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Market Research for Microfinance: Detecting the Needs Beyond the Numbers

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We have talked this morning about financial viability, governance and transformation. The focus was on the supply side of the equation—the parameters for the successful delivery of microfinance services. My theme for this afternoon is 'market research for microfinance: detecting the needs beyond the numbers.' I doubt that would have appeared on the agenda of a microfinance conference two years ago. Yet it is a 'hot topic' in microfinance today, together with the mantra of 'flexible and more diverse products.'

Market research for microfinance takes us across what often seems like a big divide, to the demand side of the equation: who is buying the MFI's services and what do they want? It is only recently that many in the industry have acknowledged that in the end, success depends on not just getting people in the front door but keeping them there with products that make sense for them. Obvious, yes, but long ignored. What I want to do today is to challenge you to revisit microfinance from a client's perspective, with an eye to delivering microfinance services in a way that is more appropriate to the client. Let me also suggest that if MFIs don't get the product line right, sustainability will be hard to achieve.

My presentation this afternoon touches on four issues:

1. The reasons for the emergence of a more market-led microfinance agenda.
2. Key questions for understanding clients.
3. Using market research to understand the nexus between:
    a. clients and products,
    b. clients and institutions, and
    c. clients and markets.
4. The tools for and costs of conducting market research.

Background

Before exploring the value of bringing the client towards the center of the microfinance discourse, let us take a minute to consider '**why**' there is a growing interest in market research, or put more broadly, a shift to market-led microfinance. This has not occurred in isolation but is the consequence of changes in the industry at large and a response to common problems experienced by MFIs in many countries. It is integral to the growing trend towards a more market-led or client-focused agenda for microfinance.

Until now, the MF industry has been largely product-led. Clients were seen as a given; most MFIs, backed by donor money, assumed that if they opened their doors clients would come flocking in. At first this is often the case, but over time the rate of new entrants slows down. There was also a cookie cutter view of products. Short-term working capital loans were dominant because they were assumed to be the product of choice. The results were competitive markets with little product differentiation, as are typical in Bangladesh, Morocco and Uganda. The diversification of the product market now visible in Bolivia, Kenya, as well as Uganda, is a much more recent phenomenon.

The method of service delivery prescribed by the new world of microfinance has primarily been solidarity group lending or village banking. Only few MFIs have offered individual loans from the beginning. Under this donor or product-led industry model the prevailing product norm was 'one size fits all.' Adherence to this paradigm made the microfinance sector one of the few remaining product-driven businesses in the world.

The impetus to move away from this product-led focus towards a more market-led or client-driven agenda has come from several directions:

- Increasing competition among microfinance service providers of all sorts is growing (NGO, banks, finance companies). In the absence of product differentiation and given small loans sizes, clients tend to jump from one lender to another as household cash demands arise. They may also borrow from multiple lenders because the level of credit is too small relative to the need. Service providers were shocked by what they viewed as a lack of loyalty which they believed was implicit in the social contract and trust that underlies much microfinance lending.
- There has been a growing awareness among many MFI's of the fallacy that they were the only game in town. In many markets this is clearly no longer the case because of competition, but I doubt that it was ever true. For most clients,

microfinance was never the only source of credit. Money lenders, partner groups and other informal finance organizations have always played a role and continue to do so.

- Drop out rates that are higher than desirable. (see Table 1)

<u>Table 1</u>: Some numbers……..

- Average number of loan-cycles before lending is profitable in Latin America: 4-5 (Brand and Gershick, 2000)
- Typical drop-out rates:
  - Bangladesh: 5-10% pa (Wright, 2000)
  - East Africa: 30-60% pa (Hulme, 1999)
  - South Africa (Northern Province): 35-50% (Stark et al., 2003)

Source: Graham Wright

We have come to a point where the industry has matured and many MFI's are realizing that they need to become more business-like if they are to grow. To raise attraction and retention rates, many MFI's have concluded that they will need to deliver products and services that are responsive to their client needs. They will also need to recognize market opportunities and develop strategies to take advantage of these possibilities. Growing a loan portfolio with existing customers needs to be more than simply larger loan sizes at prescribed intervals; it must also meet the challenges of providing access to a broader range of financial services.

Being more responsive to clients requires understanding one's market: who is the formal and informal competition? This means determining more precisely an institution's market niche, not simply identifying it as 'unbanked' in the broadest sense, but also identifying segments of this ‘unbanked’ market. In addition, we may need to be clearer about what ‘unbanked’ means. Are people who receive ‘remittances through the banking or postal system’ really ‘unbanked’?

In retailing, the customer matters. They are the key to staying in business. This means listening to one’s clients and ensuring that the institution serves them to the best of its ability. Until now this has not been so. Clients were viewed primarily as simple statistics reflecting the institution’s outreach, the percent repeat customers or number of active savers. To change this, we need to move beyond the numbers and let the clients’ voices be heard. Thus, we need to undertake market research.

Many MFIs no longer have a choice about whether or not to conduct market research—it is critical to their survival. This point hit home for me at a meeting in Moscow 10 days ago. As I talked with the staff of MFIs in Bosnia Herzegovina, it was clear that their market was so competitive that they were compelled to use market research to identify the niches where each feels it can have a comparative advantage in the market.

The entry point for understanding clients, for ‘getting the product right, getting the service delivery mechanisms right and increasing one’s market share’ is summarized in three fairly simple questions. They are:

- Who do microfinance institutions reach and who do they not reach?
- How do the poor use financial services and what are the implications for our existing and potential products?

- How do we increase the poor's access to financial services to better serve their needs?

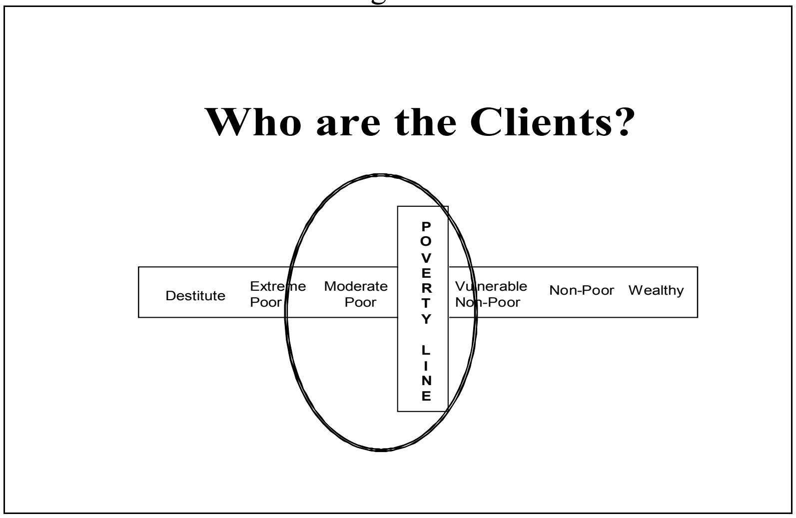
The answers not only inform the emerging market-driven microfinance agenda but also suggest ways to increase the scale and depth of outreach. By providing more appropriate products and services, MFIs should be able to attract and retain more clients and thereby expand the effective delivery of services to as broad a spectrum of poor people as possible. This includes those that:

- drop out because of the inappropriateness of what is on offer;
- are excluded because they live in areas that lack access to microfinance services of any type, possibly because they are too remote areas or are perceived as too poor;
- are deemed high risk clients by MFIs; and
- choose to self exclude.

These questions have been on the table for a while, so let me share with you what we have learned.

Take the first. Who do we reach? Drawing on data from about 50 countries we can argue that the majority of MF clients belong to the narrow band defined by this oval (see Figure 1).

Figure 1



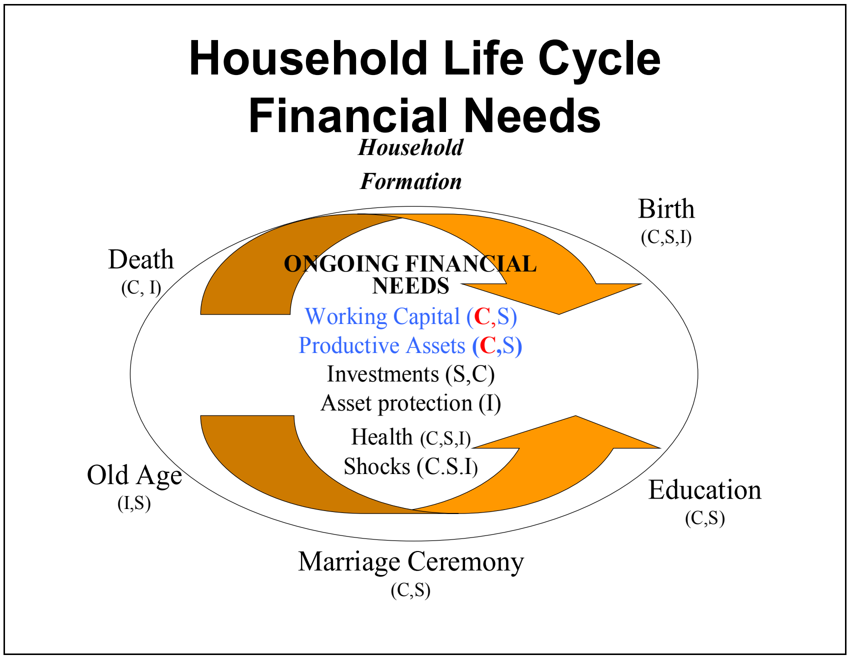
- Most clients are the moderate poor and vulnerable non-poor.
- The extreme poor are largely excluded.
- Programs reach a range of clients, but targeted programs include more extreme poor.
- The destitute are outside the reach of microfinance programs.
- Better off vulnerable non-poor and lucrative 'unbanked' are excluded by attempts to target the provision of services.

Since the renewed interest in clients over the last few years, we have learned a great deal about how clients use financial services. The needs of poor people are diverse. Broadly we find that microfinance, and predominantly credit, is used by poor households to generate income, to accumulate assets and to manage the ever present risks that can rapidly deplete their hard-won gains in assets and income.

We also know that:

- Microenterprise development is only one use of microfinance. Clients use loans to mitigate risk, invest in an array of social, financial, physical and human assets, such as home improvements or education, and to take advantage of opportunities as they present themselves. Many are uses which might be better met with more appropriate or finely tuned products.
- Vulnerability and risk are key organizing principles for clients. Together with growth objectives such as stabilizing and increasing income and building assets, they are the basis by which clients assess the value of the financial services on offer.
- Sources of risk can be structural, can be unanticipated crises such as sickness or death, and can be high cost life cycle events such as marriages, funerals or educating children.
- The 'average' product does not always respond to the client's reality, in which the need for and the use of financial services changes over time (see Figure 2).

Figure 2

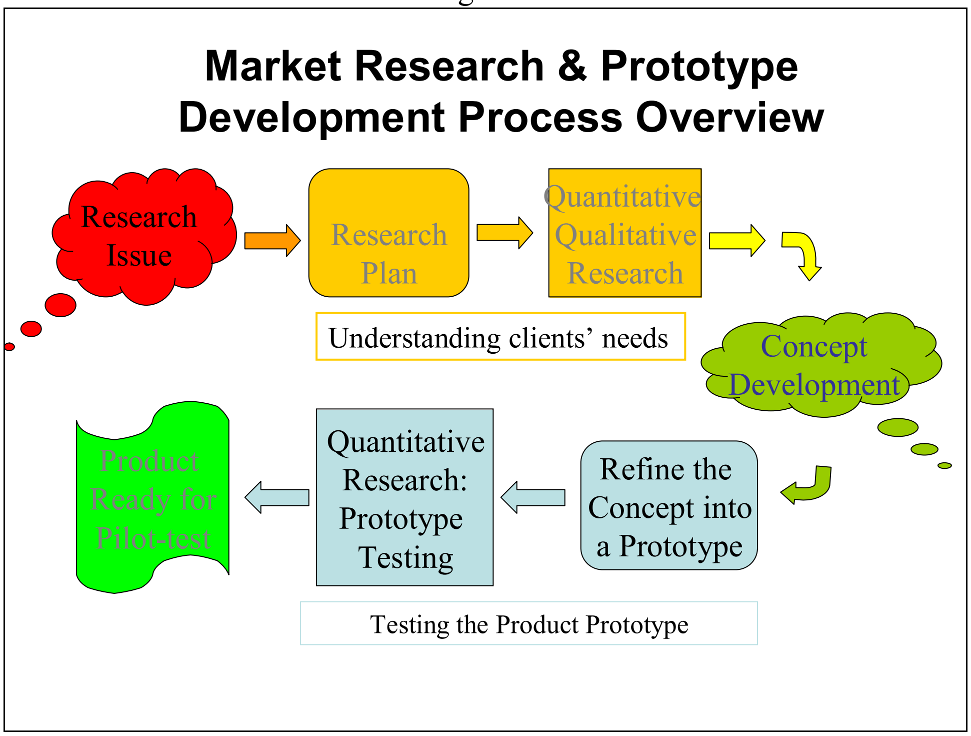


Market research offers us a way to understand not only these uses of financial services but also how to deliver products and services that best respond to these needs. It focuses on customer preferences and customer financial behavior and generates information that can be used to determine the most appropriate products. Also, market research can help determine how to assess and consolidate a MFI's position within the market.

In making the case that MFIs should conduct market research, I think we need to pause and ask, market research for what? At the beginning, I introduced the concept of market-led microfinance and I want to return to it now. If the goal is to attract and retain clients, our market research must look at the client perspective on three levels: products, institutions and markets.

First, let me start with clients and products. Much of the current focus on market research is around this nexus. It is seen as an integral part of the product development process (see Figure 3).

Figure 3



Source: Graham Wright

Recently, Teba bank in South Africa introduced a new product called GROW WITH US SAVINGS ACCOUNT. The 'Grow with Us' Savings Account provides affordable financial services to those who previously might not have had access to savings accounts, such as the informally employed and those who require facilities to keep their money safe and to save. To market its product, Teba planned to rely on its front line staff. Management presumed that success would depend on training the clients in saving and budgeting. Key messages to the clients were focused on:

- the importance of saving,

- the need to plan to save (have a budget), and
- Teba Bank can help you budget and save.

Teba Bank adopted a plan to equip front line staff with the basics of financial management. The educated staff could then help their clients. To achieve this, Teba used a wide variety of education techniques including:

- articles in the Bank's newspaper,
- a book,
- a poster,
- a brochure, and
- a competition for staff on savings.

The product was promoted via radio press releases and the sponsoring of a savings week. However, the impact of this promotion campaign fell far short of its targets. Levels of client intake were lower than anticipated, the reasons for which were several:

- Competition from the informal as well as formal sectors was greater than anticipated.
- Radio proved to be a good medium to get people to open accounts but not to move them much further forward,
- Branch staff did not fully engage in the promotion campaign – there was no product champion, few staff 'read' and thus did not acquire information to pass on to their clients.

Teba Bank learned important lessons. The approach had been too directive. The Bank focused on *what they thought people needed to know*, not on *what people actually need*. It had not done the market research to assess client preferences for the product and factors that could influence its adoption.

Equity Building Society (EBS) is in Kenya. For their directors, management and staff, market research has represented a crucial milestone in the growth, development and success of the institution. In 2000, EBS made its first deliberate attempt to gain an accurate client perspective of their institution and its products by implementing a market research program. Undertaken in collaboration with *MicroSave-Africa,* this market research made it clear to Equity that its clients **perceived** EBS as charging *exorbitant prices and attendant charges for their loans.* This told Equity that it should seek to re-price and repackage its loan products, especially if it was to counter and overcome the threat from SACCOs and other competitors.

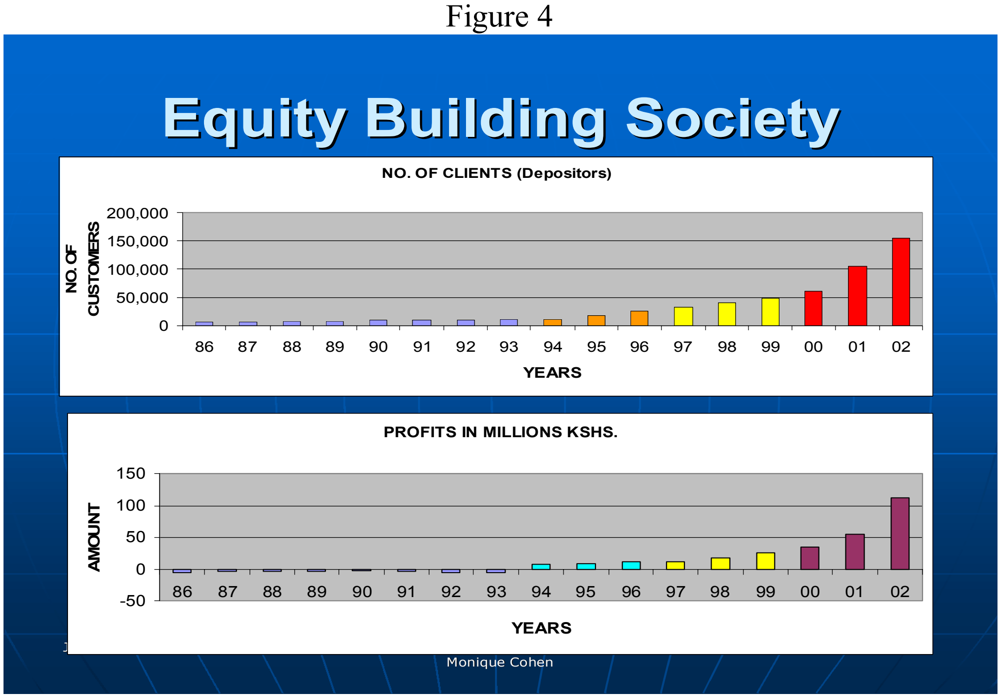
EBS felt that its priority was to do something that would diffuse the clients' negative perceptions of them, while giving management time to think through the process of product development. A first and short term step was to carry out a quick product differentiation exercise on the various features of the loan products as they relate to the needs of each market segment, small holder, microentrepreneurs and the employed. This led EBS to a strategy of reviewing interest rates and charges to make them more transparent. The marketing team was charged with carrying out these changes and transforming Equity's image in the market. The team refined the savings and loan product menu that EBS presented to clients. EBS's initiatives were:

- Restating these loan & savings terms in client friendly language.
- Printing brochures which outlined the changes by product.
- Displaying bank tariffs in the banking halls.

The effect of this initial product refinement step was an overwhelmingly positive client response towards Equity as an institution and to its products and services. Moreover, the changes were introduced without Equity having to market the new refinement measures aggressively. Rather they took a "wait and see" approach with the new initiatives. Soon after the completion of the market research exercise, the number of accounts that were opened daily jumped from an average of 20–30 to about 200.

Figure 4 shows the chronological development of Equity's move toward a demand-led approach, and the corresponding increase in clients and profitability.

Figure 4



Source: Graham Wright

In both these examples, the goal was product refinement. However, market research can be used more broadly in microfinance. Both EBS and Teba Bank have used market research for the design of new products and for determining their marketing campaign. Teba Bank is about to launch a funeral insurance product, and has used market research to define its publicity campaign. More recently, Equity has used market research and *MicroSave-Africa*'s systematic approach to costing and pilot-testing to develop two new products, including *Jijenge,* a contractual savings product that has attracted huge numbers of clients to the institution.

Second, let us turn to clients and institutions. The focus here is on systems and institutional changes that MFIs make as they seek to institutionalize a client focus. Let me touch on two issues:

a. client data base.

b. human resources: there needs to be a product or client champion within the institutions and the capacity to manage, if not do, market research.

If an MFI wants to understand its clients, a good client data base would be an obvious prerequisite. It is surprising how few MFIs have one. Last October I visited MFIs in Mexico and Honduras. All were in the throes of trying to address their higher than desirable drop out levels. All wanted to implement one of the AIMS/SEEP Client Assessment Tools, the Exit survey. The first requirement is a database that would allow them to identify who was in and who was out of the program. None had the information, and by that I mean basic names and addresses, readily available in their MIS.

Recently, I met with another Mexican MFI which has generated an enormous data base about clients and non-clients, the latter being applicants who are denied loans and those who choose not to take loans. Basic demographic and economic information from anyone who enters the door is entered into Palm Pilots by front line loan staff. This provides a wealth of information about market opportunities and helps the MFI to tailor its products to specific market segments. For example, a month before school fees are due, the database allows the MFI to assess which of its clients will need money and then market a seasonal product to that population to respond to that need. Seen from this perspective, targeting takes on a new meaning; it is not an exclusionary process but rather an indispensable business opportunity to help an MFI increase its market share.

There are lots of ways to consider human resources. Let me share the experience of a small MFI in Honduras, which I feel has moved a long way towards being client-led. Part of its strategy has been to train some of its front line staff to do market research on client satisfaction. In addition, it has set in place a reporting system that is easy for the loan officers, generates credible findings, and encourages vertical information flows between senior management and front line staff. Two other things are worth mentioning here:

- The process took time as front line staff learned to accept client criticism not as a black mark, but as an opportunity to improve the delivery of services to their clients.

- In the same way, the clients learned gradually that critiquing the MFI's services and products was not going to lead to a denial of service, but was a way to bring about changes to lower their transaction costs and in turn, lower MFI costs.

For this MFI, the costs of building human resource capacity in this area have not been very high and the benefits have been considerable. Many among the frontline staff now have a role beyond just making loans and collecting repayments. They know how to collect client information on a systematic basis. Promotion to this new market research function is a reward for the better loans officers and is now built into the staff incentive system. Among the effects have been lower staff turnover rates, higher client retention rates, and have in turn improved loan officer productivity rates. For both clients and loan officers, this process has been empowering. Each has gained a voice in how the MFI does business.

Lastly we come to clients and markets. The key questions are what is your market niche and how to secure a solid share? Competition is everywhere and not limited to just the other MFIs competing for the same clients. Competitors also include the myriad of informal sources of credit, such as ROSCAs, supplier credit, family and friends. From a client perspective, we need to take these competitors seriously. They seem to be here to stay no matter what inroads we think we have made with microfinance.

- Bangladesh: Microfinance, even when readily available, averaged 16 percent of the value of financial transactions or 10 percent of the total number of transactions among 42 households (Rutherford 2002).
- Peru: 58% of Mibanco borrowers had other debt. Total client debt was divided evenly between formal and informal sources (Dunn and Arbuckle, 2001).
- India, borrowing from SEWA Bank did not decrease women's debt from other sources, mostly informal. SEWA borrowers had as much non-SEWA debt as other groups. Few used their SEWA loans to pay down other debts (Chen and Snodgrass 2001).

Attracting and retaining clients requires marketing strategies that demonstrate value of your products to the client. Ten days ago I was on a conference panel in Moscow with Kenan Crnkic, operations manager of EKI, an MFI in Bosnia Herzegovina. He is a hardcore believer in market research and client-led microfinance. For him, this business can only succeed if we understand the 4 P's – not product, price, place and promotion but **people, people, people, and people**. He shared with us the market research that EKI conducted to position itself in the market and to distinguish its 'brand.' EKI learned that the staff's perception of their products and their advantages differed significantly from that of their clients. The staff assumed that the product attributes that mattered to clients were the interest rate and repayment period. Their market research on clients showed different results. The program attributes that clients viewed as important were the flexibility of the collateral requirements and the repayment period followed by loan amount. In the highly competitive market in which EKI operates, the need to distinguish oneself in the market is about more than just the product. This information was used by EKI to position itself in the market, to define its image as well as restructure its products. The findings from the market research also remind us once again why market research is so valuable: the staff often get it wrong, they do not necessarily know what is valued by clients.

Before ending, I want to touch on two final issues. The first is the how and the second is cost. Turning to the first, what tools do we have? The good news is that the field has already developed an array of market research tools to understand our clients and to address new product development. The two complementary tools kits that can guide MFIs through the market research steps of gathering client information, analyzing it and helping to define the product design include: the AIMS/SEEP Practitioner-led Client Assessment Tools developed by USAID and *MicroSave-Africa's* Market Research for Microfinance qualitative tools. Currently, Microfinance Opportunities and *MicroSave-Africa* are working together to combine these two tool kits into a series of training materials on VCD. The "Listening to Clients" Set of Tools will comprise 23 modules, each visually depicting live training sessions that can be used to train MFI staff to implement a selection of tools, for self-learning and by consultants for executing market research assignments.

As I close this session, I am sure some of you are thinking, can I afford to do this, does my scale of operation and the potential opportunities for growth warrant it?

The costs are:

1. Developing the market research skills within the organization.
2. Doing the market research, whether using internal or external resources.

The first are sunk costs associated with building capacity. The second can vary but should not been seen in isolation from the gains that can flow from more effective service delivery. The implementation of the tools is obviously labor intensive, so the costs will vary. Moreover, collecting the information is only one cost. There is also the time spent on analysis and convincing senior staff that a change is warranted. One institution I met took a year to convince the Board to make modifications to an existing product. But as the example from EBS suggests, if you get it right, the increase in revenues and profits can be substantial. The example from ODEF illustrates how once the staff are trained, market research can be an ongoing process of data collection and analysis, followed by incremental change undertaken quickly and at a relatively low cost. Major policy changes may require Board consultation or major changes to the MIS and other systems, which clearly are more weighty.

Conclusion:

To go back to my opening words, market research for microfinance, and *client-led* microfinance, make good business sense. It should be done by everyone, whether they are entering a new geographical market, or have been around a while and want to increase their market share as the competition increases. As the example of EBS shows the payoffs are good. As the example of TEBA Bank suggests, not doing the market research and getting it wrong can be expensive. As Kenan stressed, given current market conditions, market research is no longer a choice for many MFIs. It is necessary for survival.