

Risk Management for MFIs

MCPI Annual Conference 2017

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About *MicroSave*

- We are a **financial inclusion consulting** firm with over two decades of experience of working in Asia-Pacific and Africa
- Focus thematic areas: Digital financial services, **Inclusive finance, MSME finance** and Private sector development
- Our clients: **Banks, MFIs and other financial service providers**; bilateral and multilateral funding agencies, corporates and private foundations; regulators and policymakers

150+ banks, MFIs and MNOs which have improved operational efficiency on the basis of our advice

150+ financial products developed across the globe

40+ countries across Africa and Asia in which we have in-depth financial market intelligence

50+ countries where we have implemented projects

300+ papers, focus and briefing notes, and other print and online published

Our Services in Microfinance/MSME Finance



MicroSave
Market-led solutions for financial services

Our Experience in the Philippines

- ❑ CARD Bank - design and deliver a voluntary savings product that could be serviced through an ATM
- ❑ Technical support to OK Bank, TSKI, TSPI and ASKI to grow microfinance portfolio and diversify products and services through: Strategy development; Product development and pilot test; process optimisation; human resource development; Internal Audit and control
- ❑ Advisory on transformation of OK Bank
- ❑ Support to ASKI in setting up SME vertical; develop green finance models; analysis of agriculture value chains
- ❑ Setting up Grievance Redressal and Client Complaint mechanism at TSPI
- ❑ Designing value chain interventions for TSKI
- ❑ Support Opportunity International partners to:
 - ❑ Review and assess the feasibility of rolling out mobile money initiative
 - ❑ Incorporate a remittance company to allow such partners to offer domestic and international remittance to their customer

Our Clients



Understanding Risks and Risk Management

A Look at the Prominent Risks in Financial Inclusion (1/2)

Risk

Rank

Perspectives

Strategy

1

“Most institutions do not have strategy for next three or five years”. – Respondent from Middle East

Risk Management

2

“Very few organizations look at risk in a comprehensive way instead of realizing that it forms the foundation of their strategy” – Respondent from Asia

Change Management

3

“Since MFIs work with the lower strata of society, which are not so sensitive to economic variables, [the business is] more stable compared to commercial financing, and MFIs are more reluctant [to engage] in change management” – Nirdhan Uthan Bank, Nepal

A Look at the Prominent Risks in Financial Inclusion (2/2)

Risk

Rank

Perspectives

Technology

4

“Vastly improved user friendly, convenient ways of delivery, not only for non-credit products but also loans. Unless they adopt newer technology or collaborate with new service providers, [MFIs] face risks of client attrition and high costs” – Swadhaar, India

Credit Risk

8

“The lack of customer credit information and loose credit risk management policies have increased the incidence of this risk.” – Respondent from Ecuador

Governance

9

“Board composition is mixed, strong in the larger more international type institutions but weak across most local MFIs”. - Respondent from South Africa

The Essence of Risk Management

Comprehensive

- covering all aspects of the organisation

Continual

- not just a one-off exercise, but something that is maintained and updated

Built-in

- not an add-on, but integrated into all parts of operations and systems

Suitable

- principles, policies and practices should be adapted to the context of organisation or activity

Proportional

- keeping a sense of perspective and proportion between benefits and risks

Source: Katharine Gaskin, Risk Toolkit, The Institute for Volunteering Research and Volunteering England, 2006

Important Risks in MFIs

Strategic Risk

- Risk to earnings arising from adverse business strategies

Credit Risk

- Lending money and not getting it back

Fraud Risk

- Intentional deception for unfair or unlawful personal gain

Systemic Risk

- Includes political and regulatory risks

Operational Risk

- Loss resulting from inadequate or failed internal processes

Reputation Risk

- Risk of loss of image amongst clients and other stakeholders

Financial Risk

- Includes liquidity risk, interest rate risks

Technology Risk

- Risks related to utilisation of technology

Partnership Risk

- Risk related to partnerships or third party arrangements

Risks Associated With Strategic Choices?

Risks Associated

Risk of lack of suitability of the strategy:

Whether the strategy addresses the factors influencing the strategic position

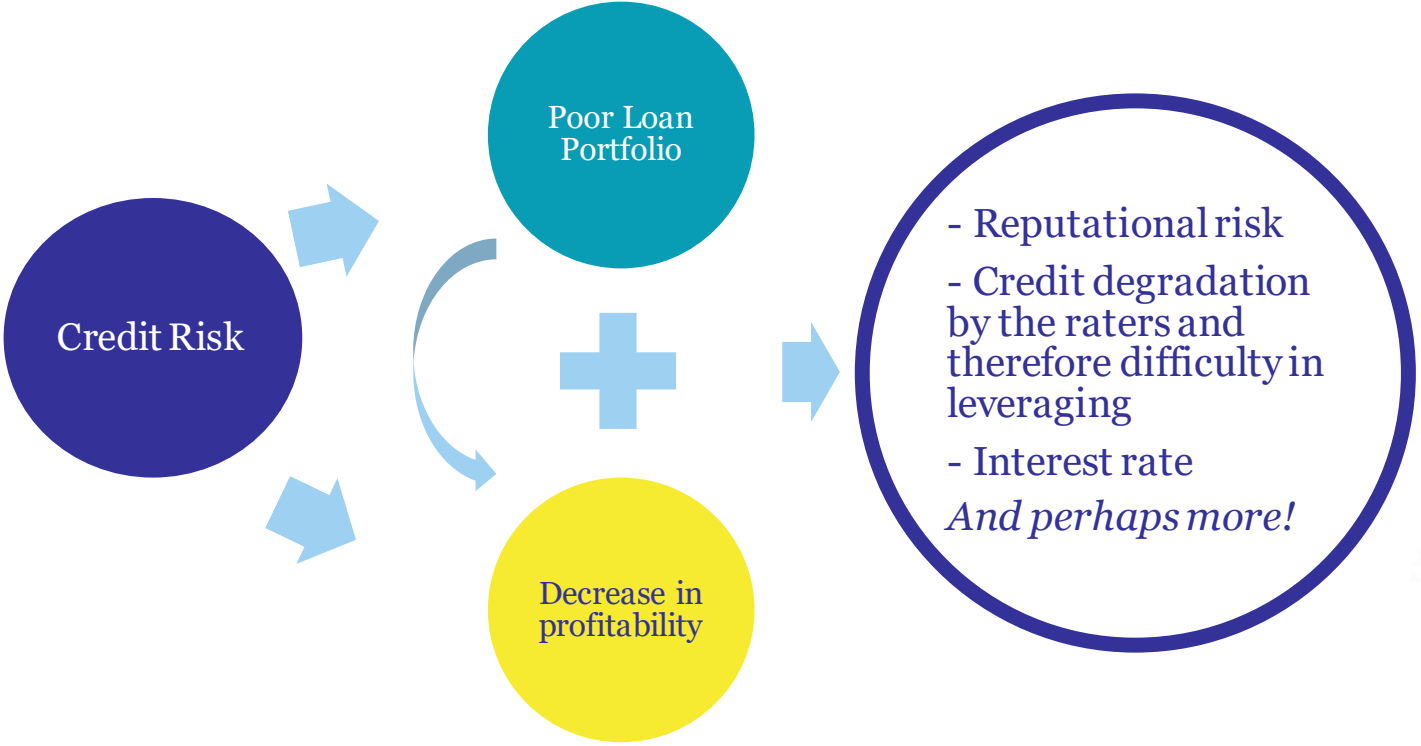
Risk of lack of acceptability of the strategy:

The extent to which the strategy meets stakeholders' and performance expectations

Risk of lack of feasibility of the strategy:

Whether the strategy could be made to work in practice; resourcing and strategic capability

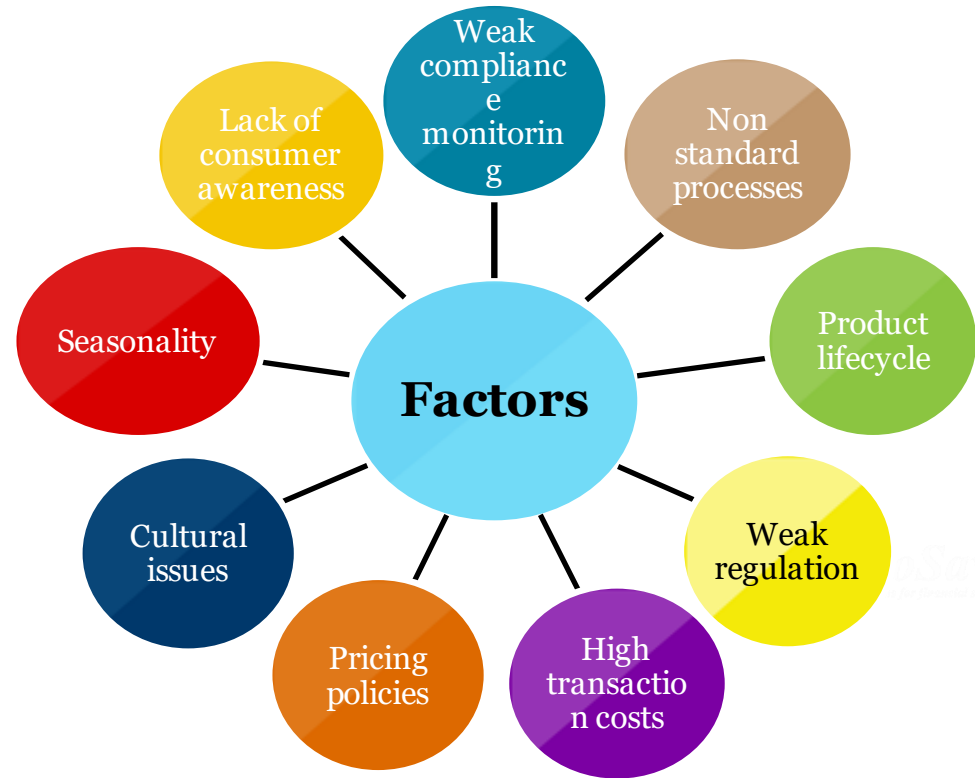
Impact of Credit Risk



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Most Common Types of Frauds in MFIs

- Falsified or Altered documents
- Fictitious loans
- Kickbacks
- Embezzlement of funds
- Cash theft
- Collusion in issuance of loans
- Manipulation of financial data



Importance of Risk Management for MFIs

Minimise Impact Of Risk
Materialising

Lowers Future Cost
of Mitigation

Understand Investment
Cost

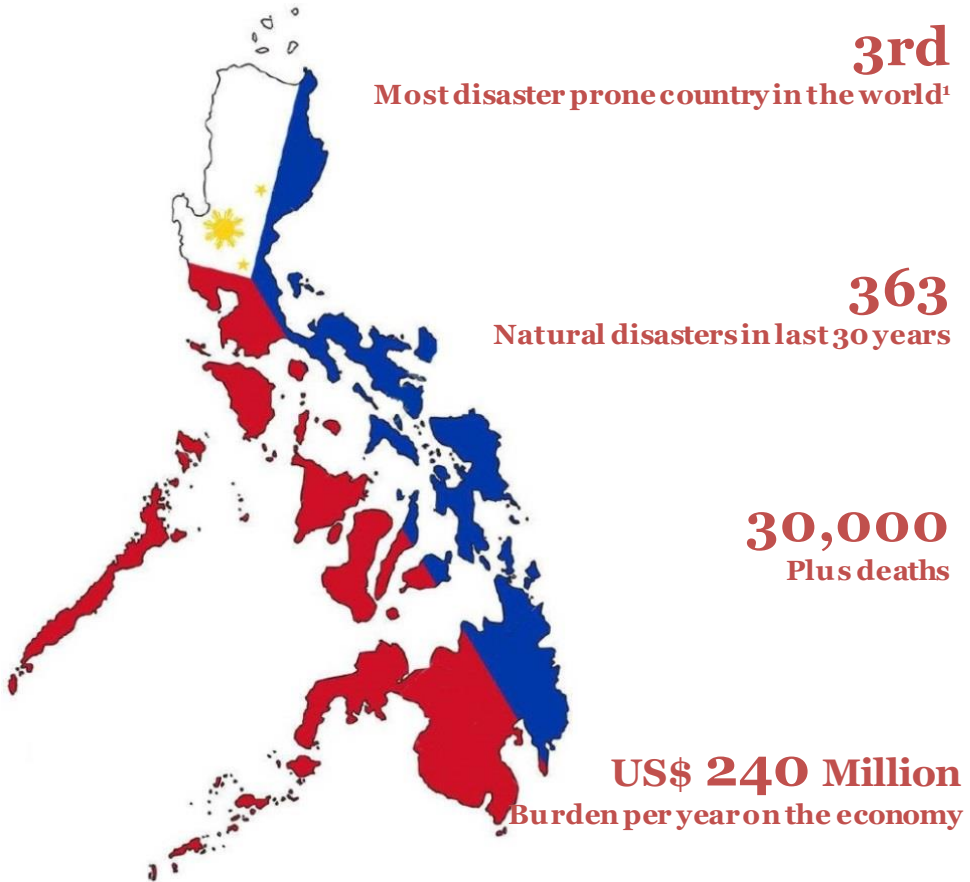
Assurance for
Management/ Shareholders

Enhance Strategic Decision
Making

Maximise Commercial
Opportunity In Uncertain
Areas

Risks in the context of the Philippines

Disaster Management for MFIs in the Philippines - *Impact*



Impact of Disasters on MFIs

Financial

Loan defaults

Loss of clients

Lack of funds

Increase in operational costs

Non-Financial

Loss of files and records

Staff related issues

Damages to power, transport, communication facilities

Disaster Management for MFIs in the Philippines - *Strategies*

Ex-Ante Strategies

Building an emergency plan

Insurance of assets, data & recovery setup, securing storage of credit records off site

Diversification of credit portfolio

In terms of geography, client segment, product types

Liquidity management

Maintain sufficient reserve in banks. MFIs should also foresee to develop and maintain emergency funds.

Client education

Awareness on insurances, policies and procedures for receiving funds post disaster.

Ex-Post Strategies

Detailed customer assessment

Quick customer surveys to reliably assess economic condition of customers and their ability to repay

Liquidity management

Sorting out liquidity issues with multiple internal & external sources

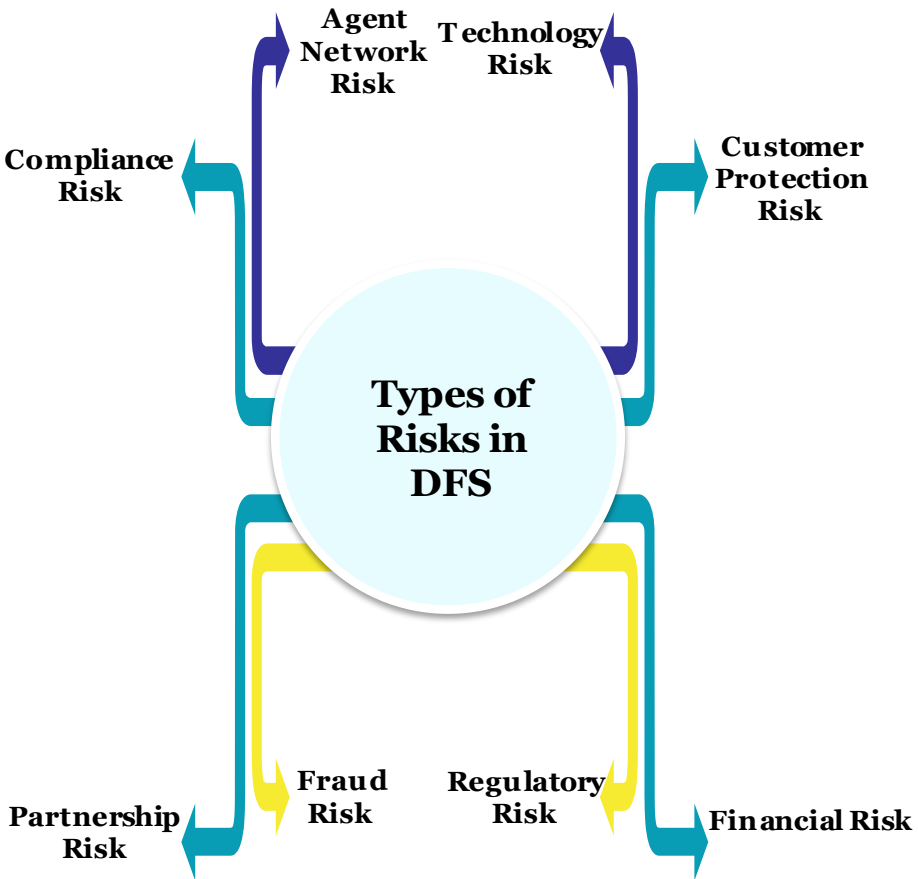
Adjustment of outstanding loans

Offering loan restructuring and rescheduling options to the clients

Avoid over indebtedness

Best possible loan adjustments to avoid over indebtedness

Risk around Digital Finance



Customer Service Risk

1. Inability to transact due to network/service downtime
2. Insufficient agent liquidity or float
3. Complex and confusing user interface
4. Inadequate provider recourse
5. Non transparency of fees and other terms
6. Fraud perpetrated on the customer
7. Data privacy and protection
8. ***Lack of available agents*** reflecting the limited number of active agents in the country.

Role of DFS in Risk & Fraud Management – an example!

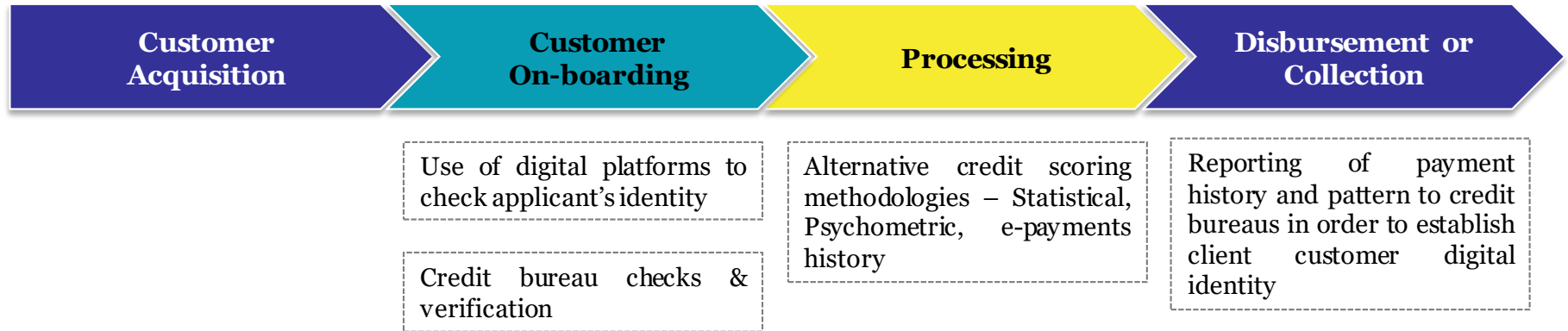
1. Credit risk assessment using new data sources & analytics

- Use alternative credit scoring methodology like, statistical, psychometric, e-payments history.
- Share credit scores across providers of credit bureaus

2. Fraud detection with digital applications & analytics

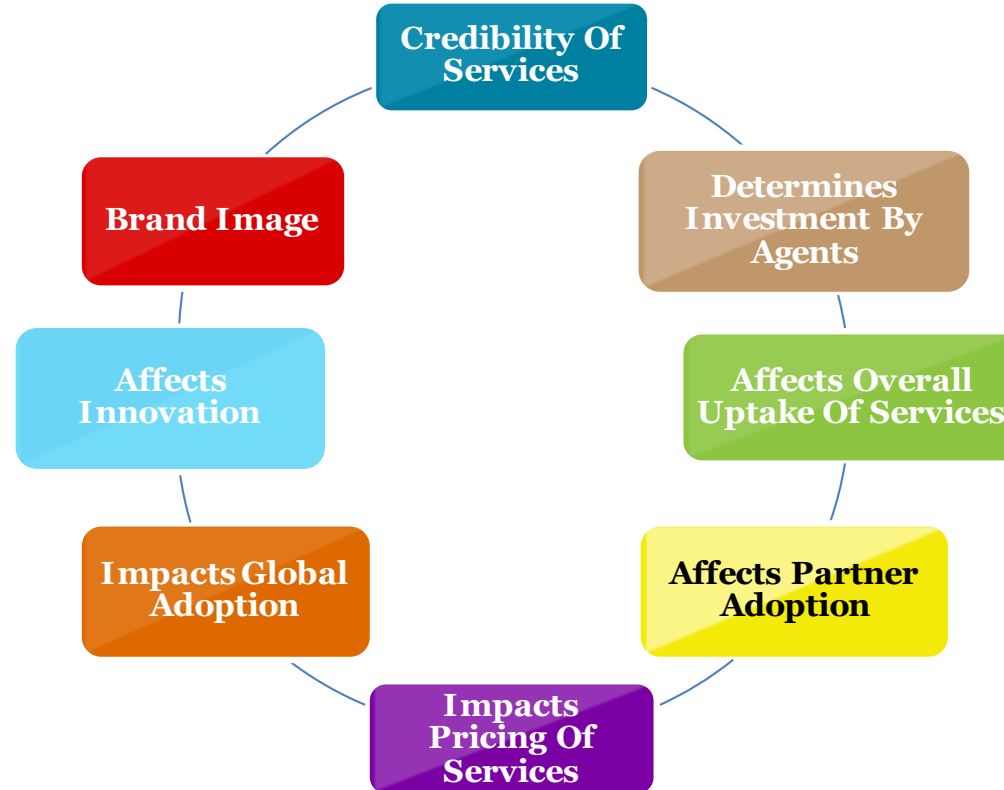
- Use of digital platforms to minimize identity fraud
- Use and implement real-time systems to monitor and manage fraud and ensure reporting of frauds

Mapping Digital Interventions in Credit Value Chain



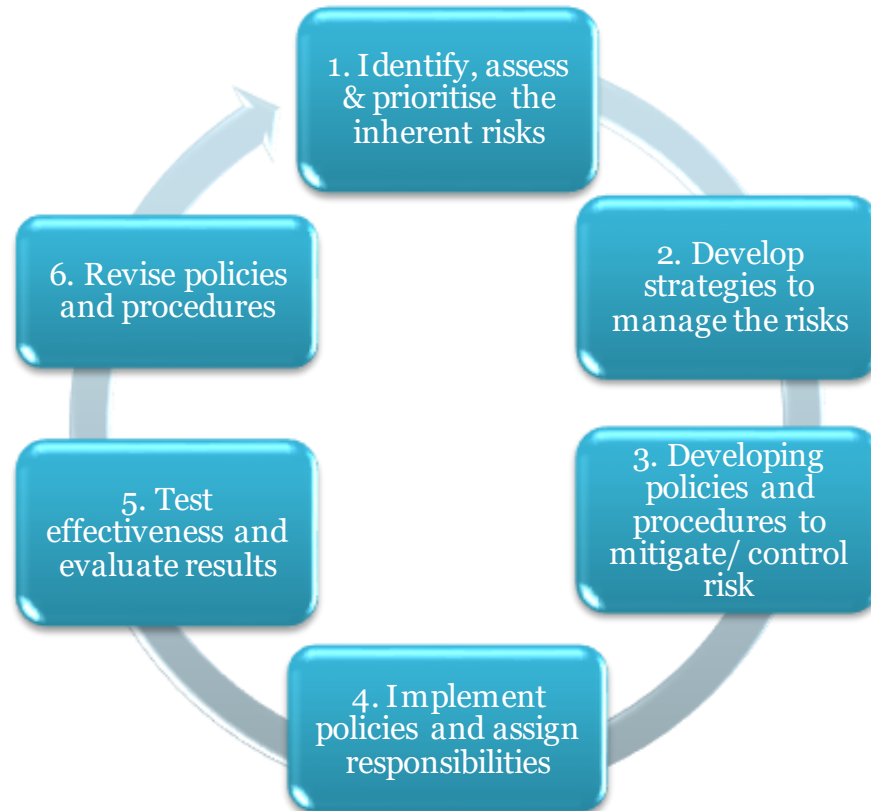
Risk Management Strategies

What is the Impact of Risk?

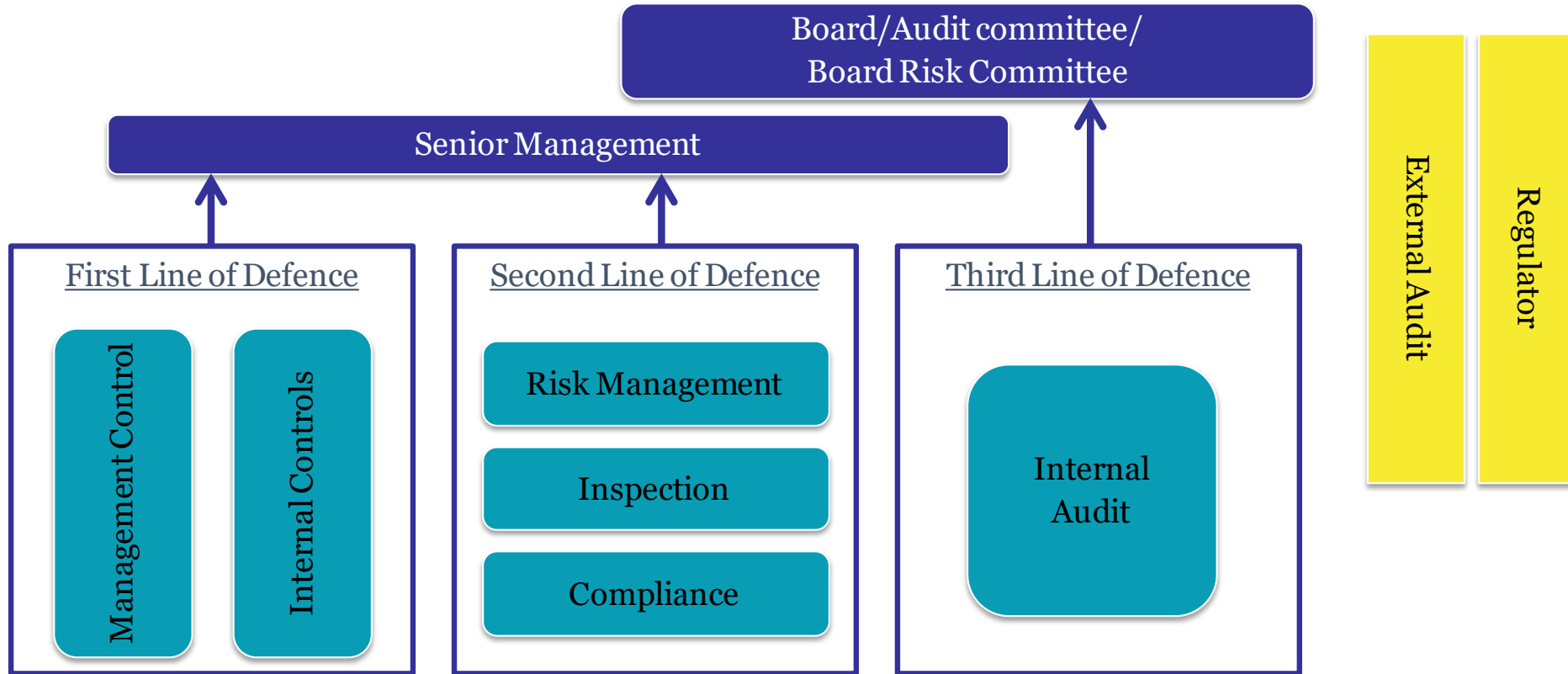


Risk is not to be feared, but to be understood so that it can be addressed.

Risk Management Process



Institutional Risk Management



Common Strategies for Addressing Risks

5 Catastrophic	Transfer risk	Transfer but monitor risk	Put rigorous controls	Avoid or Put rigorous controls	Avoid risk
4 Major	Transfer risk	Transfer but monitor risk	Transfer or Put rigorous controls	Avoid or Put rigorous controls	Avoid or Put rigorous controls
3 Moderate	Accept but monitor or Transfer risk	Accept but monitor or Transfer risk	Transfer or reasonable controls	Transfer or Put rigorous controls	Put rigorous controls
2 Minor	Accept risk	Accept risk	Accept with strong monitoring	Moderate control required	Reasonable control required
1 Insignificant	Accept risk	Accept risk	Accept risk	Accept but monitor or Little control	Moderate control required
Impact Probability	1 Rare	2 Unlikely	3 Moderate	4 Likely	5 Almost Certain

Finally.....Successful Risk Management Would Result In.....



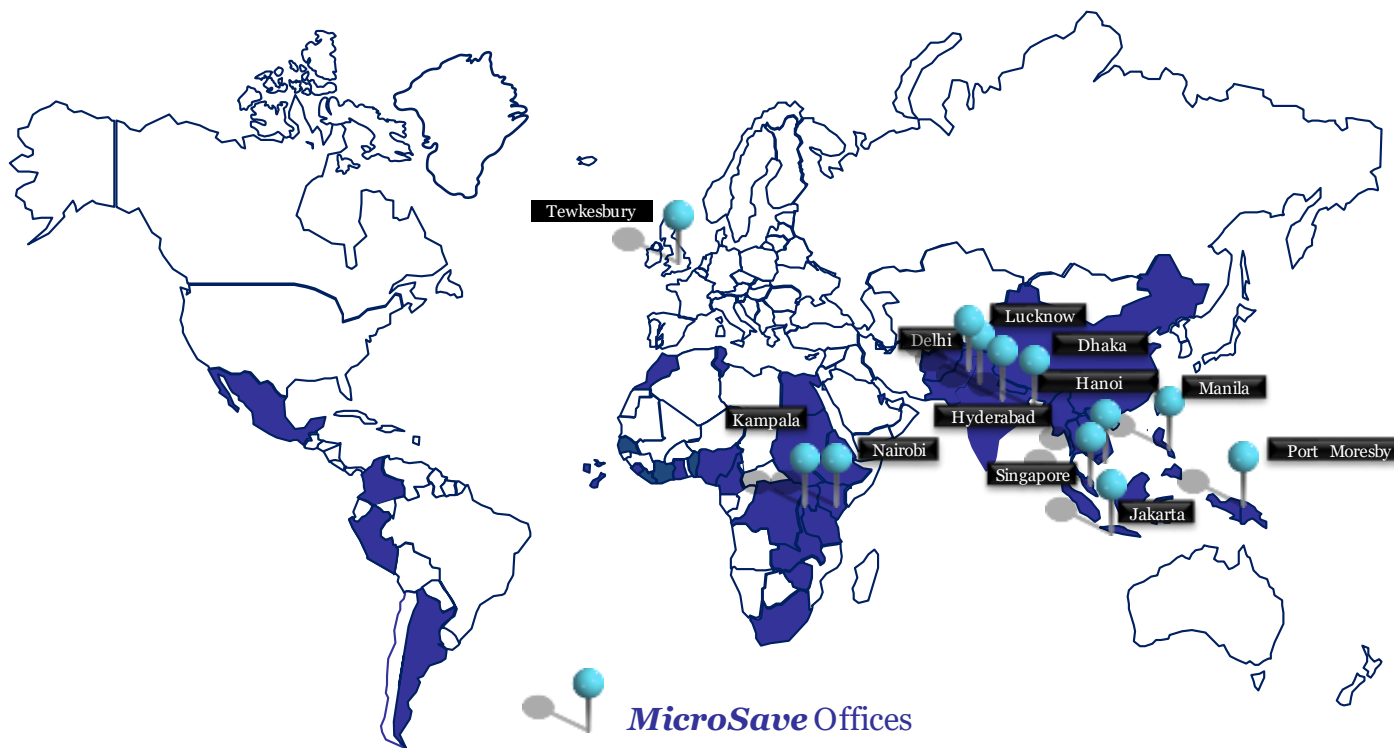
Getting suitable, new partners
Building trust among your partners and customers



Decision-tree process makes risk assessment clear, consistent and simple.
Roles and responsibilities are clear.
New tools and support make life easier



Good risk governance - reducing risk by promoting accountability, integrity and transparency of top management.



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