cheaper loans over time

Telcos
 The Hub can integrate with one or more telcos offering mobile banking, allowing customers to repay loans or transfer money on their cell phone

Established Banks

1. Lend funds to MFIs at commercial rates. MFI performance reports available thru the Hub.
2. Sell products through the Hub, leveraging MFIs as distribution networks
3. Banks can also use online banking software of the Hub to expand into MF activities themselves

NGOs / Donors
 Greater transparency from MFIs, accurate & custom reports, and electronic funds transfer

Based on our previous projects in India and Latin America, IBM is currently establishing Microfinance Processing Hubs in five regions around the world



Latin America

Working with multilateral organizations and associations of MFIs to establish a 14 million account processing hub to serve the MF market of the region

Africa

Working with CARE International to jointly establish hub to serve 10+ countries in the Sub-Saharan region

China

In conversations with global and local banks to establish a shared back office infrastructure for the rural/low income segment

Russia

Working with IBM Russia as the Kremlin announced its decision to use the country's post office network to deliver financial services to Russia's unbanked

Indonesia

Signed an agreement with the government agency promoting the development of MF to jointly establish a Microfinance Processing Hub

CARE International and IBM have partnered together to build a Hub called the “Africa Financial Grid” to help address poverty and promote development across Africa

CARE International

- MFI relationships
- Operational experience and presence in Africa (21 offices)
- Marketing and branding
- Government and regulatory insights and expertise
- Risk capital
- MFI capacity building & training

IBM

- Solution design & software selection
- Data center setup & operations mgmt
- Experience & assets from running Microfinance Hubs in other regions
- Security, governance
- Connectivity model
- MFI onboarding
- Regulatory compliance & reporting



A collaboration between CARE and IBM contains the needed elements of technology, operational expertise, risk capital, local knowledge, as well as a shared long term vision to help eradicate poverty through Microfinance

IBM has also partnered with Grameen Foundation USA to help accelerate the development of Mifos, their open source microfinance banking application

Objective

Provide MFIs with a world-class, scalable, easy-to-use MIS that is low-cost but flexible enough to handle varying business requirements

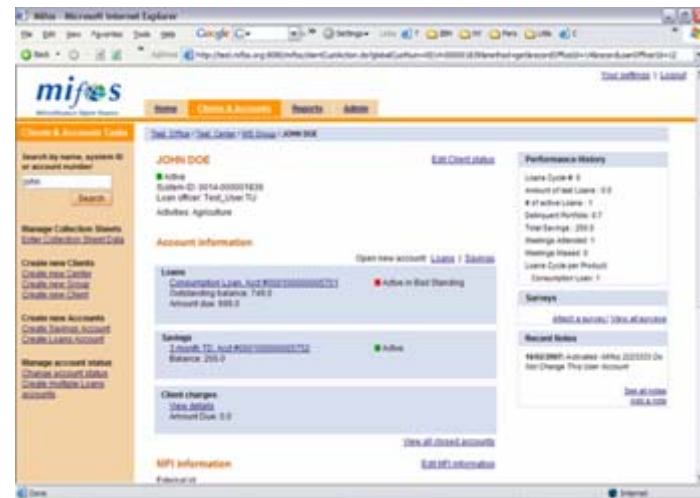
Mifos Background

Mifos is an open source & free banking software application sponsored by the Grameen Foundation USA. Mifos is installed in a number of MFIs around the world, the largest being Grameen Koota in India with over 100,000 clients

IBM Role

IBM is developing core pieces of functionality and improving the architecture, security, and stability of the application

15 FTEs in Dublin, India, New York, and Spain engaged in the project



Mifos 'single view of customer' page



Basic branch workstation running Mifos, with battery backup



Weekly payments meeting for a large lending group



A crafts business funded by Grameen Koota