Hybrid Value Chains in Financial Services

Has the time finally come for a new contract between banks and Social Enterprises to address financial inclusion?

Thoughts

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Hybrid Value Chains in Financial Services*

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* This is the extended paper. An abridged version is available from our websites.

Executive summary: time for a new contract between banks and Social Enterprises to create shared value

The 20th Century history of banking is characterised by two, great, socio-economic phenomena; moments of extraordinary innovation in banking that helped change the way people live and work and fundamentally triggered positive momentum for social change and wealth creation in economically disadvantaged sectors of the economy. And, periodically, banks have also contributed to the creation of global or regional financial crises through excessive innovation and risk taking which resulted in major wealth erosion for countries and communities.

With the Global Financial Crisis (GFC) dominating sector perception today, it is time to rediscover the industry's track record of using essentially social innovations like cooperative banking or micro-credit and micro-insurance to help millions of people improve their lives – and create partnerships with today's social innovators to write the next chapters of that history.

Despite the inherent capacity of the banking system to innovate and take risk across economic cycles, banks still exhibit exceptionally conservative policies towards partnering with Social Enterprises in modernising their own value chains and reaching out to the financially excluded. Yet today, many Social Enterprises, including some of those in the Ashoka Network of 3000 social entrepreneurs showcased in this paper, have evolved to become a 'safe bet' in the supply of banking products, platforms, services and technologies to the socially excluded sectors of the economy and society at large. (Social Enterprises: organisations set up for the primary purpose of delivering a specific social mission, using a business model where any profits are reinvested in the business to fund growth)

The time is right for a shift in approach:

- Social Enterprises are maturing and have stable business models offering low cost/high integrity solutions to multiple sectors of the economy which suffer from financial market failure.
- increasing pressure on the banks from consumers, governments and regulators to address market failure pro-actively requires more creative solutions to banks' social utility objectives.
- the business case for including Social Enterprises as business partners is increasingly commercially attractive and makes good business sense.

Both sides stand to reap enormous benefit; banks should find new opportunities for 'plug and play' integration of more Social Enterprises into the evolution of their value chains across many of the front office and back office functions they traditionally outsource to commercial third parties or build themselves. Social Enterprises would benefit from the scalability a solid corporate partner can provide through a transformative deal. By including Social Enterprises in their procurement processes, banks can help these social change agents magnify their social and economic impact.

At the same time, many Social Enterprises are innovating approaches to reaching new customers currently outside the banking mainstream. These could become valuable new high growth markets for banks. Whether these are remote rural populations, or so-called 'base-of-the-pyramid' customers whose income levels or employment status as informal economy workers currently exclude them from traditional financial services, there is a social entrepreneur pioneering a new method of reaching them and showing how they might become a credit-worthy customer. There is a massive global

The business case for including Social Enterprises in the mainstream of bank partners is increasingly attractive.

opportunity to partner with such entrepreneurs and open up whole new markets to the banking sector – we profile several such examples in this paper.

What matters most today is a new ‘contract’, both moral and economic, between banks and Social Enterprises triggered by a fundamental shift in bank procurement polices coupled to a new mindset in envisioning Social Enterprises as real ‘players’ in reinventing bank value chains rather than simply beneficiaries of a CSR strategy. Bank CEOs and Boards have a decisive role to play in nurturing this mindshift among their top management; the prize is huge and the impact on the financially excluded would be transformative.

This paper explains the compelling rationale for multi-national banks to create a new ‘contract’ with Social Enterprises to incorporate them into their commercial value chains as providers of new customers, platforms, technologies, products and services.

Social Enterprises are proven, valuable business partners. The time has come for banks to engage with them.

Acceleration to disaggregation

Banks have been disaggregating their value chains for years; the new business models of multi-national banks have moved a long way from the classical concept of ‘do it all yourself’. Even before the recent Global Financial Crisis, banks had begun to redefine their true core competencies. They realised that, through outsourcing, offshoring, using third party distribution agreements, co-opetition with other banks who specialise in back office services, and joint product development with telcos, they did not need to ’own’ all their own factors of production. Greater cost efficiency and higher revenue growth could be compatible, twin achievements, reconciled without conflict by using outside specialist providers who were better, cheaper or faster at fulfilling components of their supply chain.

Since the GFC, there have been renewed initiatives among banks to find a new size and a new shape that is fit for purpose; i.e. a new business model that will deliver sustainable and attractive ROEs (returns on equity) in the ‘new normal’ business environment that persists after the crisis.

The opportunity to include Social Enterprises in bank value chains is under-exploited

The preferred partners of the banks in designing their new ecosystems (‘Extended Enterprises’) have been confined to purely **commercial** entities, with notable exceptions in micro-finance and micro-insurance. By ignoring Social Enterprises as a legitimate class of business partners, banks are missing a huge opportunity.

If we simplify a bank value chain, we can see 3 main components (see figure 1 on page 4):

- Origination and extending credit to businesses and consumers. This includes equity funding, long-term risk capital in the form of secured and unsecured debt, working capital funding and personal lending.

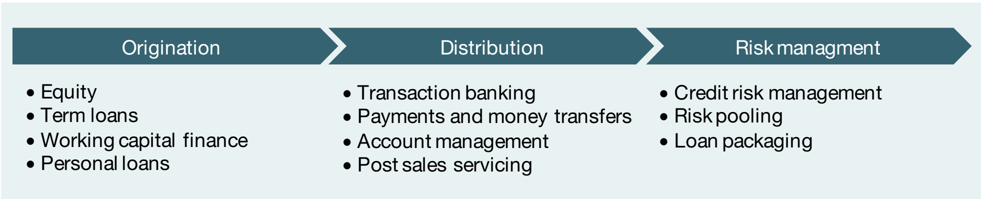

Figure 1. Bank value chain (simplified)

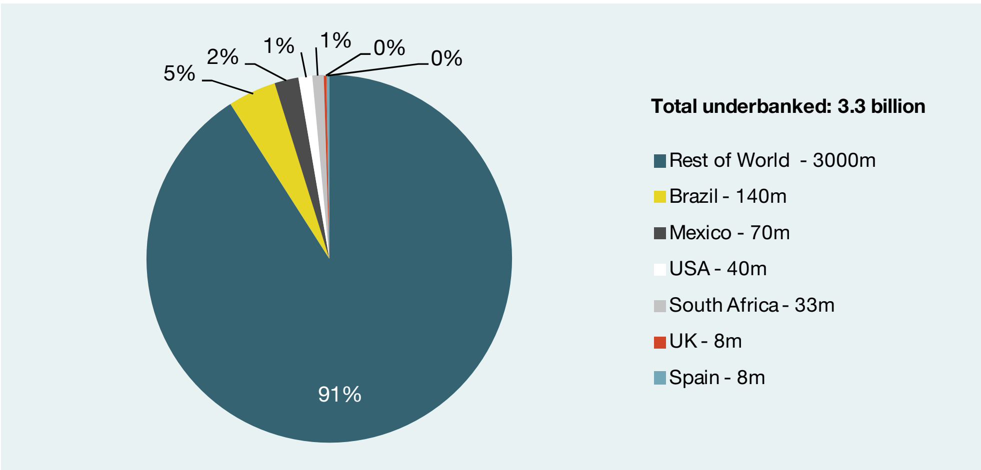

Figure 2. Underbanked population

Banks need to rediscover their birthright as catalysts for changing the way people live and work.

- Distribution, sales and servicing. This includes deposits, transaction banking, payments, remittances, money transfers, account management and post-sales servicing.
- Risk management. This includes the assessment of credit risk, packaging of risk-based assets into securitisable instruments, and the on-going risk evaluation and remediation.

Today, some 30 Social Enterprises within the Ashoka community, and many more outside, provide solutions across all three components of the traditional bank value chain. (See case studies).

Historically, the creation of the Cooperative Bank movement in Germany or the Farmers' Banking sector in Southern Europe found its origins in resolving the underlying profit motive with social inclusion by creating innovative credit, distribution and risk strategies to propel economic sectors into new eras of hyper-growth. The business models so created have proved durable, sustainable and profitable, largely through the implementation of rigorous commercial disciplines combined with a clear sense of a higher 'social purpose'.

Yet, in contrast to historical precedent, the 'modern bank' has failed to explore ways to systematically collaborate with Social Enterprises.

Correcting 'market failure' in the provision of banking services

Banks' business models have weaknesses; they were never designed to provide full economic and social coverage:

- A large, fixed cost base makes it difficult for banks to invest profitably in 'marginal' markets, geographies, products and segments. Inflexible core banking systems mean banks cannot 'get the business case to work' for new technology investments unless the market has fast and predictable returns.
- Due to their size and organisational structure, banks are poorly set up to test innovative new ways to access new markets and provide new kinds of financial services to currently financially excluded customers. It is no coincidence that major new financial platforms such as M-Pesa in Kenya, which is creating a mobile banking revolution in that country and beyond, originated not from mainstream banks but from non-traditional players such as Safaricom and Vodacom. Social Enterprises can act as the R&D 'test bed' for new ways to reach some customers, and are better set up to do so.

The causes of 'market failure' (i.e. market based commercial solutions are not available because the inherent financial returns do not meet the expected risk adjusted return-on-capital hurdles) have a common root cause in financial services; banks are reluctant to service some critical segments of the population and industry structure because they do not 'own' a social mandate. In other words, they are not constitutionally accountable for addressing the full spectrum of economic actors unless their commercial criteria are met (see figure 2 on page 4).

Equally, governments have recognised they need to step in to correct market failure in the financial system; the 1977 Community Reinvestment Act in the United States being perhaps the most famous example. Over the last 40 years in the UK, successive governments have launched new incentives to motivate banks to address neglected economic segments either by de-risking the business case for them or enhancing their returns.

Examples of market failure in financial services abound. Social Enterprises are finding solutions in areas where banks fear to tread.

- There are many examples of financial market failure; start-up loans for new SMEs; subsidies and guarantees for first time buyer mortgages; transaction banking accounts for immigrant populations and the unbanked; subsidised interest rates for funding social infrastructure projects; provision of financial education in schools.
- And, there are many examples of government intervention to reverse these market failures such as Small Firms Loan Guarantee Schemes to underwrite loans to SMEs; government-backed deposits for first time house buyers so they can get mortgages; tax breaks on Venture Capital Investment to encourage new start-ups; Enterprise Lending Schemes for the poorest regions to promote industrial regeneration.

The results have been mixed; but, the policy intent has been clearly pointed in the direction of providing ‘carrots’ to encourage the banking system to embrace a much wider accountability for its partial ‘utility’ characteristics.

Accessibility to financial services; more carrots and sticks?

Banks are now under huge political and social pressure to demonstrate their 'utility' to the wider social and economic progress of nations; even to address the needs for financial education to prevent future debt excesses and to encourage good savings habits, self-provision of retirement pensions and greater entrepreneurialism. Since the GFC, the greater social awareness of the latent 'negative externalities' caused by the near-failure of the banking system in many countries has put a new emphasis on banks to show a wider empathy for their ‘nation building’ responsibilities.

For the last 30 years, governments have been pro-active in intervening to correct negative externalities in physical markets but not in the financial markets. They have forced companies to display a wider empathy with the environment in which they operate by the imposition of taxes, fines and operational constraints across a whole range of industries from mining to forestry, oil extraction, industrial agriculture, shipping and aviation.

Unless banks adopt pro-active policies to redress market failure and the negative economic and social consequences of the segments they exclude from their normal course of business, governments will intervene in the financial services industry by public demand.

One small step banks can take in their re-invention journey is to engage with Social Enterprises to address more segments of the economic and social landscape, where their huge impact on financial exclusion is already in evidence.

Social Enterprises - attractive business partners for banks in Hybrid Value Chain creation

Innovations in financing

Social Enterprises make attractive partners for banks in creating Hybrid Value Chains. They have the capability and the appetite to bring actionable innovation by playing one of two key roles:

1. **Social Enterprises acting as ‘Principals’ in a financial transaction.** They are selling a product,

platform, service or technology capable of 'plug and play' directly into a bank value chain. (See case studies; Wizzit, Lumni and Fair Finance). They have 3 dominant genes:

a. These Social Enterprises have developed innovative solutions to the unmet financial needs of excluded potential customers such as mobile banking for the unbanked, capital funding for very small entrepreneurs, short-term loans for low income families and affordable educational loans for college students.
b. They do so with a partly or wholly profitable business model, often exploiting a critical innovation in technology, origination or credit risk assessment which banks have missed or chosen to ignore.
c. Their business models address three critical buyer values among the end-users: afforda-bility; accessibility and availability. In these ways, they have built inherently 'customer centric' offerings, which readily find demand at local scale. These offerings are attractive in their own right as they are highly customer focussed.

2. **Social Enterprises acting as 'Agents' in the Financial System or 'orchestrators' of demand and supply**. They often conform to the classical definition of an entrepreneur, connecting a bankable group of customers to commercial sources of credit and funding. They are creating 'ecosytems' to get a project completed or to transform an industry (see case studies: FASE and Agora Partnerships). Their 2 dominant genes are:
   a. Their ability to design and shape propositions that make it attractive for banks to come to the party; they can de-risk the execution of a project because they are harvesting the latent motives of multiple actors to deliver social change at a profit. These Social Enterprises, acting in an Agent capacity, succeed in getting banks to release funding for businesses and social projects, which would otherwise fall into the 'too hard' category for banks to exploit for themselves. In economic terminology, these Agents defray the fixed cost that banks would otherwise incur in structuring an attractive transaction or in originating the underlying commercial deal shape.
   b. They are 'demand aggregators', who use their own network to assemble a critical economic mass of consumers to create a market and justify the entry of commercial suppliers (including banks) to provide an attractive service. They enable wider coalitions of essential participants to come together to deliver a socially impactful project with banks at the heart of the financing dimension.

Bringing about social and economic change, at a profit, is the outcome of both these key roles of Social Enterprise. But the instances of successful collaboration between banks and Social Enterprises, in either Agent mode or Principal mode, are almost always one-off examples. Today, SEs and banks typically come together around single transactions but not around a systemic change of the financial system through an inter-locking of their respective value chains. These single instances are no less powerful as 'proof points' of positive economic and social outcomes but they do not substitute for long term partnerships which are the keys to scalability, sustainability and profitable returns.

Advantage Social Enterprise – The compelling case for collaboration

The most important elements of a sound business case for collaboration are already in place and the

advantage brought to the table by Social Enterprises are clear and compelling.

Many Social Enterprises have lower investment costs than banks - they get to market with a fraction of the investment of an equivalent bank initiative because they are lean and highly focused on a single offering. They may also have lower transaction costs for delivering an operational service (e.g. price per customer acquisition or default rate on loans).

Social Enterprises typically have faster launch processes and speed–to-market because they benefit from lower fixed costs and they are highly focused on a specific piece of the value chain. They are nimble at inventing and using technology; they are often more innovative than most banks and focus on addressing one market failure at a time. They have high integrity in their local community (e.g. in handling credit risk data); they are trusted by end-consumers and, constitutionally, they are accountable for the social responsibility they inculcate.

They provide solutions to both front office and back office challenges. Paradoxically, although banks are largely capital constrained, they have invested huge amounts in 'owning the customer' over the last 15 years by sourcing expensive commercial solutions to their customer outreach problems, rather than exploring the platforms and capabilities available among the Social Enterprise sector. At a far lower cost, and without the risk of inter-operability issues, Social Enterprises are rich in solutions for 'the last mile' of connection to the customer. The ‘sweet spot’ for collaboration in new Hybrid Value Chains is often found in the most overtly customer-facing functions of a bank, where ‘safe’ collaboration with Social Enterprises carries a huge upside for the credibility and capability of a bank’s business model. This is particularly true for customer acquisition in new market segments. The following sweet spots are especially significant:

- **Distribution channels** - providing sales force and distribution channels in remote, rural or under-populated regions of the economy to originate volume for micro-lending.
- **Risk assessment** - in conducting the initial risk assessment for short term-loans to very small businesses and low income consumers.
- **Customer acquisition** - outsourcing the identification of new banking customers (e.g. promising new start-ups) to Social Enterprises who have deep skills in specialist sectors and who can provide dedicated coaching and mentoring to prepare business owners for their next growth phase.
- **Demand aggregation** - in aggregating demand among end-consumers for social infrastructure loans.
- **Driving mobile capability** - in delivering a low cost mobile banking platform with full transactional functionality as an alternative to branch-based distribution.
- **Data origination** - in assembling complex or otherwise inaccessible data which can be packaged for conventional risk assessment purposes.
- **Technology innovations** - inventing innovative technology solutions that banks would otherwise spend too much on, take too long or never think about launching themselves;
- **Financial education** - providing financial education to young people to help them adopt prudent saving and borrowing habits at a very early stage in their lives.

A point of inflection has arrived. Social Enterprises can make it easy for banks to be partners in social change through Hybrid Value Chains.

Inflexion point - now Social Enterprises are ready to work with banks on new Hybrid Value Chains

A point of inflexion has arrived. Social Enterprises can make it easy for banks to be partners in social change by creating Hybrid Value Chains – HVC's. There are sound reasons to be optimistic:

Maturity - Many Social Enterprises, such as those showcased in this paper, have achieved a level of maturity in their own business models that makes them comfortable partners in a bank ecosystem.

Compatibility - They understand what partnering means with a commercial business; they have sophisticated MIS (management information system) /reporting/ risk management systems that are consistent and compatible with the banks' own fiduciary responsibilities.

Delivery - They are good at 'built-in' operational excellence; they understand that they need to deliver the promised service at a contracted price and quality standard.

Total solutions – Many of the Social Enterprises engaged in financial services today create total solutions, not componentry. Banks do not have to source missing components or significantly re-engineer their business processes to accommodate these new partners.

Sustainability - They are locally-scaled, and financially robust; they are long-term bets. And they are an attractive proposition for shareholders and wider stakeholders because:

- they are better equipped to measure their social and economic impact
- they understand the need for a fair profit distribution between the bank, the Social Enterprise and the community
- they are adept in co-creating solutions which enable banks to quickly demonstrate they are addressing market failures themselves.

Plug and play - Although banks worry about the cost of embracing new suppliers, like Social Enterprises, into their operating models, there is every reason to believe, based on the evidence of the Ashoka case studies, that the cost and technical complexity is actually minimal for a bank; the hidden secret is that these Social Enterprises have evolved very low cost business models themselves out of necessity. They are structurally more efficient in their operating economics than most commercially available solution suppliers.

The main challenge for banks in re-inventing themselves around more Hybrid Value Chains (i.e. supply chains linking social and commercial partners) does not lie in process re-engineering; it lies in more creative procurement policies, a more imaginative approach to risk management and in exploring alternative customer channels. (A typical bank procurement function is targeted on sourcing a price/quality mix from among a preferred list of commercial vendors. A typical spectrum of bidders would include some innovators in the field but very rarely a Social Enterprise.)

As banks get more confident about moving away from 'one-stop-shops' for the supply of their solutions and services, it creates an opportunity for their senior policy makers to mandate the inclusion of a sample of Social Enterprises in the initial RFP (request for proposal) list. 'Success and significance' can become compatible goals if banks show more willingness to take the first steps towards true Hybrid Value Chain adoption and development.

The ‘New Banking Consumer’ in 2020 will be less tolerant of structural inefficiencies in banking and less forgiving of poor customer experiences.

Banks, Social Enterprises and moving towards a new vision for financial services

If we imagine banking in the year 2020, how would it look and feel? Most banks have blueprints for their operating model in the next 5-10 years, safely stored in the vault and often titled ‘Customer 2020’ or ‘New Size, New Shape’. Yet to a great extent we can see the future today. Customers around the world are sending a clear message to banks: ‘’help me fulfill my dreams’’. In doing so:

- Banks will be much more like an ‘ecosystem’ with networks of partners coming together to solve new consumer needs.
- Financial services will form more of a fabric of the community, accessible from all channels and serving wider segments of the economy.
- Banks will have edged towards a new ’purpose’, intrinsically accountable for the real economy and conscious of their social responsibility to their community and the attitudes of society towards their function.
- They will be more innovative, mainly because society has higher expectations in all walks of life for more rapid product innovation.
- There will be more transparency in the use and purpose of ’big data’. The balance of power will shift in favour of customers deciding how much data the banks can hold and their assent will be based on how much benefit they receive in return.
- Inherently, banks will become more useful to customers and able to face (and convincingly answer) the ultimate question; ‘’can you help me fulfill my dreams?’’

The ‘New Banking Consumer’ in 2020 will be less tolerant of structural inefficiencies in the banking system (e.g. time taken to switch accounts, open accounts, make credit decisions,) and less patient towards the negative externalities inflicted on sectors of the community excluded by the banks. The New Banking Consumer will also be less forgiving of a customer experience that falls short of similar experiences dealing with other utilities, telecoms providers or retailers.

It will be hard for banks to react swiftly to these powerful tides of social and economic change without engaging in a more fundamental rethink of the flexibility and adaptability of their business model. It still takes too long to innovate and implement change in banking because of rigidity in technology architectures and cultural resistance in human capital.

In the banks’ journey towards a new vision for banking, Social Enterprises are natural allies; demonstrably ’customer and community centric’, Social Enterprises can anchor the banks in their new agenda as both accelerators of innovation and as a beacon to shine new light on shifting currents of consumer and social demands. In the complex dreams possessed by today’s banking consumers, banks can find new navigators in the world of Social Enterprises to help them plot and execute a course towards their own reinvention.

Value chains, reinvention and next steps

Many banks already connect with Social Enterprises through their CSR programmes or Foundations but they rarely include them in the progressive re-invention of their operating and business models. Why not? Ten years ago, the immaturity of the Social Enterprise sector lent credibility to banks’ ‘play it safe’ conservatism. Today, the legacy of placing Social Enterprises into a CSR ‘box’ needs to be broken. They need to come into the mainstream of

Connecting bank procurement and sourcing strategies to Social Enterprises and exploring new partnerships presents a huge opportunity to magnify their social impact.

Social Enterprises can bring speed, innovation, trust and integrity to help banks reinvent their business models and get ahead of the government and regulatory agendas.

credible partnering opportunities around profitable and socially impactful solutions, particularly in the context of so many examples of financial market failure.

It is now safe to do so; the beacons of success among the Ashoka Fellows already successfully engaged in creating bankable propositions, among sectors of the economy where the banks fear to tread, gives credibility to the new notion that banks have nothing to fear, and indeed everything to gain from closer collaboration with Social Enterprises in their value chains.

So, the leaders in the banks can take 6 practical steps to shift their own paradigms and, in so doing, change the paradigm of their own organisations:

1. **Connect** - Bank CEOs need to explicitly connect their procurement policies and sourcing strategies to Social Enterprises and explore partnership opportunities across platforms, products, services and delivery channels. In part, this involves changing behaviours but also changing the organisation's perceived attitude to risk.
2. **Collaborate** - Bank CIOs need to learn and understand how they can collaborate with Social Enterprises and investigate the breadth of technology solutions and process innovations where Social Enterprises are solving previously insoluble problems in the banking system.
3. **Disaggregate** - CEOs of the Retail, SME and Corporate Divisions need to evaluate their existing operating models to reveal a 'heatmap' of areas where their value chain can be dis-aggregated in favour of Social Enterprises and how to unbundle their own value chain to adopt products/platforms/distribution channels from the Social Enterprise sector.
4. **Prioritise** - The Boards of banks should identify areas of market failure where the bank can profitably prioritise solutions developed by social entrepreneurs to get ahead of the government and regulatory agenda - and not rely solely on channeling support for Social Enterprises through Foundations and CSR programmes.
5. **Innovate and co-create** - The Strategy Executives could set up 'intrapreneurial' new business teams, with a mandate to work with SEs as 'Innovation Partners' around specific business problems (e.g. market entry, low-income banking, low cost origination and distribution channels, market scaling, technology innovation). They should view Social Enterprises as R&D test partners for discovering and entering new unbanked markets and serving new customers, as well as supporting existing customers in new ways.
6. **Reformulate CSR** - CSR leaders need to reformulate the mission of their CSR teams to actively search out Social Enterprises who can offer viable and rapid solutions to a bank's business and operating model challenges.

The time is right for a new contract between banks and Social Enterprises who operate in their space. The paradigm of Social Enterprises as simply beneficiaries of CSR programmes fails to recognise the inherent competitive advantages that they can bring to banks' new business models: speed, innovation, trust and integrity. Once again, the banking system faces a tipping point; it can help change the way people live and work in the most financially excluded sectors of society by co-creating new Hybrid Value Chains with Social Enterprises. The prize is huge for the banks, for society and for the wider economy.

Definition of key concepts

Ashoka – System-Changing Social Entrepreneurs

Ashoka, founded by Bill Drayton in 1980, is a global community of the world's leading social entrepreneurs – Ashoka Fellows – who deliver system-changing solutions to some of the world's most urgent social problems. The Ashoka community is committed to creating an 'Everyone A Changemaker' world, and supports over 3,000 social entrepreneurs in 85 countries, of which more than 30 specialise in financial services.

Ashoka's Globalizer Programme

- In 2010, the Ashoka Globalizer Programme was launched to help the most advanced social entrepreneurs create plans to scale and internationalise their ideas. Helping Ashoka Fellows transfer their business models to regions where they are needed most is the main goal of the Globalizer Programme.
- Building and engaging with a high-level network of 80 Ashoka fellows, innovative business entrepreneurs, CEOs of multi-national companies and a Nobel Prize laureate, the programme assembles a ground-breaking ecosystem of business and social entrepreneurs to create mindshifts and tipping points across a diverse range of geographies and solutions to social change.
  For example, in 2012, Ashoka Globalizer teamed with SWIFT's Innotribe think tank to identify social finance innovations that would be attractive to banks and integrate into their value chains.

Full Economic Citizenship and Market Failure

Full Economic Citzenship (FEC) is an Ashoka global initiative designed to create a society where every citizen has the opportunity and capacity to exercise their economic, social and cultural rights. Ashoka's goal is for every individual to have the opportunity and choice to play a role in their local economies as consumers, producers and creators of wealth. Today, huge segments of the global population are denied access to financial services - which might otherwise allow them to maximise their full potential as full economic citizens. Ashoka's vision is to intervene in areas of the economy where the market mechanism has failed to provide solutions to deep-seated social challenges by empowering social entrepreneurs to design and implement their own system-changing ideas.

HVC's (see figure 3. Ashoka Hybrid Value Chain)

- Ashoka's Full Economic Citizenship programme christened the concept of collaboration between Social Enterprises and multi-national companies (MNCs) the ''Hybrid Value Chain'' in the paper written for the HBR in September 2010 entitled ''A new Alliance for Social Change'' (see References).
- In 2011, Michael Porter published a paper in the HBR which added to the concept through a model of shared value which concluded that corporate success and social welfare are co-dependent and that by collaborating with MNCs, Social Enterprises could be powerful engines of social change in an ecosystem that also makes good business sense for the corporates.
- The convergent 'big idea', now being implemented in the agricultural, food and the pharmaceutical industries is based on Hybrid Value Chains and shows that Social Enterprises can successfully partner with multi-national companies. They can play a full role as an intrinsic partner in business models across, for example, the product development cycle, distribution channel strategies and technology sourcing strategies. The end product is a chain of collaborative activity between private and social sector enterprises to bring multiple perspectives and solutions to create social and economic value.

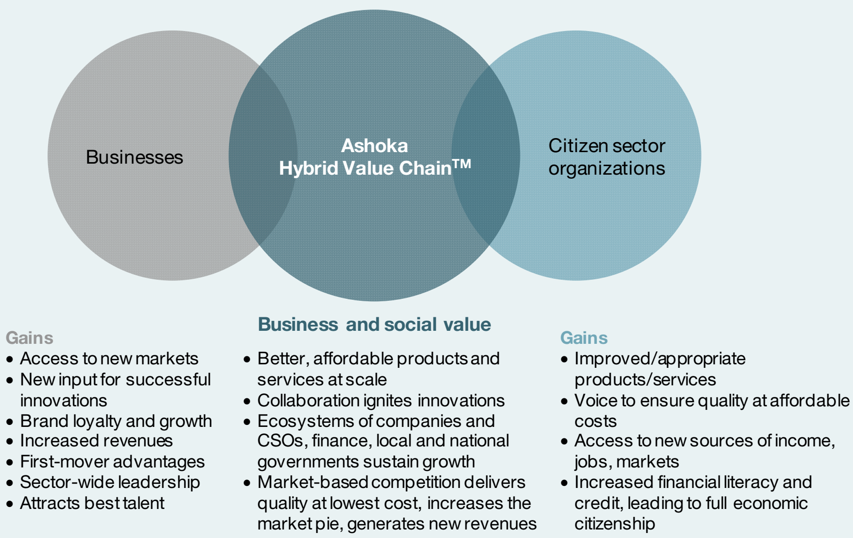

Figure 3. Ashoka Hybrid Value Chain

Proof points – the HVC approach can and does deliver value … but much more can be achieved

Today, there are more than 30 Ashoka Fellows globally already delivering financial services to financially under-served communities. They have built innovative and sustainable Social Enterprises. Yes, most of them are at their 1st stage of growth – they operate largely independently of the commercial banking sector and have yet to evolve into commercial partnerships with banks as co-creators of new distribution channels, credit risk capabilities, capital loans or infrastructure funding. There are a few exceptions, however, and these success stories represent beacons to the wider industry.

To scale into their 2nd growth stage, and magnify the economic and social benefit they can deliver, Social Enterprises will need to team with commercial banks to their mutual benefit and then to accelerate the resolution of multiple market failures in the financial services industry. The following case studies are examples of the depth of innovation and breadth of social impact created by some of the Ashoka Fellows.

1

Using innovative technology to access new markets: Wizzit International – an innovative mobile banking platform for the unbanked and remote rural communities in Africa and Latin America and other developing markets.

The mission

Brian Richardson was elected an Ashoka Fellow in 2010 but the idea of opening a mobile bank for the 16 million people in South Africa without a bank account arose from a casual conversation over dinner in 2002. Why had the commercial banks ignored the low–income segment of the population for so long? Why was it so difficult to open a bank account, make money transfers, pay bills and provide a safe haven for more than Rand 18 billion currently stored under mattresses? The impact on the economy would be immense if only a small percentage of this segment could be enticed towards a simpler, affordable, available and accessible innovation in banking provision.

The solution

Brian, together with his business partner, Charles Rowlinson, set up Wizzit International which, from its origins in South Africa, is now one of the leading mobile banking platforms in Africa and is soon extending into South America and Eastern Europe. Wizzit partners with innovative commercial banks to provide state of the art technology and a proven branchless banking model. Customers of Wizzit access banking services simply through a mobile phone; it does not have any branches. Customers open accounts through fully trained field agents called Wizzkids, who are exclusively previously unemployed people who earn a commission. The bank account is fully comprehensive (bill payment, transfers, purchase of airtime and other typical services) and includes loans, micro insurance and debit card.

Key success factors

Technology innovation: the Wizzit banking platform was designed from scratch with full inter-operability with other bank and financial service infrastructure (e.g. payment systems) and to be easy to integrate into bank legacy systems. Either as a stand-alone banking system or as fully integrated architecture, Wizzit can be implemented in under 6 months.

Customer experience: Wizzit recognised that no-one likes to be labelled 'poor' and that a bank offering a service that was designed, branded and promoted as a sub-standard experience would quickly fail. From the start, the whole Wizzit customer experience was designed around the core principles of accessible, available and affordable financial services. 'Surprise and delight' were the watchwords of the end-to-end experience and each member of the team was trained to make banking with Wizzit a rewarding and appropriate experience for the end consumer.

Social impact

- Providing employment for 8500 previously unemployed people, in South Africa alone.
- Avoiding lost productivity from days spent walking from rural villages to the nearest banking branch to pay electricity bills or buy airtime or collect wages.
- Creating millions of economic citizens who were previously excluded from affordable access to financial services.

2

Redesigning financial architectures: Agora Partnerships in Latin America helps SMEs secure funding from banks and other investors, by coaching new entrepreneurs to strengthen their business models and present information investors need to make informed risk decisions.

The mission

Ben Powell was elected an Ashoka Fellow in 2010. Many small businesses suffer from an acute shortage of capital and term loans to help them scale; they are often too big for micro-finance and too small to be noticed by commercial banks and often so specialised that banks fail to understand their business model and risk profile. Nor can they offer collateral to underpin the banks' lending risk.

Ben set up Agora and the Agora Accelerator to help investors and commercial banks discover the 'hidden gems' in the emerging economies of Latin America. The mission is to accelerate the growth of early-stage companies throughout Latin America, those who are helping solve critical problems in their community, by supporting them in accessing the capital and resources they need to succeed.

The solution

Agora provides creative, early-stage ventures with a comprehensive programme of social, human and financial capital in a 3-step process:

- Step 1: Agora exposes entrepreneurs, in a one-week retreat, to its network of investors, mentors and consultants, to help build the business plan, strengthen leadership skills and prepare the company for growth.
- Step 2: Mentors and consultants are assigned to each entrepreneur to work on preparing the business for growth, defining investable projects, gathering investor information, and coaching the management team.
- Step 3: Agora introduces these entrepreneurs to investors and commercial banks based on sound creditworthiness, robust business models and competent management.

Key success factors

Deep Insight: Agora works with many companies in highly specialised sectors, for example cocoa farming, where a deep knowledge of the industry is critical to understanding cash flow, time to market and demand volatility. Agora's teams spend the time needed to acquire deep insight into the unique elements of the business model, to enable investors to accurately assess credit risk and growth potential.

Appropriate intervention: helping an entrepreneur to scale and commercialise an idea requires a delicate balance between coaching and empowerment; avoiding a dependency relationship is critical to success. Agora's 3-step model has been refined over the last 3 years to provide effective intervention at inflexion points for the business, while enabling each business to fully own all the skills it needs to succeed.

Social impact

- Overall entrepreneurs served through training and consulting: 4000+
- Companies that Agora has helped to access capital: 58
- Total amount of capital investment we've helped facilitate: $12.6million
- Average amount of investment facilitated: $217,000
- Jobs created: several thousand which have underpinned growth in many rural economies

3

Creating new financial instruments: Lumni in Colombia, Peru, Chile, Mexico and the US is shaping new financing instruments to help students pay for their college education, increasing their chances of graduation and finding a good job.

The mission

Felipe Vergara was elected an Ashoka Fellow in 2006 and created Lumni in 2001. Felipe identified a breakdown in access to university-level education among under-privileged young people, denied conventional loans and scholarships. Lumni's mission is to revolutionise human capital financing by creating new market systems that allow individuals, organisations and communities to finance their educational projects, based on their future income flow through a venture capital-type instrument.

The solution

Lumni designs and manages two types of fund: Impact Funds, in which investors participate to obtain a financial as well as social return. And Institutional Funds, where investors make donations to a revolving fund, managed by Lumni, to help fund college access for specific student populations. (Bancolombia is launching this year a new Institutional Fund - which will be managed by Lumni, with very flexible conditions attached to each student loan.)

In exchange each student commits to repay a small, fixed, percentage of their future income, over a pre-agreed timeframe after graduation. The student's obligation is complete at the end of that period regardless of the sum paid, thus providing peace of mind for an inherently debt-averse population.

Key success factors

Institutional funds; Lumni creates different funds tailored to both the needs of specific investors and the profiles of different students in different countries, regions or cities. The characteristics of each fund vary according to the level of social and financial return on investment, based on the characteristics of supply and demand.

Compelling proposition for investors and students: In the last 3 years, the drop-out rate from Lumni's Impact Funds has been less than 5% and the default rate was less than 5.3%.

Social impact

So far Lumni has created more than 30 funds, with total commitments of US$100m.

It has financed the education of 4000 students; 80% are first generation students and 50% are women.

As part of the Clinton Global Initiative, Lumni has pledged to help 10,000 more students access financing for education.

4

Opening unbanked markets: Fair Finance in the UK is channelling bank wholesale funding to retail customers who cannot access mainstream bank credit.

The mission

Faisel Rahman was elected an Ashoka Fellow in 2007. He identified market failure among large segments of the low-income and disadvantaged minority populations in inner-city London who could not access banking services from traditional commercial banks. They suffered from two problems: limited access to credit leaving them open to exploitation by predatory money lenders; and poor credit histories that lead to a spiral of economic and social exclusion.

His system changing idea was:

1. to challenge the conventions of the retail financial system in the UK that discriminate against and exclude the most marginalised people.
2. to revolutionise access to credit, by increasing the information flow and transparency of data to key decision makers, to better reflect the true credit-worthiness of disadvantaged people.
3. Fair Finance is also seeking to reduce the impact of predatory lending by educating borrowers and developing alternative and competitive financial products.
4. Faisel believes that, by building strong relationships with borrowers, he can lend successfully to the financially excluded, design suitable products, control the risks and keep defaults to a minimum.

Fair Finance has innovated new management practices and innovative distribution channels to demonstrate that many of the most disadvantaged customers, traditionally excluded from commercial banking services, can be viable and profitable.

The solution

With an estimated market of 5 million people in the UK borrowing from high cost lenders, Faisel realised he needed wholesale funding from commercial banks to scale Fair Finance quickly. Initially, he secured start-up funding from a network of Angel Social Investors. Next he obtained a syndicated loan from Societe Generale and BNPP over a 5-year term. Then he engaged with Santander, a global bank, to provide a working capital and term loan to support the scaling of the loan book and to expand services to the financially excluded in London.

These banks engaged with Fair Finance because, while they all wanted in principle to do socially motivated deals, it had to be on commercial terms - which required conformance to normal credit procedures and to existing bank policy.

Key success factors in partnering with commercial banks

Secure capital base: start-up equity had been already raised from a group of 'angels' - which provided assurance that Faisel could deliver Stage 1 of his business plan. Commercial banks took confidence that the business model was fit-for-purpose.

Growing reputation and track record: proof that the business model worked, and the social impact was highly significant, allowed Faisel to build a network of key influencers among government policymakers, regulatory agencies and commercial lenders to generate a groundswell of commitment from the ecosystem to make his system-changing idea succeed.

More commercial lenders were attracted to the durability of the business and grasped the idea that Fair Finance would not compete with its wholesale funders but instead provided an attractive alternative.

Unique competencies: Fair Finance had a unique credit risk modelling methodology, a unique way of accessing people whom traditional banks could not access or who sat out-of-strategy, and a database covering 10,000 clients over 5 years of existing transactions.

Social impact

Since 2010, and with the help of the three banks and the Angel investors, Fair Finance has achieved an impressive inflexion in both scale and social impact:

- 75% growth per annum in loan book over 2010-2012
- Adopted productivity ideas from commercial banking partners to scale at low cost
- Bad debt rate improving – down to 5.9% - industry leading and clear evidence of its successful formula
- £5m lent. 7000 loans
- Saved its borrowers over £2m in interest charges compared to predatory lenders
- 70% of clients are women; 84% on state benefits; 70% living in social housing
- Accessed even lower credit segments
- Targeting 100% growth in 2013 and +40% in 2014. = 8000 loans

Now, Faisel plans to expand the breadth of services offered to the financially excluded and become more of a full-spectrum provider including microfinance for SME start ups; money advice services and insurance.

5

Bridging commercial and philanthropic investors: FASE - Financing Agency for Social Entrepreneurship.

In cooperation with a consortium of partners, Ashoka set up the first financing agency in Germany to bring together growth-ready social innovators with philanthropic and commercial investors based on well-defined business plans, attractive funding options and high social impact.

FASE's main mission is to unlock the broader market potential of social investing by pioneering hybrid deals between different types of funders, and by creating an open 'deal pipeline' for the social sector.

Ashoka mobilises business angels and other external expertise to coach the social entrepreneur through the business case and prepare their investment proposal. FASE facilitates the preparation of term sheets, and open sources deal documents to facilitate sector-wide learning.

Within six months of operation, FASE has already created a pipeline of investable deals, and a unique investor database based on specific pledges for funding.

Before FASE was launched, commercial banks had been reluctant to step into this market alone, because of concerns about their risk concentration and transaction cost. Now, by bringing together an 'ecosystem' of diverse funding partners under innovative deal structures, more Social Enterprises can access commercial bank participation and on terms which are attractive to all parties.

References

1. A new alliance for global change; by Bill Drayton and Valeria Budenich. Harvard Business Review, September 2010.

Noel Gordon is a member of the Ashoka Support Network (ASN) advising several Ashoka Fellows engaged in the provision of financial services to deprived and under-served communities. He was formerly Global Managing Director of the Banking Industry Practice at Accenture, an international banker and an economist. He lives in London.

Felix Oldenburg serves as Ashoka Director Germany and Europe, and launched programs at the interfaces of social entrepreneurship and finance, including an accelerator for social innovations in banking, and a Finance Agency for Social Entrepreneurship. Before joining Ashoka, he started an IT company, and worked for McKinsey. He lives in Brussels.

Nic Parmaksizian is a Director of Capco' s Global Banking Practice, based in London, specializing in customer experience design and implementation. He co-leads the New Banking Consumer area and formerly held senior roles in Barclays Retail Division. He is an expert in financial innovation and has been professionally recognized for innovation through several awards in the UK and in Italy.

Within the Global Banking Practice, Capco has developed innovative insights into the behavior of the ''New Banking Consumer'' and integrated a range of technology and process solutions to help banks reach and serve their retail customers more effectively. Capco also advises the leading banks on re-engineering their value chains and developing ecosystems of partnerships to future-proof their strategic flexibility and cost structures. Capco's ''New Customer Experience'' model uses our latest global insights into omnichannel and social networks to help banks reach and penetrate new customer segments and change the way banks serve and deliver.

About Ashoka

Ashoka was founded in 1980 by Bill Drayton, who is recognised to have named, created and pioneered the global field of social entrepreneurship. The world's leading social entrepreneurs are elected Fellows of Ashoka, and currently more than 3000 Fellows benefit from lifelong support from the Ashoka organisation to help them scale their social impact. These Fellows pioneer innovative solutions to the world's most pressing social and economic challenges by bridging the needs of deprived or under-served communities and the resources of governments, banks and commercial enterprises to design, create and deliver new solutions. Among the Ashoka Fellows, about 30 are engaged in delivering financial services to 'marginalised groups' or segments of the population who have limited access to traditional commercial banking facilities.

Each Ashoka Fellow meets 5 criteria: Creates a new idea that changes the pattern in its field and revolutionises an industry; Creativity and innovation in the design and delivery of the solution to a major social challenge; Entrepreneurial quality and a culture of changemaking; Ethical fibre; Scaleable social impact that is ''system changing''.

71% of Ashoka Fellows have changed market dynamics or national policies within 10 years of their election by: creating new markets; creating value where value did not previously exist; generating income for deprived members of society; increasing access to gods and services; changing the flow of market information

For more information about Ashoka, contact Felix Oldenburg ; foldenburg@ashoka.org

About Capco

Capco, a global business and technology consultancy dedicated solely to the financial services industry. We work in this sector only. We recognize and understand the opportunities and the challenges our clients face. We apply focus, insight and determination to consulting, technology and transformation. We overcome complexity. We remove obstacles. We help our clients realize their potential for increasing success. The value we create, the insights we contribute and the skills of our people mean we are more than consultants. We are a true participant in the industry. Together with our clients we are forming the future of finance. We serve our clients from offices in leading financial centers across North America, Europe, Africa and Asia.

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