



DEG - Deutsche Investitions- und Entwicklungsgesellschaft mbH

briefing note

Guideline # 6: Fair and Transparent Pricing

Conference:

Responsible Finance for Digital Inclusion: Investing for Impact

April 4, 2019 – Jessica Espinoza-Trujano + Dr. Thomas Koch

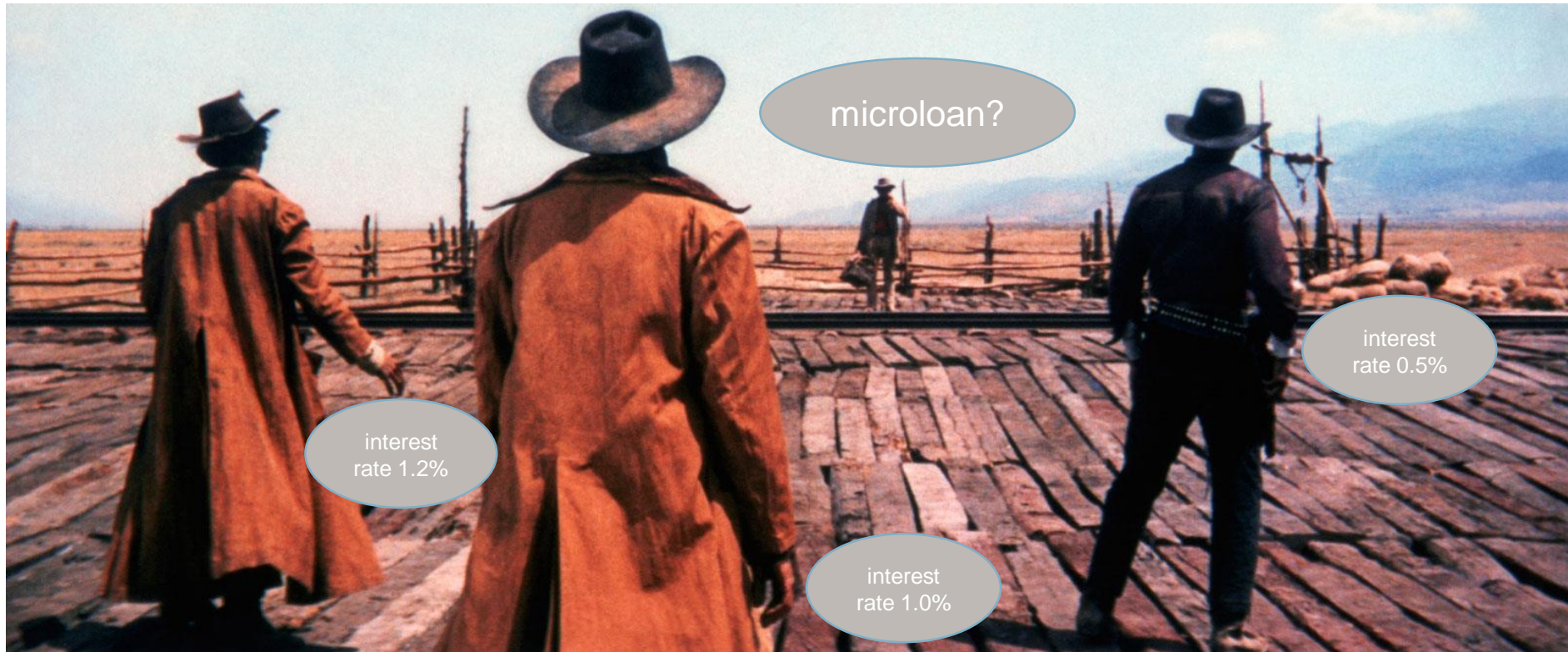




agenda

1. Fair Pricing – market-based-approach
2. Fair Pricing – balanced-returns-approach
3. Practitioner experience for promoting fair pricing
4. Transparent Pricing - practitioner experience

»» the FinTech actors „once upon a time in the West“ ...



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1.1 Fair pricing – market-based-approach

Responsible investors should analyze the overall market scenario from a clients perspective in order to make a country- and product-specific assessment.

distinguish between

- DFSP,
- informal money lenders,
- MFIs and
- banks

use criteria like e.g. ...

- interest rates;
- loan size;
- collateral
- opportunity cost

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1.2 Fair pricing – market-based-approach

How is the client`s perspective in the microloans-market?

example of market-based-approach ...

Criteria / Inst.	DFSP	Informal Money Lenders	Microfinance Institutions	Banks
Interest per Day (all-in)	0.4% - 0.53%	0.83% - 1.0%	0.15% - 0.28%	0.05% - 0.08%
Loan size and term	max. 500 LX; 30 days	200 – 2,000 LX; typically 1 month	< 6,000 LX; 6 – 12 months	> 30,000 LX
Collateral	No collateral	Guarantor	e.g. savings; group-guarantee	e.g. savings; collateral with assets;
Opportunity cost from end-client perspective	Lowest; mobile use	Highest	High; branch visit	High; branch visit

2.1 Fair Pricing – balanced-returns-approach

Responsible investors should analyze the correlation of ...

- high effective interest rates (APR/ EIR) with
- high return on equity (ROE),
- high NPLs and
- low administrative cost of digital lending.

Not acceptable would be triple-digit annualized interest rates (>100%), double-digit NPL (>10%) and low admin cost that overall would result in an excessively profitable financial situation.



2.2 Fair Pricing – balanced-returns-approach

= example of a hypothetical FinTech case

Actual and Expected Financial Results - Base Case						
Indicator / year	Real	Plan	Plan	Plan	Plan	Plan
	Year 0	Year 2	Year 3	Year 3	Year 3	Year 5
Interest rate per day	0.35%	0.25%	0.25%	0.25%	0.25%	0.15%
Loan Portfolio (Net)	156,000	421,200	758,160	758,160	758,160	1,933,308
Total Revenue	199,680	383,292	689,925.6	689,925.6	689,925.6	1,063,319.4
Equity	195,000	526,500	947,700	947,700	947,700	2,416,635
Profit After Tax	-19,500	26,325	94,770	94,770	94,770	531,659.7
NPLs 90 days	15%	10%	8%	8%	8%	6%
Cost-to-Income Ratio	140%	95%	70%	70%	70%	55%
ROE	-10%	5%	10%	10%	10%	22%

>>> 3. Practitioner experience for promoting fair pricing

guidance: responsible investors should focus on the potential for interest rate reductions ...

criteria 1: Pricing policy

rewarding clients with lower probabilities of default / repeat clients?
price differentiating factors (e.g. purpose, loan size and tenor)?

criteria 2: Pricing structure

all-in pricing? meaningful comparison for end-clients?
early repayment possible?

criteria 3: DFSP funding clauses for responsible investors

a one-time reduction of effective interest rates?
a step-down interest rate reduction tied to milestones?



4. Transparent Pricing – practitioner experience

guidance:

responsible investors promote that interest rates should ideally be disclosed as an all-in price in annualized terms (APR/EIR);

= follow “truth-in-lending”

At least, the interest rate per day as well as any additional fees should be clearly disclosed.

>>> How will the „wild west“ future of FinTechs be in 5 years?



thanks for lending us your ears...