Compartamos: Moving Away from a Cashless Bank Model

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José Maria San Juan and Alessandra Valenti
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A New Business Model

In looking to achieve more long-term relationships with their clients, two years ago, Compartamos started a pilot program in the Eastern State of Veracruz. Located at the coastline on the Gulf of Mexico, it has a population of more than 7.5 million people, which represent close to 15% of Mexico’s total population.

Loans in Veracruz are not issued through money certificates anymore; instead, each client is given a debit card, so direct electronic transfers are made. Clients in Veracruz also have access to six banks branches, two ATM’s and a new entity called banking correspondents (corresponsal bancario). The Bank is trying to find what will be the best mix between the uses of different channels (branches, ATMs and correspondents) in order to give the best number of services to clients at the lowest operational cost.

For the last 22 years Compartamos has operated without having any branches nor ATMs serving their clients. Once their clients have a loan approved they issued a money certificate that could be cashed out at any commercial bank in the country. This model proved to be very efficient not only in terms of operational costs but also regarding fixed costs. Compartamos did not need to invest in brick and mortar infrastructure by leveraging from the one already available at the commercial banks.

However, this also meant Compartamos could not retain any of their clients. Once they got their credit approved and the credit was cashed out there was not any other involvement between the client and Compartamos Bank. Few clients came back for more credit. The new debit card strategy focuses on creating a relationship with a consumer that drives repeat business and cross-selling opportunities for higher value added services.

Branches offer the best array of services together with a personal customer service, but are also the most costly ($1 USD per operation). ATMs in general are less costly but have considerably high maintenance costs ($.60 USD per operation). In both of these options the fact that money is kept dormant at each location represents a relevant cost that should also be considered.

Background

Compartamos started in 1990 as a non-governmental organization in the microfinance sector by Gente Nueva, a Catholic service organization, to aid the poor in rural areas of Chiapas and Oaxaca, in the southern part of Mexico.
In 2001 the organization was made private as a SOFOL, a limited-charter financial corporation legally bind to only take deposits from the public. At that time Compartamos received capital from international development organizations, including Accion International that provided $1 million for an 18%, and the IFC, the private sector arm of the World Bank. The IFC also provided an initial loan and later provided a partial credit guarantee for a $47 million bond offering.

In 2007 Compartamos’ owners sold 30% of their stock on the Mexican stock market in an initial public offering (IPO). The public offering brought in $458 million. Private Mexican investors, including the bank’s top executives, kept $150 million from the sale. More than half of the public offering proceeds went back to development institutions that invested in Compartamos, like Accion and IFC.

Since becoming an IPO Compartamos has received several critics, most of them related to the interest rates charged to their clients, nearly 90 percent. In much of the world, microfinance interest rates ranged from 25 to 45 percent. In fact, Muhammed Yunis, the pioneer who started microfinance gave some of the harshest critics to the bank.

Compartamos’ executives argue that in Mexico, high costs, inefficiency and limited competition push interest rates high. It is important to note that in Mexico the average interest today paid from the use of credit cards is 25% (this average comes from a high of 40% in 2008 and 35% in 2009). In contrast, since 2008, Compartamos has reported that its interest rates had been reduced by 30 percentage points over the previous five years as a result of efficiencies that were passed along to borrowers.

However, there is still a long way to go and Compartamos is interested in looking how to better serve their clients at the base of the pyramid. They have proved themselves as a successful model that reaches loans to a niche segment of the Mexican society and now they are looking to extend their line of products, so they are looking into offer saving instruments as well.

**New entity: banking correspondents**

In 2009 the National Banking and Securities Commission (CNBV) authorized certain banks to affiliate retailers and other merchants to serve as banking correspondents. This new entity offers some benefits to the different actors involved in these types of transactions.

From one side, the banks are able to reach more clients without the need to invest in more infrastructure. On the other hand small merchants are able to benefit from the flow into their stores of potential consumers looking for financial services. It is important to note that under this model the law prohibits any actor to charge the end client any fee for the service. In fact, in Compartamos case it
is the merchant who pays a monthly fee to handle these services\(^1\). Banks are responsible of training the merchants in the use of the technology to make sure the service is delivered correctly.

Under the new model, it is expected that correspondents will be allowed to open accounts for clients directly on the merchant site. These types of accounts are called low transactional accounts and only require the person’s full name, complete address and a date of birth. Transactions done with these accounts should not surpass the limit of $10,000 Mexican pesos (equivalent to approximately $850 USD). If these stage of services is achieved Mexico will be giving a very important step toward achieving a better financial inclusion. There are currently hundreds of municipalities in Mexico where only correspondents and cooperatives provide financial services, and no bank branches exist.

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\(^{1}\) Compartamos asks the merchant for a $500 pesos ($40 USD) subscription followed by $150 pesos ($13 USD) monthly payments. Compartamos gives the equipment needed to handle the operations as a loan.
Compartamos’ strategy is to seize this growth opportunity. It has already established 2,000 correspondents to serve its pool of clients located in the State of Veracruz. To better understand the Bank strategy it is valuable to put some numbers into the national perspective:

This means that there are on average 25 banking correspondents for every 100,000 adults in Mexico, whereas Compartamos has established a network of 37 correspondents for each 100,000 adults at their pilot model for the State of Veracruz.

Table 1. Heavy investment in Veracruz bank correspondents.

<table>
<thead>
<tr>
<th>México Total</th>
<th>Compartamos in Veracruz</th>
</tr>
</thead>
<tbody>
<tr>
<td>10,998 Branches</td>
<td>6 branches</td>
</tr>
<tr>
<td>36,803 ATM</td>
<td>2 ATM</td>
</tr>
<tr>
<td>20,000 Correspondents</td>
<td>2,000 Correspondents</td>
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One of their biggest challenges to grow is the paperwork required to bring merchants into the network. More traditional banks have been able to grow their network faster because they have partnered with franchised chains of convenience stores like OXXO, which have around 10,500 stores in Mexico and Walmart with 1,000 stores (other banking correspondents in Mexico are Soriana, Chedrahui, Farmacias Benavides and Farmacias del Ahorro). However, most OXXOs are located in urban areas that have a highly served banked population. Compartamos is interested in reaching the
underserved population by partnering with un-branded convenience stores located at the poorest communities in Mexico. Each individual negotiation with the convenience stores needs to get an authorization from the CNBV. This process usually takes around 2 months.

The long-term plan is to become the biggest network of correspondents in Mexico by offering 36,000 sites. Compartamos believes this channel is the one that could offer the better balance between cost and services offered to clients.

Yastás

Yastás is the commercial name given to Compartamos’ correspondent network. Yastás is an expression that in Mexico means “done in seconds”, which refers to the amount of operations an individual is able to do in a small amount of time. Today, Compartamos’ correspondents are already handling the following operations:

- Service payments: water, electricity, land line, cable and sales by catalog (AVON and Arabela)
- Cellphone top-ups
- PIN updates
- Account balances
- Bank deposits/withdrawals
- Credit payments

Correspondents are key to avoiding dormancy among the new accounts. In India, for example, account penetration is nearly 35%, but fewer than one in four accounts is used to make debit payments once or more per month; and in rural areas the share of active debit accounts falls to one in seven. Enrolling new customers in underserved areas constitutes an up-front investment that must be amortized through regular services in payment, savings, credit or insurance. To change habits either for bill payment or for person-to-person transfers, the correspondent network must have a large footprint and a compelling case for convenience.

85% of Compartamos’ correspondents are grocery stores and 8% are stationary shops. On average these shops have 50 to 60 square meters of construction and have been operating for more than 3 years (to ensure the business is mature). Correspondents also need to have at least two people serving the stores at any given time. This is important because the money handled belongs to the store not to the bank and if the correspondent’s account runs out of money, one will need to go to the bank to make a deposit to increase the money in their account. Stores recognize that there is an increment of 25 to 27% in sales once they started operating as correspondents. CNBV estimates that the
breakeven transaction volume for bank correspondents is about one thousand transactions per month.

Yastás first 2,000 booths cost around $500 pesos ($40 USD) to produce and were mainly made of metal. However the next 10,000 for their expansion plan of 2013 will cost $100 ($8 USD). One of their biggest understandings of the Mexican market is the fact that these booths are able to print and stamp a receipt for every transaction made, including cellphone top ups. Booths not only are located within stores that people within the community trust but also are able to ease the fear of not having a “proof of payment” by issuing receipts. Also, clients are able to experience some savings. Compartamos made a study that showed that people spend around $35 ($3 USD) a week in transportation cost to make services payments.

Banking operations, handled by correspondents, are cheaper, compared to branches and ATMs. Their cost of operation is around $.38 USD. However this highly depends on the infrastructure already available at each community. Some communities in Mexico do not have the infrastructure to support the use of land lines nor Internet, and the only option available to generate banking instructions is through the use of mobile devices. For this reason Compartamos in some case needs to invest $700 USD on antennas that allow the communication of the banking instructions. However all of these obstacles are not stopping Compartamos bank in investing today, because they understand that there is a very big underserved segment that is already demanding financial services that the traditional bank is not able to provide. Compartamos is expecting to have a return of their investment in a three-year time frame, if this happens, Compartamos will be in a great position to keep with the innovation of product to serve this segment of the population.

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2 Cellphone top ups is a very spread service in Mexico. However, most locations do not issue a receipt.