New Product Development for Microfinance:

Evaluation and Preparation

Technical Note Number 1

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MICROENTERPRISE BEST PRACTICES

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New Product Development for Microfinance: Evaluation and Preparation

by

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PREFACE

This technical note — the first of two on new product[1] development — is intended to serve as a guide for microfinance institutions (MFIs) looking to expand their reach both in breadth (new markets) and depth (new products). This technical note explains the critical institutional and market analysis required of an MFI in making the decision whether or not to expand its product line. Specifically, "New Product Development for Microfinance: Evaluation and Preparation" aids an MFI to:

- Understand the implications of the competitive landscape many MFIs increasingly face;
- Define more fully the product line MFIs sell to clients and by which they are correspondingly evaluated;
- Identify the steps required in the process of new product development as set forth by conventional business practices;
- Recognize the signals for new product development from customers, other market players, and within the institution;
- Evaluate the opportunity for new product development, taking into account financial, institutional, and methodological implications of proceeding;
- Determine whether undertaking the process of new product development is suitable for an MFI's particular stage of growth and the market realities it faces; and
- Create an organizational culture primed for product innovation.

The companion piece in this series, "New Product Development for Microfinance: Design, Testing, and Launch," is the follow-up guide for those MFIs that decide new product development is indeed an appropriate strategy for growth, based on the analysis outlined in this technical note. Specifically, it outlines how an MFI would pull together the necessary resources to design, test, and — if the prototype is well-received — implement new products.

Both technical notes focus on the *process* of new product development, regardless of the actual products developed.[2] Accordingly, both technical notes — like the entire product development process — should be looked on as a continuous document. The goal of both technical notes and the key to success is for an MFI to institutionalize a continual process of product refinement based on market forces. Becoming more attuned and responsive to client needs is a critical part of an MFI's methodological evolution, financial viability, institutional soundness, and social impact.

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[1] For simplicity, new product development includes financial services (such as savings or insurance) and product features (loan term, amortization schedules, interest rates) as well as tangible products (such as smart cards).

[2] For this reason, the process of developing savings products is among the case studies analyzed, though the primary focus of this technical note is the evolution of credit methodologies.

These technical notes provide ideas and strategies for MFIs to expand their reach economically and effectively. Systematic or methodical approaches to new product development among MFIs are limited. Accordingly, these technical notes are based heavily on conventional business practices of market research, product design and marketing, staff training, and making profitability projections. Nonetheless, the research for these technical notes drew on the experience of a full spectrum of financial institutions, both large and small, that pursue a mixture of financial and social goals, to inform best practices for MFIs.[3] Among those surveyed were conventional banks in the United States and Latin America, "hybrid" institutions (community development financial institutions—CDFIs),[4] and mature MFIs to understand better the constraints posed by different organizational forms.

[3] Annex A summarizes the research methodology; Annex B provides a definition of conventional business terms to serve as a reference. Business terms that are defined in Annex B appear in italics throughout the text for easy reference.

[4] A CDFI is a U.S. financial organization that provides access to capital in underserved areas in order to promote economic development. As such, CDFIs have both financial and social goals.

TABLE OF CONTENTS

LIST OF FIGURES

CHAPTER ONE

MICROFINANCE MARKETS AND RELEVANCE OF PRODUCT DEVELOPMENT

Because most microenterprise credit programs have little direct competition, they must challenge themselves to control their costs, provide efficient service, and become self-sufficient.[1]

Many MFIs were born in the precompetition era. Characterized as a "monopoly with monoproducts" the microfinance industry has been likened to the automotive industry in its infancy in the United States: MFIs market their products much like Henry Ford marketed his automotive prototype, the Model T, offering his customers "any color they want, as long as it's black."[2] Similarly, the institutional mentality of most MFIs has been *product* driven rather than *market* driven, in which an MFI issues highly standardized loans with little variation or field officer discretion. Monoproducts are simple to administer and costs and fraud are easy to control. Indeed, for the microfinance monopoly, organizational effectiveness was more important than choice when it was the only game in town.

But times and markets have changed. Many MFIs no longer enjoy the near-monopoly position they held even five years ago. MFIs are now disciplined by markets as well as their own internal controls. This new competitive environment implies that to serve their markets effectively, MFIs need to become more attuned to their clients' needs and competitive threats. An MFI can communicate this attention through its products and services, which it continually refines, to maintain the loyalty of the consumers who are key to its sustainability.

This chapter assists the reader to:

- Identify the market trends that are spurring new product development
- Understand the different approaches to product development used by MFIs
- Recognize the implications of competition on an MFI's operations & client relationship
- Explain how competitive markets create opportunities to build stronger institutions
- Define three component parts of a "product"
- Outline the steps used in conventional approaches to new product development

MARKET TRENDS IN MICROFINANCE

Realities have been brought on by changes in the landscape — external and internal — that MFIs now face. While the implications of trends are described in greater detail in Chapter II, the following trends have been instrumental in defining the new microfinance landscape:

- **New players:** MFIs are facing competition from both ends of the financial spectrum. New nongovernmental organizations (NGOs) are forming in response to increased

[1] Katherine Stearns. *Interest Rates & Self-Sufficiency*, GEMINI Technical Note, December 1991, p. 20.

[2] Michael Chu. "Competition in Microfinance: Markets, Products, and Staff." Presented at the MicroFinance Network, 5th Annual Conference—Moving Microfinance Forward: Ownership, Competition, and Control, Alexandria, Egypt, 21 October 1997.

availability of donor funds to promote microfinance activity, which has become the current philanthropic "flavor of the month."[3] In addition, as seasoned MFIs have transformed from NGOs into formal (i.e. regulated) financial institutions and in so doing demonstrating that the market can be profitably served, traditional (regulated) financial institutions are beginning to seriously explore the micromarket segment.[4] Market segmentation is the inevitable result of competition as the players begin to more narrowly define their niches and tailor their products accordingly.

- **Discriminating customers:** As successful microenterprises grow and develop a record of accomplishments, their need for comprehensive financial services similarly evolve. Institutions must respond to clients' demands for more sophisticated products to meet the changing needs of enterprises. This evolution is reflected in new, more deferential terminology to describe the entities that MFIs serve: microentrepreneurs, who were initially looked upon as beneficiaries, have further evolved from *clients* with demands[5] to *customers* to be served. Even the most sophisticated of MFIs have suffered the consequences of failing to anticipate their customers' needs in the form of increased desertion.[6]

- **Increased accountability:** As MFIs become profitable and transform into regulated commercial entities, they have become accountable to new stakeholders. Providers of funds, particularly private investors, are becoming more vocal in requesting demonstrated performance and strategic plans that anticipate market changes.[7] Transformed NGOs are accountable not only to their shareholders, but to sophisticated boards of directors, parent NGOs, and regulatory authorities that also monitor their activity. In addition to formal governing bodies, some MFIs that have network partners are responding to performance

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[3] The international MicroCredit Summit held in February 1997 significantly increased the visibility of the field, especially among donor agencies.

[4] Commercial banks are looking for new niches as the market for small and medium-size clients become saturated. This topic is the subject of another recently published Microenterprise Best Practices deliverable, *Commercial Banks in Microfinance: New Actors in the Microfinance World,* by Mayada M. Baydas et al., August 1997.

[5] Deborah Drake and Maria Otero. *Alchemists for the Poor.* October 1992, p. 47.

[6] BancoSol, for example, lost some of its seasoned peer borrowers by not anticipating their eventual demand for individual loans.

[7] For example, Alex Silva, General Manager of Profund International, explained that investors have demanded that MFIs in their portfolio that hold monopoly positions align their loan pricing with market interest rates, despite the immediate income impact, because inflated prices attract competitors and can mask operating inefficiencies. Interview, 2 October 1997.

pressures that are introduced by being compared with their affiliate peers[8] and institutional assessments that are often a requisite part of membership.[9]

These trends have forced MFIs to rekindle the client-centered emphasis that was supposedly at the heart of their methodologies. Competition will no longer allow them to be complacent.

Most of the 7,000 MFIs worldwide still face relatively little competition, and currently are not subject to these forces.[10] Indeed, most MFIs are in the enviable position in which demand for their services far exceeds supply, creating what Robert Christen has labeled the "yellow pajamas" mentality toward product development: "If an MFI announced tomorrow that it would offer credit to any microentrepreneur wearing yellow pajamas, you can be sure that the next morning there would be a line of pajama-wearing borrowers waiting outside its branch."[11]

But this imbalance is changing with increased visibility of microfinance as a demonstrated, effective tool to promote economic development. The consequent increase in donor support and corresponding proliferation of MFIs, in the context of the overall trend of market liberalization throughout the developing world, has ignited market competition. Indeed, in Bangladesh, Bolivia, Indonesia, and Nicaragua competition governs the microfinance market landscape; whereas oligopoly institutions are evaporating in Peru, South Africa, and Thailand.

Nonetheless, product development has occurred in a variety of market landscapes, and product development varies according to the type of MFI and its market orientation and competitive advantage, as illustrated in Figure 1:

[8] Steven Gross, Vice President of Network Relations for ACCION International, says that subtle but healthy competition exists among ACCION affiliates partly because monthly performance rankings (in loan volume, new clients, savings mobilization, and delinquency) are published and distributed throughout the network. Interview, 25 July 1997, Somerville, Massachusetts.

[9]ACCION International periodically conducts a CAMEL evaluation (based on a similarly-named assessment tool developed by U.S. bank regulators) to assess the financial and managerial soundness of its affiliates. These CAMEL ratings often uncover inefficiencies or incorrect pricing that are brought to the attention of management and the board. *Performance and Standards in Microfinance: ACCION's Experience with the CAMEL Instrument,* Washington, DC: ACCION International Discussion Paper, 1998.

[10] Telephone interview with Don Henry, of Development Alternatives, Inc., who helped launch the Smart Card™ in Swaziland, 30 October, 1997. Nancy Barry, president of Women's World Banking, estimated the number of microfinance institutions globally at the MicroCredit Summit held in Washington, DC, in February 1997.

[11] Robert Christen, Director of Microbanking Advisory Services, S.A. Telephone interview, 11 October 1997.

FIGURE 1:
APPROACHES TO PRODUCT DEVELOPMENT, DEPENDING ON MARKET ENVIRONMENT AND INSTITUTIONAL ORIENTATION

Market Environment:	Monopolistic	Competitive
Institutional Approach:	Subsidy-based	Financial system
Competitive Advantage:	Below-market rates	Client-focus
Product Development:	Splashy/monoproduct spin-offs	Utilitarian
Motivation:	Supply driven (or donor request)	Customer driven

Most MFIs hold a monopoly or oligopoly position because they were the first to exist or because donors subsidize their presence in an otherwise unprofitable area. Without competitive pressure, monopoly MFIs will not expand their product offerings. There are exceptions of course, but the products of monopoly MFIs are typically different from those of institutions that have more competition. For example, some monopoly MFIs have expanded their product offerings, but some of these innovations have been initiated by an interest in a given product, rather than in response to an expressed customer demand.[12] Moreover, an MFI's monopoly position typically means that it has the resources and time to make big investments in splashy products without fear of competition immediately piggy-backing on its research and development (R&D) efforts. While possibly serving a client need, these products are created at the top and are inspired by an MFI's interest in the innovation rather than in response to client demand. This motivation is different from the commercially oriented MFI, which *must* be client driven in order to survive. If the market-oriented MFI fails to develop products that are tailored to customer demand, it will continually lose clients to competitors.

Regardless of the type of product developed, a monopoly status quo is not sustainable. Markets transform quickly and many MFIs are unprepared for unanticipated competitive developments. Few have devoted the resources to marketing or R&D. Accordingly, for those MFIs that have responded to competition, their response has been more reactive than proactive and for the most part has involved adjustments to credit terms of existing products. Many more MFIs have tried to ignore or resist these changes, not realizing that opportunities exist in competition.

[12] Janney Bretz Carpenter, Managing Director of Shorebank Advisory Services, clarified this "product-driven mentality," explaining that such a strategy offers efficiency and cost-effectiveness at the expense of reaching narrower market niches or meeting unique local demands. Interview, 6 October 1997.

BENEFITS OF COMPETITION

The silver lining in this competitive cloud is the realization that the profitable, win-win, client-centered strategy of product development and continual refinement are key to fending off competitive threats. Some of the benefits are listed below:

- **Stronger client relationships:** Competition forces MFIs to improve customer service, lest they lose clients. This service improvement satisfies clients, which in turn reduces desertion[13] (i.e., increases the number of repeat loans) and strengthens the relationship between the customers and the MFI. Improved services and expanded outreach come from "the addition of new and better products, [which] helps the intermediary satisfy more of the demands for financial services from existing and potential clientele."[14] ACCION International has begun developing specialized internal expertise in marketing and product development to aid its affiliates to improve customer service. Thus, although competition initially can be unsettling, "in the end it makes our affiliates more effective in serving our clients."[15] The enhanced image that comes from this improved quality of service improves an MFI's relationship with its lenders and investors, as well as with its borrowers, as high-quality service is perceived as institutional permanency.[16]

- **Learning opportunities:** Competition also creates learning opportunities through strategic collaboration or just attentive observation. That an MFI can learn from its competitors was never questioned by Fundusz Mikro, which actually invited Opportunity International into Poland to serve adjacent markets and to learn and share how to serve the uncharted waters of this young capitalist country.[17] Competitive information-sharing has also been a benefit in Bolivia, where microfinance NGOs share information about delinquent clients "to signal that there are repercussions for not paying. If we pass along bad clients (someone who is in arrears), then everyone loses."[18] Thus, a bad debtors list

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13 Clients who are satisfied with well-designed products and services are far less likely to leave a program or institution. Desertion implies a shortcoming of the service provider, in this case the MFI, which has in some way failed to meet the client's needs.

14 Claudio Gonzales-Vega, Mark Schreiner, Richard Meyer, Jorge Rodriguez, and Sergio Navajaf. "BancoSol: The Challenge of Growth for Microfinance Organizations." In: Economics & Sociology Occasional Paper #2345. Columbus: Ohio State University Department of Agriculture, Environmental & Development Economics, 1996, p. 129.

15 Carlos Castello, ACCION International, interview, 30 July 1997.

16 Claudio Gonzales-Vega, "Stages of Evolution of Thought on Rural Finance," Columbus, Ohio, 1994.

17 Fundusz Mikro actually subsidized Opportunity International's market entry. Rosalind Copisarow, "New Product Development." Presented at the MicroFinance Network, 5th Annual Conference—Moving Microfinance Forward: Ownership, Competition, and Control, Alexandria, Egypt, 21 October 1997.

18 Fernando Romero, President of PRODEM, speaking at the MicroFinance Network, 5th Annual Conference, said that cooperation is voluntary because the Bolivian superintendency requires transformed MFIs, which are regulated financial institutions, to submit a list of borrowers in progressive stages of delinquency (default, write-offs etc.).

serves as an informal credit bureau in containing delinquent clients. In Kenya, competitors came together to establish "rules of engagement". . . to check new, inexperienced entrants for 'unfair practices' — like subsidized credit."[19]

- **Increased operating efficiency:** Competition also typically creates incentives to reduce costs and improve operating efficiency. For the most part, the lending affiliates of ACCION International that operate in competitive environments (Bolivia, for example) have much lower operational expenses as a percentage of their portfolio than those that are monopolies.[20] ACCION has increasingly focused on improving operating efficiencies by modifying credit approval procedures, for example, that both save money and improve client satisfaction (through expedited application process).[21] In the long run, clients also reap the reward of these operating efficiencies through the lower prices that competition typically brings.

Thus, whether competition results in operational improvements or more tailored loan features, the entire "product," including application turnaround time, loan terms and conditions, interest rate, branch wait time to make deposits, and so on, becomes more client-focused.

BORROWING LESSONS FROM CONVENTIONAL BUSINESS

Based on these realities, some MFIs are starting to preempt their competition and anticipate client needs through a concerted new product development process. These MFIs are, however, exceptions to the rule. Thus, this note aims to bring to the world of microfinance lessons culled from conventional product development strategies. The task is ambitious. Successful new product development has become increasingly difficult in today's modern economy; in fact, the new product failure rate for conventional financial products and services — such as credit cards, brokerage services, and insurance plans — has been estimated at higher than 75 percent.[22] Increased competition has brought about increasing market fragmentation and shorter product life cycles, as rivals are quick to put out "me-too" knockoffs. Accordingly, competition makes it increasingly difficult to realize a return on the investment in R&D that goes into commercializing new products.

Markets are dynamic, so competition exerts a continual pressure. Thus, the product-development approaches outlined in this technical note must be part of a broader effort among MFIs to create an organizational culture that is innovative, customer-driven, and attuned to market

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[19] Kimanthi Mutua, Managing Director of the Kenya Rural Enterprise Program, at the MicroFinance Network 5th Annual Conference.

[20] ACCION's internal database. ACCION International tracks performance statistics for all of its affiliates.

[21] An analysis of ACCION's internal database indicates a positive correlation between client retention and improved levels of operating efficiency for those affiliates surveyed. Carlos Castello, ACCION International.

[22] Kevin J. Clancy and Robert S. Shulman. *The Marketing Revolution: A Radical Manifesto for Dominating the Marketplace.* New York: Harper Business, 1991, p. 6. The authors estimate the failure rate of product line extensions among packaged goods to be even higher.

demands.[23] Most MFIs have been shielded from these forces because of their monopoly status. Accordingly, this note draws its insight from institutions that have had to operate in competitive markets, based on the presumption that MFIs will increasingly have to respond to their customers' demands to prevent desertion.

TRADITIONAL APPROACH TO NEW PRODUCT DEVELOPMENT

A product, broadly defined, is anything that satisfies a customer's need or want.[24] From an institution's point of view, a new product represents an opportunity to create value, and in so doing, offers a strategic competitive advantage.[25] Because this technical note deals primarily with financial services, it takes the broadest definition of product to include its component parts:

- **Core product:** The reason *why* the customer pays money — a benefit (e.g., financial return, security) or the need it fulfills (e.g., liquidity, livelihood);

- **Actual product:** The specific features that characterize *what* the customer is buying — including how it is designed (terms, interest rates, eligibility requirements) and packaged (length and clarity of the application, color of the passbook);

- **Augmented product:** *How* the customer receives the product — the way in which it is delivered and serviced (application turnaround time, hours of operation, waiting room facilities, and customer service — in terms of friendliness, accessibility before and after the loan is closed; product knowledge of loan officers).

New product development involves refining and expanding these component parts in a methodical and systematic manner. Corporate approaches to new product development have been consistent over the last couple decades, and have followed a sequence similar to that depicted in Figure 2.[26] Although the development of management information systems has launched an innovative field of database marketing, the use of sophisticated models to forecast demand and

[23] To this point Rosalind Copisarow claims that product success at Fundusz Mikro is half dependent on its features, and half based on the loan officer's belief in the product and consequent enthusiasm and ability to sell it. (i.e., new product development).

[24] Philip Kotler, *Marketing Management: Analysis, Planning, Implementation, and Control,* ninth edition. Upper Saddle River, NJ: Prentice Hall Inc., 1997, p. 9.

[25] Robert J. Thomas, *New Product Development: Managing and Forecasting for Strategic Success,* New York: John Wiley & Sons, Inc., 1993, p. 107.

[26] A more comprehensive description of the sequential new product development process can be found in *New Product Management for the 1980s*, a 1982 booklet that was produced by Booz-Allen & Hamilton, one of the largest management consulting firms in the United States.

segment markets is not widespread in corporate America.[27] In fact, the focus group[28] is still the dominant market test method in use, followed by limited product roll-out and concept testing.[29]

Figure 2 depicts five stages of new product development. The first two are covered in this technical note:

1. **Opportunity identification** in untapped markets is about the signals from within and outside an institution that give rise to new product ideas. An MFI's new market opportunities include increasing its product line's depth (new products and services to existing customers) and breadth (current products to new target markets[30]).

2. **Analysis and evaluation** deciphers opportunity signals to determine whether developing new products makes strategic sense based on an assessment of client needs, competitive threats, and its own institutional resources.

Once the decision is made to try out a new product, the companion technical note walks an MFI through the remaining stages of designing, testing, and launching new products. Emphasized in both notes and depicted in Figure 2 is that new product development is an ongoing process of refinement based on client feedback and market analysis. Successful new product development is as much about revising and repositioning existing products as they evolve as it is about innovation. It is the process as much as the features of the product itself, that will ultimately determine success.

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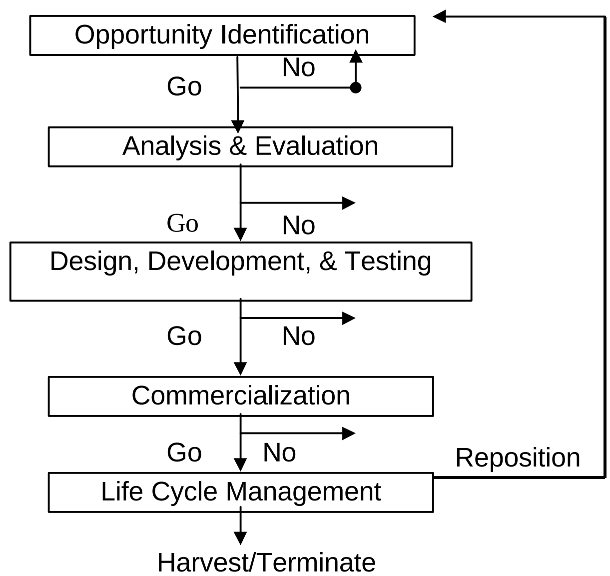
[27] Vijay Mahajan and Jerry Wind. "New Product Models: Practice, Shortcomings, and Desired Improvements," *Journal of Product Innovation Management*, vol. 10, January 1993, p. 37.

[28] See definitions in Attachment B. This method of market research is covered in the companion technical note.

[29] Robert J. Thomas, p. 140.

[30] A firm might also choose to develop products for new markets, but this diversification is typically undertaken by experienced organizations in later stages of development when they are better able to shoulder the risk. Philip Kotler, p. 79.

FIGURE 2:
TRADITIONAL APPROACH TO NEW PRODUCT DEVELOPMENT[31]



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[31] Derived from Glen Urban, John Hauser, and Nikhilesh Dholakia, *Essentials of New Product Management,* Englewood Cliffs, NJ: Prentice-Hall, Inc., p. 26; and *New Product Management for the 1980s.*

CHAPTER TWO

CONDITIONS AND MOTIVATIONS FOR NEW PRODUCT DEVELOPMENT

There are five types of companies:

- *Those who make things happen;*
- *Those who think they make things happen;*
- *Those who watch things happen;*
- *Those who wonder what happened; and*
- *Those that did not know anything had happened*

Philip Kotler, *Marketing Management*[32]

Competition can be either a boon or a boondoggle to an MFI, depending on how prepared it is for change and its ability to evolve to meet dynamic market conditions. This preparedness is about how well an MFI can anticipate and deal with change, as well as how agile it is in responding to an immediate crisis (such as a sharp increase in delinquency or desertion.) This chapter examines the different pressures that goad an MFI to expand its product line. The first half of the chapter discusses the signals from within the institution and externally from the marketplace (from clients and competitors) that are the source of new product ideas. The second half explains how an MFI might interpret these signals and, based on its capacity, decide whether to proceed with the product development process. This decision must also take into consideration how aligned certain product opportunities are with an MFI's own core competencies and its financial and social goals — all of which are covered in this chapter.

This chapter assists the reader to:

- Identify signals from customers that can spur new product ideas
- Decipher market messages to anticipate changes in customer demand
- Interpret internal financial trends that signal product refinement
- Undertake a strategic assessment to evaluate the competitive and social implications of launching a product
- Evaluate the institutional capacity (human resources, systems, and infrastructure) to undertake new product development

Product line extensions are part of a broader process of internal and external institutional analysis. Successful product development requires that an MFI balance market awareness with its operational capacity to meet client preferences. Offering new products is not always the appropriate response for an MFI facing a changed market environment. This analysis applies both to fast-growing MFIs that might expand their product lines too quickly or carelessly as well as to mature, monopoly MFIs that must analyze the risk of *not* diversifying.[33] This chapter is intended to help an MFI make its first go or no-go decision to embark on the process of product development further outlined in the companion technical note.

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[32] Philip Kotler, p. 62.

[33] An illustrative example is the Colombian microfinance company CorpoSol, documented in the Microenterprise Best Practices study, "The Rise and Fall of CorpoSol: The Challenges of Managing Growth," by Jean Steege, which simultaneously introduced three distinct products without pilot tests.

OPPORTUNITY IDENTIFICATION: MARKET DRIVEN APPROACH

Organizations develop new product ideas by anticipating customer needs or reacting to demands from clients or actions taken by competitors. Almost regardless of the source of the idea, an institution must be market driven — understanding its clients' needs and being mindful of its internal bottom line — in order to successfully develop new products. This orientation — what Otero and Rhyne have characterized as a financial systems approach to microenterprise[34] — is an important component of new product development. Among the principles that define this financial systems approach is a "market perspective that understands the preferences of the client group."[35]

This section discusses the financial systems approach of how an MFI becomes aware of opportunities for new product development. The first signals are those that come from the market — customers, competitors, and the environment within which an MFI operates—all of which have changed dramatically as the field has evolved. While some MFIs have looked upon the onset of competition as a crisis, dynamic marketplaces provide opportunities to gather new sources of information. The other set of signals come from inside the MFI: its own bottom line—the internal competitor to which transformed MFIs have begun responding. These signals are typically financial issues, and revolve around liquidity and profitability, which often prompt new product development.

Listening to Customers

Customers are clients who have some experience with debt and repayment. They have a more sophisticated understanding of an MFI, and their own enterprises have evolved since receiving their first loan. These empowered, knowledgeable customers know how to voice their demand and, increasingly, they understand that they have choice. Thus, a signal for new product development can come in the form of direct feedback to loan officers who have established relationships with these customers. This customer-provider interaction is often built into the methodology, as is the case with many group-based lending strategies. For example, the mission of SEWA Bank in India is to create "people's economic organizations." Accordingly, SEWA has helped organize its microenterprise borrowers into trade unions and smaller committees to address different needs, such as sourcing, networking, and bulk purchasing. During group meetings, ideas for new products are generated: "We have many forums in which women can talk — trade unions, executive committees, cooperative bank meetings; just by listening we hear what their needs are; that's how we get our ideas for new products."[36]

If credit officers are not attentive to this dialogue, or if they are unable to translate customers' needs into product refinements, negative signals can spur new product development.[37] When clients' needs are not met, an MFI will typically experience slowed growth as word-of-mouth marketing

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[34] Maria Otero and Elisabeth Rhyne. *The New World of Microenterprise Finance: Building Healthy Financial Institutions for the Poor.* Hartford, CT: Kumarian Press, 1994, p. 11.

[35] Ibid.

[36] Jaysyree Vyas, Managing Director, SEWA Sahakari Bank Ltd. Interview, 16 November 1997.

[37] Of course, if the need for capital is great and the MFI holds a monopoly, these negative signals will take much longer to surface, if they do at all.

dissipates. The signal that often prompts an MFI response is desertion, as frustrated customers look to the competition to meet their needs for lower rates, better terms, more convenient service, different products, and so on. Unfortunately, most MFIs do not carefully track the reasons clients leave, and lose a valuable information opportunity. Other negative signals could be increased delinquency or default, which triggers a loan officer follow-up with the borrower. Many MFIs do this after one day of arrears, including Banco Solidario (BancoSol), in Bolivia, and Cajas Municipales, in Peru.

This instantaneous delinquency trigger, which is part of most strong methodologies, can be a source of new product development, if an MFI can incorporate the valuable business information that late payment signals. A business might face repayment difficulties because of a change in cash flow needs (e.g., seasonality, rapid growth), external economic factors (e.g., industry downturn, recession), personal factors (e.g., sick family members) or, simply, because it was a poor credit risk. Understanding these differences is important because there may be mutually beneficial product development opportunities that can meet customer needs while improving the bottom line.

In particular, MFIs have addressed repayment problems brought on by a business cycle or a particular stage of growth by refining their products. In Thailand, the affiliate of Freedom from Hunger, for example, extended its typical monthly loan cycle from four months to six to accommodate the silk harvest, in which many of its clients were engaged. "We have to be responsive to the borrower's needs. Rice farming has a rapid cycle—four to five months—so short-term loans are easily serviced. With mulberry trees and silk worms, it takes longer. So rather than force our borrowers to sell bananas to meet rapid repayment schedules, we tailored the loan product to meet the need."[38] Similarly, Buro Tangail, in Bangladesh, is testing new credit facilities to accommodate its clients' different liquidity needs during various stages of growth. It is testing a supplementary loan system to provide additional working capital to businesses that are tight on cash during rapid growth phases.[39] Cajas Municipales de Peru offers a similar product, called parallel loans, which provides short-term working capital to seasoned borrowers for periods of high productivity.[40]

In almost all cases, these MFIs offer multiple loans only to clients with established records of repayments, as simultaneous loans to the same borrowers introduce certain risks. First, even borrowers with good credit records can get in over their heads, so the MFI must ensure that the client's capacity to pay covers the increased indebtedness created by simultaneous loans. In addition, customers can borrow from one source of funds to repay another, using the loan for refinancing rather than productive purposes. Although this practice may be justified to take advantage of attractive financing, it is speculative activity. Still, the MFI must be aware that a client's needs grow more sophisticated as their business expands, and modify financial products accordingly.

Real profit opportunities can be had by tailoring products to the evolving needs of clients. In addition to reduced delinquency, which inevitably comes when cash flow from operations is better aligned with repayment schedules, is the relationship that is built upon customer service. Loyal

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[38] Kathleen Stack, Senior Vice President, Freedom from Hunger. Telephone interview, 1 October 1997.

[39] Graham Wright. *Beyond Basic Credit and Savings: Developing New Financial Service Products for the Poor* (forthcoming), p. 15.

[40] Borrowers must be in good standing for at least one year. Parallel loans are typically used for inventory build-up during seasonal sales increases, such as before Christmas or at the start of school. Jill Burnett, *Cajas Municipales of Peru: An Organizational Review* (Calmeadow: forthcoming), p. 40.

borrowers are a source of profits for most MFIs because of borrowers' increased demand for new services, their lower risk of costly delinquency, and their invaluable word-of-mouth publicity, which has been demonstrated clearly by Bank Rakyat Indonesia (BRI).[41] As a customer's enterprise grows, so does its need for tailored financial services, adjusted terms, and new products. For example, Cajas Municipales de Peru offers automatic credit to clients with a proven repayment history,[42] which provides instant access to up to three loans within an established limit, and which can be adjusted based on client demand. The financial benefit to the MFI is threefold: increased sales to strong clients, reduced transaction costs because of streamlined credit assessment and delivery, and improved customer satisfaction and loyalty. "Cajas Municipales of Peru aims to build strong relationships with clients through good service."[43]

The Swaziland Business Trust similarly wanted to strengthen its relationship with its growing companies, so it designed an intermediate loan product with higher denominations and faster cycles for customers who had successfully made three consecutive rounds of loan payments. In a similar vein, many group-based lending programs will offer individual loans to borrowers who "graduate" from their program because of the unique needs of their businesses. More specifically, MFIs have learned from deserting clients that there was an unfilled demand for individual loans (versus group loans) of higher denominations. That is why BancoSol of Bolivia relaxed its restrictions on loan maximums and solidarity-group requirements to meet this market need. This new individual product allows BancoSol to retain its strong clients, with the added financial benefit of lending larger, more profitable loans.[44] In fact, most of the new product development by MFIs have been for the less risky, known quantities, or what Cajas Municipales of Peru calls "preferential" clients — borrowers who are essentially prequalified because they are demonstrated repayers.

Market Signals: Paying Attention to New Actors and Trends

With competition comes new ideas and opportunities for growth. Competitors themselves can be a resource, rather than a threat, to further educate and screen clients and to develop new product ideas. An MFI can copy a competitor's product offerings and then improve upon it, the way BancoSol created "catch-up" individual loans to stem the desertion of its clients to the neighboring Cajas de Ahorro y Prestamo Los Andes. BancoSol combined the best of its current product — the efficiency and accessibility with which it was delivered — with the flexibility of its competitor's loans, to go beyond the solidarity group methodology. An MFI can also pick up signals based on investors' intentions to back new players, much like the Chilean government subsidy that encourages

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[41] Reputation is BRI's main form of marketing. Marguerite Robinson, *Introducing Savings Mobilization in Microfinance Programs: When & How*, pp. 9–10.

[42] Borrowers who have averaged less than one day late for all payments during that year are eligible for automatic credit. Jill Burnett, p. 40

[43] Ibid., p. 41.

[44] Hermann Krutzfeldt, General Manager of BancoSol: "Marketing Strategies in a Competitive Microfinance Market." Presented at the Microfinance Network, 5th Annual Conference—Moving Microfinance Forward: Ownership, Competition, and Control, Alexandria, Egypt, 21 October 1997.

banks to enter the micromarket.[45] In anticipation of this competition, MFIs often develop new products or refine existing ones to reaffirm customer loyalty.

Demographic trends can also spawn ideas for new product development. Increasing urbanization can encourage an MFI to offer products that are better tailored to the business needs of the market. For example, BRI, after launching SIMPEDES, its voluntary rural savings program in 1984, introduced SIMASKOT, a similar product specifically for the urban market, based on the relatively higher growth of its branches in the cities. SIMASKOT offered higher return than its rural counterpart because its urban customers are more interest-rate sensitive.[46] Another demographic trend, the increased affluence of older segments of the population in some countries (coincident with improved health care and successful development strategies) has prompted new products from commercial and micro-size financial intermediaries. Just as U.S. financial institutions are trying to capitalize on the lucrative market of baby boomers[47] with retirement accounts and financial planning services, some MFIs, such as Banco Solidario of Ecuador, have begun introducing pension accounts.

Other macro-level economic, industry, or environmental trends also can create a demand for new products. Following are some examples.

- **Macroeconomic factors:** High inflation would spark a need for highly liquid savings products.[48] Not surprisingly, the majority of BancoSol's depositors keep small balances in the most liquid types of accounts and choose the U.S. dollar option to maintain value.[49] Other MFIs, such as Grameen Bank in Bangladesh and the Rural Finance Facility in South Africa, have responded to housing shortages in their markets by offering a residential credit product for their customers, especially since many microentrepreneurs run their enterprises from home.

- **Dominant industries** can affect local economies, as was the case with Prodem-Bolivia, which shifted away from ACCION International's typical practice of offering fixed amortization schedules for its products after it spun off many of its urban branches to BancoSol.[50] Left to serve rural areas of Bolivia, Prodem was subject to seasonal fluctuations of its agricultural-driven markets, which affected the cash flow of its clients' enterprises regardless of whether they were directly involved in this sector. Accordingly,

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[45] Robert Christen, Telephone interview.

[46] To compensate for the higher rate, SIMASKOT requires higher minimum balances.

[47] This pop-culture term refers to the rapid birthrate during the post-World War II era, when soldiers returned home to their wives. Most of the babies born during this population "boom" are turning 50 during this decade.

[48] For the same reason, BancoSol's U.S. dollar-denominated savings product was more attractive than the relatively less stable Bolivar product.

[49] Maria Otero noted, however, that since most developing countries operate in only one currency, the option of offering loans denominated in more stable, foreign currencies would be prohibitively expensive for many MFIs.

[50] BancoSol is a for-profit, regulated financial institution that was created by transforming part of its NGO parent, PRODEM, which still operates as an independent competitor.

Prodem refined its loan product to tailor repayment to the seasonal nature of the economy within which its microenterprises operated.

- **Public health:** The FINCA affiliate in Uganda developed a life insurance product to address the nation's high mortality rate. Partnering with a local commercial insurer to provide access to insurance to its members, FINCA takes a fixed percentage of the village bank loan as premium for life and limited disability insurance.[51]

- **Environmental factors:** SEWA Bank in India also introduced an insurance product after a survey of defaulted borrowers revealed that cyclones, floods, and other natural disasters wiped out their customers' resources. SEWA also realized how important it was for women to have landed assets, especially for their daughters' marriage dowries, and began offering a credit program to help its customers repurchase pawned property.

- **Technology** is also spurring new product development. In Swaziland, a number of players have creatively used the increased capacity and versatility of technology to reach new micromarkets. Recognizing the expense of building brick-and-mortar branches and staffing them, the designers of Swaziland Business Trust instead decided to use the existing bank infrastructure to reach countrywide.[52] Using technology that encrypts personal identification numbers on debit cards, Swaziland Business Trust created a mechanism to provide convenient, nationwide access by having banks install a simple terminal device that fits into the general teller environment. Existing technology also allowed it to design a back-end accounting system that kept track of lending transactions, and make daily reconciliations.

Technology can also provide more facile access to credit through efficient processing or streamlined loan analysis, as demonstrated by MFIs in Latin America. Banco del Estado in Chile has a management information system, set up by its staff of engineers, which automates some of the credit analysis and actual product design and tailors the repayment to the borrowers' projected income capacity.[53] Cajas Municipales in Peru is beginning to use automatic teller machines in some of its branches to reduce the delivery costs of its already streamlined automatic credit product, which offers borrowers who have been in good standing for a year instant credit analysis and access to capital. ADEMI, in the Dominican Republic, has also developed a credit card for its larger businesses.

Financial Signals: Looking within the Institution

These external signals are most noticeable when an MFI operates in a competitive market. The reality, however, is that new product development is often instigated internally on the basis of financial considerations. Preparing and analyzing monthly statements is not only critical for financial

[51] Michael McCord, Chief of Party, FINCA Uganda, telephone interview, 25 November 1997.

[52] Don Henry, Development Alternatives Inc., telephone interview, 30 October 1997.

[53] This type of credit scoring has enabled many large banks in the U.S. to move downmarket to serve smaller business needs. Robert Christen, telephone interview.

control, but it also can spawn product refinements or new offerings. Some of the financial signals that spur new product development are outlined below.

- **Liquidity:** Limited and excess liquidity can both serve as signals to an MFI to develop new products. Such a signal occurs, for example, when an MFI cannot meet its loan demand. An MFI might also determine that its funding sources are too concentrated or too expensive and seek to diversify to in order to manage its liquidity risk or reduce the cost of capital. Such liquidity issues typically drive an NGO's desire to transform into a regulated MFI, which can allow it to mobilize savings and possibly attract a broader array of private investors. Thus, new product development arises from a need to increase the source, stabilize the flow, or reduce the cost of capital funding. Accessing a stable source of funds to finance expansion were motivations for both BRI and BancoSol in their savings mobilization efforts. An MFI might, however, have excess liquidity following a capital infusion, successful savings mobilization campaign, or changes in the market demand for existing loan products, which can lead an MFI to develop new lending products quickly, thus reducing excess liquidity.

- **Profitability:** Profitability pressures arise when an MFI strives to maintain its self-sufficiency as an NGO, or to meet investors' and stakeholders' demands as a transformed financial institution. These financial demands can motivate an MFI to develop new products (other than the traditional working capital and fixed asset loans) tailored to the needs of lucrative repeat borrowers or to attract new clients in profitable markets. These profitability pressures typically arise in MFIs that are overcapitalized and in those that track returns by establishing separate profit centers, as explained below:

1. Overcapitalization: An overcapitalized institution can improve its profitability by increasing its leverage.[54] This is calculated by dividing risk assets by equity. Overcapitalization was one of the factors that led Banco Solidario de Ecuador — which was formed from the merger of two financieras — to simultaneously introduce a flurry of new products, including leasing, factoring, credit lines, and savings.[55] The desire to generate more attractive returns to shareholders by increasing leverage can prompt an MFI to develop new products.

2. Operational incentives: A desire to more closely manage returns can lead an MFI to separate profit centers, either geographically by branch or functionally by product or line of business. Both BRI and BRAC treat their branch units as separate profit centers that are accountable for their own bottom line. Whether this kind of accountability encourages product innovation depends on the incentives established. Even though BRI, for example, has a profit sharing plan

[54] In this way, financial leverage measures how many dollars of assets an institution is able to deploy profitably for each dollar invested by its shareholders or other suppliers of capital.

[55] Following this merger, investors put pressure on Banco Solidario de Ecuador to improve its profitability because they wanted to see returns sooner than would occur if loans were offered in a traditional step-lending method. Cesar Lopez, Senior Director of Latin American Operations, ACCION International, Interview, 25 July 1997.

with its employees, in order to prevent fraud, loan terms are rigidly standardized and interest rates are not negotiable.[56] BRAC, in contrast, takes a decentralized operational approach that encourages program organizers at branch offices to meet regularly with their customers ("members") and to identify new programs. Both programs seek financial self-sufficiency (the equivalent of "profitability" in conventional finance parlance).

DECIPHERING THE SIGNALS

Once an idea for new products arises, an institution must assess whether it is prepared to embark on the lengthy and dedicated process of new product development. This initial "inventory" of an MFI's physical and human resources is a crucial step to ensure buy-in and support throughout the organization, which will be critical to assuring successful product launch. Accordingly, the process is done twice, once before pilot testing, because it is such a resource-intensive endeavor; and once after, because the market research might indicate a need for additional resources and skills for implementation (covered in the companion technical note, "New Product Development for Microfinance: Design, Testing, and Launch"). The initial evaluation—required for an MFI to decide whether to proceed with the product development process—involves an analysis of physical resources, competitive strategy, and social and financial goals.

Strategic Assessment: Goals and Mission

Once an opportunity has been identified, an MFI should question whether it is appropriate to undertake the initiative. Among the strategic factors an MFI should consider are:

1. **Core competencies:** Most formal financial institutions will define their competitive strengths in terms of core competencies. For an MFI, these include its methodological approach, staff skills and orientation, and corporate culture. In Bangladesh, for example, ASA has distinguished itself as an efficient, low-cost provider. Its competitor, Buro Tangail, differentiates itself by offering a diverse line of products to meet unique business needs. While no MFI should lock into a particular strategy, it should consider the challenges it will confront by stepping outside of its established area of expertise. For example, for a transformed microlender to begin mobilizing savings requires a different market orientation and image. An MFI must decide if a product will complement its current mix or if it will stretch it too far afield, as was the case with CorpoSol, in Colombia, when it introduced three new products outside its area of expertise.[57]

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[56] BRI had problems with loan officers taking bribes "in exchange for arranging "sweet deals," such as low interest rates with a long lag time before repayment," says Mr. Suharsono, Managing Director of BRI, in his "Fraud and Internal Control" presentation at the Microfinance Network, 5th Annual Conference, Alexandria, Egypt, 21 October 1997.

[57] The three microfinance projects were Mercasol, which provided lines of credit for the purchase of supplies via a retail outlet chain; Agrosol, a rural credit product with repayment schedules that were distinct from the urban program for larger borrower groups; and Construsol, for financing home improvement. CorpoSol had little experience in either retail credit or the rural marketplace. For a fuller discussion of the CorpoSol case, see the forthcoming Microenterprise Best Practices publication by Jean Steege, "The Rise and Fall of CorpoSol: The Challenges of Managing Growth."

It is for this reason that FINCA has to date not diversified its front-end products, because its core competency is about delivering its village bank methodology to a specific target market. [58] “We have a recognized comparative advantage in serving a segment of the population whose needs were satisfied with the standard village banking product. Though there is a small proportion of members who want to grow, we weren’t ready to abandon our core focus on poverty alleviation.”[59] FINCA instead focused its energies on diversifying its back-end products, including credit training, oversight, and delivery systems. In so doing, FINCA developed its ancillary products in the form of better customer service and improving security of client deposits. In a sense, serving these client needs and developing streamlined, replicable operations were more a part of FINCA’s core competency than modifying a product to serve a niche market. FINCA has positioned itself in the market as a specialized provider of village banking loans, not a one-stop-shop for a menu of financial services.

2. **Competitive strategy:** An MFI needs a strategy if it is faced with competitive threats. It might decide to focus on a particular niche and concentrate on a circumscribed customer base or preempt and secure the larger market share before its competitor does. This latter strategy might require an MFI to capitalize on first-mover advantages, building a strong relationship with customers so that they are less likely to switch just because the competitor offers lower rates, for example. This resource-intensive relationship building often involves a “loss leader” strategy in which an MFI invests more money in its customers up front (through special promotions or tailored services) in hopes of winning their loyalty.

   Another competitive strategy might involve an institutional reorientation, such as occurs when a traditional microlending organization tries to transform into a more comprehensive financial services organization. It might be motivated to launch a new product to engender an entrepreneurial, market-driven culture, which is necessary for a for-profit, regulated financial intermediary to succeed. In addition, it might offer certain products to convey an image, even if the products are not profitable. For example, Cajas Municipales in Peru allows both customers and nonclients to pay water and electricity bills, school tuition, and municipal taxes through their branches, even though these staff-intensive services are costly to administer. They make these service available because they are “an important client service and help to develop our public image as part of the financial system.”[60] Convenience and variety are definite competitive advantages in the microfinance world, as customers prefer one-stop shopping for financial services. Cajas Municipales has lost depositors to other bank institutions because those competitors offer checking facilities as well.[61]

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[58] Each FINCA village bank offers four-month loans with equal installments paid at the weekly group meetings, at a fixed and (within a given program) unchanging rate of interest. However, many other village banking models have adjusted terms based on local market needs.

[59] Till Bruett, Manager of Policy and Program Development, FINCA International. Phone interview, 25 November, 1997.

[60] Jill Burnett, p. 18.

[61] Ibid., p. 8.

3. **Financial considerations:** Pilot testing will determine if the revenue of a new loan product will cover the additional costs of implementing it and over what time period.[62] Like most investments, launching a new product will not generate an immediate return for an MFI. As an MFI transforms into a for-profit institution with private investors, each of whom has varying degrees of patience, there may be pressure for relatively quick payback. Other financial considerations are whether the new product complements or cannibalizes existing products. In other words, whether the new product simply shifts revenues between products so that customers buy the new one instead of — rather than in addition to — the existing products. Such has been the case in some group-based lending methodologies, including a few ACCION affiliates, which introduced individual lines of credit with poor criteria for differentiation among clients.[63]

   But management could undertake an intentional cross-subsidization. An MFI might, for example, offer a lucrative product, such as larger-scale loans or consumer credit, which will help maintain a possibly less profitable product, but which has strong client support (e.g., reaching a particular market segment, expanding smaller loans to poorer clients, or retaining good customers.) Another strategic rationale for initial cross-subsidization is the first-mover advantage of getting an early foothold in a particular market. Nonetheless, the benefits of the cross-subsidization strategy — consumer loyalty and social impact — must be weighed against social and financial perils, in terms of mission drift and masking operational inefficiencies. The two issues are related: in the latter, the pressure to reduce the costs of delivering a particular product might be eased if proceeds from another product are helping to sustain or cover up operational inefficiencies. Accordingly, an MFI might become dependent on pursuing the more lucrative products to help them stay afloat, even if the products cause them to drift away from their more socially needy, core market, which they were initially designed to serve.

4. **Social impact/mission:** The issue of mission drift focuses on the social motivations and effects of introducing new products. MFIs often undertake social as well as financial analyses of the implications of new product development. For example, the debate between client retention and graduation (if indeed the formal sector is truly prepared to absorb the seasoned microentrepreneur) has social and financial implications. Product development is often completely in line with an MFI's mission by serving client needs more comprehensively or reaching new market segments. For example, SEWA Bank in India designs different credit and savings products to accommodate the "full life cycle of a woman: to expand a business, we offer short-term working capital; for housing repairs, medium-term credit; for emergencies, we offer very liquid savings accounts; for her children's marriage or to plan a pilgrimage, we have medium-term deposit accounts; and long-term savings for her retirement."[64] SEWA Bank has also designed a number of insurance products for the unique characteristics of its target market (women) to cover postnatal and prenatal maternity needs, and disaster relief during cyclones and floods. Social and financial goals are aligned, though such is not always the case. For example, ADEMI, in the Dominican Republic, had a profitable, donor-driven opportunity to offer larger loans to small enterprises, rather than to microenterprises, which it undertook even though it

[62] To undertake this kind of cost/benefit analysis to make an informed financial decision, the MFI must separately track the cost and income of the product, segregating it from the rest of the portfolio, during the pilot phase.

[63] Carlos Castello.

[64] Jayshree Vyas, Managing Director, SEWA Sahakari Bank Ltd.

pulled the MFI away from its original target market.[65] The point is not to promote the primacy of either financial or social goals when they are at odds, but rather to encourage a thoughtful consideration of the real tradeoffs that must sometimes be made.

5. **Stakeholder analysis:** Whether financial or social goals receive priority depends on the varying levels of control and power held by different institutional stakeholders, all of whom will have different objectives that will influence the decision to introduce new products. Sometimes internal stakeholders (management and staff) and external stakeholders (investors, shareholders, board members, parent company) are aligned because of well-developed incentives and strong governance. However, there may be resistance to the introduction of new products from:

    - Investors, based on the changed risk profile of the portfolio or initial financial loss;
    - Staff, based on the increased burden of work and fear of change;
    - Board members or veteran managers, based on loyalty to a particular methodology; and
    - Parent companies, based on competitive threats.

Thus, new product development will require planned and compelling justification (depending on the strength of the resistance) to get the necessary buy-in.

Institutional Assessment: Having the Capacity to Undertake Product Development

Once an MFI has decided that it makes strategic sense to diversify its product line, it must assess the practical issues of the resources it requires for such an undertaking. In evaluating its capacity to handle an additional product, an MFI must examine the following major items:

1. **Staff:** New products might require specialized expertise or a more highly educated credit officer, depending on the complexity of the product. An MFI must assess whether its current credit officers can be trained to deliver the new product, or if it will have to hire new, more experienced staff. At issue is both the staff skill level (in terms of experience and education) and their willingness to modify their job or accept increased responsibilities. An MFI must think carefully about training and incentives to ease the transition because there is often resistance to change.[66]

2. **Delivery channels:** If an MFI is going to successfully expand its product line, it must have sufficient capacity within its delivery channels to market and distribute the new product. These delivery channels include the physical infrastructure, which includes a branch system with extensive coverage in the target market area that provides easy access to customers. If an MFI's coverage area is limited, it can partner with affiliate organizations that can market and deliver the product. Freedom from Hunger, for example, partners with local credit unions to deliver larger

[65] ADEMI negotiated with its donors to lend the revolving proceeds to microentrepreneurs, once the small business loans were repaid.

[66] The companion technical note, "New Product Development for Microfinance: Design, Testing, and Launch," covers staff training and incentive schemes to implement new products.

loans for graduates of its solidarity groups. An MFI should not build expectations among its customer base unless it can meet the demand it elicits. Few things damage an institution's reputation more than unfulfilled promises, especially for a transformed MFI trying to build its image as a professional, financial services intermediary.

3. **Systems:** An MFI's management information system (including both accounting and portfolio monitoring) needs to track, manage, and in some cases disburse the new product. A new product will require separate bookkeeping systems at first to track demand and analyze profitability. Back-office systems might need to be versatile if the new product has nonstandard payment terms or other unique characteristics that differentiate it from existing products. For example, Buro Tangail is experimenting with supplementary loans and prepayment facilities flows (in the form of cash crunches and excess liquidity, respectively), which allow its member borrowers to manage working capital. During its pilot phase, an MFI must determine whether its systems can handle the disbursements and collections necessary for the fluctuating terms of such loan products.

4. **Risk management:** While diversification usually reduces portfolio risk, new products can create liquidity problems if they are not managed carefully. For example, introducing highly liquid savings accounts means that an MFI must manage its capital carefully to respond to sudden withdrawals by depositors. Also, if an MFI introduces longer-term credit facilities, it must ensure that it has other sources of short-term capital to meet its interim cash needs. In addition to this "term" matching between assets and liabilities, an MFI must measure inherent risks in certain loan instruments. For example, issuing lines of credit, especially those considered "ever green," in which the loan is continually rolled over (rather than the balance being paid in full and a new loan issued) are riskier than fixed asset or term loans. An MFI might be able to shoulder this risk, but it needs to have robust management information and accounting systems, in addition to skilled, responsible staff for periodic portfolio monitoring. In general, there is a trade-off between the MFI and the client in meeting their respective needs for cash flow.

5. **Training procedures:** Staff need to be trained on the specifics of the product, how to promote it to customers, and how to track it. MFIs that offer a monoproduct might use on-the-job training, which is generally inadequate, when diversifying a product line. Manuals will need to be developed and courses designed in order to ensure quality implementation. Other MFIs have used dedicated mentors (or floating specialists) who travel between branches, offering on-the-job training to other credit officers. Thus, training is a staff-intensive but critical part of new product development to which an MFI must devote resources.

An MFI must develop a specific plan to supplement its resources if it is deficient in any of these areas before it embarks on the product development process. If, for example, an MFI determines it has insufficient delivery channels to undertake new product development, it might consider opening new branches or partnering with existing institutions to temporarily establish a geographic infrastructure. Moreover, an MFI might decide to train its staff to prepare them for an expanded product line. For example, the chief of party of FINCA Uganda brought in a business school professor from a local university to teach a four-day training session on the basics of marketing. "My loan officers did not understand how to sell a product. We needed to establish a marketing mentality."[67] Understanding an organization's readiness to undertake new product development is a critical piece in the decision-making process.

[67] Michael McCord, Chief of Party, FINCA Uganda.

CONCLUSION

This chapter outlined different types of signals that often illicit new product ideas. An MFI should not, however, treat these signals as a indication to automatically embark on an expansion of product lines, nor to determine that new product development is forever beyond the scope of an MFI's capability. The material in this chapter should assist an MFI to undertake its own self-analysis in determining the appropriateness of evolving its products based on its stage of growth. If an MFI is not currently prepared to continue the product development process—because of staff resistance, institutional limitations, or other reasons—then there are a number of steps it can undertake to bring about organizational change. This process of organizational adjustment to create an institutional environment that is ripe for innovation is the topic of the next chapter. For those MFIs that have thought through the strategic, financial, and social implications and are ready to proceed with product development, they can move directly to the companion technical note, "New Product Development for Microfinance: Design, Testing, and Launch."

CHAPTER THREE

INSTITUTIONALIZING INNOVATION

Some people look at the world the way it is and ask "Why?"
I dream of things that have never been and ask, "Why not?"

Robert F. Kennedy

If an MFI determines that it has insufficient support or capacity to develop product ideas, it can refine its institutional capacity and readiness to enable it do so in the future. More specifically, for an MFI to notice the internal and market signals outlined in the previous chapter, it must have the structure and culture to translate competitive information into strategy. Accordingly, this technical note concludes with suggestions[68] on how an MFI can establish an organizational culture that is *entrepreneurial*, where innovation is encouraged and ideas flow freely, and *client-centered,* where improved products and services focus on high customer satisfaction. Such an organization is better positioned to notice and absorb the external signals from clients and competitors that should drive innovation and high-quality service. An MFI can create a climate of creativity by modifying its operating procedures, organizational structure, and governance systems.

This chapter assists the reader to:

- Decide whether to proceed with the remainder of the new product development process ("New Product Development for Microfinance: Design, Testing, and Launch")
- Identify four operating procedures that will make an MFI more attuned to signals for new products
- Understand how flat organizational structures facilitate product innovation
- Identify three features of organizational culture that are more tailored for new product development

SYSTEMS AND OPERATIONAL PROCEDURES

Many financial organizations establish systems and procedures to help them generate and detect signals for new products. Regular portfolio reviews can uncover rich information about untapped demand in existing markets. The most useful portfolio reports are disaggregated by product type and geographic region to identify potential market opportunities. These tracking systems can be produced from an MFI's management information system and made part of regular activity reports that are set up to monitor a program's progress. Typically, such reports will provide updated measures on loan demand and average loan size, operating efficiency (expenses as a percentage of average portfolio), staff productivity (such as number of clients or loans per credit officer), delinquency, leverage, and earnings, all of which can provide signals about product performance. It is critical, therefore, that these reporting systems be accurate, up to date, comprehensible, and accessible (i.e., user friendly) to staff and management if they are to support new product ideas.

[68] A complete discussion of orchestrating organizational change is beyond the scope of this paper, but successful models exist. See, for example, Chapters 2 through 4 in *Managing Growth: The Organizational Architecture of Microfinance Institutions* (Washington, DC: Microenterprise Best Practices Project, July 1997), by Craig Churchill.

MFIs also have anecdotal ways of tracking loan demand and customer satisfaction. The client-credit officer relationship is often an MFI's most valuable asset in designing new products because client feedback is unfiltered information and can be used to refine product offerings. In fact, SEWA Bank of India identifies as one of its main sources of product ideas the simple act of listening. As their managing director explains, "when women get together they talk about their needs. At SEWA, the [client] is in the center. She is the source of product ideas."[69] In fact, SEWA, actively consults with its group leaders to stay abreast of its customers' needs. Similarly, in Pakistan, Buro Tangail organizes members' consultative groups to generate similar client feedback. Credit officers, thus, are an important source of signals for new products.[70] In fact, commercial banks increasingly encourage credit officers to voice their ideas during weekly staff meetings, periodic strategic planning sessions, or less frequent management retreats.[71]

Another valuable procedure that most conventional banks — but few MFIs — undertake are exit interviews with clients who have decided to terminate their relationship with the financial institution — either temporarily or permanently. Exit interviews provide valuable information about market realities and possible product shortcomings that can sometimes be addressed in a mutually beneficial manner. Accordingly, Banco Solidario in Ecuador and FAMA in Nicaragua hold focus groups with exiting clients.

Most banks are successful at getting customer feedback when the exit interview is voluntary. Feedback is less valuable when an MFI terminates a loan, as occurs in default. But some MFIs, especially those that employ group-based lending strategies, maintain strong relationships even with their delinquent clients. SEWA Bank in India, for example, will periodically survey its defaulters to determine causes of delinquency. Learning that most defaults were brought on by physical and natural hardships (family needs, political upheavals, and natural disasters), SEWA designed various insurance products to support its customers during adverse times.[72]

Some MFIs have product development systems built into their methodology, in which the product line expands as the organization evolves. Some turnkey methods involve "rolling out the carpet" for the product as soon as the MFI hits certain milestones, such as number of years in operation or loan volume. For example, Cajas Municipales in Peru established a turnkey product that starts with savings accounts and leads to pawn, personal, and business loans.[73] Each enterprise grows at a different rate depending on its needs. Accordingly, an MFI's program must evolve according to its members' growth. Such organizational growth markers can serve as a signal for new product development.

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[69] Jayshree Vyas, Managing Director, SEWA Sahakari Bank Ltd.

[70] Graham Wright, p. 12.

[71] One danger of relying too heavily on these type of subjective signals is that loan officers will sometimes have a vested interest in the status quo, and thus will "conveniently misinterpret client interests." Carlos Castello.

[72] Jayshree Vyas. SEWA surveyed approximately 500 defaulted borrowers before designing the insurance product.

[73] Jill Burnett, p. 11.

ORGANIZATIONAL STRUCTURE: COLLAPSING LAYERS AND CROSS-FUNCTIONAL COLLABORATION

Ideas for innovative, market-driven products can be hampered in hierarchical organizations, where top managers are separated from field officers by bureaucratic layers. In contrast, flat organizations generally take a participatory approach to management, in which lower-level staff are empowered to make decisions for which they are accountable. Flat organizations — the goal of organizational restructuring efforts among conventional banks — allow ideas from the field and feedback from clients to flow more easily into operational systems.[74] Flat organizations encourage interdepartmental, or horizontal collaboration, which is key for introducing new products. It also allows product champions — the staff who identify a profitable market opportunity and oversee its development — to pursue their ideas with the faith that their efforts will not go unnoticed.[75]

The Self-Help Credit Union (formerly the Center for Community Self-Help), one of the most successful development credit unions in the U.S., has collapsed traditional management layers to encourage self-initiative.[76] With encouragement from its entrepreneurial founder, Martin Eakes, Self Help took the risks to diversify from the concept of worker-ownership into financing child care facilities and microenterprises.[77] Many of Self Help's staff have diverse responsibilities that allow them to avoid tunnel vision, or what Robert Christen refers to as "birthright mentality," in which an MFI gets locked into the methodologies with which it was born.[78]

Other financial institutions have created separate, stand-alone R&D departments to undertake market research and product development. Many conventional banks have a team of analysts who are dedicated to researching unserved market niches and uncover untapped pockets of profitability. Some larger MFIs, such as BRAC, also have centralized research divisions, but they are usually geared to investigating particular industries or programs that will spur economic development.[79] Some of these more market-oriented MFI R&D efforts involve having staff in branch offices undertake field research. This field integration is key if an MFI is to create a dedicated R&D effort, because ideally, new product ideas should flow inward from the market rather than being decided in centralized offices. Whether or not an MFI decides to create a separate department that focuses on R&D, the creation of a new product will nonetheless involve interdisciplinary collaboration in order to integrate the critical functions that allow successful product management. Products that have the highest rate

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[74] See Churchill, *Managing Growth: The Organizational Architecture of Microfinance Institutions*, pp. 60–61.

[75] The important role of product champions in the development process is covered in the companion technical note.

[76] Mitty Owens, Director, Microlending, Self-Help Credit Union. Telephone interview, 28 October 1997.

[77] Bob Schall, Director, Commercial Lending, and President, Ventures Fund, Self-Help Credit Union. Telephone interview, 21 October 1997.

[78] Robert Christen, telephone interview.

[79] BRAC established its Research and Evaluation Division in 1975, four years after the program's inception. BRAC 1996 Annual Report, p. 11.

of success[80] are those that are developed by conventional businesses using cross-functional teams that have strong leaders (or product champions) and followers that have adequate incentives.[81]

GOVERNANCE STRUCTURE AND CONTROL

Establishing the incentives that will allow product champions to develop their ideas is tied to the governance structure of the organization. Investors and board members of formal MFIs will encourage market-driven strategies and hold management accountable for performance. This orientation can make an MFI more aware of market opportunities than can a publicly funded NGO, because the owners, investors, and other new stakeholders become a new source of signals from customers. For example, private investors are more likely to view losing seasoned borrowers as desertion rather than graduation, and accordingly endorse strategies to retain them: "The key is to get people to renew their loans . . . It's critical that the R&D department stay ahead of the [market] changes."[82] In addition, commercial MFIs have board members from conventional businesses who anticipate competitive threats and come up with active steps, as occurs in product development.

The NGO structure has its own set of advantages, based on the actors who signal the need for new products. First, NGOs can take more risks with new products because donors measure return in both social and financial terms. Although NGOs do not have the flexibility to carelessly spend money lest they threaten future donations, they are usually not under the same time pressure as commercial MFIs to show immediate financial return. NGOs do not have as much at stake if another MFI takes up the NGO's R&D efforts, which is a common occurrence because donors encourage the sharing of best practices. In contrast, a commercial MFI can suffer greatly and have difficulty recouping its investment if a copy-cat competitor exploits its R&D investment and introduces a similar product. Thus, NGOs have more flexibility to act on new product ideas offered by donors and management.

Yet these signals are insufficient if MFI staff do not have the resources, control, and incentives to act on them. Entrepreneurial risk taking is part of organizational culture, but specific control issues can encourage product innovation. For example, management should be flexible in order to reallocate resources to profitable, new product ideas.[83] For example, branch offices could be eligible for additional capital if they successfully introduce a new product that increases sales over a particular time period. BRI, for example, manages the capital needs of its lending units by regulating the transfer prices for capital. By increasing the cost of capital, branches are given incentives to

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[80] Robert Thomas. *New Product Development: Managing and Forecasting for Success*, New York: John Wiley & sons, p. 15.

[81] Cross-functional teams, product champions, and staff incentives for new product development are all discussed in further detail in "New Product Development for Microfinance: Design, Testing, and Launch."

[82] Alex Silva, General Manager of Profund, interview, 2 October 1997.

[83] Bob McNeely, Senior Vice President, Union Bank, interview, 24 September 1997. Control of resources can be as strong an incentive as financial reward because of the prestige that is associated with such command.

mobilize savings, which they will typically do by adjusting existing terms or designing new products.[84]

ORGANIZATIONAL CULTURE: CREATING ENTREPRENEURIAL, CLIENT-DRIVEN INSTITUTIONS

Organizations, like countries or demographic groups, have distinct cultures that differentiate them from others. Moreover, there is no proper organizational culture; each develops in response to the specific realities of the market in which it operates and is shaped by the goals of its founders. Nonetheless, to paraphrase Robert Kennedy's words at the beginning of this chapter, some organizations are tailored to take the risks that are required to develop new products. This openness is part of the culture an MFI establishes through its company norms and values. It includes communication (whether critical thinking and open dialogue are encouraged) and decision-making (whether authority is delegated to enable risk taking) Described below are some organizational features that characterize entrepreneurial financial institutions and foster the development of new products.

- **Fluid information flow:** An advantage of flat organizations is the free flow of ideas, which leads to product innovation, both horizontally across departments, as well as vertically between senior management and the field. If field workers have only discretionary financial control authority, communication with senior management becomes even more important. Management can encourage this critical communication through regular staff meetings, management field visits, organized retreats, or informal open-door policies. The communication format is unimportant, but the free flow of information and ideas does matter.

- **Company norm of risk taking:** The ease with which honest communication between management and field officers can take place is driven by management tolerance for risk and dissent. Management can create open dialogue by encouraging critical thinking. BRAC, for example, has tried to push accountability and responsibility down to the branch level, training its regional and branch managers in forecasting and budgeting, to make each unit a separate profit and loss center. BRAC is also challenging its field officers to think critically about managerial policies and encouraging them to question superiors, something that is antithetical to BRAC's (and more generally, Bangladeshi) culture.[85] These changes have been coincident with recent efforts by BRAC to develop new products,[86] including a voluntary savings instrument and an enterprise loan for successful village borrowers to start restaurants.

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[84] Consultative Group for Assisting the Poor Working Group. *Comparative Analysis of Savings Mobilization Strategies: Case Study of Bank Rakyat Indonesia (BRI), Indonesia.* Washington, D.C.: The World Bank, forthcoming.

[85] Janney Bretz Carpenter, Managing Director, Shorebank Advisory Services, telephone interview, 12 November 1997.

[86] Most of BRAC's new "programs" are development driven to diversify economic activity for sustainability, health, and education reasons.

- **Valuing innovation:** What is true in human nature holds for corporations: change is difficult. This truism is especially relevant in financial institutions because of the risk-averse nature of the industry. Add to this NGO resistance, which has been defined by stability rather than the dynamism of competition, and the difficulty in inspiring innovation becomes clear. Most conventional financial institutions have encouraged product innovation through employee recognition, which is done deliberately at the Center for Self-Help, in North Carolina. "Having a 'product champion' is not only key to successful implementation, it becomes part of your identity."[87] Most product champions get the attention of the charismatic founder, Martin Eakes, and thus the entrepreneurial distinction becomes a source of prestige because it is clearly valued by the company.[88]

Implementing these suggestions requires patience and dedication from top managers. The goal is not necessarily to launch new products, because this path is only appropriate for certain MFIs during particular stages of growth and facing specific market realities. As Marguerite Robinson notes, "remember that the successful MFI is a financial institution — not a supermarket . . . Most microfinance clients will prefer expert microfinance service to a mix of mediocre services."[89] Creating a customer-focused, entrepreneurial environment will have benefits far beyond any new products or ideas that are generated. The outcome will result in an organization that can focus its energies on continually improving its operations and products to better serve its customers and help insure its long-term sustainability.

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[87] Laura Benedict, Director, Community Facilities Fund, Self-Help Credit Union, telephone interview, 14 October 1997. Laura developed a new credit product for facilities financing.

[88] Bob Schall, Director, Commercial Lending, Self-Help Credit Union, telephone interview, 21 October 1997.

[89] Craig Churchill, ed. *Microfinance Network 5th Annual Conference Summary—Moving Microfinance Forward: Ownership, Competition, and Control of Microfinance Institutions.* Washington, DC: Microfinance Network, 1998.

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ANNEX A

RESEARCH BACKGROUND

RESEARCH METHODOLOGY

Although some MFIs have undertaken new product development, rarely has the process been systematic or methodical. Accordingly, the research for this technical note focused on analyzing and documenting the practices of conventional financial institutions. Although companies in industrialized marketplaces typically have many more resources to devote to R&D and marketing, there are applicable lessons for MFIs in developing countries as well. In a dynamic and competitive marketplace, institutions must spend money to make money. The types of institutions that were consulted in developing this technical note and the rationale for interviewing them is described below in order of emphasis.

Conventional Banks

Some leading commercial banks in the U.S. were tapped for their sophisticated knowledge and experience with new product development, even though they are not directly comparable with MFIs. In the face of market[1] and regulatory[2] pressures, many banks have in fact been moving aggressively downmarket with new products to serve the needs of the long neglected small business sector. Despite great operational differences, both ends of the spectrum are facing competitive threats and struggling to meet the needs of the small business borrower. Few conventional banks, however, have moved far enough downmarket to serve the microentrepreneur.[3] In addition, some banks have begun to expand into developing countries—euphemistically referred to as emerging markets—using similar development processes. Among those interviewed for this technical note included representatives of Citibank, Bank of Boston, Union Bank, America's Trust, and another of the top ten largest national banks, who asked to remain anonymous.

Hybrid Financial Institutions

The term "hybrid" describes the dual social and financial goals pursued by these U.S.-based community development financial institutions (CDFIs). Although most of the CDFIs interviewed are considerably larger than typical MFIs, these hybrids are similar to MFIs in their motivations and stage of development. Among the CDFIs that were generous with their time and information were Southshore Bank (Illinois), Self-Help Credit Union (North Carolina), the community development bank affiliates at Bank of America (California), Chase Manhattan (New York), and First Community Bank (Massachusetts) (see list of interviews below.) Those surveyed (mostly via telephone and electronic mail conversations) typically were senior credit officers or portfolio managers who oversee a staff of loan officers or are part of a dedicated marketing or R&D division that focuses

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[1] Banks have watched their more affluent client base being won away by nonbank competitors, including mutual funds, credit card companies, and other nonbank financials.

[2] The Community Reinvestment Act, passed in 1977, is a U.S. federal law that stipulates that "regulated financial institutions have a continuing and affirmative obligation to help meet the credit needs of the local communities in which they are chartered."

[3] Though still the exception rather than the rule, commercial banks venturing into microfinance markets in developing countries is the subject of a significant research effort under the Microenterprise Best Practices Project.

exclusively on identifying new product opportunities. The resulting information was then adjusted for the realities that face MFIs in developing countries.

Microfinance Institutions

A sample of mature MFIs that have recently developed new products were based on their geographic diversity and the following new product categories:

- **Client-tailored loan products:** lines of credit versus amortized term loans, credit and debit cards;
- **Ancillary financial services:** insurance, pensions, factoring, and licensing;
- **Individual and group methodologies:** how MFIs use solidarity groups and how village banks deploy individual loans;
- **Voluntary savings services:** [4] how an MFI exemplifies some of the best practices in the field in systematic approaches to developing new products.

The MFIs highlighted in this technical note do not fully represent the diverse new product development activities that have been undertaken.[5] Accordingly, the MFIs that were examined should be taken neither as an endorsement of a particular institutional approach, nor should exclusion be taken as repudiation of another.

INSTITUTIONS INTERVIEWED AND EXAMINED

Conventional Financial Institutions

1. Banco Popular de Ecuador and America's Trust Bank: Enrique La Motta, Consumer Finance
2. Bank of Boston: Melody Bohl, Vice President of Marketing
3. Chase Manhattan: Elliot Hobbs, Real Estate Lending; Michael Flemming, Strategic Planning
4. Citibank: Ann Miles, Financial Services; David Davenport, Community Development Finance

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[4] Savings mobilizations is covered in depth in separate MBP research and future publications dedicated to this topic. Moreover, the macroeconomic, regulatory, and political conditions—in addition to the institutional strength—that must be in place to enable savings mobilization, limit the audience of MFIs appropriate for this particular product. (Marguerite Robinson, *Introducing Savings Mobilization in Microfinance Programs: When and How*, pp. 2–3.)

[5] The main criterion used in selecting the MFIs to examine was how systematic they were in their approach to developing new products. Strong efforts were made to have as broad a geographic and methodological coverage as possible within the different product categories.

5. Union Bank: Robert McNeely, Vice President, Community Development Department

6. Top Ten U.S. bank: Anonymous small business lending officer

Community Development Financial Institutions

1. Bank of America, Community Development Bank: Susan Nakata, Vice President, Small Business Lending

2. Chase Community Development Bank: John Stokes, Small Business Lending

3. First Community Bank (affiliated with the Bank of Boston) Jeffrey Zinsmeyer, Director of Small Business Lending

4. Self-Help Credit Union: Mitty Owens, Microlending Director; Laura Benedict, Community Facilities Financing Director; Bob Schall, Commercial Lending Director

5. Southshore Bank: Janney Bretz Carpenter, Managing Director, Southshore Advisory Services; Leslie Davis, Vice President, Commercial Lending; Karen Bowman, Commercial Lending Marketing Analyst

Microenterprise Finance Institutions

People whose names appear in italics were not interviewed; their statements and views were gleaned from transcripts of presentations they have made.

1. Alexandria Business Association—Egypt: *Nabil A. El Shami*, *Executive Director*; Craig Churchill, Calmeadow

2. Association for Social Advancement—Bangladesh: *Shafiqual Haque Choudhury, Chief Executive*

3. Banco del Estado—Chile: Bob Christen, Microbanking Advisory Services

4. Banco Solidario—Bolivia: *Hermann Krutzfeldt, General Manager*; Carlos Castello and Jean Steege, ACCION International

5. Banco Solidario—Ecuador: Cesar Lopez and Lisa Lindsley, ACCION International

6. Bank Rakyat Indonesia (BRI): *Jarot Eko Winarno*, *Product Development Manager*; Marguerite Robinson, Harvard Institute for International Development

7. BRAC—Bangladesh: Janney Bretz Carpenter, Shorebank Advisory Services

8. Buro Tangail—Bangladesh: Graham Wright, independent consultant

9. Caja de Ahorro y Prestamo, Los Andes—Bolivia: Alex Silva, Profund

10. Cajas Municipales de Ahorros y Creditos (CMAC)—Peru: Jill Burnett, Calmeadow

11. CorpoSol—Colombia: Jean Steege and Carolos Costello, ACCION International

12. Foundation for Integrated Agricultural Management [FIAM, former Freedom from Hunger affiliate]—Thailand: Kathleen Stack, Senior Vice President, Freedom from Hunger

13. FINCA—Uganda: Michael McCord, Chief of Party; Rosemary Pugh, Senior Program Manager, FINCA International

14. Fundusz Mikro—Poland: Rosalind Copisarow, Executive Director

15. Kenya Rural Enterprise Program: *Kimanthi Mutua, Managing Director*

16. PRODEM—Bolivia: *Fernando Romero, President*

17. SafeSave—Bangladesh: Stuart Rutherford, independent consultant

18. Self-Employed Women's Association (SEWA) Sohakari Bank Ltd.—India: Jaysyree Vyas, Managing Director, Inez Murray, Women's World Banking

19. Swaziland Business Growth Trust: Don Henry and Eric Nelson, Development Alternatives, Inc.

ANNEX B

DEFINITION OF TERMS

Cannibalization: the lost sales of an institution's own product when it introduces another product in the same market

Clients: individuals who purchase an institution's products or services, which implies a transactional, one-time relationship (as differentiated from "customers")

Customers: individuals who purchase an institution's products or services, which implies a longer-term, more intimate relationship (as differentiated from "clients")

Desertion: A client's abandonment of a program. Clients often switch to a competitor because of dissatisfaction with an MFI's product and service offerings. Desertion occurs when an MFI fails to anticipate and/or address the changing needs of its customers.

Flat: (versus hierarchical) organizational structures are characterized by a participatory approach to management (versus top-down mandates from senior staff who are separated from field officers by bureaucratic levels of authority), whereby lower levels of an organization are empowered to make decisions for which they are also accountable.

Focus group: a gathering of six to ten people (often potential customers) who are invited to spend a few hours with an objective moderator to give feedback on a product, service, or an organization

MBP: Microenterprise Best Practices project, a five-year study sponsored by the U.S. Agency for International Development, to research timely issues in the field of microfinance

MFIs: Micro Finance Institutions

Monoproduct: a nondifferentiated product offered by most MFIs. Monoproducts can include different price and term structures for various clients, but are not tracked separately

NGOs: nongovernmental organizations. Often contrasted with MFIs that have transformed to regulated, for-profit financial institutions

Transformed MFIs: MFIs that have transformed from NGOs into for-profit, regulated financial institutions