



TEMENOS
THE BANKING SOFTWARE COMPANY

The Existential Threat to Credit Unions



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Executive Summary

A major existential threat faces credit unions today due to their inability to scale; losing their member base to virtual, internet-based, financial-technology platform companies (fintechs) offering quick, easy and consumer-friendly services via mobile third-party payment applications, albeit at onerous rates. This would be a huge loss to many emerging market economies.

Credit unions, also known as savings and credit co-operative societies (SACCOS) or financial co-operatives, make a hugely important contribution to social and economic development. Unlike many financial market interventions over the past 30 years aimed at increasing access to financial services, credit unions monetise local assets and distribute them to qualified borrowers. Local distribution is fundamental to local economic sustainability.

These community-based, co-operative financial institutions have been operating in emerging markets for at least 50 years and have become local institutions. The relationships they have built are real and tangible, including teaching financial literacy, thrift and investment in community. This is important because their work leaves a positive long-term legacy to members, members' families and the communities in which they live.

Historically, they have been found in rural and remote areas of many emerging economies and are often the only financial institution available to the community. Private, member-owned, they offer high social value by keeping the economic benefits of their lending activity within the community – all profits are returned to members and/or are reinvested into the communities in which they operate.

In most developing countries, credit unions are the predominant providers of external financing for micro, small and medium enterprises (MSMEs), which **contribute up to 33 per cent of national income** and create four out of five new jobs, according to the World Bank.



Credit unions arose to provide the common person with access to financial services and a self-help alternative to predatory money lenders. Credit unions still have a role in providing lower-cost access to financial services and an ethical alternative to predatory lending via easy-access payments.

Brian Branch - president and chief executive officer of the World Council of Credit Unions



In Kenya, for instance, SACCOS have been reported to contribute more than 45 per cent of gross domestic product and it is estimated that at least one in two Kenyans directly or indirectly derives their livelihood from these co-operative organisations. In Tanzania, co-operatives (including SACCOS) contribute about 40 per cent to the country's GDP and employ 94.7 per cent of school leavers every year by financing SMEs, the majority of which are located in rural areas and wholly depend on the co-operative system for external financing.

The challenge faced by credit unions today is the ability to scale and retain their community-based attributes.

The Fintech Boom

With modern fintech in emerging markets exploding at a phenomenal rate, credit unions have the opportunity to leverage their social relevance with the internet, using technology platforms to deliver modern banking services to their members. The ability to digitise without having to acquire and manage technology has the potential to unlock the massive investment of the credit union social network.

60.500 Credit Unions in **109** countries on **6** continents

serve **223 million people**

8.3%
penetration

\$1.5 trillion in savings & shares (USD)
\$1.2 trillion in loans (USD)

\$185 billion in reserves (USD)
\$1.8 trillion in assets (USD)

There are some nine countries in Africa where credit unions comprise more than 1 million individual members and six such countries in Asia. Worldwide there are 233 million individual members in 109 countries. This represents a vast potential base to digitise and on which to build a global campaign for sustainable access to finance with all of the associated benefits of the investment in human capital and community that credit unions represent.

Being member owned, pricing is consumer friendly and profits tend to be modest, leaving little opportunity to accumulate the levels of internal capital needed to invest in modern technology. Many use simple distributed software or rely on manual processes. This gap creates opportunities for fintechs working with mobile network operators (MNOs) to

introduce new, fast modern payment services. With member bases in the millions and physical branches throughout the countryside, credit unions are ideal targets as fintech agents and their members as fintech customers.

The result: there is a fintech boom in developing countries. Fintech in Africa, for example, has become the second most-popular destination for venture and private equity funding in the technology sector, attracting nearly 30 per cent of total funding in 2015, according to figures from the African Tech Start-ups Funding Report.

If credit unions in emerging economies are to survive disruption, they need to start offering the modern services that their members want.



Beware the Trojan Horse

At the heart of the issue is the ubiquity of mobile phones and the huge growth in mobile banking services, particularly in emerging markets. Those organisations that can provide mobile payment services will grow; those that can't won't. It's about providing a modern service that fulfils the needs of customers.

Credit unions reach into remote communities through networks of members, branch offices and experienced, trusted staff. But access to the technology required to provide a mobile banking experience, whether owned, rented or managed, as mentioned above, tends to be beyond most of them.

Fintechs have already tapped into those networks by providing their services using credit unions as agents. The credit unions receive a commission for each member transaction on the fintech platform. Ostensibly, this seems like a great commercial idea: the credit unions are offering modern payment services while getting a commission with little or no effort.

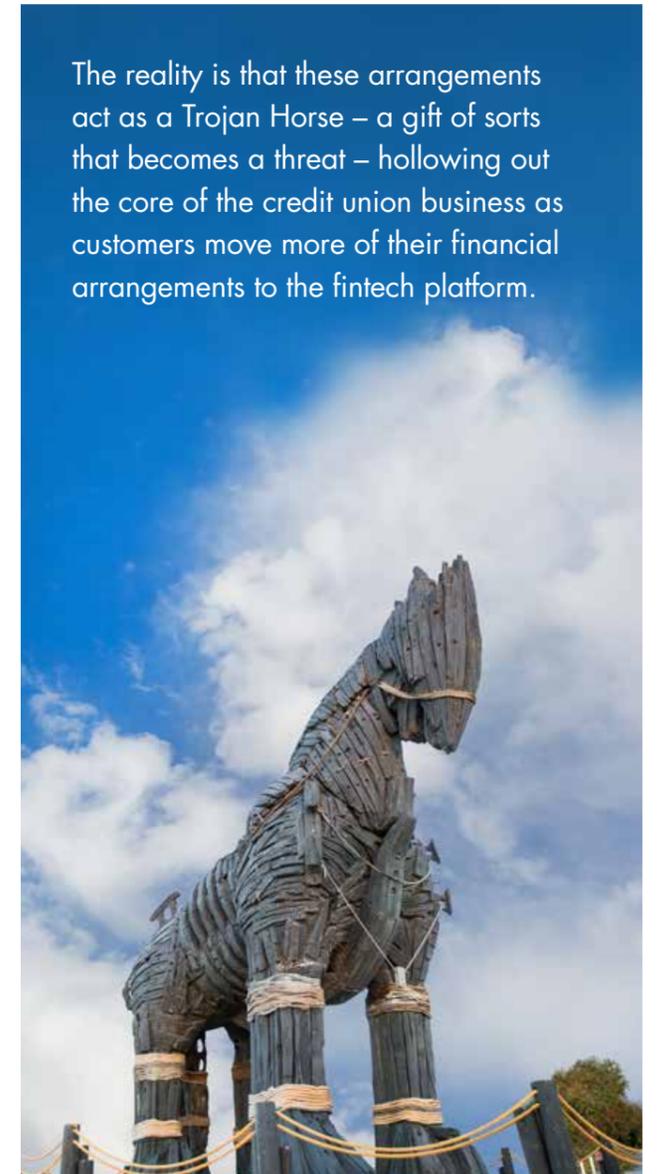
The co-operative network quickly becomes a well-staffed physical agency for the fintechs, providing essential locations for on-boarding clients and cash pay-points. Members move money out of the credit union on to the competitor's platform and spend a significant amount of money in fees for payments there. The transaction revenue is lost to the credit union and members are soon targeted for short-term consumer credit fuelling indebtedness at rates of up to 600% APR¹. Higher net-worth members are targeted for a wider set of financial services.

Credit unions are delivering their members to direct competitors. A seemingly quick and smart mobile credit and payment solution results in the loss of decades of work and trust built up in the co-operative institution.

Without modern services, credit union members, especially youth, will go elsewhere for their financial services needs. The credit union needs to find a way to compete with the fintechs, MNOs and other commercial financial services providers.

Credit unions need to employ the same technology as the fintechs to retain and grow their membership. Using technology to build their own payments platforms, in order to remain financially viable, will attract new members and help communities continue to create wealth and improve lives.

The reality is that these arrangements act as a Trojan Horse – a gift of sorts that becomes a threat – hollowing out the core of the credit union business as customers move more of their financial arrangements to the fintech platform.

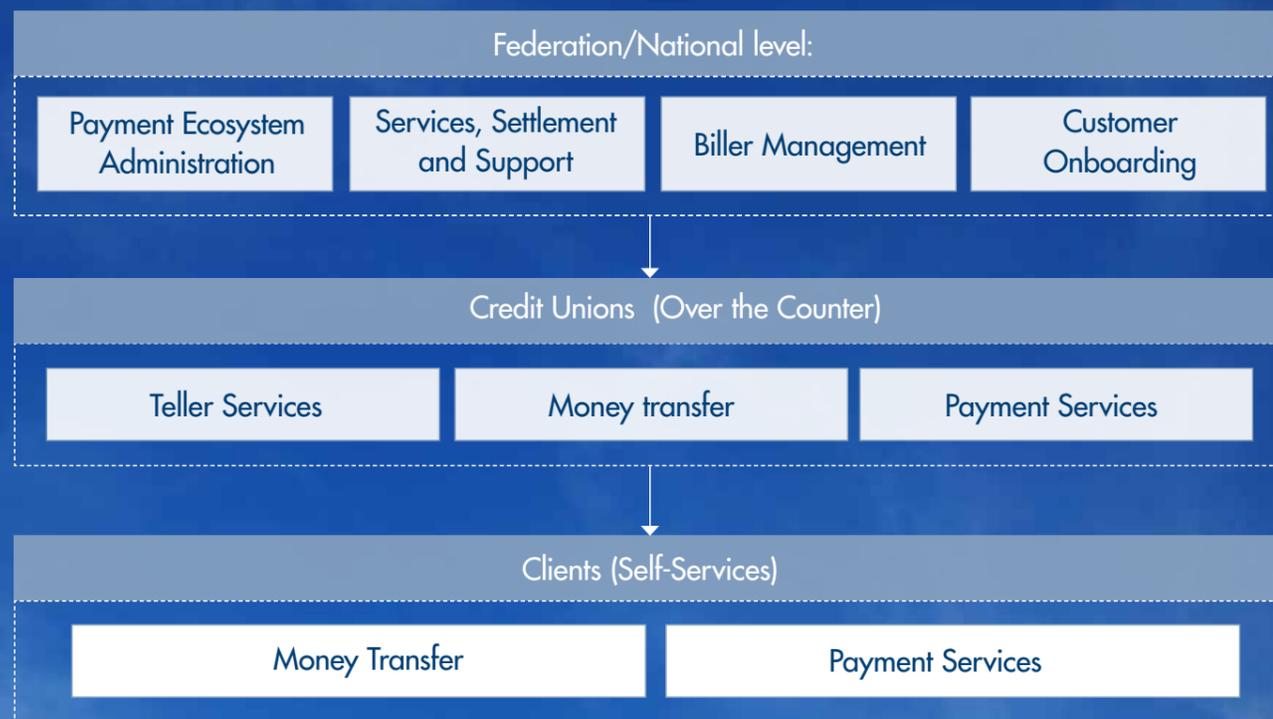


The Solution

The solution is to advance a concept that has long been advocated by credit unions: shared networking. Mobile and cloud technology can be leveraged to deliver a payments platform that is shared across a network of credit unions. Once such a platform is available, members can subscribe to credit union-owned digital platform services at a lower cost and access payments, savings, loans and other credit-union financial services from mobile devices.

Using mobile payments and core banking with subscription-based Software as a Service (SaaS), credit unions can own the business of payments and digital services without having to own or manage the software or hardware behind them. SaaS is a hosted solution so there is no need for in-house technical expertise, further reducing risk and cost, while satisfying the demand of members for quick, easy mobile payments, as well as other services accessible from a shared platform.

The shared platform business model



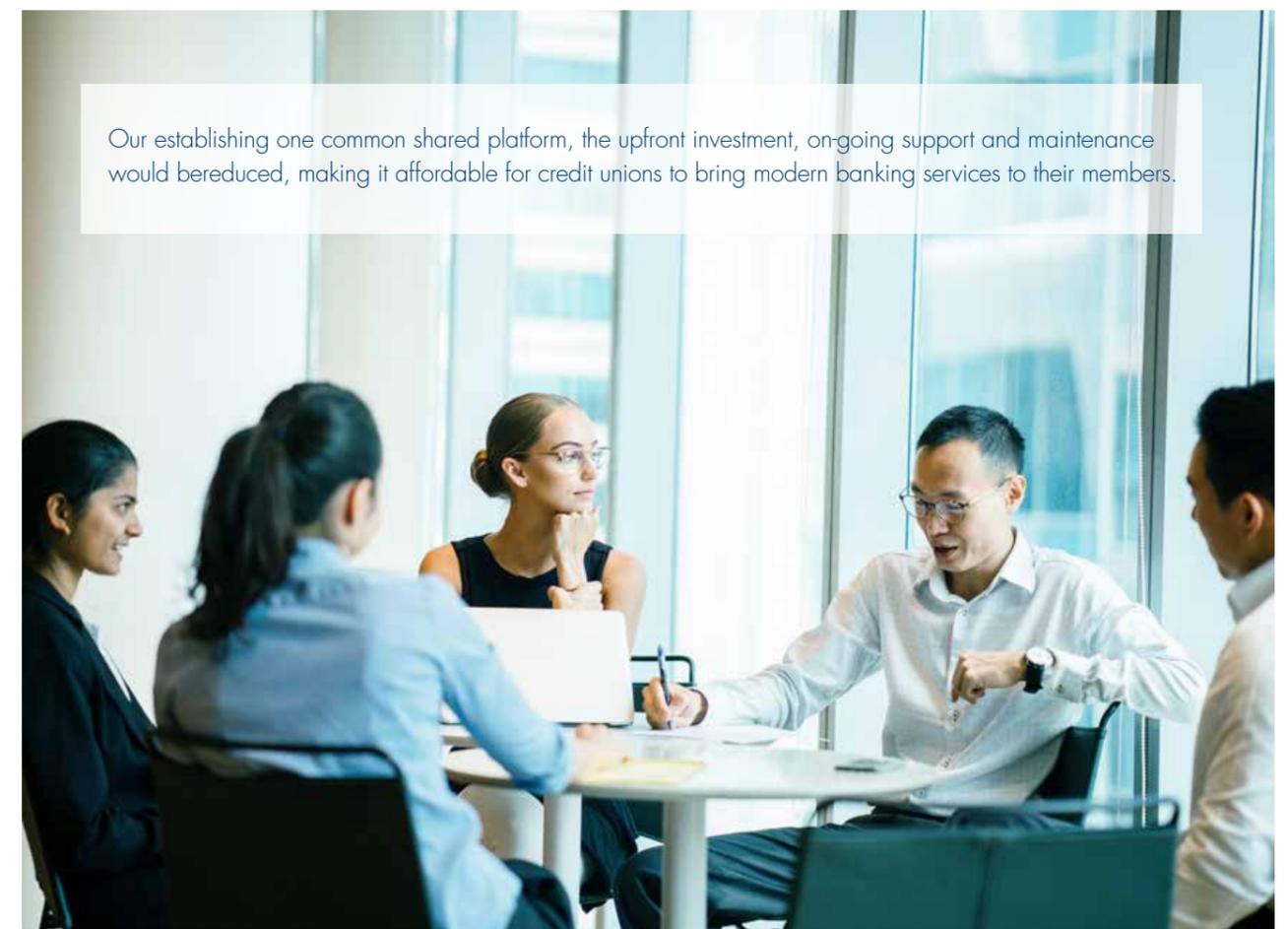
By using SaaS, IT becomes an operating expense; by sharing the scalable services, it becomes affordable. It does not require changes to credit unions' back office, they can keep what they have or adopt the SaaS option. The APP does not replace a credit union's IT systems. Rather it extends existing capacity and offers choices without demanding more people, skills or capital.

In Action: the Asian Confederation of Credit Unions

In south-east Asia, a group of credit unions has built its own common payment platform that provides modern banking services to their members.

The ACCU is a regional group of national credit-union associations and second-tier financial institutions that follows international credit-union operating principles. It serves more than 21,947 credit unions with 38.1 million members in 26 countries across Asia. In 2015, it started work on a common banking and payment platform – the APP (ACCU Payments Platform) – as part of its strategy to build a self-sustaining business that supports co-operative technology and payments throughout the region.

ACCU's APP offers access to modern, competitive payment services as well as integration with third-party networks, thereby expanding the range of services available to members and retaining revenue within the credit-union network, contributing to institutional sustainability and meeting member needs for modern mobile financial services.



Copycat

The ACCU model, provided in partnership with Temenos, its digital banking partner Software Group, and cloud service provider Microsoft, opens up access for credit-union networks to a modern payment platform in an affordable way.

The benefits are multiple: the credit unions are meeting members' needs;

members enjoy access to their accounts from their mobile phones;

credit unions within the network can access payments through a web interface (screen).

Where a credit union has suitable back-office technology, the ACCU APP can connect direct; where the credit union does not have suitable back-office core banking technology, it can use a web interface (screen) or migrate its share, savings and loan accounts to the cloud-based system.

Large or small, rural or urban, all credit unions and other financial co-operatives can provide their members with a credit union-owned payment platform accessible via their mobile phones.

One connection at the national level gives members access to payments and all the other services available through modern platforms including ATMs, remittances, bill-pay, account information, P2P and so on. Additionally, air-time top-up, insurance and other online services can be delivered the same way.

The arrangement allows credit unions to protect their businesses from competing fintechs, escape the costs and overheads of managing local systems and accelerate their digital strategy without subordinating themselves to competing financial services and payment providers. It means credit unions can unlock the potential of their own social networks, grow their membership and really achieve scale.

Short, Medium and Long-term Benefits

A common, shared payment platform across a network addresses many issues facing credit unions. It allows them to protect their unique position within the community so they can continue to promote financial literacy and foster a culture of saving and responsible borrowing. In addition, the platform connects all members across the network. No longer are they a member only of the branch where they joined. Now they can conduct business at any credit-union office in the country, strengthening the credit-union brand and services. The entire network becomes more efficient, bringing down operating costs with more access to services and accurate reporting metrics to inform national risk management and training programmes.

Finally, the subscription service is low-cost and allows the credit union to recapture the sums members are currently spending on competing platforms. And market-based fees usually quickly recoup the technology costs. Typically, the first two or three transactions covers them all. Excess fee revenue flows directly to the bottom line to enhance services, be invested in the community or returned as dividend to members, or be retained as capital.

The business model overcomes the problem of having to find the capital to build expensive infrastructure and allows credit unions to digitise without having to acquire and retain the technical skills to manage complex technology.

The result

Credit unions can make an important contribution to financial inclusion goals while delivering high socio-economic value. Indeed, accelerating the growth of established **community-based financial institutions** is a far more efficient and valuable way to expand and sustain financial inclusion than trying to start a new institution from scratch.



Seize the Moment

Credit unions are at a crossroads; they can invest in the future or risk being marginalised to the point of irrelevance. Critical and difficult decisions need to be made now. It will only be harder next year and it will not be long before we see some of our most promising credit unions become moribund. This would be a tragedy that future leaders will tell us could have been avoided. If we don't act now, not only will some of the world's most vulnerable communities lose access to affordable, trusted and effective financial services, but they will be poorer. And sadly all those who could have joined and benefitted will not be able to realise their potential.

Fintechs don't hold all the cards. Credit unions have a great deal of information on members and enjoy a relationship of trust. Members, their families and their communities can build on the social fabric of the network that has been nurtured over decades.

People are the greatest asset of the credit-union system and technology can unlock the real potential.

The ACCU APP model is practical and within reach of every credit-union network that has the foresight and courage to embrace it. Credit unions no longer have to deliver their members to the competition to give the impression of modernity in return for the poisoned chalice of a commission.

They can own their own payment platform and keep all the members' spend within the credit-union system, building on their relationships and their members' trust.

Credit unions can then use their strategic investment in people, communities and infrastructure to compete directly with fintechs, MNOs and third-party payment platforms.

The solution gives credit unions and members of all economic status equal access to innovative tools and financial resources to take control of their futures and see their communities thrive.

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The World Council of Credit Unions (World Council or WOCCU) is the leading international trade association and development agency for credit unions and cooperative financial institutions. World Council promotes the self-sustainable development of credit unions and other financial cooperatives around the world to empower people through access to high quality and affordable financial services. World Council advocates on behalf of the global credit union system before international organizations, and works with national governments to improve legislation and regulation. Its technical assistance programs introduce new tools and technologies to strengthen credit unions' financial performance and increase their outreach.



Next Steps



Find out more about Temenos solutions for Credit Unions.
Contact us at info@temenos.com

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Temenos AG (SIX: TEMN), headquartered in Geneva, is the world's leader in banking software, partnering with banks and other financial institutions to transform their businesses and stay ahead of a changing marketplace. Over 3,000 firms across the globe, including 41 of the top 50 banks, rely on Temenos to process both the daily transactions and client interactions of more than 500 million banking customers. Temenos offers cloud-native, cloud-agnostic front office and core banking, payments, fund management and wealth management software products enabling banks to deliver consistent, frictionless customer journeys and gain operational excellence. Temenos customers are proven to be more profitable than their peers: over a seven-year period, they enjoyed on average a 31% higher return on assets, a 36% higher return on equity and an 8.6 percentage point lower cost/income ratio than banks running legacy applications.





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