



Chapter 4

Products for the BOP Market

Low-income people need a full range of financial services—often the same services most readers of this book take for granted. What’s more, these services make an important impact on the quality of their lives. It comes as some surprise that so few inroads have been made to widen the range of services that reach the poor beyond a very basic loan or savings account.

Before we explore the keys to product design for bottom-of-the-pyramid (BOP) clients, we ask readers to consider how meaningful financial products can be for people’s lives. These products are not luxuries. They are intimately connected with some of the deepest human needs: safety, shelter, and family. Lacking good financial services, people either find informal solutions

which are often unsatisfactory, or they have no solution at all. Without health insurance, they may not get medical treatment. Without housing finance, they may wait years before they obtain decent housing. When they use informal money transfers, the money too often goes astray. Imagine the range of products that could be developed to fill the unmet needs in this realm.

It is precisely because the needs these products address are universal and basic that their market potential is so great. Hundreds of millions of families around the world will value and therefore be willing to pay for these services.

H1 Designing Effective Products

H2 The Sub-Prime Fallacy

The private sector brings deep expertise and often deeper pockets to the research, development, and market testing of new products. But successful product design for the BOP market also requires a new outlook. While a suite of financial products for these clients may sound like a standard banking mix—insurance, savings accounts, leasing—underneath the surface they operate very differently. Why? Because the people they serve are different.

The first lesson for any financial-service designer for the BOP market is this: products for low-income people are not just scaled-down versions of products for the middle class. We call this the sub-prime fallacy. At ACCION we frequently encounter bankers committing the sub-prime fallacy, especially those who have been working in the United States. We try to convince them that the sub-prime lens prevents them from seeing the right solutions for the BOP market in developing countries. With deep and sympathetic understanding of the economic lives of their clients, product designers in developing countries can avoid the sub-prime fallacy. And after the sub-prime crisis in the United States, developed markets are also crying out for a fresh approach.

In U.S. and European markets, sub-prime loans look a lot like prime loans, only worse. Sub-prime loans are smaller versions of standard loans, but because they are small and the clients have poor credit ratings, they are riskier. To compensate, sub-prime loans are higher priced and

often carry stiff fees, especially for late payment or pre-payment. The sub-prime game often boils down to a risk/cost/return calculation with little product adaptation.

Group-based microcredit illustrates one answer to the sub-prime fallacy. The pioneers of group lending—Grameen Bank in Bangladesh and ACCION in the Dominican Republic—modeled their products on local folkways. They observed poor people, especially women, forming groups to help each other save and borrow, and even covering for a member who had a short-term problem. They saw that people preferred small, frequent payments. The group loan products used today by millions of women around the world incorporate these features. The loans that result are more expensive than standard commercial-bank loans (because they are small), but they are not riskier—often quite the opposite.

H2 Housing Microfinance

Housing microfinance in Andean countries demonstrates another way to avoid the sub-prime fallacy. It meets clients where they are, rather than where the bank expects them to be.

In Bogota, Lima, and Quito migrants from the countryside squat on unoccupied land at the urban fringe. Over time, they upgrade from tin shacks to small brick huts and eventually to larger houses with improvements, all on the same plot of land, to which they gradually acquire the rights. They build the houses themselves or hire skilled, informal builders from their local communities. This pattern is an integral part of the culture of urban Latin America.

Traditional mortgage lenders have ignored the housing-finance needs of these migrants (who number in the millions). The lenders simply could not scale down the mortgage product to make it affordable, nor would they lend to clients with quasi-formal land title and informally-built structures. This is classic sub-prime thinking.

Mibanco, the Peruvian microfinance bank we met in the profile of Delia, has a better solution. Mibanco devised a home-improvement product—Micasa—that follows the progressive building patterns of slum residents in Lima with loans of one to three years, each financing a

specific home-upgrading project. Rather than scaling down a mortgage product, Micasa is an adaptation of Mibanco's standard microenterprise loan; it is cashflow-based rather than asset value-based. Mibanco has seen excellent results with Micasa and keeps about 15 percent of its US\$320 million loan portfolio in this product.¹

H2 Radical Simplification

Only simple products can be delivered at affordable prices to low income people. Simple products also fit the life circumstances of BOP clients and may even reduce psychological barriers. Some researchers point out that complex processes may heighten clients' fear of banks because they signal mistrust and reduce the transparency of the transaction.² At the same time, simplified products must incorporate risk reduction in creative ways. Group microloans meet the simplicity and risk control tests: they omit elaborate business analysis and reduce risk instead through peer guarantee. Mibanco's housing microfinance is simple: it does not register formal mortgages; instead, it ensures that borrowers have longstanding and locally accepted claims to their residence even if they lack a formal title. The need for simplicity is very apparent in insurance, where the claims process must be stripped to its barest essentials to become affordable. For example, some health insurance programs for BOP clients skip expensive screening for pre-existing medical conditions. That may mean that the policies provide less complete coverage, but at the base of the pyramid the alternative to good enough coverage is usually none.

H2 Partnering for Product Creation

Product design may require creating relationships that do not already exist, especially through partnerships that bring providers closer to customers. Many of these partnerships involve

¹ Warren Brown, "Building the Homes of the Poor—One Brick at a Time," ACCION International *InSight* No. 4 (January 2003).

² Marianne Bertrand, Sendhil Mullainathan, Eldar Shafir, "A Behavioral-Economics View of Poverty," *American Economic Review* 94, no. 2, (May 2004): 419-423.

delivery channels, but some also involve specialists such as schools, hospitals, home builders, or energy companies. This book features many partnerships between companies and microfinance institutions, such as the health insurance examples cited in the next chapter. In Ghana, Barclays Bank has even created a linkage with the indigenous *susu* system. Traditional *susu* collectors act as barefoot tellers. They roam the markets collecting deposits from clients and depositing them in the bank at the end of each day. These collectors have been around for decades or even centuries without a formal link to a bank. Barclays's program improves the safety of deposits for the collector's customers even as it widens Barclays's customer base.³

H2 Raising the Bar on Market Research

Of course the starting point for solid product design is market research, the gathering and refining of knowledge about clients. Mainstream market research companies may not be adept at learning about the BOP customers, making it worthwhile to contact organizations that specialize in this market, such as MicroSave, a pioneer in financial-services market research for low-income populations in Africa and South Asia.⁴

H2 A Warning: Disruptive Entrants

When mainstream financial-services providers ignore large markets, they provide an opening for other players to step in. "Disruptive" entrants from the non-financial world may step in because they need to ensure that their customers have access to finance for their products. Consumer-goods retailers are a classic example, and in the next chapter we will see a cement company (CEMEX) and a land developer (ARGOZ) involved in finance for this reason. Non-financial companies may enter because they are already dealing with customers and can turn their infrastructure, customer knowledge, and brand name into a significant market advantage. Delgado

³ William Derban, "Becoming More Inclusive," Barclays' *Sustainability Report 2007*.

⁴ www.microsave.org or www.microsaveindia.org.

Travel, a travel agency turned money-transfer organization, shows how a small, side foray into finance became one of the agency's principal business lines. Financial institutions may not find the market available if they wait too long.

H1 The Innovation Premium

To offset the added cost of designing and delivering products and services for the grassroots, many are saying that the process stimulates out-of-the-box thinking in stagnant industries—innovation that trickles upmarket, even if the specific innovations themselves have limited applicability beyond the BOP. As Christopher Beshouri, writing in *McKinsey Quarterly*, points out, “Some of the factors that raise the cost of serving poor consumers are actually acute forms of challenges that businesses confront across all consumer segments.”⁵

H1 Mind the Gap – Services that are Not Being Provided

New ideas for BOP product design come from identifying the service gaps. According to statistics on access to financial services, the vast majority of people enjoy very limited choices: a rigid group loan or a single savings account. Consumer lending and microfinance have historically focused on credit. Microfinance typically measures its success by counting borrowers, and, on that dimension, its 60 to 130 million worldwide borrowers represent an important achievement. But for other financial services, the access gap is breathtaking.

Neither consumer lending nor microfinance is strong in savings, one reason the Gates Foundation has launched a major campaign to increase savings services for the poor. Frequently, consumer lenders and microfinance institutions work under regulatory frameworks that prohibit savings mobilization outside of commercial banks. As a result, most of the low-income savings accounts around the world are offered by public sector institutions, especially post-office savings

⁵ Christopher Beshouri, “A grassroots approach to emerging-market consumers” *McKinsey Quarterly*, Number 4, 2006.

banks. These institutions have traditionally provided notoriously poor service. I have never forgotten the shock I felt when interviewing clients of Indian public sector banks in the 1990s and hearing repeatedly about bribes they had to pay for the most basic services. For these clients, payouts to corrupt petty clerks were a fact of life. While post-office savings banks usually safeguard savings, they have provided few other services. The best of such institutions have reformed and improved their services. However, the poor quality of these banks offers a gaping opportunity to companies prepared to do business better.

The remittances market—expatriate workers sending money home—is large and growing at US\$300 billion or more per year.⁶ The majority of these transfers take place between BOP participants. Although customers may feel comfortable with traditional informal channels, they may actually be better off switching to formal money transfer services. They will spend less as a proportion of the amount sent, and their hard-earned money will be safer, too.

BOP customers typically use money-transfer organizations, such as Western Union and MoneyGram, as well as smaller specialized companies, rather than banks. The remittances corridors between the United States and Latin America are almost completely dominated by money-transfer companies, even though the enormous scale of remittance flows attracts the attention of major banks. Banks have potential cost advantages over money-transfer companies, but have not yet changed established customer behavior patterns on a large scale.

Insurance companies are beginning to wake up to the BOP market as well. While the numbers of insured are rising fast, at 78 million people in the microinsurance arena, only a fraction of BOP market households have meaningful insurance coverage today.⁷

Other services have hardly penetrated the BOP market at all. Their potential value to millions of families means that they represent tremendous opportunities in the hands of the right

⁶ “Sending Money Home,” International Fund for Agricultural Development, 2.

⁷ Jim Roth, Michael J. McCord, and Dominic Liber, “The Landscape of Microinsurance in the World’s 100 Poorest Countries,” The MicroInsurance Centre, LLC, April 2007, ii.

players. Consider the following financial services that could help make low-income people better off while furnishing providers with profitable lines of business.

H3 Renewable Energy Loans. Inclusive finance can play a small but important role in combating climate change. Developing countries can move toward a low-carbon development path if they bring renewable energy to clients who have previously had no energy or used kerosene, charcoal or other environmentally destructive sources. The up front cost of a solar home lighting system is too high for most people to buy it all at once, making financing a necessity. Solar Electric Light Company (SELCO), a solar energy supplier in India, arranges for banks to make loans that finance SELCO's products. Most of SELCO's hundred thousand or so customers financed this way gained access to electricity for the first time. Many small energy companies seek partnerships with financial institutions to help finance their clients' acquisitions, but so far SELCO is one of the few companies to have brought such arrangements to scale.

H3 Education Loans. In poor communities, children are an asset because of the future support they will provide to the family, and education improves their income-generating potential. School loans help families with the need to pay large (for them) lump sums when fees come due. In Kenya, Equity Bank's education loans allow families to keep children in school and improve their future standard of living. This product seems like such an easy win that it is surprising it has not already spread widely. Opportunity International, a microfinance organization, is taking a similar approach in Ghana.

H3 Pensions and Mutual Funds. Low-income families need pension benefits to protect them from destitution during old age or disability, but in many countries government provides no old age safety net. In 2006, Self Employed Women's Association (SEWA) Bank, a specialized microfinance bank, launched India's first micro-pension scheme as a joint venture with the Unit

Trust of India's (UTI's) asset management company. As distributor, SEWA Bank collects regular contributions as low as Rs. 50 (US\$1.20) and forwards them to UTI for a 3 percent commission. UTI opens individual retirement accounts, through which customers can invest in the Indian stock or bond markets.⁸

Most of these products are at an early stage of development, but the needs they address—energy, education, and old-age security—are fundamental. Products like these offer a next generation of opportunities for first movers.

⁸ "UTI Retirement Benefit Pension Fund," Sewa Bank, www.sewabank.com.