

**Author**

Arjan Schütte,  
Associate Director  
The Center for  
Financial Services  
Innovation

**CFSI Director**

Jennifer Tescher

## Innovation Trends in Nonprofit Financial Services to the Underbanked

The financial services industry continues to look to underbanked consumers for fresh avenues of profitable growth. To accelerate their entry into this potentially lucrative market, forward-thinking financial institutions can benefit from looking at nonprofit innovators and engaging in creative collaborations with nonprofit organizations. By their very nature, nonprofits offer unique insights and access when approaching the market of unbanked consumers. They can act as incubators to develop pre-market products, and leverage their deep relationships with constituents to pilot new channels of distribution. These partnerships build on the core capabilities of each collaborator and provide a springboard for more robust solutions.

To support and encourage this trend, the Center for Financial Services Innovation (CFSI) seeks out and funds the most innovative nonprofits providing financial services to this market. In 2005, CFSI received almost 1,000 inquiries that yielded just under 100 applications for funding. While four projects were selected for funding the breadth and scope of all of the applications yielded a compendium of critical thinking, best practices and creative solutions. (See Appendix for list of 2004 and 2005 grants). An analysis of the applications uncovers emerging patterns that provide context for understanding where future opportunities lay for organizations – both for-profit and nonprofit – interested in serving these markets.

CFSI sought to maintain the momentum of its inaugural innovation fund by another round of support, sponsored by the Ford Foundation, for original thinking and new approaches from nonprofits which improve financial services to unbanked consumers. Innovations submitted to CFSI fell into three broad categories: financial products, marketing or distribution channels and business or revenue model. The most promising applications relied heavily on collaboration, niche marketing, and an energetic outreach program to develop appropriate products and services that acted as a gateway to the larger system. The innovations, below, will highlight these categories and practices.

### The Path to Wealth Creation

The ability to acquire assets and build personal wealth is a critical factor in achieving economic well being. For most low-income consumers, their path to wealth creation is long and nonlinear, a process described by Alternatives Federal Credit Union (Alternatives) as the Credit Path. The Credit Path starts with transactional services, which serve as an onramp to the financial services system. Next are savings products, followed by lending and credit building tools. Finally, once the previous bases are covered, an individual is ready for asset ownership.



The Credit Path developed by Alternatives Credit Union

While some proposals targeted a single product or service, several included a suite of services that addressed the needs of consumers along the Credit Path. The Greater Philadelphia Urban Affairs Coalition (GPUAC), for instance, presented a strategy to leverage the economics of consumer cooperatives to create scale and negotiate an array of reasonably priced products and services to serve primarily low- to moderate-income consumers. These would include discounts on consumer loans and insurance; reduced fees for bank accounts; attractive interest rates for savings accounts; reduced prices for a selection of consumer goods; financial counseling and education and, linkage to asset-building programs, such as Individual Development Accounts (IDA), the dedicated savings accounts that match the participants' contributions to the account at very favorable ratios by private and public institutions.

### Access to Financial Services through Transactions

Approximately one third of the proposals included basic transaction-based products to open the door to those currently outside the system. The Center for Community Change (CCC) proposed a pilot program using an established network of worker centers for a unique distribution strategy for Stored Value Cards (SVC) cards. The overall objective is to develop worker centers and other community-based organizations into a major distribution channel for a cutting-edge SVC: a premium pre-paid debit card program not exclusively tied to employers. By coordinating with three national networks of worker centers, the National Day Laborers Organizing Network, Enlace and Interfaith Worker Justice, the project gains scale and momentum. In addition to using the growing acceptance of stored value cards to entice un- and underbanked consumers into their program, the model also offers a potential revenue source to the worker centers acting as distribution channels.

Another example of innovative transactional services is the collaboration that joined together NCB Development Corporation's (NCBDC) National Disability Institute (NDI), the State of Florida, JP Morgan Chase, and the Center for Self-Determination. Together, they proposed to reach out to the unbanked subsegment of individuals with disabilities. It's proposed that Chase will offer financial services through a Freedom Account that will

include a menu of responsive, affordable deposit accounts, including stored value card technologies, to reach customers who might not otherwise qualify for a bank account.

The burgeoning remittance market has become a significant means for consumers to enter the financial mainstream. The Neighborhood Trust Federal Credit Union is a community development credit union that serves the predominantly Dominican community in Upper Manhattan. Neighborhood Trust looked to form a partnership with Asociación Dominicana para el Desarrollo de la Mujer (ADOPEM), a Dominican Development Bank and Non-Governmental Organization. Together they would develop a remittance product delivered by a shared savings account mechanism that would be affordable, facilitate savings, and serve as a form of collateral and creditworthiness in the underwriting for a shared loan product.

One Economy Corporation introduced an innovative, ultimately self-sustaining model targeting America's renters, who represent a high-proportion of unbanked consumers (more than 15 million). One Economy engaged two of the nation's largest housing development organizations and Citibank to provide a package of electronic and branch banking services to residents of affordable housing. Coupled with financial incentives for the use of electronic methods of paying rent, the strategy addresses a variety of barriers that low-income families must overcome to become banked. What is so unique is the creative pricing structure in which the housing organization trades a 5-10% loss on uncollected rents for a 3% rebate to tenants in return for electronic payment through a new bank account.

### **Protecting Against Setbacks with Savings**

Most applications included some savings feature, a likely reflection of the nonprofit community's recognition of asset building as a critical step on the path to self-sufficiency and economic well being. However, the Urban Insurance Partners Institute (UIPI), the insurance industry's nonprofit urban markets resource, distinguished itself with a category expanding proposal. Since mortgage lenders require insurance, insurance plays a critical role in helping lower-income consumers buy homes and build assets. While more companies are looking seriously at urban markets, they often cite a lack of underwriting or marketing expertise as a barrier to doing business. In collaboration with Pattern Recognition Systems, UIPI proposed improved modeling software for insurance underwriting in urban markets, to be followed by the development of a specialized platform adaptable to individual companies. A successful outcome should improve the capacity to accurately underwrite in urban markets, with the goal of substantially increasing insurance activity in these markets. In turn this should lead to better, cheaper products being available to serve a wider array of customers. By expanding the view of insurance beyond its common definition of an investment or risk management tool, the proposal offers a powerful tool to help consumers acquire and protect their hard won assets.

Southern Good Faith Fund (SGFF) joined with Southern Bancorp (Southern), First Bank of the Delta (FBD), and Southern Financial Partners (SFP) to develop a range of financial products designed to appeal to low income consumers and move them from simple transactional products to asset building products. A Credit and Savings Builder CD combines elements of a consumer loan with a traditional CD. As an example of how this product might work, the customer will put up \$100 of her own money, possibly from her tax refund savings account, and take a loan for \$900. The total \$1000 will be used to open a CD, which will be used to secure the loan. The term of the loan and the size of loan payments will be designed to be achievable by the customer. At the end of the loan repayment, the customer will have a positive credit experience that will be reported to the credit bureaus, and she will have \$1000 in savings.

### **Finding the Key to Building Credit**

The development of credit scoring technology has had the most significant effect on the evolution of financial institutions. Widespread use of computer models to evaluate and predict credit risk reduces underwriting costs and increases the opportunities to identify new customers. However, its ubiquity has closed off opportunities to those who do not have a formal credit history. A significant number of applications sought to redress this with a number of proposals related to credit score and credit reporting applications.

The barrier of credit scoring is further complicated by the fact that many small microenterprise and housing loan funds and the clients they serve have found themselves shut out of the mainstream credit bureau reporting system. The three major credit reporting agencies (Experian, Transunion, and Equifax) have instituted minimum account requirements in order for loan funds to report on their borrower's repayment history. Central Vermont Community Action Council proposed developing an intermediary organization, Credit Builders of America that would help those borrowers not served by the conventional lending market. B First centralizing and streamlining loan repayments for multiple organizations, Credit Builders would then aggregate and format the data for reporting to the three major credit bureaus. This in turn would provide credit building opportunities for the end customers and an important entry to more traditional funding sources.

As the credit scoring and data industry evolve with financial institutions becoming increasingly dependent on their services, advocates for the unbanked and low-income consumers are finding cost-effective and efficient ways to work with the system. Many immigrants consistently send home remittances in excess of several hundred dollars a month. These regular payments are evidence both of reliability and income, yet they cannot use them to build a credit history. The Appleseed Foundation is working to partner with banks and money transfer organizations to set up pilots that would collect data on remittance senders and test the predictiveness of remittance payments.

### Transitions into Ownership

Acquiring assets and building personal wealth is the last and most critical step along the Credit Path, providing the financial foundation of economic well-being for all income levels of society. In an effort to open doors, expand possibilities and transform low-income consumers into owners, nonprofits pioneered intriguing product hybrids that combined features from disparate products to create solutions that targeted the needs of low-income consumers. One example is Southern Good Faith Fund's CD loan product that can be used to purchase a home. An example is a collaboration of AFA Financial, SAVEDAILY.COM and the University of Akron's School of Business to combine features of IDA programs with features of Individual Retirement Accounts (IRA) to develop the Individual Retirement Development Account (IRDA). The model would use the same incentives that have helped low-income individuals attain homeownership and other assets to help increase retirement savings, by matching money with contributions from the public and private sector. The IDRA will be the first IDA focused on a long-term financial goal, retirement.

WECO Fund is working on a financial planning service for low-income people that provides individual planning services, facilitates the purchase of financial products, works with financial products providers to create new products more appropriate for the market we seek to serve, provide or organize educational workshops and seminars, and link this service with the other WECO programs and established partnerships. The overall goal is to demonstrate to financial market providers that this is an opportunity for them, a minor leagues for financial development.

### A note on Financial Literacy

Financial literacy remains at the core of every discussion about the unbanked with financial education components seen almost equally across a majority of the proposed projects. A study prepared for Alternatives indicates that clearly placing financial education programs alongside the different financial products helps financial institutions acquire new customers and build lasting, profitable relationships by moving customers along a product pathway to higher margin products, like mortgages.

### Conclusion

The role of nonprofits in developing financial products and services for unbanked consumers and low-income workers has changed dramatically. Once supporting players, they've now assumed a leadership role in articulating the needs of their constituents. The proposals cited in this paper hold important implications for the industry as a whole as mainstream financial markets look with greater eagerness to capture this growing market. From dissecting demographic segments into easy-to-target consumer groups, to blending and bending product categories to give birth to original products, to pioneering dynamic new channels for distribution, nonprofits offer important lessons in responding to the



needs of underbanked consumers. A key factor in the success of these collaborations for financial institutions is the enhanced ability to evaluate the performance of new ideas at the earliest stages of development and to make more informed decisions concerning future strategies. Most important, nonprofits are actively developing solutions that are viable, sustainable, and potentially profitable creating opportunities for the broader business sector.

## Appendix: 2004 and 2005 CFSI Grants and Investments

### 2004 Grants and Investments

- CD Tech and Community Empower's enhanced stored-value-card and web-based credit counseling services offered to low-wage workers in Los Angeles.
- Circle Lending's unique interpersonal loan credit reporting product, offered nationally, enabling consumers and entrepreneurs to leverage informal loans into traditional forms of credit.
- Community Action Project of Tulsa County's web-based benefits eligibility screening tool for use by low-wage Oklahomans via employers, to link government benefits to savings opportunities at area banks and credit unions.
- US Committee on Refugees and Immigrants' initiative to serve refugees across the U.S. via bank accounts with electronic deposit and travel loan repayment system; refugee-specific financial education and training, and employment incentive payments.

### 2005 Grants

- Appleaseed Foundation, which will research the transparency of foreign exchange rate markup charged for remittances and then launch a fair exchange rate branding campaign. These fees are often poorly disclosed and can represent as much as 90% of total fees.
- The Center for Community Change will select and deploy a stored-value card solution pilot to unbanked workers in coordination with three national networks of worker centers which organize workers, undertake advocacy campaigns, and provide a range of critical social services to low-income workers.
- Central Vermont Community Action Council and Association for Enterprise Opportunity will research and implement a method to integrate microlending data into the established credit system, enabling low-income entrepreneurs to build and improve their credit scores.
- The Urban Insurance Partners Institute has accepted a challenge grant to apply new analytical tools to non-traditional insurance data and prototype improved urban underwriting practices.

**For further information contact:**

Arjan Schütte  
Associate Director  
The Center for Financial Services Innovation  
2230 S. Michigan Ave  
Chicago, IL 60616  
312-881-5840  
312-881-5801 (fax)  
arjan@cfsinnovation.com  
www.cfsinnovation.com

The Center for Financial Services Innovation (CFSI), an initiative of ShoreBank Advisory Services with support from the Ford Foundation, was founded in 2004 to encourage the financial services industry's efforts to serve un- and underbanked consumers. The Center provides funding for innovative solutions, a meeting place for interested parties and resources for testing products and services. CFSI also identifies, develops and distributes authoritative information on how to respond to the needs of the underbanked profitably and responsibly. CFSI works with banks, credit unions, technology vendors, alternative service providers, consumer advocates and policy makers to forge new relationships and pioneer products and strategies as it seeks asset-building opportunities that create value for both customers and companies. For more on CFSI, go to [Hwww.cfsinnovation.com](http://www.cfsinnovation.com)

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v1 **To Contact CFSI**

2230 South Michigan Avenue  
Suite 200  
Chicago, IL 60616

312-881-5856 (Phone)  
312-881-5801 (Fax)

info@cfsinnovation.com  
www.cfsinnovation.com