BUILDING THE BUSINESS CASE FOR YOUTH FINANCIAL SERVICES:

FURTHER INSIGHTS FROM THE YOUTHSTART PROGRAMME

BRIEF

The MasterCard Foundation

UNCDF

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YouthStart's most recent publication, 'Building the Business Case for Youth Financial Services: Further Insights from the YouthStart Programme,' is a concise summary of an elaborate study executed by the Frankfurt School of Finance & Management on the business case for youth financial services (YFS) in selected financial service providers (FSPs) of sub-Saharan Africa.

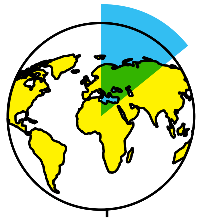
The publication outlines the importance of YFS for sub-Saharan Africa, provides the reader with three case studies tackling the profitability question of youth savings and loans with integrated financial education components, and offers recommendations for future endeavours. The publication, which is clear and accessible, will be of interest to a wide audience, from FSPs and practitioners, national and international NGOs, to central banks and other policy-setting bodies.

For a complete overview of the research, please visit our website and download the publication:

http://www.uncdf.org/programme/publications?field_program_tid=428

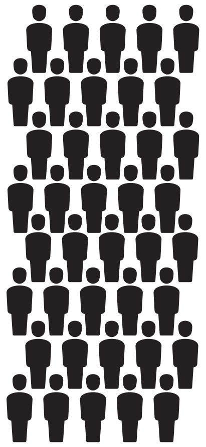
SUMMARY IN PICTURES

WHY?



CURRENTLY, THERE ARE ABOUT **1.2 BILLION** PEOPLE AGED 15 TO 24, REPRESENTING AROUND **1/6** OF THE WORLD'S POPULATION

WITH ALMOST **200 MILLION** PEOPLE AGED 15 TO 24, AFRICA HAS THE YOUNGEST POPULATION IN THE WORLD



AFRICA'S YOUTH POPULATION IS SET TO **DOUBLE BY 2045**

The International Labour Organization estimates that:

60% OF AFRICA'S UNEMPLOYED ARE YOUNG PEOPLE

ON AVERAGE 72% OF AFRICAN YOUTH LIVE ON LESS THAN **US$2** PER DAY

GREATER FINANCIAL INCLUSION

SHORT TERM:

HELP YOUTH MANAGE THEIR FINANCES

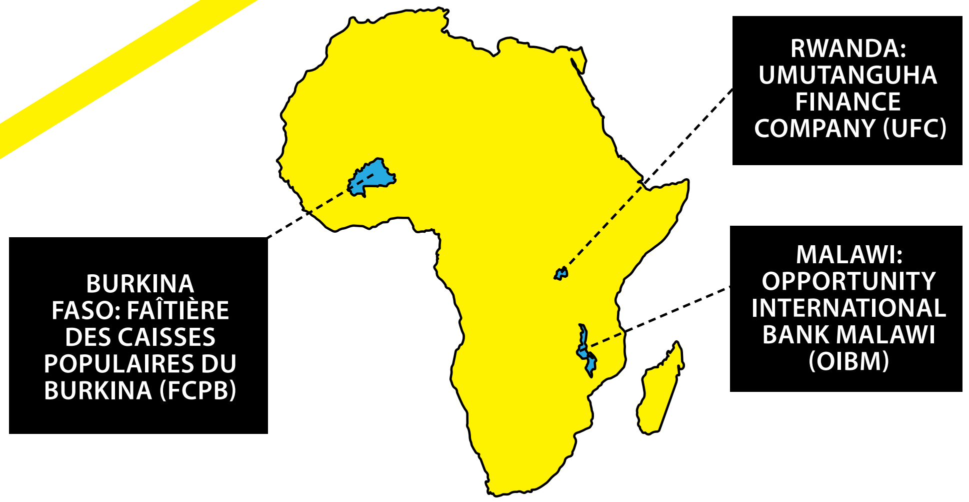
LONG TERM:

HELP YOUTH REALIZE THEIR ECONOMIC POTENTIAL

HOW?

YouthStart, a **$12 million UNCDF programme** in partnership with The MasterCard Foundation, was launched in **2010** to spur innovation and delivery of financial services to youth in Africa and mainstream them into inclusive financial sectors.

THE FRANKFURT SCHOOL CONDUCTED AN **IN-DEPTH PROFITABILITY ANALYSIS** OF 3 OF YOUTHSTART'S 10 FSP PARTNERS:



THE STUDY ATTEMPTED TO **ANSWER THIS QUESTION:**

What makes youth accounts (both savings and loans targeting youth between the ages of 18 and 24) attractive—or not—for financial institutions in different contexts?

The study resulted in **NEW INSIGHTS:**

- For there to be a business case for youth financial services, they must be integrated into the overall approach of the FSP and not be simply stand-alone offerings.
- Standardization of processes helps an FSP increase efficiencies (lower costs) to deliver services to youth.
- YFS in tandem with financial education should be viewed as a means to financially educate youth, hence creating financially responsible clients.

THE IMPORTANCE OF INCLUDING YOUTH

With almost 200 million people aged 15 to 24, Africa has the youngest population on the globe. Sub-Saharan Africa is also the only region of the world in which the number of young people continues to grow substantially,[1] predicted to double by 2045.[2]

Each year, there are an estimated 10 to 12 million youth entering the labour market in sub-Saharan Africa,[3] and unfortunately, there are insufficient jobs to accommodate the number of young people in search of work. Youth unemployment rates are double those of adult unemployment in most African countries,[4] and amongst employed youth, the proportion of underemployed is significantly higher than that of adults. The costs of inadequate employment are high. Poverty is the most obvious consequence. On average, 72 percent of African youth live on less than $2 per day. Additionally, widespread unemployment in Africa's largest population cohort can lead to social unrest.

Financial inclusion is an effective tool for empowerment of the poor as well as a means to improve efficiency of capital allocation and job creation.[5] It is an effective tool that can be implemented relatively fast. Focusing on how best to design and deliver youth financial and complementary non-financial services makes a lot of sense, in particular for sub-Saharan Africa.

YouthStart, a UNCDF initiative established in partnership with The MasterCard Foundation, aims to increase access to financial services for low-income youth in sub-Saharan Africa. The programme supports FSPs to design, test and scale up sustainable services tailored to the needs of young people, while helping to create an enabling regulatory environment for young people to access the right financial and other services they need to make sound financial decisions, build a strong asset base, and create sustainable livelihoods for themselves. As of December 2014, over 514,000 youth (46 percent young women and girls) had saved close to $14 million either in the form of an individual savings account or a group-based savings mechanism; close to 72,000 had received an individual or a group loan to start up or expand their own business; and over 502,000 had participated in financial education sessions.

FIGURE

Summary of YouthStart programme achievements (December 2014)

SAVINGS	OVER **514, 000 YOUTH** (46 PERCENT YOUNG WOMEN AND GIRLS) HAD **SAVED** CLOSE TO **$14 MILLION**
LOANS	CLOSE TO **72,000** HAD RECEIVED AN INDIVIDUAL OR A GROUP **LOAN** TO **START UP OR EXPAND** THEIR OWN **BUSINESS**
EDUCATION	OVER **502,000** HAD PARTICIPATED IN **FINANCIAL EDUCATION SESSIONS**

For more information, visit http://www.uncdf.org/en/youthstart

THE FRANKFURT SCHOOL STUDY

In 2014, The MasterCard Foundation commissioned the Frankfurt School to conduct an in-depth profitability analysis of three of YouthStart's FSP partners. The objective was to deepen understanding of (1) the institutional revenue and cost drivers that affect profitability of serving the youth segment (age 18–24),[6] and (2) the external market, institutional and segment specific levers that will influence a decision to enter the youth market and how to design the products. To achieve the research objective, the Frankfurt School applied a multidimensional study using both quantitative and qualitative tools. This two-pronged approach led to a cost/revenue analysis for products targeting youth, analysed within a qualitative assessment of the market and institutional contexts. By spending three weeks at each FSP, the Frankfurt School was able to apply an activity-based costing method, modelled on a proprietary Product Costing Tool.

This study differentiates itself and delivers meaningful insights due to its focus on operational processes required to produce a single loan or savings account and the corresponding allocation of costs, resulting in the calculation of the marginal cost per savings or loan account issued. The methodology not only concentrates on the origination of costs but also determines the income produced by the manner in which those costs were used. As such, the study uses the concept of opportunity costs for the calculation of the profitability of youth savings accounts.

CONCLUSIONS

The main finding related to the business case for YFS at the selected FSPs is that it remains challenging to implement a profitable savings product for youth, even more so than for adult small savers. The business case for youth loans appears to be in reach for well-managed FSPs.

To make an immediate business case for youth savings, an FSP would need to have a commercial approach towards the youth clients it targets. It would also need to make accounts more user friendly through alternative channels, multiple functions and possibly interest payments to ward off competition of commercial banks. FSPs approaching youth savings from a developmental perspective—focusing on rural, vulnerable, early youth—should familiarize themselves with best practices and strive to be as efficient as possible. They should realize, however, that a business case for youth savings is not likely to be made, even in the mid- and possibly the long term. They will either need to subsidize their youth savings product internally or receive external funding. Fortunately, the business case for youth loans is possible even for those FSPs that foster a more social agenda. When an efficient FSP is good in underwriting its normal loan portfolio, resulting in low portfolio-at-risk levels and profitable products, it is likely that the FSP can do the same for prospective youth clients. It is critical, however, that the FSP clearly segment its youth market and understand the needs and capacities of the youth. Doing so requires in-depth market research. One of the FSPs clearly illustrates that a meaningful pre- and post-disbursement training that ties into the needs and capacities of the youth can have

1 'The power of 1.8 billion: Adolescents, youth and the transformation of the future' (E.14.III.H.1-E/9,500/2014).

2 The Brookings Institution, 'Foresight Africa: Top Priorities for the Continent in 2013,' January 2013. Available from http://www.brookings.edu/research/reports/2013/01/foresight-africa-2013

3 Brandon Routman and John McArthur, 'Youth Unemployment in Sub-Saharan Africa: Varying Solutions to Complex Challenges,' 12 August 2014. Available from http://www.brookings.edu/blogs/africa-in-focus/posts/2014/08/12-youth-unemployment-africa-mcarthur

4 Alexandra Hervish and Donna Clifton, *Status Report on Adolescents and Young People in Sub-Saharan Africa: Opportunities and Challenges,* The State of World Population 2014 (Johannesburg, South Africa, UNFPA, 2012) p. 12. Available from http://www.prb.org/pdf12/status-report-youth-subsaharan-Africa.pdf

5 Peter Kasprowicz and Elisabeth Rhyne, 'Looking Through the Demographic Window: Implications for Financial Inclusion—Financial Inclusion 2020 Project: Mapping the Invisible Market,' Publication 18 (Washington, D.C., Center for Financial Inclusion, January 2013). Available from https://centerforfinancialinclusionblog.files.wordpress.com/2013/02/looking_through_the_demographic_window.pdf

6 The minimum age for youth financial services, particularly savings products, can be lower in certain countries.

a positive influence on the credit risk costs that ultimately represent a key driver towards product profitability in an efficiently managed FSP.

Financial education is a key element by which youth products differentiate themselves in operational procedures from standardized products. Financial education is about the combination of attitude, knowledge, skills and self-efficacy needed to make money management decisions.[7] When looking at the business case for YFS at the selected FSPs, it is important to examine the approach used for financial education, as it is both a necessary complement to YFS as well as an additional investment. Two of the FSPs use the 'critical minimum' approach. This methodology provides youth with multiple short and targeted sessions, which allow them to internalize content and effectively nudge them towards a culture of building financial capabilities.
To achieve a high impact at low cost, the method uses minimal materials with a focus on key messages, through standardized sessions with simple facilitation techniques.

KEY LESSONS

YFS need to be part of the overall market approach of an FSP. The processes of service offerings must be well integrated, and traditional products must be connected with YFS.

Standardization of processes helps an FSP increase efficiencies (lower costs) to deliver services to youth. Whilst products seem differentiable to clients, the actual production process is best organized when it is similar across all products, with the exception of the financial education component.

YFS in tandem with financial education should be viewed as a means to financially educate youth. This approach will facilitate youth to become financially responsible and capable clients who will increase their savings balance over time and/or utilize other financial products. Initially, however, youth savings accounts can lead to the accumulation of large numbers of dormant accounts with very low balances. The main challenge for an FSP is to engage these dormant account holders over time and ensure that a certain percentage become financially and economically active.

FSPs could consider establishing a clearer segmentation of their youth clients and cross-subsidizing more vulnerable youth with services provided to better-off youth. For example, if one of the FSPs in the study successfully converts a savings account into an actively managed savings account with a balance of $280, the revenues generated within just one year compensate for the cost of an additional nine accounts that remain dormant. Another form of cross-subsidization is seen between youth products. When eligible for a youth loan, one youth savings client from the same FSP will recover the losses of 33 dormant youth savings accounts.

The use of technology for creating alternative delivery channels is viewed as a necessary path to engage youth to actively use their savings account, as it will reduce disproportionately high transaction costs, reduce time spent by clients and provide clients with an active medium to manage finances. The study, however, also shows that technology does not necessarily have a significant impact on the opening costs for youth accounts, in particular when considering the financial education component.

[7] Microfinance Opportunities for Center for Financial Inclusion, 'What Is "Financial Capability?"' 1 November 2013. Available from http://cfi-blog.org/2013/11/01/what-is-financial-capability/

Youth loans have a different set of characteristics. The first challenge for an FSP is to institutionalize YFS beyond the youth savings product. As FSPs have limited resources, there can always be a tendency to divert resources to more lucrative lending products. The second challenge for the FSP is to design the product in such a manner that the perceived risks are sufficiently mitigated. A large part of the risk mitigation can be realized through meaningful financial training. The Frankfurt School research also shows how a slight improvement in portfolio at risk already covers the costs of financial education.

An important observation of the youth loan products is that the institutional muscle of the FSP has a direct positive or negative correlation on the performance of the youth loan portfolio, i.e. good institutions make good loans.

RECOMMENDATIONS

Considering Africa's burgeoning youth population and the accompanying high unemployment rates, financial inclusion initiatives should include a clear youth strategy. As many of the financially excluded youth are vulnerable and hard to reach, incorporating them into the formal financial system in a sustainable manner will remain a challenge.

The following is therefore important:

- For all stakeholders to realize that the traditional brick-and-mortar approach will not be effective for furthering meaningful access to youth savings accounts.
- For all stakeholders to further research the impact of alternative channels on the costs and usage of youth savings accounts.
- For all stakeholders to expand research over a longer period of time to understand under which circumstances vulnerable youth can become more economically active, support higher savings balances and require other financial services. It is important to understand what kind of financial education and business and entrepreneurship training is required, what the best delivery mechanisms are, and what the impact is on youth savers.
- For policymakers and donors to understand the importance of youth financial inclusion and to not be discouraged by the long road to commercial success. Given what is known now, donors should facilitate more targeted and focused experimentation and innovation, particularly around business models and delivery mechanisms.

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