

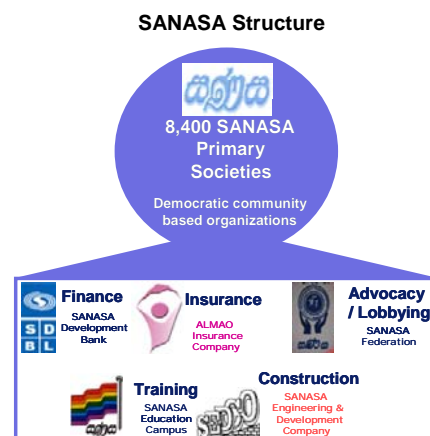
Proposal for an 'IT Support Services Unit for Primary Societies'

Part 1: Description of IT system for Primary Societies

1. Description of SANASA Primary Societies

There are 8400 SANASA Primary Societies in Sri Lanka, already providing basic savings and loans services to 800,000 households, and hence serving approx 2,000,000 people or 10% of the population of Sri Lanka. The majority of these households are in rural areas and surveys have confirmed that they are predominantly from poorer sectors of society. The Primary Societies are cooperatives – they are owned and controlled by the members, not by a central organisation. Many have full-time managers.

There is a national 'support structure' that allows the Primary Societies to benefit from scale economies. This support structure is also owned and controlled by the Primary Societies along cooperative principles. This support structure contains a commercial bank that provides inter-lending and support to financial operations – the SANASA Development Bank.

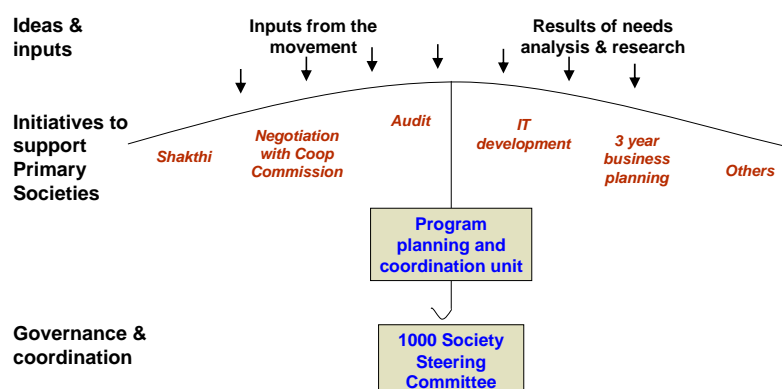


2. '1000 Society Program'

SANASA has decided to focus on building up the capabilities of its most effective societies across the whole country. This initiative is known as the '1000 Society Program'. The overall objective of this program is to achieve a step-change in the performance of these Primary Societies.

Work is starting on this program. A rally of 1000 societies has been held in Colombo, attended by 6000 members and leaders. A number of sub-projects have been kicked off, some of which are being funded by international partners. Implementation of IT into Primary Societies will be a major part of this program.

1000 Society Program Structure – many components with central coordination and support



3. Outline to IT program

SANASA Primary Societies – which handle a large volume of transactions and have a considerable burden of accounting requirements, would gain benefit from implementing new IT systems. They would reduce their costs, increase customer loyalty, develop new sources of income and reduce their operational risk.

Understanding these benefits, a number of Primary Societies have already implemented IT systems independently. These independent IT implementation do not normally bring good results – systems often do not work and are not well supported.

To help the Primary Societies and achieve the economies of scale possible from supporting a network of approximately 1000 societies, a central unit to provide IT services to Primary Societies should be set up – identifying the needs of the Primary Societies for IT, rolling-out IT services to the Primary Societies and supporting the Primary Societies to use the IT.

4. The case for IT in Primary Societies - Outline business case

Primary Societies are keen to develop an IT system for their transactions. Approximately 200 Primary Societies have already automated – using a stand-alone PC. In a recent survey, Primary Societies said that their major need was to automate and standardise operations. They wanted to lower costs from handling transactions, introduce standard approaches to accounting and transaction handling to reduce operational risk, standardise their product set and, if possible, be able to make inter-bank payments and transfers.

Analysis confirms this need. As a result of implementation of a transaction system, Primary Societies will achieve the following benefits:

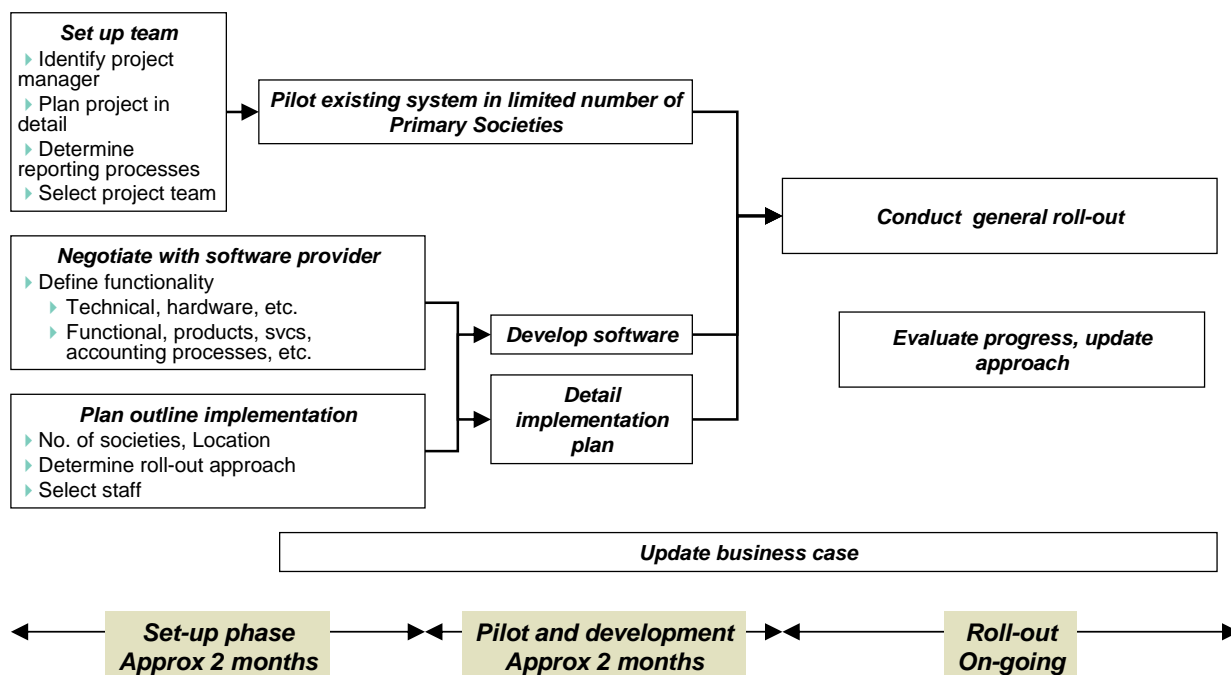
- Reduced costs^(*). Analysis in a typical Primary Society indicates that 50% of staff costs currently spent on transactions will be eliminated
- Improved customer perception^(*). Some (urban) Primary Societies report that up to 50% of their savings have been lost as customers transfer to larger banks with better IT. In recent customer surveys, the main shortcomings of SANASA in the eyes of customers is their lack of central support, their inability to offer transfers and their 'old-fashioned' image
- Reduction of complexity. Primary Societies are not able to expand, since maintenance of paper records and monthly accounting processes are too complex to handle at large scale
- Reduction of operational risk. Primary Societies currently do not have standard accounting processes, do not keep back-ups, have variable operational controls. Introduction of a standard set of processes through the introduction of IT will reduce risks of loss. One of the initial motivations for focusing on IT was the experience of Primary Societies impacted by the Tsunami, which lost all of their records.
- Improved product set. Each Primary Societies currently defines their own product set. Some Primary Societies are not offering products that have proven successful in other locations, others use interest rates that are not attractive to members. Introduction of IT would standardise the product set.

The benefits marked with a ^(*) above have been quantified. The annual uplift in revenues after 3 years are 150% and the uplift in profits (taking into account the costs of IT depreciated over 3 years) are 166%. Hence, once the system is developed, Primary Societies should be able to cover the costs of IT implementation from the benefits that they will receive.

An initial overall business case for the project has been created – see below. Under conservative initial assumptions, the overall project has a positive NPV of \$1.0m and in IRR of 69%. Under a more realistic scenario the project has NPV of \$5.7m and IRR of 142%. This business case will be updated as the project progresses.

5. Overall work-plan during 2007

The main tasks of this program are as detailed below:



Components requiring external support.

Component	Objectives	Time-table
Prepare roll-out to Primary Societies	<ul style="list-style-type: none"> Define detailed system requirements and approach to roll-out to Primary Societies Determine product set, processes and approaches that best meets the needs of Primary Society members Conduct pilot in two Primary Societies Set-up unit to manage roll-out to Primary Societies. Fund the unit for first year of operation 	<ul style="list-style-type: none"> April 2007 to July 2007
Support Implementation of 'Core Banking System' for Primary Societies	<ul style="list-style-type: none"> Co-fund the hardware, software and implementation of the system to Primary Societies Roll-out to up to 1000 Primary Societies 	<ul style="list-style-type: none"> July 2007 onwards Costs can be shared with Primary Societies
Develop additional functionality for the 'Core Banking System'	<ul style="list-style-type: none"> Components to be determined, based on needs from Primary Societies 	<ul style="list-style-type: none"> To be determined

Proposal for an 'IT Support Services Unit for Primary Societies' Part 2: Detailed proposal and approach

1. Project Objective

- Develop a unit to support the development of IT in Primary Societies, and so improve the efficiency of delivery of micro-finance to the poor in Sri Lanka.

2. Project scope

The proposed project will cover the staff, their equipment and incidental costs of SANASA's program during the set-up, pilot and development and initial 6 months of the general roll-out. It does not include IT equipment, systems integration or software development for the systems to be provided to Primary Societies.

3. Project Goals

- During the set-up phase
 - Determine:
 - Role of software provider in implementation
 - Degree of standardisation that will be implemented in Primary Societies
 - Number of societies expected to implement system
 - Determine type of hardware (PCs alone, or PCs and hand-helds)
 - Cost recovery approach
 - Conclude negotiations with software provider
 - Create detailed plans for pilot implementation
 - Create outline plans for general implementation
- During Pilot and Development Phase
 - Implement IT in Pilot Primary Societies
 - Initial roll-out
 - Determine lessons learnt
 - Conduct formal review of effectiveness and create recommendations for next steps
 - Oversee any required software customisation / development. Details and time-frame required to be determined
- During General Roll-out
 - Oversee roll-out
 - Provide support to IT systems

4. Mechanisms employed

A specific team will be set up to implement IT in Primary Societies.

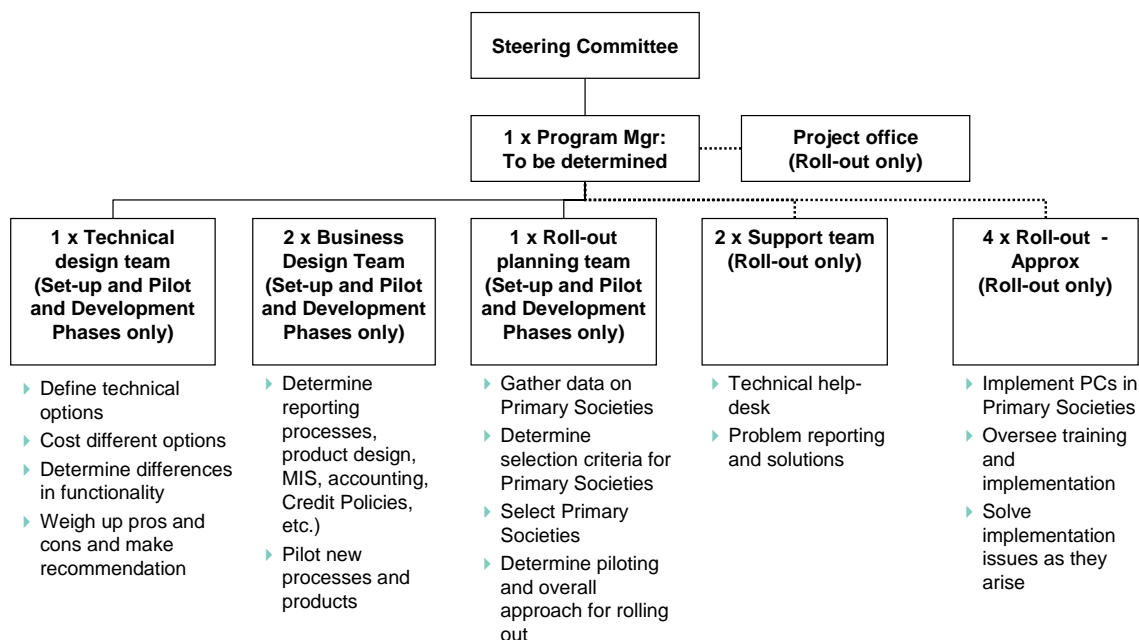
This team will vary in size through the different phases of work. See numbers and skills required in the 'Staffing model' section below.

The unit should initially be located in [to be determined]. It should work closely with the SDBL IT department, since the department has detailed expertise in IT system development and implementation. In time, the unit may be spun out into a separate IT services company, which would increase financial accountability and ensure focus on the needs of the Primary Societies.

The project will need to work closely with the on-going DID project which is conducting related work.

The unit should report to the ‘1000 Society Program’ Steering Committee. In addition, a technical advisory team will be set up to provide technical inputs when required.

5. Staffing model



Staff	Skills needed
<ul style="list-style-type: none"> Project manager 	<ul style="list-style-type: none"> Mature outlook – able to lead meetings with potential vendors Some experience of IT – detailed technical knowledge not required Business modelling experience Able to take initiative and self-direct Very focused on on-time delivery Highly disciplined and structured Able to lead a team
<ul style="list-style-type: none"> Technical design team 	<ul style="list-style-type: none"> Detailed technical knowledge (hardware, software, communications) Knowledge of existing IT systems an advantage
<ul style="list-style-type: none"> Business design team 	<ul style="list-style-type: none"> Knowledge of operations processes Knowledge of products Knowledge of MIS and reporting needs
<ul style="list-style-type: none"> Roll-out planning team 	<ul style="list-style-type: none"> Knowledge of Primary Societies (number and need) Likely to be gained from previous programs, such as Shakthi
<ul style="list-style-type: none"> Support team 	<ul style="list-style-type: none"> Detailed knowledge of technical solution, hardware and software Less complex role
<ul style="list-style-type: none"> Roll-out team 	<ul style="list-style-type: none"> Able to travel Understand how Primary Societies work Similar to Shakthi officers
<ul style="list-style-type: none"> Number of staff 	<ul style="list-style-type: none"> Set-up : 5 staff Pilot / dev. 5 staff Roll-out c. 8 staff

6. Risks and mitigation plans

Risks	Mitigation Plans
-------	------------------

Primary Societies do not demand IT system	Conduct more detailed market assessment during set-up phase
Unit does not have sufficient skills to implement a new IT system Unit does not have sufficient leadership for staff to know what to do day by day	Likely to be a major issue. Potential solutions <ul style="list-style-type: none"> • External Technical Assistance • Assistance from local systems integrator • Software provider takes major role in implementation

7. Budget – to be determined

- SANASA Development Bank will provide:
 - Office space
 - Overall coordination and technical advisory committee
- External funding is sought for general costs for the unit for the initial [XX months] of operation. After 2 years, revenue from Primary Societies should cover at least part of the cost of the unit.
 - Salary costs
 - IT costs
 - Administrative costs

Item	Unit	# of unit	Total (Rs)	SANASA	Partner
Manager costs	50000	12	600,000		600,000
Staff costs	30000	84	2,520,000		2,520,000
Office space cost	20000	36	720,000	720,000	
IT equipment - PCs	120000	5	600,000		600,000
IT equipment - Printer	100000	1	100,000		100,000
Additional materials	20000	36	720,000		720,000
Negotiation trips to BK	60000	4	240,000		240,000
Total (Rs)			5,260,000	720,000	4,780,000
Total (€)			37,220.00	5,090.00	33,820.00

Appendix: Project business case

See following pages for business case of the overall project. The business case makes the following assumptions. The 'Base' assumptions' in the business case are very conservative.

'Base' assumption	Source /Rationale	'Likely' assumption
Investment costs in larger Primary Societies will be \$6,900 (3 terminal solution). Investment costs in smaller Primary Societies will be \$4,100 (1 terminal)	Bottom-up estimate of hardware, software, systems integration, training costs	Same
50 larger Primary Societies will join the program, 50 smaller Primary Societies (over first two years)	Currently at least 80 Primary Societies are large enough to make the 3 terminal solution economic 200 societies have already bought a PC with banking software	25 societies will continue to join every year
Incremental Revenue up-lift in Primary Societies of 10%	Estimates from Primary Societies. Many Primary Societies estimated considerably higher revenue impacts (up to 30%)	Uplift of 20%
Cost income ratio in Primary Societies falls from 87% to 75% in larger Primary Societies and 80% in smaller Primary Societies	Bottom-up analysis of current costs and revenues in Primary Societies, and bottom-up impact assessment of automation on staff and on operating costs. Assumes only 50% of the expected benefits are achieved.	Falls to 75% in both cases
Discount rate	15%	Same

Results of business case

\$m	'Base' assumption	'Likely' assumption
Total investment cost	.7	2.1
Increase in profits (2013)	3.2	15
NPV	1.0	5.7
IRR (%)	69%	142%
Members impacted (2013)	30,000	100,000

Calculation of 'Base assumption' is given below

Initial investment	Unit \$ (Approx)	2007	2008	2009	2010	2011	2012	2013	total
		Initial software development	100,000	1					
Institutional development of IT dept	25,000	1							
Prepare roll-out to Primary Societies	50,000	1							
3 PC based solution (unit cost)	6,933	20	30						50
3 PC Based Cumulative		20	50	50	50	50	50	50	
1 PC based solution	4,090	20	30						50
1 PC based Cumulative		20	50	50	50	50	50	50	
Investment costs		395,448	330,672	-	-	-	-	-	726,120
Revenue Assumptions									
Unit revenue in 'PC' societies	10%	25,000	27,500	30,250	33,275	36,603	40,263	44,289	
Revenue in 'PC' societies, no automation		500,000	1,375,000	1,512,500	1,663,750	1,830,125	2,013,138	2,214,451	11,108,964
Unit revenue in '1 PC based' societies	10%	12,500	13,750	15,125	16,638	18,301	20,131	22,145	
Revenue in '1 PC based' societies, no automation		250,000	687,500	756,250	831,875	915,063	1,006,569	1,107,226	5,554,482
Total revenue, no automation		750,000	2,062,500	2,268,750	2,495,625	2,745,188	3,019,706	3,321,677	16,663,446
Unit revenue in 'PC' societies	20%	25,000	30,000	36,000	43,200	51,840	62,208	74,650	
Revenue in 'PC' societies, Automation		500,000	1,500,000	1,800,000	2,160,000	2,592,000	3,110,400	3,732,480	15,394,880
Unit revenue in '1 PC based' societies	20%	12,500	15,000	18,000	21,600	25,920	31,104	37,325	
Revenue in '1 PC based' societies, Automation		250,000	750,000	900,000	1,080,000	1,296,000	1,555,200	1,866,240	7,697,440
Total revenue, Automation		750,000	2,250,000	2,700,000	3,240,000	3,888,000	4,665,600	5,598,720	23,092,320
Incremental Revenue		-	187,500	431,250	744,375	1,142,813	1,645,894	2,277,043	6,428,874
Cost assumptions									
Cost income ratio (current)	87%								
Expected costs (no automation)		652,500	1,794,375	1,973,813	2,171,194	2,388,313	2,627,144	2,889,859	14,497,198
Cost income ratio (with 3 PC)	75%								
Expected costs (in 3 PC socs)		375,000	1,125,000	1,350,000	1,620,000	1,944,000	2,332,800	2,799,360	11,546,160
Expected costs (in 1 PC based socs)	80%	200,000	600,000	720,000	864,000	1,036,800	1,244,160	1,492,992	6,157,952
Total expected costs		575,000	1,725,000	2,070,000	2,484,000	2,980,800	3,576,960	4,292,352	17,704,112
Total impact upon costs		(77,500)	(69,375)	96,187	312,806	592,487	949,816	1,402,493	3,206,914
Primary Societies profit impact									
Baseline profit		97,500	268,125	294,938	324,431	356,874	392,562	431,818	2,166,248
Project profit		175,000	525,000	630,000	756,000	907,200	1,088,640	1,306,368	5,388,208
Incremental profit		77,500	256,875	335,063	431,569	550,326	696,078	874,550	3,221,960
Total cash impact									
Investment		(395,448)	(330,672)	-	-	-	-	-	(726,120)
Profit from Primary Societies		77,500	256,875	335,063	431,569	550,326	696,078	874,550	3,221,960
Primary Society cash impact		(317,948)	(73,797)	335,063	431,569	550,326	696,078	874,550	2,495,840
Number of active clients		12000	30000	30000	30000	30000	30000	30000	
Discount rate	15%								
									NPV IRR
									1,038,101 69%

(*) Based on customer and Primary Society Surveys