

»» DEG - Deutsche Investitions- und Entwicklungsgesellschaft mbH

Guidelines for Responsible Investing in Digital Financial Services

briefing note

Guideline # 6: Fair and Transparent Pricing

webinar May 28, 2019 – Jessica Espinoza-Trujano + Dr. Thomas Koch



»» agenda

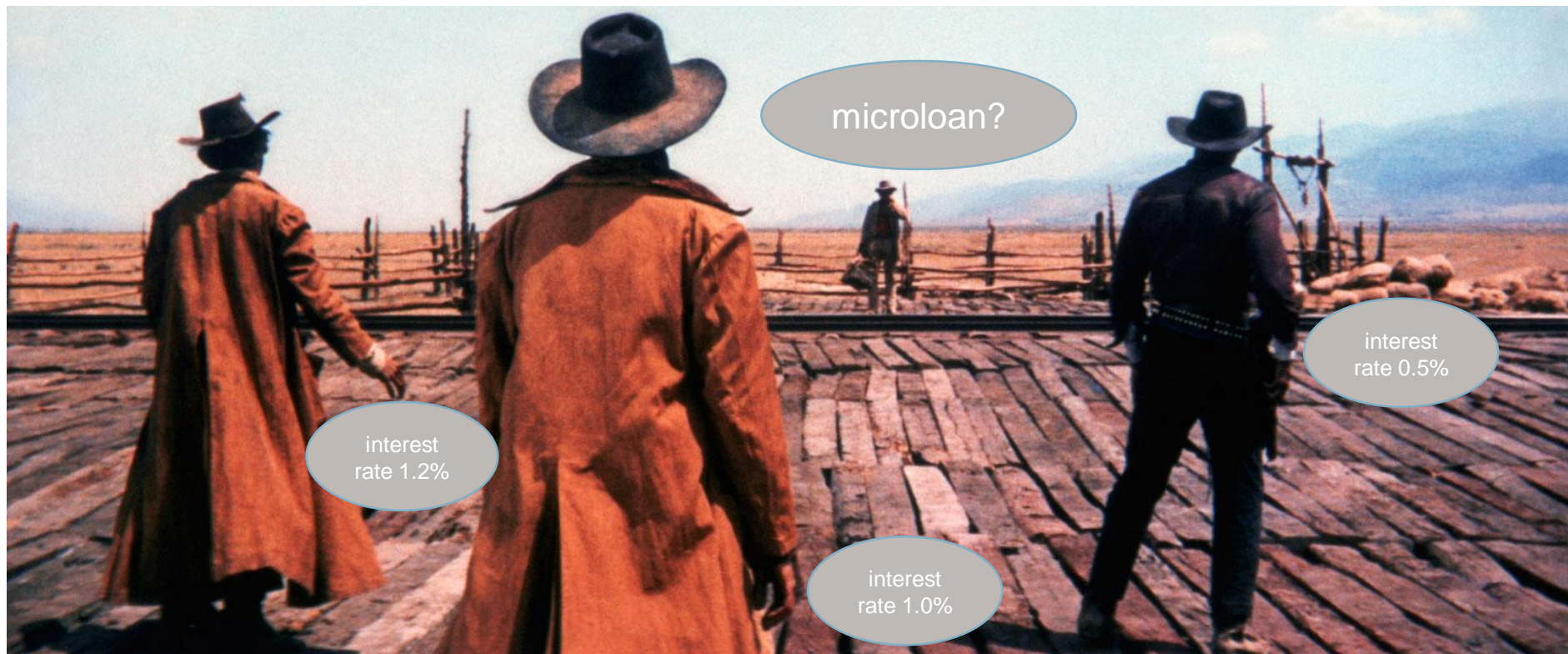
1. Fair Pricing – market-based-approach

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“ ...



»» 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

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

original western movie „Trinity is still my name“



micro-entrepreneurs
interest 0.15%

FinTechs
RoE 20%



investors?



regulators
at ease ...

thanks for lending us your ears...