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Findings Dissemination Workshop.

Financial Sector Deepening Uganda Project-
Linkage Banking Pre-Feasibility Study

14 August 2007



Audit • Tax • Consulting • Financial Advisory.

Agenda

- Background of the Study
- Constraints in the Financial Services Sector
- Linkage opportunities identified
- Other considerations for the evaluation of identified linkages
- Conclusion & way forward
- Q&As

Background of the Study

- MDI regulation led to significant increases in branching costs
- Operations of MDIs, Tier I and Tier II Financial Institutions, as a result, restricted to urban & semi-urban locations
- FSDU supporting eligible regulated Financial Institutions (Linkage Implementers), to work with Consultants to undertake feasibility studies for linkage banking interventions aimed at serving Tier IV Financial Institutions

Constraints in the Financial Services Sector

- Security Factors
- Infrastructure
- Socio-Economic Factors
- Regulatory Factors

Constraints (Cont'd)

Security factors:

- Historically, the Physical Security of Personnel & Assets has been threatened by the LRA insurgency in Northern Uganda:
e.g in 2005, a newly opened branch of Agarú SACCO in Pader was ransacked by rebels – it was closed thereafter; in another incident, a Branch Manager of Kitgum SACCO was killed by LRA rebels
- Perception of insecurity is high. Despite on-going peace talks, there is still little confidence within the financial sector to invest in Northern Uganda

Constraints (Cont'd)

Infrastructure:

- **Unreliable & insufficient electricity:**
e.g. Pakwach Nam SACCO is run entirely by diesel generator, while Alutkot SACCO does not even have that luxury
- **Poor road network in terms of quality, accessibility & transport medium:**
e.g the only public means of transport from Kitgum to Pader is single cabin pickups
- **Low ICT penetration:**
this was especially evident in Pader

Constraints (Cont'd)

Socio-economic factors:

- Poor savings culture & distrust of commercial banks
- High % of economically inactive population
- Depression of economic activity as a result of IDPs
- Skills gaps
- HIV/AIDS
- Gender & cultural factors

Constraints (Cont'd)

Regulatory factors:

- The MDI Act 2003 has increased investment & operating costs, thus limiting branching activities
- Weak regulatory framework of SACCOs

Linkage Opportunities Identified

MFI shortlisted for detailed study:

- Agarug SACCO
- Kitgum SACCO
- Alutkot SACCO
- Pakwach Nam SACCO

Discussion of Linkages

Classification of Partnership Opportunities:

1. Branching
2. Products & Services
3. Technology & Operations
4. Risk management & governance

Discussion of Linkages

1. Branching:

Major variations of Branching activities identified:

- Mobile banking
- Micro-finance service centre
- Agency
- Franchise

Discussion of Linkages

1. Branching (Cont'd):

Mobile banking:

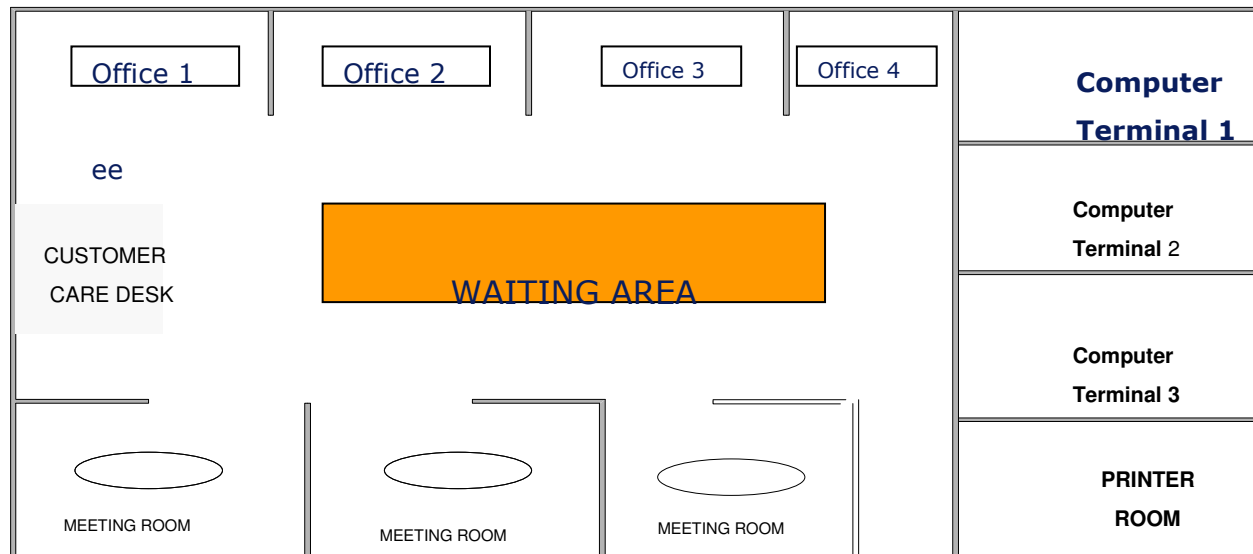


Vehicle equipped with modern GSM communication makes periodic trips to strategic locations to allow SACCOs & their clients access banking services

Discussion of Linkages

1. Branching (Cont'd):

Microfinance service centre:



Post Bank operates a specialised service unit that allows SACCOs to make use of several services e.g back-office support, internet resources, administration support, etc.

Major benefit - allows SACCOs to concentrate on core activities

Discussion of Linkages

1. Branching (Cont'd):

Agency:

- A mini-branch with basic banking services located at strategic locations & not operational on a full-time basis
- It is comparable to the bank branches that Stanbic Bank opens at URA collection points. Strategic locations for agencies include areas where SACCO members sell their produce to a marketing cooperative or pay for agricultural inputs in bulk

Discussion of Linkages

1. Branching (Cont'd):

Franchise:

The franchise model's features include:

- Integrated IT systems to help cut costs, improve compatibility and efficiency
- Customers conduct business from any SACCO under the Franchise Umbrella
- Wider accessibility to a range of services & shared costs in product development
- SACCOs comply with minimum operating standards

Discussion of Linkages

1. Branching (Cont'd):

Franchise:

Example of a franchise model: Cooperative Bank of Kenya

The strategy was identified because

- Cooperative Bank viewed SACCOs as a strategic means of achieving cost-effective outreach; but
- SACCOs operated in an independent, unsupervised & isolated manner; therefore
- The franchise model was seen as an innovative way of expanding outreach in a controlled environment where both SACCOs & the Cooperative Bank gain

Discussion of Linkages

1. Branching (Cont'd):

Franchise:

Challenges facing the franchise model include:

- Regulatory barriers
- Integration of MIS & Business Processes
- Suspicion between Franchiser & Franchisee

Discussion of Linkages

2. Products & Services:

- Money Transfer
- Point of Sale systems
- Re-financing
- Lease financing
- Mortgage finance
- Mobile Phone banking
- Short-term credit lines
- Insurance

Discussion of Linkages

3. Technology & Operations:

- Low-cost, high value training by Post Bank
- External audit services by Post Bank
- Franchised integration of operations
- Network marketing
- Data warehousing & business continuity provisions
- Product development support

Discussion of Linkages

4. Risk management & governance:

Possible Partnership considerations:

- Treasury Management Support
- Post Bank to occupy Seat on SACCOs' Board
- Shared strategic planning to ensure long-term growth & compatibility in linkage opportunities

Other Considerations

Highlights of Feedback from SACCOs

- Strong resistance towards Post Bank occupying a seat on their Boards - not viewed as a benefit
- Strong resistance towards the Franchise model - viewed as a form of takeover & as an infringement on the confidentiality of Customer information
- Low-cost high value training the most demanded linkage opportunity

Other Considerations

Highlights of Feedback from SACCOs

- Other partnership opportunities that were well received include:
 - ✓ mobile banking,
 - ✓ micro-finance service centre,
 - ✓ money transfer services,
 - ✓ refinancing
 - ✓ treasury management support &
 - ✓ external audit services

Other Considerations

Legal Implications

- Implementation of several linkages would probably require BoU approval:
Section 4 of the FIA 2004 - any bank seeking to make any major changes &/or additions to its licensed business has to seek Central Bank approval
- In terms of the branching opportunities identified, it is important to ensure there is clarity in what is construed as operating a new branch:
Section 116 of the FIA requires all banks seeking to open or operate any new branches to seek Central Bank approval

Other Considerations

Legal Implications

- The regulatory framework for SACCOs is hindered by a number of factors including insufficient capacity, weak laws & inadequate reporting. This would be a major concern for both Post Bank & BoU
- It is important to ascertain whether the constituent documents of the SACCOs seeking to enter into linkage arrangements allow for such a relationship

Conclusion & way forward

- Numerous constraints & gaps in the delivery of financial services in Northern Uganda uncovered
- Post Bank's outreach strategy favours partnerships with SACCOs in areas considered commercially unviable for opening of full branches
- SACCOs business models viable in semi-urban & rural areas – but are constrained by operational, technological & financial barriers to grow their businesses

Conclusion & way forward

- Based on the study & feedback from Post Bank & SACCOs, several potential partnership opportunities exist
- A strong case for Linkage Banking in Northern Uganda exists & a detailed study would be necessary to establish viability of proposed linkages

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