Triple Jump
impact-focused investment manager

Lessons from the **Pandemic**

Making digital transformation in microfinance work for the poor

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Making **digital transformation** in microfinance **work for the poor**

A study of 89 Triple Jump microfinance investees worldwide

Amsterdam, March 2021 [1]

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About Triple Jump

Triple Jump is an impact-focused investment manager that provides capital and advisory services to support the development and scaling up of viable financial service providers in emerging markets.

Its investment portfolio of financial service providers across Africa, Asia, Europe, and Latin America has enabled more than 2 million entrepreneurs to access finance over the past 15 years.

Triple Jump aims to support its investees in leveraging the benefits of digital technologies to expand their outreach and improve their social performance and financial returns.

www.triplejump.eu

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Background and **key findings**

This study assesses the current levels and future trajectories of digital transformation within the microfinance industry, gauges the impact of digitalization on institutions' operations and performance, and discusses lessons learnt. It identifies opportunities for external stakeholders to deepen financial inclusion by supporting, improving and accelerating socially responsible digital transformation across the entire microfinance sector.

Background

Over the past decades, microfinance has enabled millions of entrepreneurs and small businesses in emerging markets to access financial services and thereby generate employment and economic growth. However, many microfinance institutions still struggle to offer products and services in an efficient and affordable manner to low-income customers and those in remote areas. Digital transformation can significantly support their efforts to deepen financial inclusion by facilitating geographical outreach and lowering transaction costs.

The study is based on an August 2019 survey of 89 Triple Jump microfinance investees in 46 countries, in-depth interviews with 7 institutions, quantitative analyses of the links between institutions' current levels of digital transformation and their performance, and the insights and experiences of senior Triple Jump staff. During the pandemic, in late 2020, Triple Jump additionally interviewed multiple investees in Africa, Eurasia, India, and South America to learn how the digital transformation impacted their operations during the pandemic, and how those experiences have shaped their future plans.

Key Findings

1

Most institutions in the survey are still in the early stages of their digital journeys, but virtually all aspire to achieving a higher level of digitalization. There is no clear relationship between the overall level of digitalization achieved by an institution and its portfolio size or geographical region. However, there are significant regional differences in the types of digital technologies that institutions have already introduced or are planning to introduce.

2

Digital transformations can improve outreach and operational efficiency. Triple Jump's data supports the widespread belief that microfinance providers can deepen financial inclusion by pursuing digital transformation. Investees who have adopted digital technologies report benefits in terms of both enhanced geographical outreach and improved operational efficiency, while slow movers are coming under increasing pressure from competitors.

3

The pandemic has caused the industry to accelerate its digital transformation efforts. The COVID-19 pandemic highlighted the benefits of digital transformation for microfinance institutions. Many Triple Jump investees adopted new processes and rolled out new payment tools to enable clients to access services from their homes. At the same time, client uptake of digital tools has sharply increased.

4

Strong leadership from the top, effective risk management and a commitment to responsible digital finance are required to ensure that digital transformations yield positive results for both institutions and their clients.

5

Supporting the digital transformation requires a balanced approach. Investors catering to the strong demand for financial and technical support by microfinance institutions have to maintain a strong focus on the broader goal of deepening financial inclusion. Successful engagement will require pursuing opportunities while carefully managing risks to institutions, clients, and the future of the socially driven microfinance as a whole.

6

Triple Jump supports the industry wide shift towards digital transformation and recognizes its potential to deepen financial inclusion if deployed wisely. Supporting a socially responsible transformation will entail selecting investees with strong digital potential, monitoring social impact, safeguarding institutional sustainability, building the digital capacity of both staff and clients, and promoting responsible digital finance.

Levels, trajectories and patterns of **digital transformation**

A large majority of the institutions in the survey are still in the early stages of their digital journeys, but almost all institutions aspire to achieving a higher level of digitalization. There is no clear relationship between the overall level of digitalization achieved by an institution and its portfolio size or geographical region. However, there are significant regional differences in the types of digital technologies that institutions have already introduced, or are planning to introduce.

Five levels of digital transformation

Digital transformation is a "strategic business transformation that requires cross-cutting organizational change as well as the implementation of digital technologies".[2] Triple Jump assessed the current level of digital transformation of the respondents by assessing the extent to which they have automated their lending processes and operations (digitization), and the extent to which they leverage technology to increase customers' access to and use of financial services (digitalization). Based on survey results, the 89 respondents were categorized into five different levels, from non-digital to advanced.

Non Digital — **Reliance on manual processes**

Novice — **Low level of digitalization**
- One alternative channel or data analytics application in use or in pilot

Starter — **Digitalization of some processes**
- At least three alternative channels and/or data analytics applications in use

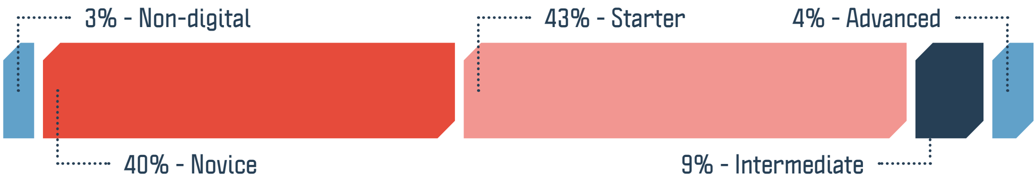
Intermediate — **High level of digitalization**
- At least six alternative channels, data analytics applications and/or other applications in use
- At least 20% of transactions processed digitally

Advanced — **Very high level of digitalization**
- At least six alternative channels, data analytics applications and/or other applications in use
- At least 50% of transactions processed digitally
- Credit process mostly or fully automated

2. "Digitization, Digitalization, And Digital Transformation: Confuse Them At Your Peril", Forbes, 29 April 2018 https://www.forbes.com/sites/jasonbloomberg/2018/04/29/digitization-digitalization-and-digital-transformation-confuse-them-at-your-peril/#5e6423bc2f2c

Most microfinance institutions are just **starting out on their digital journeys**

While almost all institutions in the survey have started out on their digital journeys, a large majority are still in the early stages. Overall, 40% are at the 'novice' level, with a low degree of digitalization. A further 43% are slightly more digitalized 'starters'. Only 13% have reached the higher 'intermediate' or 'advanced' levels.



Institutions have **strong ambition** to go digital

Over 90% of Triple Jump investees reported wanting to reach a high (63%) or very high (30%) level of digitalization. The latter figure is especially remarkable as the survey question defined 'very high' as "fully digitalized with minimal in-person client contact". Virtually all institutions reported ambitions to move beyond their current level of digitalization. An overwhelming majority of institutions either already have a digital strategy (60%) or are in the process of developing one (33%), and many have already budgeted additional funds to achieve their goals.

Average **level of digitalization** is similar across regions

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Relationship between level of **digitalization and portfolio size** is unclear

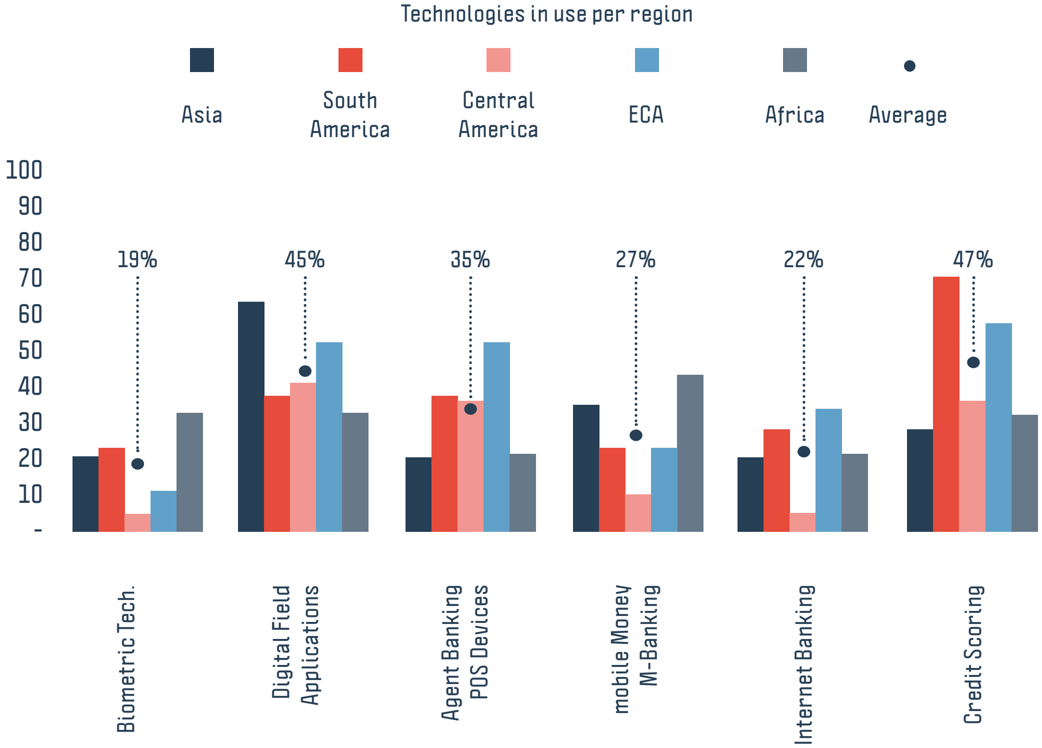
The data do not support the assumption that larger lenders are always more digitally advanced. True, across all 89 institutions worldwide, larger portfolio size is correlated (+0.33) with a higher level of digitalization. However, the correlation between size and digitalization varies strongly by region (+0.8 in Eastern Europe & Central Asia versus -0.1 in Africa), and some small institutions perform strongly while a few of the larger players lag behind. Thus, the relationship between portfolio size and level of digitalization is unclear.

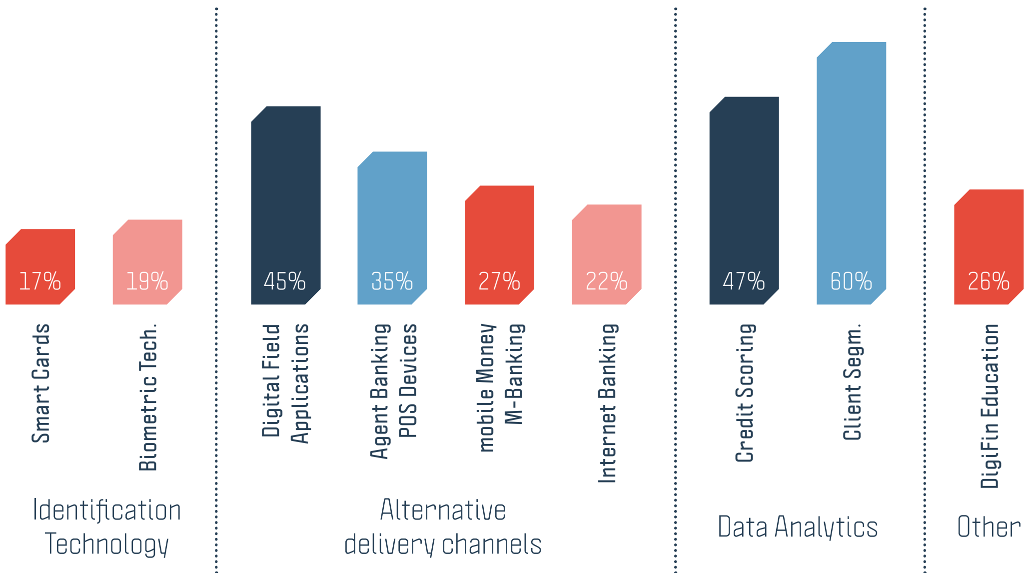
Some **technologies** are far more **widely used** than others

Globally, some types of digital technology are being far more widely used than others. Already, 60% of the surveyed institutions are using data analytics for client segmentation, and 47% are using digital solutions for credit scoring. The picture is more mixed for alternative delivery channels; while 45% of institutions use digital field applications (such as tablets for loan officers), only around a quarter offer mobile money services (27%) or internet banking (22%). Less than one in five institutions use biometric technology (19%) and smart cards (17%) for client identification.

Significant **regional variations** in the types of technology used

The uptake of some types of technology varies strongly between regions. For example, 44% of micro-finance institutions in Africa offer mobile money, compared to less than a quarter in the Americas and Eastern Europe & Central Asia ('ECA'). Similarly, credit scoring is far more prevalent in South America (71%) than in Asia (29%), while the use of digital field applications is far more widespread in Asia (64%) than anywhere else in the world.





Impact Of Digital Transformation On Business Results & Financial Inclusion

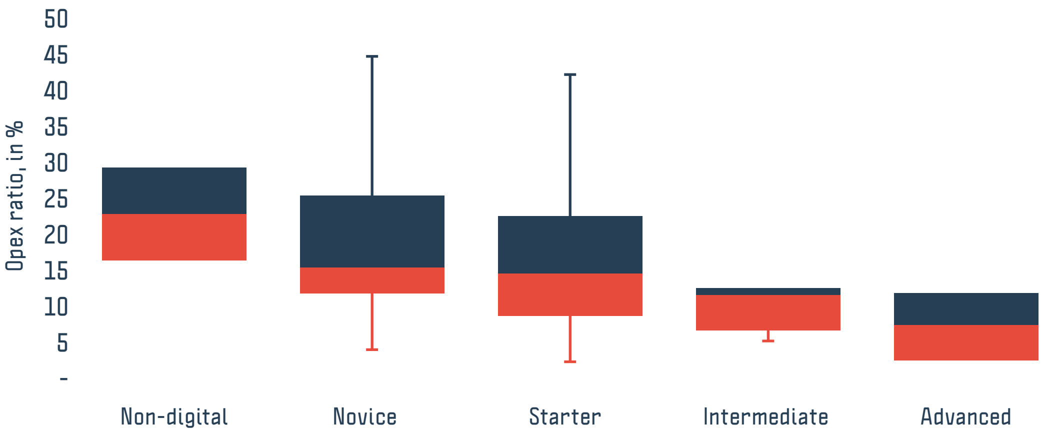
Triple Jump's data supports the widespread belief that microfinance lenders can deepen financial inclusion by pursuing digital transformation. Investees who have adopted digital technologies report benefits in terms of both enhanced geographical outreach and improved operational efficiency, while slow movers are coming under increasing pressure from competitors.

Deployment of financial technologies has generated significant benefits

The microfinance institutions in the survey reported substantial benefits from their past deployments of financial technologies. Survey respondents reported observing "slight" or "great" improvements in a variety of areas, with customer satisfaction (81%) topping the list. The only downside, reported by around a quarter respondents, was a worsening of credit risk, but this was balanced by a similar number who had observed credit risk improvements.

Digital maturity correlates with **operational efficiency**

A comparison of survey results with Triple Jump monitoring data shows a correlation between a higher level of digitalization and improved operational efficiency at all stages of the process. On average, the operational expense ratio for 'intermediate' and 'advanced' institutions is 8.8%, dropping to 16.8% for 'starters', and 18.3% for novices.



Digital maturity goes hand in hand with **strong client focus**

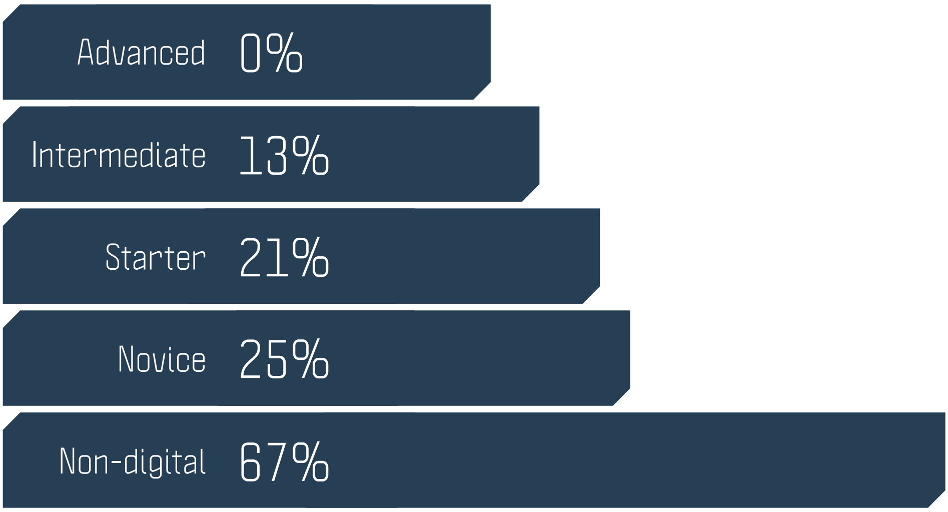
Triple Jump internal data on investees' performance show that digitally advanced microfinance investees tend to have higher quality product offerings and lending operations. Ninety percent of survey respondents who have reached the 'intermediate' and 'advanced' levels are in the top quartile of investees in terms of product and operational quality, indicating that these are institutions that place the client at the centre of their operations.

Low levels of digitalization could result in **competitive disadvantages**

As an increasing number of financial institutions embark on digital transformation, those that lag behind face greater competitive pressures. Over half of Triple Jump investees report that they do not yet face digitalized competition in their markets. However, among survey respondents that do, a third report that poaching of their clients has increased, more than one in five find it increasingly hard to offer competitive rates, and one in ten report decreases in portfolio quality or profitability rates.

The survey results show that the more digitalized an institution is, the less likely it is to suffer competitive disadvantages. While 50% of 'novice' level institutions facing pressure from digitalized competitors have already experienced negative effects, this figure drops to 37% for 'starters' and just 25% for institutions in the top two digital maturity brackets (with 'advanced' investees reporting no negative effects at all). For example, digitally sophisticated institutions are far less likely to report difficulties in offering competitive rates, as the following chart shows.

Percentage of institutions reporting difficulties in offering competitive rates (n=89)



Digital transformation in times of covid: **early lessons**

Triple Jump investees report that the pandemic has highlighted the potential benefits of digital transformation for the microfinance industry, leading many of them to significantly accelerate their efforts in this area.

"Without our software, we wouldn't have been capable to deal with the challenges COVID brought in all the dimensions of the business."

"It enabled us to adapt our business to the new context and maintain control over operations and financial aspects."

"Also, we were able to create a wide array of facilities in favor of our clients."

Triple Jump investee
South America

Business continuity assured

Several investees noted that their ability to continue operating and servicing clients throughout 2020 was a direct result of their previous investments into digital infrastructure. Many microfinance institutions were able to switch to fully working remotely within a matter of days.

Customer service maintained and improved

Digital tools enabled many institutions' clients to take out new loans, restructure existing loans and make repayments without ever leaving their homes. Against the backdrop of a severe economic downturn, institutions with a high level of digital transformation were able to maintain contact with their clients and maintain high collection levels.

Acceptance of digital tools by clients improved

With options for visiting branches and making cash payments curtailed, the proportion and number of clients using lenders' existing digital platforms increased strongly, including in rural areas. In one case, the proportion of clients using the lender's mobile app increased from 3% to over 80% in the course of less than a year. Microfinance institutions expect this change to have a positive long-term impact on clients' acceptance of digital channels.

Digital transformation accelerated

The pandemic brought into focus steps in the lending process that still relied on face-to-face interaction and paper documents. In response to the pandemic, some Triple Jump investees accelerated their overall digital transformation plans, while other focused on developing, improving and rolling out new processes and tools such as mobile wallets and WhatsApp payments. As a result, the range of services that clients are able to navigate digitally has expanded, often considerably. However, one lender noted that legal requirements for paper signatures on some documents prevented them from going fully digital across their entire spectrum of services, and economic uncertainties led another lender to temporarily suspend automatic credit scoring. Overall, Triple Jump investees concurred that the pandemic had highlighted the benefits of digital transformation and motivated them to further accelerate the process.

COAC Azuayo

Ecuador

Founded in 1996, COAC Azuayo is the second-largest cooperative in Ecuador. Its network benefits from partnerships with hundreds of grocery stores, where members can make withdrawals. When the pandemic hit, COAC Azuayo was already far along the digital transformation curve, with software solutions developed by a strong in-house IT team and a sophisticated Management Information System. These factors enabled the cooperative to allow its partner stores to also register loan payments and disbursements.

Over the course of 2020, COAC Azuayo accelerated its digital transformation efforts, completing what had been planned as a three year process within a single year. Members can now make payments, open new deposit accounts, and even request loans online. In addition, the lender launched mobile wallets and improved an existing WhatsApp transaction system. Users rapidly adopted these new technologies.

COAC Azuayo estimates that without its novel credit solutions, 21% of its portfolio would now be in arrears or at risk of default, as opposed to its current actual PAR>30 rate of under 5%.

Crystal

Georgia

A high level of digitization enabled Crystal in Georgia to maintain unbroken business continuity throughout a national lockdown, while its clients were able to continue loan repayments via POS terminals and transfer money through a mobile wallet app, which by now is being used by one in ten active borrowers.

The microfinance institution was also able to restructure loans and negotiate grace periods remotely, with granting borrowers the possibility to sign agreements online.

In response to the pandemic, Crystal accelerated its digital transformation plans in order to take advantage of what it describes as "huge possibilities". The lender has concluded that its clients want and need greater remote access to its services. Currently, Crystal is working on introducing a facial recognition system that will allow it to fully digitalize the process from loan origination to disbursal, and a separate system that will digitalize the loan monitoring process by allowing borrowers to upload monthly income statements and sales reports.

KMF

Kazakhstan

KMF equipped all of its employees with tablets so that they could work from home, ensuring uninterrupted business continuity even during the national lockdown. Early on in the crisis, KMF actively encouraged its clients to switch to digital channels, with remarkable success. During the lockdown, existing loans continued to be repaid exclusively through remote channels, and new loans were issued using digital loan agreements confirmed by SMS message.

In parallel, the microfinance institution further improved its mobile application, making it more user friendly and adding new services. KMF also brought forward the implementation of new tools like remote borrower registration using biometric validation, business client evaluations via video calls, and the disbursement of loans directly into clients' bank accounts.

According to KMF, these innovations boosted client satisfaction by improving service speed and quality. Within less than a year, the share of customers using its mobile app increased from 3% to over 80%.

Challenges

The challenges encountered by institutions pursuing digital transformation differ according to their degree of digital maturity, and appear to have changed in recent years.

Key challenges

Lack of capital to invest in their digital transformation was the challenge reported most frequently by respondents, but financial resources top the list of concerns for 'non digital', 'novice' and 'starter' institutions only. In contrast, 'medior' and 'advanced' institutions rarely encounter steep financial hurdles. Instead, these more digitally mature institutions start running up against external barriers such as poor national infrastructure and clients' low technological literacy. Meanwhile, a similar percentage of institutions at all levels report having to navigate challenges related to human resources and acceptance by staff or clients.

Changes over time

Institutions' concerns may also shift with time due to changes in the external environment. For example, in a previous Triple Jump survey many African microfinance providers reported difficulties with establishing relationships with mobile network operators and FinTech companies; these issues seem to be less of a concern today. Similarly, many of their Latin American counterparts flagged technological hurdles and weak connectivity as problems; these too seem to have largely been overcome by now. [3]

Key risks

Many microfinance institutions fear that the process of digital transformation entails the risk of losing contact with bottom of the pyramid clients. Nearly a thirty percent of institutions see 'lack of in-person contact and resulting detachment from clients' (22%) or 'mission drift' (7%) as key risks. A significant minority of institutions also worry about fraud and cyber security risks (23%),[4] or the risk of potential short term inefficiencies and business continuity challenges (19%).

At the same time, a quarter of respondents identified no potential risks whatsoever. None of the investees mentioned data privacy risks or data ownership issues, suggesting that financial institutions' awareness of these potential pitfalls may still be limited.

3. Triple Jump. 2017. "How Microfinance is Navigating the Fintech Revolution in Africa"
https://Triple Jump.eu/wp-content/uploads/2018/05/How-Microfinance-is-Navigating-the-Fintech-Revolution-in-Africa-1.pdf
Triple Jump. 2017. "FinTech in Latin America", unpublished internal research
4. However, one investee commented that digitalization at his institution has helped to mitigate financial, criminal and operational risks.

Key **success factors**

Triple Jump's experience with supporting digital transformations at microfinance institutions shows that the key factors underlying a successful transformation are a focus on clients, strong change management, and building staff capacity.

"Some of the critical success factors were to manage change, plan in advance, effective training and communication, cross functional buy in to the technology, and developing technology that can work in offline as well as online mode."

Satin Creditcare Network, Ltd
India

Focus on clients

Successful digital transformation processes are geared towards meeting clients' needs. In other words, successful institutions seek to apply financial technology to solve their clients' problems, rather than their own. They leverage technology to build processes and products that improve and facilitate clients' access to financial services, and that improve the service offer itself. In Triple Jump's experience, when a new technology genuinely and significantly benefits end users, clients learn how to take advantage of it far more rapidly than institutions initially assumed they would.

In parallel, successful institutions educate and train their clients to ensure that all of them can take full advantage of the innovations on offer. By popularising the use of digital financial services across all client groups, including the technologically less literate, they deliberately strive to ensure that their digital transformation results in deepening financial inclusion.

"Key success factor for digitalization is to understand that the customer solution is not technology; it is to solve problems with technology."

Crezcamos
Colombia

Strong change management

A successful digital transformation requires strong change management, considerable 'soft' skills, and a continuous focus on people as well as processes and technology. At the level of the Board, this means drawing up a digital strategy that sets out a clear and coherent roadmap towards a digitalized future for the institution, its staff and clients. The Board must be prepared to manage teething problems including technological hitches, potential staff resistance and initially low take-up by clients.

The Board itself should take the lead in clearly communicating the aim of the process throughout the institution, explaining how it will benefit clients and staff, and spelling out in detail when and how new technologies and processes will be adopted. Process redesigns should focus on client-relevant results such as efficiency, flexibility and ease of access. New processes should initially be piloted on a small scale, and staff should be given training prior to rollout.

Not coincidentally, nearly half of 'intermediate' and 'advanced' microfinance institutions score in the top quartile on a management quality metric that Triple Jump uses to evaluate its investees. In addition, 80% of these institutions have a digital strategy, 70% rated their senior management's ability to lead the digitalization of their business as "very high" in the survey, and 65% reported having made organisational changes to support the process of transformation.

Building staff capacity

A successful digital transformation requires building the capacity of staff at all levels, not only within the IT department. Institutions should conduct a thorough assessment of capacity gaps up front, set clear capacity goals, and develop and implement an institution-wide capacity building plan.

The survey shows that digitally more mature institutions have invested the time and effort required to build internal capacity. More than seventy percent of the 11 most advanced Triple Jump investees have provided some trainings on digitalization to their staff. While a quarter of 'novices' and 21% of 'starters' still cite gaps in in-house expertise and human resources as the major barrier to their digital transformation, 'intermediates' and 'advanced' institutions have largely overcome these problems.

Capacity building, together with clear communications, can also help to reduce or eliminate staff resistance to change. Triple Jump's experience shows that staff will welcome and rapidly adopt innovations that yield tangible benefits that matter to them, such as reducing their workload or eliminating tedious repetitive tasks. Therefore, the design of new systems and processes should always take staff perspectives into account.

Supporting digital transformation: the road ahead

Investors will play a strong role in supporting the digital transformation of the microfinance sector. While demand for financial support and technical assistance is strong, investors also have to take the wider impact of their efforts into account. The digital transformation has considerable potential for deepening financial inclusion, but in order to make it work for the poor, investors have to select investees wisely, monitor social impact, and promote responsible digital finance.

Demand for investor support

While institutions differ in the pathways they have followed and the distances they have covered, virtually all Triple Jump investees are keen to achieve a higher level of digitalization. Institutions across all 46 countries surveyed indicated a need for investor support to achieve their digital ambitions.

Financial support. Triple Jump's survey indicates that many institutions require external financial support to make their digital transformations a success. This is especially true for the large majority of investees that are still in the early stages of the process.

Board support and capacity building. Both the survey results and Triple Jump's own experience show that institutions in the early stages of the transformation will require support with high-level strategy development and tailored technical assistance.

Triple jump's digital transformation accelerator

Triple jump has developed the digital transformation accelerator to support microfinance institutions in fast forwarding their digital transformation through a comprehensive approach that puts the customer at center stage, is embedded in the corporate strategy, and is driven by the entire leadership team, with deepening financial inclusion as the end goal .[5]

Making digital transformation **work for the poor**

Digital transformation is a means to an end – to foster financial inclusion and better serve people.

The central question for investors is how to support digital transformation so that it fully realises its potential for deepening financial inclusion, enabling socially oriented institutions and their clients to survive and thrive in the digital age. Thus, the challenge is not how to foster digitalization per se, but how to improve the livelihoods of people at the bottom of the pyramid by making digital transformation work for the poor.

5. For more information, visit the Digital Transformation Accelerator website: http://digitalinclusivefinance.org/

Selecting investees with both digital and social **potential**

Past technology initiatives have generated substantial benefits in terms of enhanced geographical outreach, improved operational efficiency, and higher client satisfaction. Conversely, institutions that are behind on the digital transformation curve may struggle to compete – and ultimately, survive – once more digitally advanced rivals enter their markets.

Armed with a strong understanding of the conditions for successful digital transformations, Triple Jump is well positioned to select institutions with the greatest potential for leveraging digitalization to deepen financial inclusion through enhanced outreach, improved services, and lower costs.

Promoting **responsible** digital finance

Investors need to carefully monitor the opportunities and risks that digital transformation could pose to investees and their clients. Socially oriented investors in particular will need to be alert on potential trade-offs that can arise between a focus on optimization of efficiency and scale on the one hand, versus maximizing positive social impact on the other.

Triple Jump supported the development of the Investor Guidelines for Responsible Digital Finance in order to help its investees – and the sector as a whole – to appropriately manage the risks generated by digital transformations. Triple Jump is strongly committed to aligning its work, and that of its investees, with the principles and practices set out in the guidelines.

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