

Donors as Silent Partners in MFI Product Development: *MicroSave-Africa* and the Equity Building Society in Kenya

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This case study describes how donors successfully supported MFI product development. Initiated by Swisscontact (a nongovernmental organization), led by Micro-Save Africa (a donor-funded project providing product development services), and supported by DFID, EU, UNDP, and AfriCap, Equity Building Society's product development capacity has grown rapidly.

Overview

By December 2002, Equity Building Society (EBS) emerged as one of Kenya's leading microfinance institutions, with over 155,000 savings clients and 41,000 borrowers. Although once insolvent, EBS transformed itself into a profitable financial-service provider by rigorously focusing on the needs of its clients—in particular, by developing a wide range of market-based financial products and services.

Strong technical training laid the groundwork for EBS's strategy of customer-oriented product development. The NGO Swisscontact awarded EBS an initial grant of US\$150,000, with which it hired *MicroSave-Africa* in October 2001 to intensely train EBS's staff in product development. Applying what it learned, the staff embarked on a systematic program of product development, tailored to the needs of its clientele. The resulting popular products have effectively reduced EBS's client drop-out rates, attracted new clients, and expanded its outreach. The transformation from a product-led to market-led institution has also improved EBS's institutional stability and financial sustainability.

Setting the Stage

EBS was established in 1984 as a registered building society, and was insolvent within a decade. In a 1993 institutional rating of EBS, the Central Bank of Kenya noted inadequate board and management supervision, as well as unsatisfactory asset quality. EBS's capital had become fully eroded by accumulated losses, and its deposits were being used to meet daily operating expenses. Time had come to turn the institution around and refocus its mission.

EBS Changed by Focusing on Clients

"MicroSave-Africa helped us to discover that our products did not meet our clients' needs. [It also] helped us identify competitors, make charges transparent and provide information for clients on our products, repayment schedules and statements. We worked with MicroSave-Africa on financial modeling, product design, costing and pricing....

"Our savings clients increased from 61,000 in 2000 to 155,000 in 2002, and as of June 30, 2003, we [had] over 182,000 deposit accounts."

James Mwangi, Finance & Operations Director, EBS

Central to the effort was the strong leadership of CEO John Mwangi, and Finance and Operations Director James Mwangi. They redirected EBS's mission to focus, for the first time, on microfinance clients. EBS evolved from a building society dedicated to financing mortgages, to a financial institution committed to providing a variety of flexible and responsive financial services to low-income clients.

In 1999, EBS started to work with international partners—initially with the Micro-Enterprise Support Programme (MESP) of the European Union (EU) and the MicroStart program of the United Nations Development Programme (UNDP). Partnerships with Swisscontact and *MicroSave-Africa* (a donor-funded provider of product development services) followed in 2001. More recently, EBS has established partnerships with the UK Department for International Development (DFID) and the AfriCap Microfinance Fund (AfriCap).

Building Product-Development Capacity

In October 2001, Swisscontact contracted *MicroSave-Africa* to train the staff of EBS in microfinance market research. According to Ralph Engleman of Swisscontact in Nairobi, one of Swisscontact's goals was to help EBS refine its product portfolio. Together, they decided *MicroSave-Africa* was the region's best technical-service provider. Some 26 EBS staff members, including Finance and Operations Director Mwangi, attended the market-research and fieldwork training in product development. The goal was to build EBS's internal capacity to refine and develop its products.

After the training, EBS established a product development team of seven staff members. Their commitment during training convinced *MicroSave-Africa* to enroll EBS as an Action Research Partner (ARP). *MicroSave-Africa*, with funding from various donors, provides its ARPs with additional technical services free of charge. EBS itself is covering its other program-related expenses.

As an ARP, EBS agreed to:

- commit senior-management time to the program
- nominate a "product champion" to supervise and guide its action-research program
- provide reports on the progress it was making on an agreed work plan every two months

In return, *MicroSave-Africa* agreed to assist EBS in:

- developing a process by which it could cost products
- providing quality control for an EBS study, which also looked at its success factors and problem areas
- reviewing its portfolio of products against client demand
- creating and adopting new products through a systematic product development process

To accomplish these commitments, *MicroSave-Africa* provided EBS with further training, specifically in:

- product-development market research
- pilot tests of products
- product monitoring and final evaluation

The results were striking. EBS's Research and Product Development department became more effective and productive, launching new efforts to:

- cost new products

- refine existing products
- develop and improve its operating systems

The improvements in EBS's product development led to even more fundamental changes in how it does business. In particular, a recent focus on strategic marketing is proving extremely useful in increasing its market share, enhancing operational efficiency and maximizing the return on its assets.

As of December 2002, the audited financial statements of EBS showed a profitable institution with over 155,000 depositors, using five different savings products. Deposits were valued at approximately US\$ 27.5 million (2.1 billion Kenyan shillings), and its loan portfolio at approximately US\$ 14.4 million (1.1 billion Kenyan shillings). Outstanding loans from EBS were held by 41,000 borrowers. By June 2003, these numbers jumped to 180,000 depositors and 56,000 borrowers, who were served by 12 branches and 24 mobile units. The institution had 2,469 shareholders, 256 staff members, and 8 directors.



Mundoro Mobile Banking Unit, Thika Branch, April 3, 2003. Photograph by George Maina, courtesy of EBS.

In early 2003, external funding to EBS began to be coordinated through a steering committee of EBS's funders (donors and investors) and *MicroSave-Africa*. External funding (from Swisscontact, DFID, EU, and AfriCap) has concentrated on capacity building and (from UNDP) on systems development. This method of managing its funding has helped increase the efficiency of all EBS's programs.

What Factors Led to Success?

1. Donors left product development to the managers of EBS. Donor involvement in product development at EBS has focused exclusively on helping it obtain quality training and other technical assistance. Actual product development and delivery are left to EBS management. Donors also do not push EBS to offer products and services or work in new regions before it is ready. “EBS is in the driver’s seat,” observes *MicroSave-Africa* Director Graham Wright.

Donors Appreciate the Approach of *MicroSave-Africa*

“The long-term viability of MFIs, as with all businesses, depends on the wider environment in which they operate—not just on the level of the legal and regulatory framework but also on more sector-specific information, business services and resources. *MicroSave*, with DFID’s support, is addressing a critical gap in the sectoral support infrastructure needed to build a client-driven industry. Its research, development and support work addresses the practical business needs of MFIs looking to take a market-driven approach...”

Dr. David Ferrand of the DFID office in Nairobi

2. Product design is driven by client demand. The poor are not homogeneous. Therefore, the challenge is to develop a variety of flexible financial services to meet the diverse needs of the poor—that is, with terms suitable to client cash flow. Such tailored products offer the poor the most help in managing the risks they face in their daily lives.

3. EBS put the basic institutional capacity in place needed to embark on product development. The commitment of the EBS board and management ensured that adequate staff and systems were allocated to the product development process. Moreover, management understood the capacity issue and realized it would need additional staff and systems to implement changes. The early assignment of a “product champion” was a crucial part of the additional staff.

4. EBS followed a systematic product development process. The methodology of *MicroSave-Africa* helped EBS avoid common pitfalls, such as higher-than-anticipated setup costs, products with limited demand, and a staff insufficiently trained to market and deliver new products. Most important, they avoided product proliferation. EBS and *MicroSave-Africa* chose a

strategy to reprice and repackage existing products before embarking on the development of new ones.

Benefits of Product Development for EBS

EBS is already reaping the benefits of its product development. These include increased staff satisfaction, customer loyalty, developmental impact, and profitability.

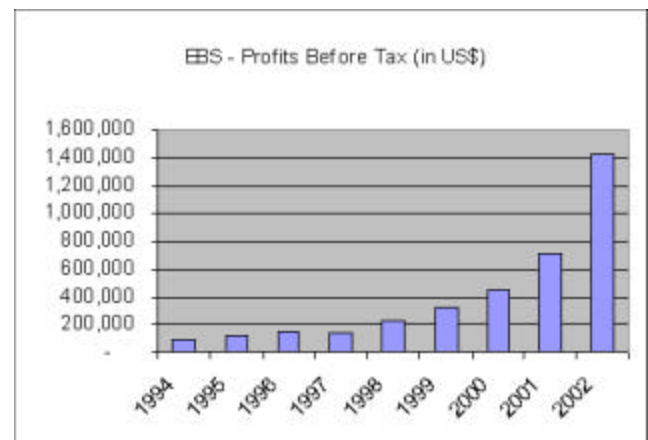
Stability. EBS’s new, wider range of products have proven highly popular among clients. Consequently, EBS enjoys greater client retention, increased new-client numbers, improved outreach and higher long-term sustainability.

Efficiency and productivity. EBS’s new training and client focus has improved its management’s view of costs and cost control, which has resulted in increased efficiency and productivity. EBS management has also:

- established performance benchmarks for individuals, branches and the institution as a whole
- focused staff evaluation on rewarding performance
- set up a new organizational structure that has steered EBS through its client-focus transition and will lead it into the future.

Profitability. EBS responded to market and field research by revising its price structure by:

- decreasing its interest rate on fixed deposits and simultaneously matched competing rate, making the product profitable.
- revising the structure and marketing of its loans.
- tracking its interest-rate margin on a weekly basis.
- adjusting its account chart to reflect income and costs on a product-by-product basis.



Source: EBS, Audited Annual Reports and Accounts

These changes produced a 35% increase in deposits and a 47% increase in loans in just one year. Together with other capacity-building measures, they resulted in a remarkable 104% increase in pretax, year-over-year profits in 2002, even though total assets only increased by 37% for the same period.

Benefits of Product Development for EBS Clients

Wider variety and flexibility of products: EBS now offers a diversified product menu tailored to client needs. For example, its Jijenge (meaning “build yourself”) product is an increasingly popular, contractual savings plan. It allows a customer to commit to save a specific amount of money within a certain period for a specific purpose, such as school fees or business expansion. The client, not EBS, determines both the amount and the timeframe.

EBS PRODUCT MENU

Savings

Ordinary Savings Account
Business Savings Account
Super Junior Investment Account
Jijenge Account
Call and Fixed Deposits

Loans

Education Loans
Business Loans
Medical Loans
Development Loans
Salary Advance
Farm Input Advance
SAKO Plus Loan (pilot)

Clear product terms: Market research made EBS realize it needed to remedy the misperception that its loan prices were too high. This was largely because EBS stated its rates on an annual, declining-balance basis, while its competition used a

flat, monthly interest rate on the original balance. Consequently, EBS’s rates, which were actually lower, appeared higher. The remedy was that EBS began using “client language,” printed brochures outlining product changes, and prominently advertised its fees.

Improved access. EBS’ commitment to its customers is evident in its expanded operating hours. No longer following traditional banking hours (9:00– 15:00), it opens at 8:30 and closes at 16:00.

Conclusion

While product development is not an obvious donor activity, EBS’s experience illuminates some important lessons for donors looking to support such efforts by MFIs. It is vital for a donor, as a “silent partner,” to:

- Help identify and connect the client institution to quality technical expertise
- Look for partners that explicitly seek feedback from clients when designing products
- Support the organizational changes necessary for market-led product development, such as staff training and information systems improvements
- Initiate and encourage information exchange between financial institutions and donors to maximize the replication of successful product development efforts
- Take a patient, long-term approach to funding that rewards institutional performance and outreach
- Recognize that refining or introducing new products is a complex process that takes time

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