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Responsible Investor Challenge: M&As, Exits, & IPOs

Buyer Selection in a Responsible Equity Exit

NpM/FIEC/e-MFP Research Project

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Presentation Outline

- Background
- Scope of study
- Research methodology
- (Very) preliminary survey results
- Next steps and possible applications/outputs

Background

- What does it mean to exit ‘responsibly’?
- In a financial inclusion equity exit, what if any responsibility does the seller have to select an ‘appropriate’ buyer? How is this responsibility compatible with fiduciary obligations?
- What are potential consequences of an *irresponsible* exit – selling to highest bidder without any other considerations? Raise prices; reduce service quality, focus on less-needy segments; gutting of an MFI’s pro-poor mission in place of consumer lending and profit-maximisation(Silva & Riecke, CFI, 2017).
- Diversification of FSPs and investors means this is more relevant than ever. Growth of the **strategic buyer** – not an MIV, DFI, or some other double-bottom line impact investor – but a bank, telco, consumer finance Co.
- Building on previous research, including 2014 CFI paper *The Art of the Responsible Exit in Microfinance Equity Sales*

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Scope of study

- FIEC, NpM, e-MFP commissioned study – e-MFP's Daniel Rozas co-author
- Narrow focus on **buyer selection in financial inclusion/microfinance exits**
- Remit: to better understand **current industry thinking** in seller's obligations vis-à-vis buyer selection/evaluation – is there a consensus?
- Output: Checklist/tools/draft guidelines that synthesise industry attitudes

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Research methodology

- Desk research and industry outreach
- Interviews with equity investors, Aug-Sept, including FIEC members
- Online qualitative and quantitative survey, Oct-Nov
- Follow-up interviews
- Short case studies

Preliminary survey results: Survey Structure

- Preliminary questions – Name, org, title, confidentiality, number of exits
- Part I: (Dis)agreement with statements (*strongly disagree* to *strongly agree* – plus open-ended comments)
- Part II: Rating of buyer selection criteria in importance (1-10, plus open-ended comments)
- Part III: Open-ended questions on due diligence, past examples of buyer rejection based on due diligence, preference with respect to category of buyers, due diligence resources, internal decision-making processes

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Preliminary survey results: Part I – Statements by category

1. Buyer's geographical proximity/footprint in region where asset is based
2. Buyer's track record in financial inclusion sector
3. Buyer's undertakings
4. Importance of management/staff support
5. Importance of prior relationship with buyer
6. Perceived value of industry guidelines or other standardisation
7. Perceived value of mission focus versus financial offer
8. Proposed retention of management
9. Reputation of buyer within industry and public press

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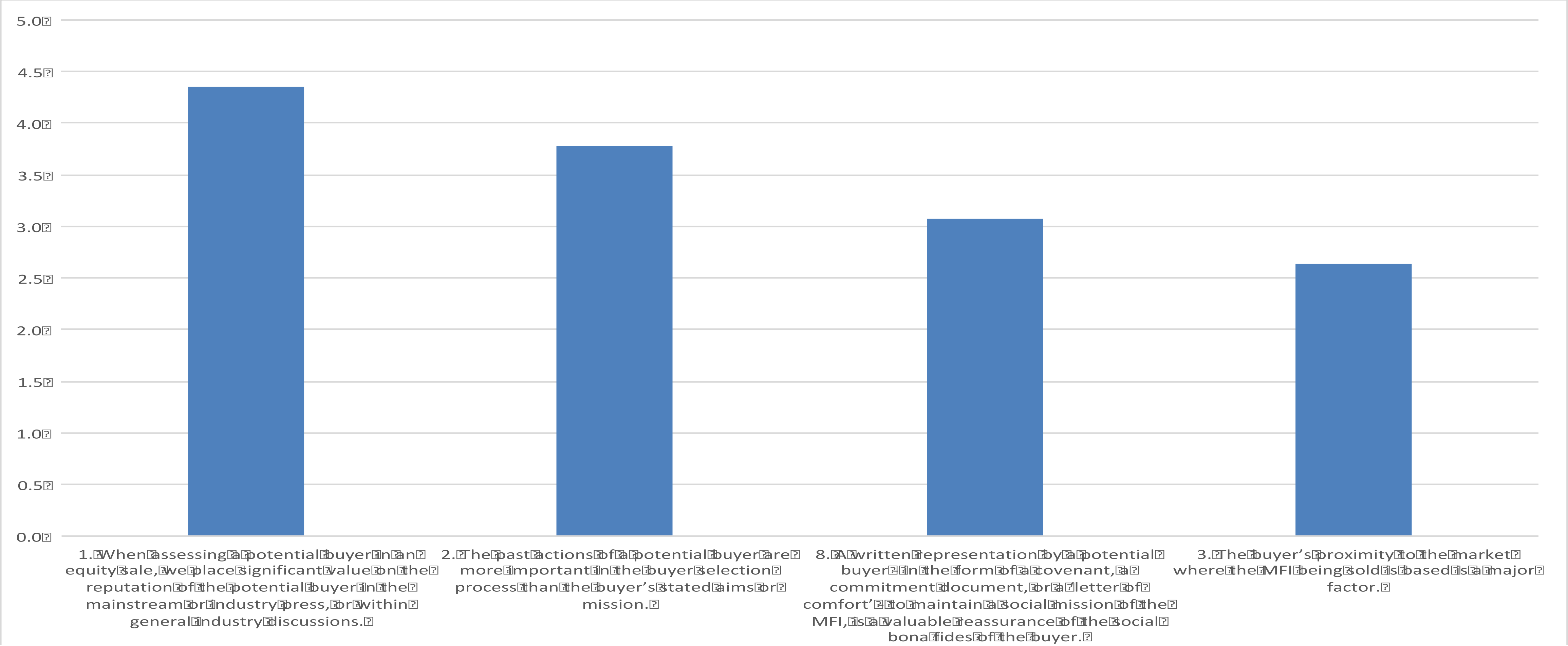
Preliminary survey results: Part I – Agreement with Statements (rankings)



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Preliminary survey results: Part II – Buyer selection criteria by importance: Options

- Buyer’s established track record/experience in financial inclusion
- Clear evidence of buyer’s past commitment to social mission
- Expected ease of regulatory approval of the buyer
- Financial offer
- Financial resources of buyer (“deep pockets”)
- Geographic proximity of buyer to investee
- Investee management’s confidence in buyer
- Long-term investment perspective of buyer
- Overall reputation (not necessarily in financial inclusion)
- Potential technical assistance/capacity building available to investee
- Previous relationship between seller and buyer
- Remaining shareholders’ confidence in buyer (especially in case of minority exits)
- Social offer - commitment to maintain social mission (e.g. ‘letter of comfort’, statement of principles in shareholder’s agreement, or similar covenant)
- Strategic value to investee (ex: as a large financial institution, fintech, etc.)

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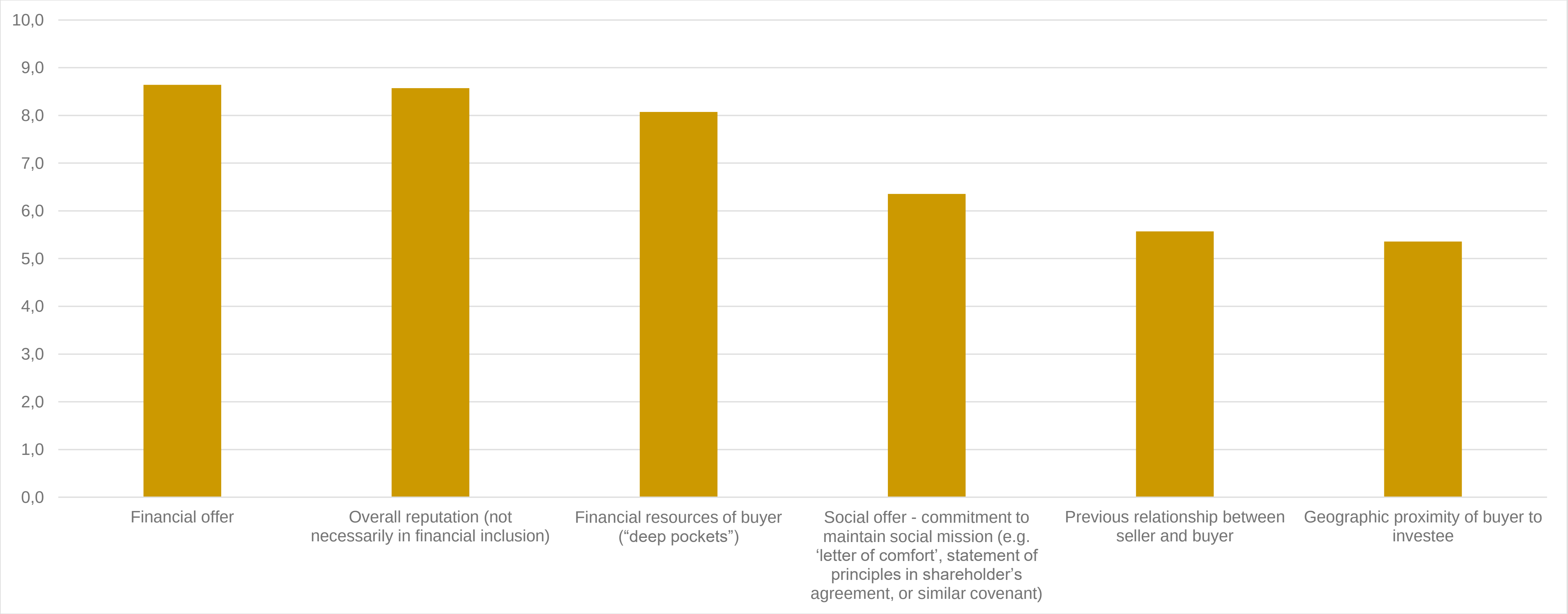
Preliminary survey results: Part II – Buyer selection criteria by importance: Results



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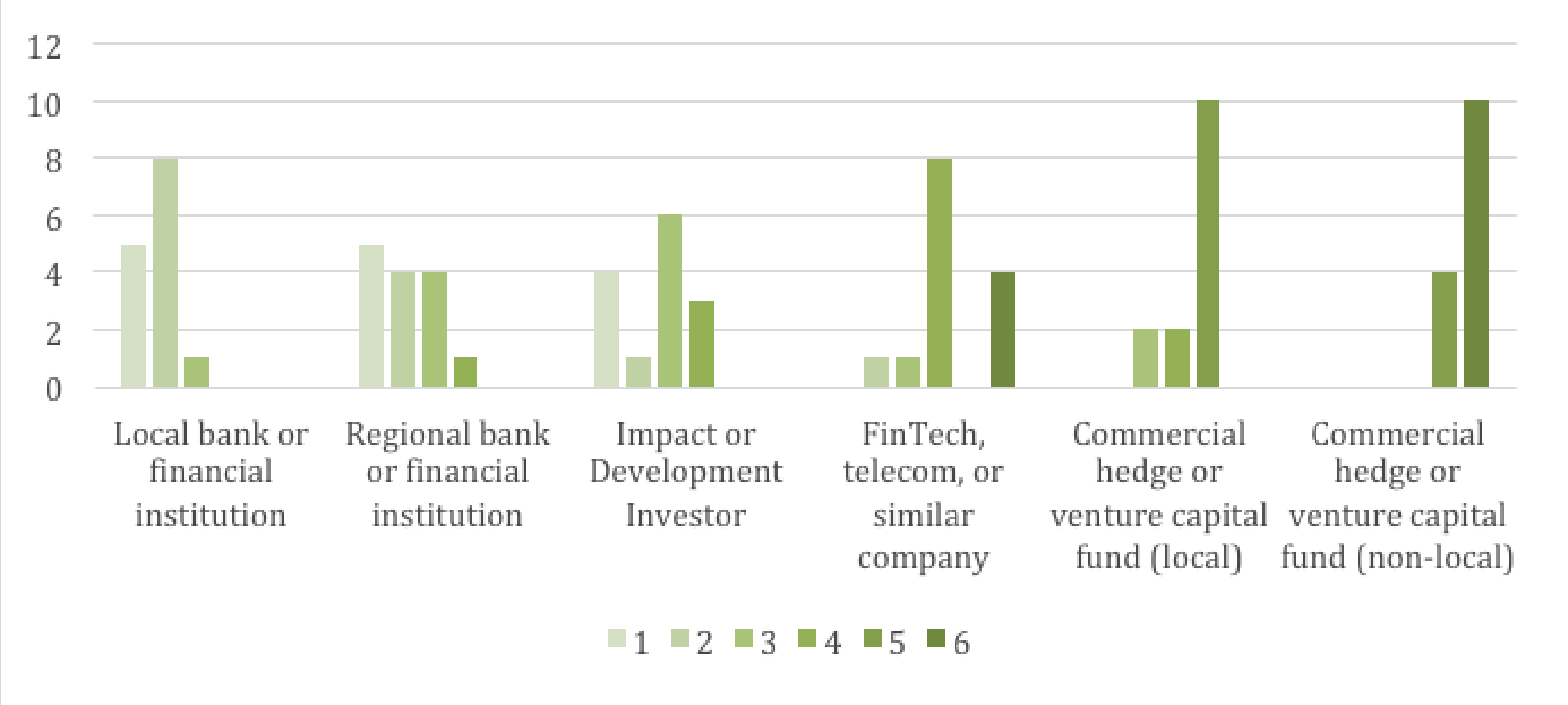
Preliminary survey results: Part III – Preferences by buyer 'type'



Selected emerging themes

- Reputation matters – including both industry gossip and public record knowledge
- Resources that are useful are very diverse – specialised databases, reference checks, Google News
- FinTech companies *may* require special attention…
- …and financial institutions (especially local) are preferred to hedge funds or new entrants
- Past actions speak louder than words, and written representations mean fairly little..
- …and nor does the geographical proximity of the buyer to the MFI - although experience in financial inclusion *does*

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Selected emerging themes

- SPM certification (e.g.SMART) of the MFI doesn't affect the DD required of a buyer, except that there is some degree of self selection, which helps
- A past relationship between seller and buyer is less important than what the seller can learn about the buyer
- Opinions of MFI management, and willingness to keep them on, is relevant
- Role of advisors

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Thank you!