Business Model Innovation: Supporting Scaling Up Microfinance

Elaine L. Edgcomb, FIELD at the Aspen Institute
Ginger McNally, National Federation of Community Development Credit Unions
Session Goal and Objectives

Goal:
Identify opportunities to improve microfinance business models to achieve greater effectiveness, efficiency and scale.

Objectives:
- Examine the role of business model innovation in microfinance survival and growth
- Explore issues of pricing, structure and sustainability
- Consider ways to increase an organization’s “innovation IQ”
- Identify opportunities for continued technical assistance
Getting Started

• Your organization
  - CDFI type: loan fund, credit union, bank, hybrid structure
  - Loan portfolio: Under $5MM, between $5MM-$25MM, over $25MM

• Your role in your organization
  - Senior management (CEO, COO, CFO, Director of Lending, Director of Programs)
  - Mid management (administration, finance, lending, programs)
  - Volunteer (Board member, Committee member, other)
Agenda

• How can a business model support scaling up microfinance?
  - What is a business model?
  - What is scale?
  - What is microfinance?
• Creative destruction and continual innovation
• Business model canvas
  - Using the business model canvas tool in your organization
• Case studies & discussion
• Nurturing innovation in your organization
• Opportunities for collaboration and strategic partnership
Shared Definitions: Business Model

How can a **business model** support scaling up microfinance?

“A **business model describes the rationale of how an organization creates, delivers and captures value”**

Shared Definitions: Scale

How can a business model support scaling up microfinance?

The goal of scale is reaching large numbers of people...Scale is a significant leap forward, a transformative change.

Shared Definitions: Microfinance

How can a business model support scaling up microfinance?

• **Financial products for low-income/low-wealth clients:**
  - Small loans – business, consumer, credit building
  - Small savings products
  - Affordable transactional products

• **Often combined with:**
  - Financial education, IDAs, and other income generation and asset development programs
Business Models and Scaling Up Microfinance

• Every business – small or large – has an implicit or explicit business model
  - Customers, value proposition, infrastructure, costs & revenues

• Every CDFI has a business model, too, in the way it:
  - Creates value for its clients
  - Creates a sustainable revenue and cost structure for the organization
Business Models and Scaling Up Microfinance (continued)

• In order for a CDFI to scale up its microfinance activities, the components of its business model need to be consistent in focus:
  - Customers
  - Value proposition
  - Infrastructure
  - Cost/revenue structure

• Every organization’s business model is different
  - No “one size fits all” or cookie cutter approach
Developing business model innovation is a process. A fact in the corporate world. A fact in the microfinance world.
Consider...

Change in Microenterprise Development Organizations 2002-2008

359

Out of Business

2002

2008

U.S. Microenterprise Census
The Trend Continues...

Change in Microenterprise Development Organizations 2008-2010

New Organizations: 45

Out of Business: -16

U.S. Microenterprise Census
In Credit Unions too…

Change in number of Credit Unions from 1969 to June 2011

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of Credit Unions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1969</td>
<td>23,866</td>
</tr>
<tr>
<td>2011</td>
<td>7,380</td>
</tr>
</tbody>
</table>

Thriving depends on continual business model innovation
A Practical Tool to Support Innovation: The Business Model Canvas
How to Use the Business Model Canvas

1. Plot the canvas on a poster
2. Put the poster on the wall
3. Sketch out your business model
Business Model Canvas

- **Partners**
- **Activities**
- **Resources**
- **Channels**
- **Relationships**
- **Segments**
- **Value Proposition**
- **Offer**
- **Costs**
- **Revenues**
- **Infrastructure**
- **Customer**

**Financial Viability**

- **Profit**
Business Model Canvas: Box 1: The Customer

- **Segments**
  - Who are we creating value for?
  - Who are our most important customers?

- **Customer Relationships**
  - What kind of relationship is most important to our customers and how do we develop that?

- **Channels**
  - How do our customers want to use our services?
  - How do our customer want us to reach them?
Business Model Canvas: Box 2: The Offer

• **Value Proposition**
  – What distinguishes us in the marketplace?
  – What key resources do we require to maximize our competitive advantage?
  – What are we doing now that is **not** consistent with our core value proposition?
Business Model Canvas: Box 3: The Infrastructure

• Key Activities
  - What are our key lending activities?
  - Our key savings, financial services, or programmatic activities?

• Key Resources
  - What kind of financial and nonfinancial resources are required to make our key activities successful?

• Key Partners
  – Who are we working with or might we work with to strengthen our scope, sustainability, and impact?
Business Model Canvas: Financial Viability
Box 4: The Cost/Revenue Structure

• Cost Structure
  – What are the most important costs inherent in our business model? (Key Resources? Key Activities?)
  – What would need to change to scale up our microfinance focus?

• Revenue Structure
  - What are our customers really willing to pay for? (How do we know this?)
  - Does this match what we are charging for our products and services?
Small Table Discussion

• Describe your organization’s business model
• Pick one of the key components of your organization’s business model and describe how it helps or hinders scaling microfinance
  - Your customer
  - Your offer/value proposition
  - Your infrastructure
  - Your cost and revenue structure/financial viability
Applying the Concepts: Two Case Studies
Part of a national nonprofit with multiple affiliated institutions
- Two credit unions (national and state)
- A higher-risk loan fund for small business and affordable housing
- Nonprofit focused on research and advocacy
- Nonprofit dedicated to fund development

Formed Self-Help Federal Credit Union in response to foreclosure crisis in California
- Completed multiple mergers with CDCUs in California
- Tested and expanded Micro Branch model
Self-Help Federal Credit Union Business Model

VALUE PROPOSITION
Bring unbanked into financial mainstream

RELATIONSHIPS

CLIENTS
Very low-income, pre-bankable
Low-income, under served

CHANNELS
Purchase check-cashing outlets

REVENUE STREAMS
Check cashing fee income

COST CENTRES

KEY RESOURCES

***

KEY ACTIVITIES
In-line financial education

KEY PARTNER
Progreso Financiero: Overview

• For-profit CDFI launched in 2005
• Providing consumer and business microfinance for a largely immigrant, Latino market
  – Through retail sales points in Latino supermarkets and other outlets
  – Disbursing small dollar loans on prepaid cards and helping clients build credit by reporting borrower performance to credit bureaus
• Emphasizing speed, efficiency, scale, and return
Progreso Financiero Business Model

**KEY PARTNER**
- Quantitative scoring model

**KEY ACTIVITIES**
- Offer SDL quickly and cheaply
- Offer prepaid card

**VALUE PROPOSITION**
- In-store kiosks and stand-alone branches

**RELATIONSHIPS**
- Unbanked Latinos needing SDL

**CHANNELS**
- 36% APR fully loaded

**KEY RESOURCES**

**CLIENTS**
Fostering Business Model Innovation in Your Organization
Increasing Your Organization’s Innovation IQ

An organization’s capacity for innovation can be increased.

Case examples demonstrate that:

• Innovation is ongoing and iterative
• Organizations go through multiple stages of development
• Focus can be on both big ideas and in-depth process improvements
• External models and internal assessment are sources of inspiration
Increasing an Organization's Capacity for Innovation

- Intentionally support innovation
- Seek out multiple perspectives
- Explore many ideas
- Develop a theory and test it
- Tolerate and learn from failures
Innovative Thinking in Action: Market Research

Analyze market channels

- Are there sectors we could be reaching?
- Clusters of potential clients served by distribution points we can tap?

Listening to the market

- What does market research tell us about customer needs, demands, preferences?
- What does informal listening and market scanning tell us?
Innovative Thinking in Action: Mining the Data

• Where do your customers come from?
• How do you hear about them?
• Where do they drop off in your lending or business development services process?
• What do they complain about?
• Where are the “speed bumps” or potential crisis points in your process?
• Who best fits your program services?
Innovative Thinking in Action: Listening to Staff

• What’s the biggest avoidable headache our clients endure?

• In what ways is our efficiency bogged down by policies worth examining?

• What’s changed in our operating environment since we last redesigned our processes?
Opportunities for Collaboration and Strategic Partnership

• Back office operations and platforms
  - Accion Texas’s Microloan Management System

• Product development
  - Opportunity Fund’s Easy Pay Loan

• Market segmentation and deal referrals
  - Santa Barbara Bank and Trust’s revised loan application and referral process to Cal Coastal

• Areas for future exploration
  - Liquidity management
Examples of Collaboration

• Credit Unions and 501(c)3 nonprofits
  - Santa Cruz Community Credit Union and Santa Cruz Community Ventures (Child Care and Individual Development Accounts)

• Loan Funds and Credit Unions
  - The Support Center and Generations Credit Union (Business Loan Underwriting)

• Loan Funds and Loan Funds
  - The Reinvestment Fund and the Low-Income Investment Fund (Child Care and Charter Schools)
More Examples of Collaboration

• Mainstream Credit Unions and CDCUs
  - The Bridge Project (Formal and Informal Financial Education)

• CDFIs and Educational Institutions
  - The Reinvestment Fund and La Salle University (Improving Access to Healthy Food)
  - IFF and University of Chicago (Increasing Child Care and Education Options)
Small Table Discussion

• What types of partnership or strategic collaboration does your organization participate in?

• Are there collaborations that might help your organization scale its microfinance activities?
Additional Resources

• Business model canvas
  - Business Model Generation by Osterwalder and Pigneur

• Innovation
  - Permanent Innovation by Langdon Morris

• Collaborations
  - “Partnerships for Community Impact: Higher Education and CDFIs Working Together” by OFN
Additional Resources (continued)

• Comparison of international and U.S. microfinance activities
  - For-profit and nonprofit structures
  - Mobile/remote solutions
  - Niche financing
  - Leveraging intellectual capital