SOCIAL PERFORMANCE MANAGEMENT OF MICROFINANCE INVESTMENT VEHICLE

ANALYSIS OF RECENT DEVELOPMENT

DISSERTATION

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Dedication

To my wife Amie Barry, my son Omar Choi and daughter Naffie Choi, whose love, support, patience and understanding have never been diminished. Also to the joyful memory of my late father, Matar Choi who implanted the values of integrity and compassion in me; and to my mother, Fatou Choi who shaped my early notions of ambition, determination and independence.

Disclaimer

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Executive Summary

The plight of poverty continues to hamper socio-economic development in under-developed countries by shattering the ambition of many young men and women due to lack of much needed capital to fund related development projects. With the intervention of microfinance, such dreams are now being realised.

Microfinance is still in its early stage, thus offers additional scope for further development. For example over the past decade, a few Microfinance Institutions (MFIs) have started developing a range of services and products including micro-insurance and instruments for facilitating international remittances. This additional capacity building means that microfinance institutions, which offer banking services to micro-entrepreneurs in poor and developing countries, are increasingly turning to mainstream capital markets to raise funds. Microfinance Investment Vehicles (MIVs) have been created to meet this demand for capital. MIVs raise funds from public, institutional and private investors to support MFIs worldwide mainly through loans. This funding mechanism reflects the framework of what is known in the global financial market as Collective Investment Schemes (mutual funds).

Despite its overwhelming popularity and the notion that microfinance can actually help turn around the development paralysis being experienced by the poor and marginalized people of the world, still very little is known about how effectively such instrument can actually help the poor and improve their lives. According to recent body of literature, three key questions are being raised by both investors and regulators: Can funding institutions (MIVs, MFIs and their network) prove that clients are better off because of the services they provide to them? How can social return be realised in the most effective and efficient way? How can these social returns be measured and monitored over time?

This research looks into the main progress of Social Performance Management (SPM) to date; approach to implementation; its measurable variables and benefits to stakeholders including investors and end users.

It is with hope that the research findings will contribute to existing body of knowledge and to Luxembourg Microfinance and Development Fund’s (LMDF) double-bottom line strategy of financial returns for the benefit of the investor and social returns for the benefits of end-users. The key findings of the research are summarised below:

Summary of Key Findings

- The results show that most of the of social performance tools that are available are tailored for microfinance institutions (MFI) and not for MIVs, therefore, emphasising the urgency of developing more appropriate tools for MIVs in respond to increasing call from investors for transparency.

- There is a trend of in-house development and implementation of SPM tools for MIVs. For example, the ECHOS of Incofin, the rADER of ResponsAbility and the SPI-Investor, a joint initiative of Oikocredit and CERISE. This trend suggests the need for MIVs to take full control of their SPM to address their specific needs.

- In terms of challenges from Investors' perspective, overindebtedness and lack of transparency represent a major concern. Therefore an important recommendation to MIVs is to embrace the Client Protection Principles as a grass-root attempt to tackle these issues.

- In terms of social performance reporting, many proponents warn that only information that can be easily gathered, tabulated to draw simple, meaningful conclusions should be used. Based on this advice, I propose to MIVs considering the implementation of SPM to follow the approach of ResponsAbility Social Investments AG, which in my view reflects this adage.

- Evidence from the study of Incofin and Oikocredit show that effective SPM of MIVs is possible. Therefore, if experience is any guide mainstreaming and standardization of SPM is also possible.

- The study also shows that the diverse nature of the structure of MIV is not a hindrance to its success. In fact, if managed properly with the correct tools and expertise for effective performance measurement, MIVs based in Western Europe can zoom into their activities well beyond their territories to monitor, control and measure and most importantly, replicate successfully, initiatives across the countries of their partner MFIs.

List of Abbreviations and Acronyms

ADA	Appui au Développement Autonome
CERISE	The Microfinance Knowledge Network
CGAP	Consultative Group to Assist the Poor
CMEF	The Council of microfinance Equity Funds (CMEF)
CSR	Corporate Social Responsibility
ESG	Environment Social and Governance
IAMFI	International Association of Investors in Microfinance
LMDF	Luxembourg Microfinance and Development Fund
Luxflag	The MIV Labelling Agency in Luxembourg
MFI	Microfinance Institutions
MIV	Microfinance Investment Vehicles
MIX	Microfinance Information Exchange
SP	Social Performance
SPI	Social Performance Indicators
SPM	Social Performance Management
SPTF	Social Performance Task Force
SR	Social responsibility
SRI	Socially Responsible Investment

Note

For ease of reference, I use the term "Microfinance Investment Vehicle" (MIV) to refer to the Investment companies mentioned in this study. I am aware of the fact that some of these companies actually manage one or more MIVs (funds) in their investment portfolio.

Concepts and Rationale [1]

Baseline	People deemed eligible to obtain financial services that can lead to income generation, repayment of loans, savings, and the building of assets.
Benchmarking	A measurable variable used as a relative baseline or reference in evaluating the performance of an organization.
Client Assessment	The process of gathering and assessing information about clients. It includes quantitative and qualitative methodologies.
Client Protection principle	A microfinance industry-wide initiative coordinated by CGAP which aims to develop codes of conduct and practices to ensure that low income clients are treated fairly and protected from potentially harmful financial products.
Double Bottom-Line	A framework for measuring and reporting an organization's performance against financial and social standards.
Feedback Loop	A continuous cycle by which information is processed within an organization. It starts with the collection of information followed by consolidation and analysis. The data is then used to make, communicate, and implement decisions.
Fungibility	The quality of money that makes one individual specimen indistinguishable from another. The fungibility of money makes it difficult for lenders to ensure that borrowers use the loan funds in the way lenders wish.
Indicator	A piece of qualitative or quantitative information that provides meaningful insight into the performance of organizations or their beneficiaries.
Microfinance Institution	A financial institution specializing in providing financial services to low-income persons or to persons otherwise systematically excluded from formal financial services. It may also offer business development or other non-financial services. It includes non-governmental organizations, cooperatives, credit unions, non-bank financial institutions, and commercial banks.
MIV	A Microfinance Investment Vehicle (MIV) is an investment entity that has microfinance as a core investment objective and mandate. It is either self managed or managed by an investment management firm or by trustees. It receives money from

[1] Most of the information from the "Concept and Rationale section is obtained from the SEEP Network - 2006

	investors through the issuance of shares, units, bonds, or other financial instruments
Microfinance	The provision of financial services adapted to the needs of micro-entrepreneurs, low-income persons, or persons otherwise systematically excluded from formal financial services, especially small loans, small savings deposits, insurance, and payments services.
Outreach	Active attempt to target, attract, serve, retain or otherwise interact with a clientele in selected populations, geographic areas, or targeted initiatives.
Performance Management	The process of translating an organization's mission into practice, which includes setting social objectives, tracking social performance and using this information to improve practice.
Social Performance	Social performance is not just about measuring the outcomes, but also about the actions and corrective measures that are being taken to bring about those outcomes.
Triple Bottom Line	A framework for measuring and reporting an organization's performance against financial, social, and environmental standards.

CHAPTER 1

1 Aim of the study

To ensure a wider outreach, enhanced capacity, profitability and sustainability, microfinance is gradually being integrated into mainstream finance, hence the emergence of microfinance Investment Vehicle in recent years. A Microfinance Investment Vehicle is an investment entity that has microfinance as a core investment objective and mandate. It is either self managed or managed by an investment management firm or by trustees. It receives money from investors through the issuance of shares, units, bonds, or other financial instruments

While such integration is a cause for concern, it is welcomed by some commentators including key actors. For example CGAP (2004) states that “microfinance will only realize its potential if it is integrated into a country’s mainstream financial system”. Many commentators indeed often the same ones have also expressed apprehension that the growing commercialisation of microfinance is leading to an over-preoccupation with profitability at the expense of poverty reduction and other development goals (CGAP, 2001; Christen & Drake, 2002, p. 4; Hulme & Mosley, 1996; Otero, 1999). The worrying concern derived from such contradictory statements is the possibility of mission drift.

The evolution of microfinance towards “commercialisation” is running the risk of veering off course, where financiers will be able to turn towards commercial banks considered more professional, more reliable, more capable of reaching a general public, penalizing institutions that seek to carry out a social mission and which, up until now, had enabled innovations (François Doligez, IRAM-University of Rennes 1 & Cécile Lapenu, CERISE SPI3 – DISCUSSION PAPER N°1 November 2006). All these assertions represent earnest concerns that need addressing immediately.

Embarking on such a study is to really see how such mission drift can be prevented through adopting an effective Social Performance Management system capable of safeguarding the social mission of MIVs. Since bulk of the MIVs’capital comes from socially conscious investors (both private and Institutions) keen to contribute in global poverty reduction, this study seeks to understand thoroughly the reporting arrangements necessary to convince such investors that their funds are indeed being invested in accordance with their social objectives.

2 Research Questions

Recent studies have pointed out several social, economic and environmental problems in some of the microfinance programmes. Example of such issues are the high interest rate (Hossain, 2002), the risk of ending up in a circle of debt (Snow and Buss, 2001), Climate Change (Rippey 2009) and the risk of over commercialisation. Added to the list is the concern that microfinance may still not reach the very poorest, as some borrowers still experience credit rationing in micro-credit programmes, including inequality in terms of benefits and loan sizes as well as limited access to services (Baydas et al., 1994; Stix, 1997; de Meza and Webb, 1999).

While all these issues cannot be addressed in this paper, they all deserve mentioning to help develop an overview of the opportunities and constraints facing the microfinance sector today and to stimulate further debate. This paper is rather specific and focuses mainly on social performance of MIVs, which is mainly anchored on the double-line principle of people and profit. The double-bottom line concept refers to economic benefits for both investors and clients. While this concept is growing in popularity its integration in MIV's Social Performance Management remains to be seen (CGAP- 2009).

2.1 Summary of research questions

How important is social performance for Investors?

How is social performance being communicated to the public?

What performance monitoring tools/indicators are being used by MIVs?

What are the major challenges facing MIVs when implementing these tools?

Do such tools meet public demand/expectation?

3 Research Methodology

3.1 Literature Review

The literature review covers academic publications on a wide range of relevant topics, mainly sourced from the University of Luxembourg online library and ADA's Library. Publications from CERISE, CGAP, Luxflag, SEEP Network, Imp-Act Consortium and various United Nation bodies offer an important source of information. Where appropriate, reference is made to various social performance annual reports of MIVs around the world. With such a wealth of literature, I have established a strong theoretical framework for my research. I have applied both theories and concepts from the literature directly to the study.

3.2 Brief Examination of the Status Quo

It is necessary to understand current developments relating to social performance management of MIVs including reporting and indicators. Therefore in order to understand what tools might be appropriate for the social performance measurement of MIVs, I have conducted an in-depth review of various social performance tools.

3.3 Analysis of the experience of two MIVs- Incofin and Oikocredit

The aim of this exercise is threefold: Firstly, to gather best practices developed over the years by leading MIVs, from the time they conceived the idea of social performance management to its implementation. Secondly, to learn and understand the huddles these organizations came across during the implementation process. Thirdly, to take stock of any material benefits attributed to their social performance management since implementation.

The social performance management of Oikocredit of The Netherlands and Incofin of Belgium is studied by reviewing their internal documents and where possible, by conducting interviews with their respective social performance representatives. Both companies are socially responsible lenders with reputable business ethics and extensive outreach, hence active advocates of SPM.

The findings from the study are supplemented by relevant literature drawn not only from the microfinance literature but also from the Social Responsible Investment (SRI) literature which is rapidly developing in terms of both volume and quality.

3.4 Interviews with key actors

The interviews conducted reflect three important levels of the social performance implementation.

1) **The investor level (funding institutions that target MIVs)**
   An interview was conducted with the Mr Gregory CLAUDY, Director at Fortuna Bank, Luxembourg. The aim of the interview was to understand investors' expectations and opinions in terms of social performance reporting.

2) **MIV practitioners**
   An interview was conducted with Mr. David DEWEZ, Senior Investment Management Manager at Incofin, Belgium. Since Mr. Dewez currently resides in Colombia, the

interview was conducted via Skype. The aim of the interview was to understand social performance from practitioner's perspective; take stock of industry initiatives and to understand challenges and the necessary actions for addressing them.

3) **Consultations with the staff of LMDF and ADA, Luxembourg.**
In order to understand the expectations of LMDF in terms of the priority level and importance assigned to SPM implementation, the research topic was discussed with the fund's management staff and advisors including Mr Kaspar WANSLEBEN, the fund's Executive Director and Axel De Ville, Executive Director of ADA. All consultation sessions were informal.

- ❖ *Please refer to appendix no 6 for further details regarding these interviews and consultations.*

4 Shortcomings of the methodology

4.1 Time factor

Even in its slimmed down version, the topic is very broad and complex and deserves several months if not years of research. My approach is to be selective; therefore I am aware of the risk of failing to address certain thematic areas that might be crucial to the main topic.

4.2 Bias

By selecting one interviewee from each level of the social performance components identified above, I am aware of the fact that my findings are less representative as they ideally should be had more than one representative been interviewed from each group to ensure wider opinion. Due to the hectic schedules of certain senior representatives, I was not able to conduct all the interviews as previously foreseen. In this regard, I am conscious of any potential flaws.

Due to the variable structure of MIVs and lack of standardization in their social performance reporting, conducting a comparison of MIV practices is rather challenging. As a result, there are some inconsistencies in the way I present certain thematic areas.

4.3 Lack of previous background in microfinance

My theoretical understanding regarding microfinance and its operations is constrained by the fact that I am a newcomer to the field.

5 Introduction

New poverty estimates reveal that 1.4 billion people in the developing world (one in four) were living on less than US$1.25 a day in 2005 with no or little access to shelter, clean water and health care (World Bank 2008). Despite their extensive outreach and diversity in terms of areas of intervention, there is a widespread consensus that the current charity model is really in need of a make-over. However, their endeavours to solve endemic problems of the marginalised people of the world tend to revolve around conventional aid handouts in the form of cash or material goods and food. Donations in these forms can make an immediate impact on the lives of these people. Unfortunately this approach only helps to alleviate poverty on temporary basis.

Thanks to the intervention of microfinance in recent years with potential for greater outreach and sustainable success, microfinance is widely regarded as the solution to poverty and widely recommended and perceived by many as a turn-key for unlocking opportunities for the impoverished people of the world. With the help of philanthropic capital within a capitalist framework, entrepreneurs, farmers, and artisans are aided with the tools, skills, capital and most recently energy supplies to successfully adopt a sustainable approach in their quest to escape from the poverty trap in which they are deeply anchored.

Many proponents of microfinance take it for granted that such financial interventions have positive effects on poverty reduction. The unfortunate reality is that until recently many funding institutions have concentrated on the financial viability of their organisations while paying little attention to its Social Performance Management (SPM) (Cerise 2003).

In recent years, following the creation of the social performance task force, an industry-wide initiative aimed at making microfinance more effective in achieving its social mission, the presence of the concept of SPM in the microfinance literature is becoming more and more apparent. Consequently this has led to an increased interest in the subject among various MIVs and their networks. In microfinance, the process of measuring and managing organizational progress toward social objectives is known collectively as Social Performance Management (The SEEP report, 2006).

Social responsibility is classified at four levels: towards clients, staff, community and environment (Source: CERISE 2009). While the environment is not the current focus of many MIVs, its exclusion from their development strategy could prove to be fatal in the long-run. In support of this view, the CGAP 2009 survey of MIVs reveals MIVs' effort to include environmental considerations in their investment policies, due diligence, and monitoring. Since any impact may be irreversible, addressing such problems requires a Social Performance Management system with holistic approach and deeply anchored on the need to protect the environment.

Climate change and poverty reduction may well be the two greatest challenges of the century. Finding innovative solutions and long-term responses require that we think of climate change and poverty reduction as intricately linked and mutually reinforcing. (Paul Rippey March, 2003).

The word sustainable is not a stranger in microfinance literature but has tended to be used narrowly, mainly referring to the long-term financial viability of microfinance institutions (Paul Rippey March, 2009). He further asserts that microfinance which is deemed sustainable should meet the definition of sustainable development offered by the Bruntland Commission (1987): Meeting the needs of today, without compromising the ability of future generations to meet their needs.

An increasing number of investors are now searching for green, ethical and more stable financial products. Social Investors do not only provide much needed funding to microfinance directly but also lay the foundation for other less "social" investors to also participate in funding microfinance. In order for the social investor to play this pivotal role, they must be convinced that there is a true social dimension to their investment and need to have access to reliable, transparent information that validates the social value of microfinance (Lisa Sherk, Director of Investment Analysis and Sandra Mai Hamilton Senior Investment Analyst, BlueOrchard)[2.] These assertions epitomise the current momentum of social performance management which shows no signs of abating in both the MFI and MIV funding community.

The essence of this study is to take stock of SPM progress to date focusing mainly at MIV level in terms of best practices pertaining to measuring, monitoring and reporting their own social performance and that of their partner MFIs to meet not only investor demand but also demand from the public and regulatory agencies whose missions are deeply embedded in their common pursuit of poverty alleviation.

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[2] Revealed in an interview with MFC (The Microfinance Centre for Central and Eastern Europe) 2007.

CHAPTER 2

6 Theoretical and Conceptual Framework

The growing body of theories and concepts can be very instrumental in stimulating and providing a useful basis and deeper understanding of any academic subject. Therefore the reason for aligning my study with theoretical and conceptual framework is to better describe, understand and explain the topic of SPM.

An array of literature and theories have pointed out that SPM can significantly improve the effectiveness of Microfinance Institutions and other funding organisations, thereby helping them reduce financial exclusion and poverty in poorer societies around the globe. Added to this benefit is the notion that effective SPM can enhance microfinance institution's reputation and give them a competitive edge in an increasingly business environment where ethically compliant products and services continue to strive.

This current ethical impetus offers challenges as well as new opportunities to both MIVs and MFIs. To better deal with the challenges many institutions are now expanding their capacity to provide an additional focus necessary to realise their social objectives and those of their shareholders. In harnessing the opportunities, many firms are adding the concept of SPM to their marketing strategy since being green and social is regarded as a relevant product and an important business characteristic (Bert Scholtens, 2008).

Although relatively new to the microfinance agenda, SPM has a long history outside the sphere of microfinance. Paradoxically, perhaps much of the activity and progress in SPM is taking place in the private sector with initiatives such as corporate social responsibilities (CSR) and the Balanced Scorecard (The SEEP Network, 2006). Therefore to really understand the background of SPM, I will utilize the concept of CSR as an analytical lens.

In his book, "Give and Take", Levy asserts the belief that corporate philanthropy and social initiatives are the heart and soul of business (Levy R 1999). Considered an active source of competitive advantage, CSR can be a proactive business strategy and an effective marketing tool to create and sustain a competitive advantage (Moskowitz 1972 - cited in the article of Chin-Huang Lin-2009). Preston also echoed such assertions by arguing that social issues can be just as important as market factors in determining long-run success, and thus deserve the same attention and rigorous analysis that have been devoted in the past to the market environment (Preston 1990).

This link between social responsibility and economic reward has prompted various authors to express varying, and at times contradictory opinions on the subject. Friedman for example affirms that a business's primary responsibility is to make money, and the only interests that matter when making managerial decisions are those of the shareholders. (Friedman 1970). Given shareholders desire today to be associated with ethically compliance financial product, I find such affirmation partly interesting, in that, it is ironically in favour of the concept of CSR since the primary focus of business is on the shareholders.

In recent years, stakeholders are not limited to shareholders alone. Instead, extended extensively to include all stakeholders who play an integral part in the process of initiating, representing, translating, and delivering their expectations to the firm. Different stakeholders will emphasize different aspects of CSR, and although they play an important role in the CSR debate, their angle is slightly different, as they want to further their specific interests and their view of what CSR is or should be (Frank G. A. De Bakker, Peter Groenewegen and Frank Den Hond - Business Society 2005; 44; 283). Sethi (1979) put forward a cautionary note which is worth looking into by stating that firms will put social responsibility over financial performance in a quest for legitimacy and when they are under pressure from stakeholders.

While all these arguments are crucial, I am more inclined to justify those which are in favour SPM/CSR, thus aligning them with the importance of financial performance. Establishing a linkage between such contrasting elements may not be easy without properly understanding each. Regarding financial performance, (Yaron1992) and (JAMES COPESTAKE, University of Bath, UK (2003) argues that improved financial performance is necessary for growth, to mobilize resources and reach more clients.

As for social performance, Zeller Lapenu and Greeley (2003) call for social performance management requirement with minimum operational standard geared towards consumer protection. The later argument is interesting as it is intended to defend the notion that additional stringent checks to govern social performance can be very time consuming and for that matter too expensive. Comprehensive definitions of financial and social performance will surely assist in sharpening and deepening my understanding of any possible trade-offs between the two.

Financial Performance refers to organizational performance measured by financial metrics, such as profit, net operating margin, return on investment, return on assets, or operational efficiency. On the other hand, Social Performance refers to the effective translation of an organization’s social mission into practice. Social performance is not just about measuring the outcomes, but also about the actions and corrective measures that are being taken to bring about those outcomes (CGAP- cited from the SEEP Network).

Where necessary, the concept of governance is applied to provide an important angle for discussion towards understanding any institutional arrangements between MFIs and MIVs to ensure successful implementation of social performance. In his article (CSFI 2008), Roy Mersland pointed to the need to search for governance mechanisms which can bring benefits to both the MFI and customers.

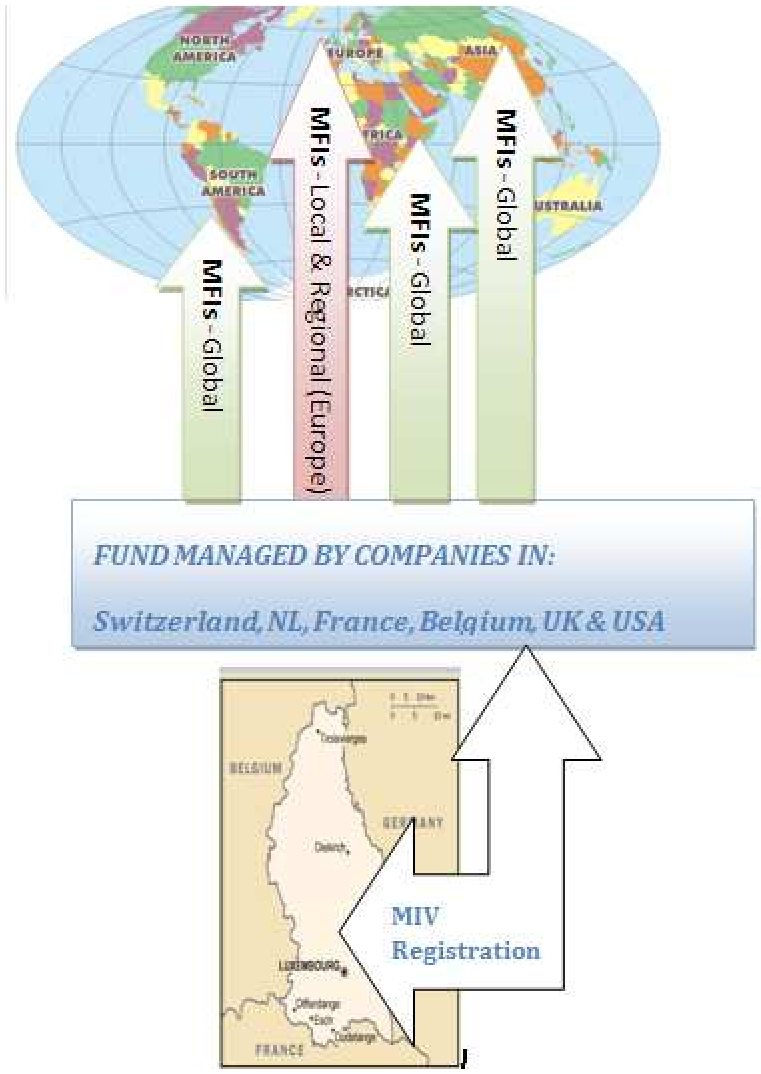
In microfinance literature, the term governance first appears in 1997 (CGAP) and usually refers to the relationship between the board of directors and the management of MFIs. However, the good functioning of board of directors is not enough to guarantee the mission and the assets of MIVs and MFIs. Therefore successful implementation of SPM requires effective coordination between donors, bank partners, shareholders, loan officers in the field and clients to facilitate the exchange of experience; disseminating of research findings; learning and reporting.

While there is a progress in the debate surrounding the topic of SPM, concerns have been pointed to the fact that many business ethics scholars do not significantly build on each other’s work but mainly repeat or criticize each other without providing underlying causal relationships (Collins, 2002).

Where necessary, throughout the report I seek to encapsulate and test theories and concepts to give my study full academic footing and to see how deeply such concepts have been embedded in those management sciences that can best explain the delivery process of the microfinance and most importantly to see if my findings have any interesting relevance or contribution to make in the academic literature as opposed to Collin’s (2002) assertions.

6.1 Spatial Constellation of Microfinance Investment Vehicle

Figure 1



Map source: Education Place

Illustration: Mustapha Choi

Beneath the fragmented structure of MIV, lie various socio-economic, political and geographical factors. While most of these factors deserve mentioning, I have chosen to be selective and mention only those considered to be the most pressing and relevant to this study. Among these are the inherent potentials and constraints that underpin MIV's presence at ***local, regional*** and ***international*** levels. These factors are discussed below:

6.2 MIV Registration – Luxembourg a significant player

Luxembourg represents the base of this illustration because of the significant influence it has in the microfinance sector. Most of the world's MIV funds are registered in Europe, mainly

Luxembourg because of its favourable tax and regulatory frameworks. The Netherlands is also an important player. North America hosts only 7.6 percent of MIV assets, and no specialized fund has been registered by a market authority in the United States. (CGAP brief Sept 2009).

6.3 MIV Fund Management

The fact that Luxembourg play host to majority of MIVs does not mean that all funds registered in Luxembourg are actually managed in Luxembourg. In fact, only a small percentage of such funds are managed in Luxembourg. The crucial task of fund management takes place in other countries. Among these countries are France, Germany, Belgium and Netherlands.

6.4 MIVs as a source of foreign capital – Key figures

According to the united nations, the total cost of supporting the Millennium Development goals financing gap for every low-income country was estimated at $73 billion in 2006 and will rise to $135 billion by 2015 (Transparency International 2006). Foreign capital investment in microfinance has been booming over the past four years. Commercial cross-border debt and equity invested in microfinance surpassed US$11 billion in 2009, representing an estimated 20 percent of the funding base for specialized microfinance providers. Foreign investment brings important benefits for microfinance institutions (MFIs). It can provide longer term debt maturity and risk capital that often is not available in the local market, but it can come with a significant string attached: foreign exchange risk (CGAP April 2010 - David Apgar and Xavier Reille).

6.5 Current Spatial Representation of Microfinance

Geographically, microfinance assets remain highly concentrated within Latin America and the Caribbean (LAC) and Europe and Central Asia (ECA). Africa, South Asia, and East Asia and Pacific, in addition to LAC and ECA, all nearly doubled in size from 2006 to 2007 (MicroRate, 2008). Globally, it is estimated that a total of over 10,000 MFIs exists that is made up of a large array of types of MFIs such as credit unions, NGOs, cooperatives, government agencies, private and commercial banks and various permutations of these forms (Raimar Dieckmann - Deutsche Bank 2007).

Despite the phenomenal growth of microfinance over the last 25 years, most parts of the developing world remain undersupply with microfinance products, a scale of which is described as "services vastly outstripping demand" (Thankom Arun and David Hulme, 2008), thus pointing the need to fill this wide demand gap with appropriate products.

One of the emerging concerns in the growth of microfinance is the uneven degree of provision of microfinance within countries (Rhyne and Otero, 2006). For example, in India most MFIs operate in the relatively developed south of the country and provision in the poorer north and east of the country is low. In Indonesia there is a vibrant microfinance market in Java and the Western islands but provision in the disadvantaged Eastern provinces is much lower. This regional inequality may be matched by a quality gap, and clients in low microfinance density areas may receive lower quality services at a higher price. Similarly, there are significant differences between urban and rural supply of financial services in Latin America and Africa (Thankom Arun and David Hulme 2008).

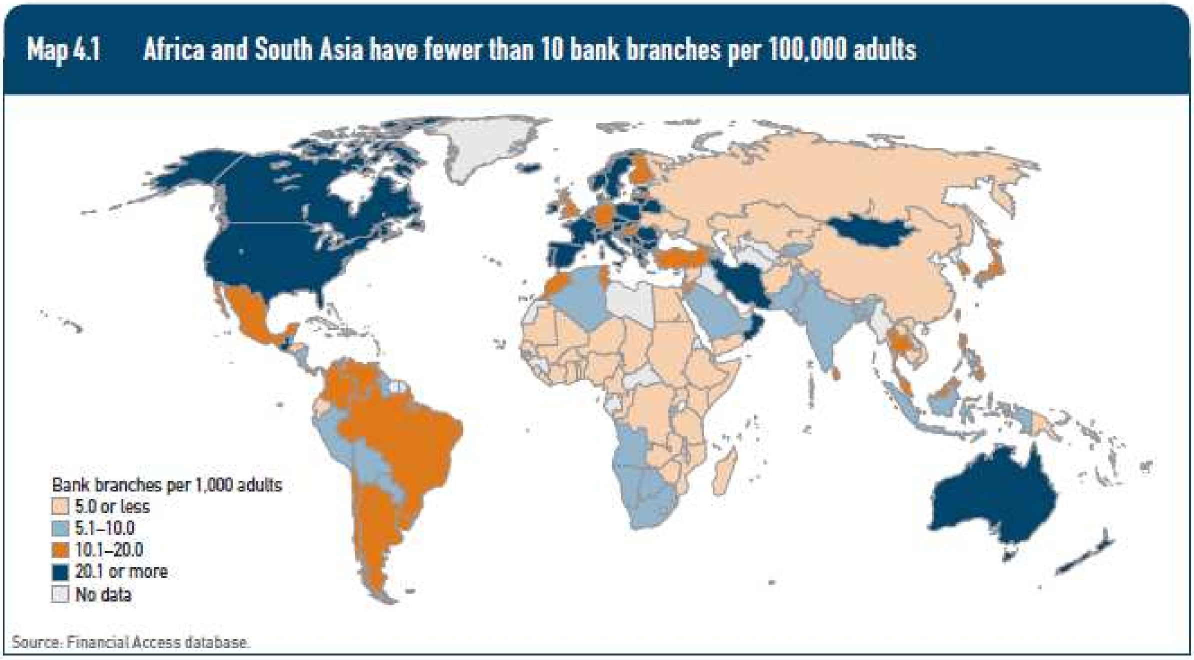
Only in a limited number of areas – parts of Bangladesh, Indonesia, Uganda, Kenya and Bolivia – is there a competitive microfinance market where low-income people have access to a range of services and providers. Across South Asia, Southeast Asia, Latin America and Eastern Europe microfinance provision seems to set to rise, through specialised MFIs and through formal banks setting up microfinance programmes. However, the likely patterns of evolution in sub-Saharan Africa and China are less clear, according to various leading stakeholders including MicroRate. The different regions have distinct characteristics which determine the nature of microfinance programmes (Thankom Arun and David Hulme 2008).

6.6 Potential investment opportunities and constraints

Geographical overview and Analysis

The following map illustrates the scale of demand for microfinance around the world

Figure 2



As can be deduced from the map above, opportunities for MIVs to invest in microfinance exist across a diverse range of sectors and geographies. The limited access to finance around the globe means that MIVs are set to grow significantly in coming years to tap into this niche. However, this will depend on their preparedness to deal with the infinite challenges that punctuate the entire labyrinth structure of MIVs.

At its best, the international structure of MIV represents a very conducive environment where best practices and ideas can be propagated, nurtured and "cross-pollinated" throughout the world.

Photo credit and illustration: Mustapha Choi

Poor infrastructure and red tape limit geographical expansion. Among the countries that provided data on rural and urban branches in the Financial Access Survey (as per the above map), there are more bank branches per person in urban areas than in rural ones. Therefore the need to build more branches to reach rural dispersed population is highlighted.

Furthermore, the need for **optimal location** of bank/MFI branches is underscored as distance remains one of the main obstacles in countries with a low population density. The Survey also warns that bureaucracy and corruption can also increase the costs of doing business, including the costs of opening and operating bank branches. Establishing a clear framework for opening branches and reducing red tape can facilitate geographical expansion (CGAP Financial Access around the World Report 2009).

MIVs are rapidly growing in number and assets under management (AUM). ***There were 96 MIVs at fiscal year-end (FYE) 2007; half were created in just 3 years (2005 - 2007***). MIV AUM increased from US$637m at FYE 2004 to US$3.7bn at FYE 2007 and US$5.4bn in October 2008 (Microfinance Insight vol 13 Aug 2009). In parallel with this rapid growth of MIVs is competition to invest in top tier MFIs which seem less risky due to their well earned reputation associated with their investment profile. To this effect, according to a reputable rating agency, MIVs are beginning to increase presence in Eastern Europe and Central Asia (MicroRate, 2007).

While this surge does not affect the African market significantly, one can almost predict that the excitement will end up there once MIV practitioners begin to realise the essence of further diversification. On the other hand, for Africa to fully operationalise its pull-factor, which is now almost in a state of inertia, it must support the building of congenial financial infrastructure as well as desirable regulations.

In many developing countries, governments are still struggling with how to regulate microfinance (Arun, 2005). Many (particularly central bankers) are inclined to attempt to regulate MFIs in the same way as they do formal sector banks. Whilst in theory this will provide savers with security, in practice it discourages the evolution of MFIs and often means that established MFIs cannot develop savings products. This keeps depositors ‘safe’ from unscrupulous or poorly-managed MFIs, but means that they have to use other savings mechanisms (hiding cash in slum dwellings, buying livestock or asking a trader to hold cash). These other mechanisms are often riskier than the services that MFIs can provide (Thankom Arun and David Hulme, 2008).

While scrambling into new markets are often characterised by competition which can be sometimes detrimental to players among themselves, MIVs should play such competition wisely. New entrants should forge relationship with existing ones through collaborating in issues of mutual interest. Such relationship can also help new entrants to gain insight into new markets.

CHAPTER 3

7 Research findings and Analysis

The findings are drawn from extensive literature review and the interviews conducted with key industry stakeholders including institutional investors such as banks and MIVs. To gain a more comprehensive insight into pertinent and topical issues from microfinance practitioners and investors perspectives, secondary interviews (interviews conducted by other researchers) were also consulted as an additional data collection method to ensure a greater richness of data.

Although my interviews were not comprehensive, hence the small number of industry representatives surveyed, I believe that the report has somewhat captured the state of the field today. Furthermore, I hope that my analysis will spark and stimulate the infinite debate of measuring and reporting social performance of MIVs. The key findings are summarised under the following headings below. The reason for choosing such a structure is to try to ensure than no research question is left unanswered.

7.1 The importance of measuring social Performance for MIVs

The past few years have witnessed the emergence of several new Microfinance Investment Vehicles to tap into the rapidly growing microfinance industry. Also due to the current financial crisis of which its impact is still unfolding, as this thesis is being written, an increasing number of investors are now searching for green, ethical and more stable financial products, therefore further unleashing opportunities for stakeholders. As a result, many fund managers are becoming more selective in their investment products in favour of ethical principles.

In order to take all these factors on board and to ensure that microfinance stays responsible and differentiates itself from other malicious financial practices an integrated, coherent and transparent way of reporting and monitoring the actual social and environmental outcome to investors and other interested parties is crucial. The importance of such scrupulous reporting is attested by CERISE: “Investors who cannot give compelling evidence of their social performance risk overstating microfinance benefits and seeing their own reputation discredited when “problematic” aspects are publicized (CERISE- SPI Investor).

MIVs are addressing these issues by pro-actively anticipating investors' questions and communicating on topics such as interest rates, over indebtedness, outreach in terms of both geography and social groups etc. Adopting such social approach will enable MIVs to distinguish themselves from competitors, thereby acquiring unique edge. The following points reflect the wide opinion of various researchers, microfinance practitioners and investors in terms of the importance of social performance reporting of MIVs:

7.1.1 Education

As microfinance is becoming more recognized as an important poverty alleviating tool, more and more social investors are being drawn into its favour. Although some of these investors are fascinated by its vital role in alleviating poverty, they lack insight into how exactly it can help turn around positively the lives of the poor. Therefore investors need to be educated through comprehensive reporting of social performance of the companies in which they invest into or planning to invest so that they will no longer take for granted the positive development impact of microfinance. ***"Investors choose Oikocredit expecting an investment with a strong social effect and a modest financial return. They want to know if we are fulfilling our social goals of reaching the poor and helping to bring about positive change in their lives and we need to be able to demonstrate that" (***Ging Ledesma, SPM Manager, Oikocredit, April 2010).

7.1.2 Attracting additional funding

A consensus has been reached among the investment community that communicating results is crucial to encouraging additional funding. A recent study argues that whether growth in the field comes from the investment community, the philanthropic community, or a combination of the two, a serious increase in the scale of social investment capital will only occur if there are solid data about both the financial and social results (Kramer Mark and Cooch Sarah 2006). Dedicated social investors are very much inclined to see tangible results; attributed to their actions. Therefore, measuring and communicating social performance is vital in helping them to renew their commitment thereby increasing further capitalisation.

7.1.3 Positive results can influence government policies

A growing body of literature argued that well documented social performance can trigger favourable government policies at both local and international level. This could be manifested in the form of attractive fiscal policies (tax incentives) or congenial regulatory framework that supports the investment activities of MIVs. Well documented results are therefore an important tool for promoting social investment both in the field and the countries representing the funding sources. With its MIV labelling agency, Luxflag as well as its attractive fiscal policy, Luxembourg is set to be a leading example in this nuance. Its current supportive and encouraging position has a great potential to influence MIVs to commit to high quality social performance reporting standard.

7.1.4 It helps mitigate risk and increase transparency

Demonstrating transparency by voluntarily disclosing a broader set of information to stakeholders can help mitigate risk. Many MFIs are now adopting a more client-centred approach (Imp-Act 2005), developing services which are responsive to client needs. Understanding and selecting acutely suitable products to satisfy consumer demand is crucial for running any business successfully, as any inherent risk is reduced. Even outside the microfinance industry, wrong product offering is said to be blamed for many business failures. Social performance management enhances these kinds of business practices where the end-client is central in the core strategy of organisations.

7.1.5 Enhances the balancing act of financial and social objectives

It assists MIVs in aligning their financial and social objectives more coherently and to make better business decisions based on a more thorough understanding of the trade-offs each involves. Among MIVs that follow this approach is Oikocredit.

7.1.6 Prevention of mission drift

SPM can help MIVs to identify strength and weaknesses in terms of their social mission, thereby improving overall social performance. Problems can be identified at an early stage before they become damaging for the organisation. Moreover effective social performance reporting enables MIVs to evaluate which of their programmes have a strong social focus, and prioritize or strengthen their support accordingly.

7.1.7 Evaluating investment opportunities

Social performance reports can serve as an important tool for identifying microfinance institutions with investment potentials. When selecting MFIs, certain MIVs consider the overall performance of MFIs of which social performance is an important factor. As soon as the Investment officer visits the candidate institutions, the investment officer incorporates the MFI's social performance into their analysis (Incofin-2008).

SPM enables managers (in the case of institutional investors) to test and improve their judgment about which projects are most promising and how best to structure them to achieve both financial and social return. It is also the basis for determining which MFIs merit follow-on funding and which do not. For example Incofin Investments Management and Oikocredit are both using result of their performance evaluation in their investment decision-making process to determine which investees will receive seed capital or additional funding. Moreover, social performance data can help them improve their own operations or give investment staff valid reasons for recommending changes vital in increasing social returns. Consistent and credible reporting form the basis for all these practices.

7.1.8 Benchmarking

The vast majority of international investment in microfinance takes place through Microfinance Investment Vehicles (Rhyne Elizabeth). In their quest to invest, potential microfinance investors might begin their search by reviewing various MIVs which they can find in the MIX database. The International Association of Investors in Microfinance (IAMFI) and the Council of microfinance Equity Funds (CMEF) also represent an important platform for information exchange, where these investors can compare an array of MIVs in terms of their propensity to fulfil the double bottom line of financial and social performance. Most microfinance actors and academics have agreed that this benchmarking exercise is a much welcome one as the industry is currently plagued by weak regulatory framework. While MIVs continue to take hold in the investment community, these platforms represent an important forum for best practices.

7.1.9 Conclusion

Effective social Performance increases transparency and improves credibility of not only the MIV but also among its investees, clients, banks and donors. In the long run this is crucial for ensuring effective governance at all levels. Since poverty does not only mean lack of access to basic necessities but also exclusion from decision-making processes, social performance measurement represents a vital tool for empowering the poor and the voiceless by giving them the opportunity to take integral part in decisions that affect them. Increased transparency at each level can help in combating poverty at the lower pyramid of society. An important aspect of social performance is to serve clients better. By monitoring progress towards your social objectives, you will know where you are and where you have to go (ACCION International-2005). The Client Protection Principles serve as an important tool that can draw the microfinance client closer to the decision making table, thereby claiming greater responsibilities of the microfinance products they consume.

At its worst, social performance reporting can be perceived as a mere marketing gimmick. On the other hand, this initiative can be beneficial to the end client if the underlying reason is to raise much needed capital necessary to fund life-elevating projects of the poor. At its best, it represents genuine attempts by MIVs working with stakeholders at both client and MFI levels to address the ever increasing social challenges of our times.

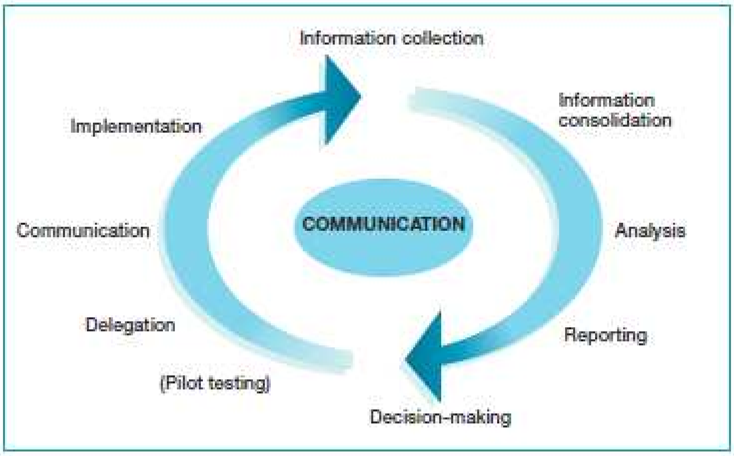
Making information about social performance of MIVs easier to access, use and understand means that investors can more easily hold MIVs and MFIs to account for investing their money in accordance with their social wishes. Transparency creates better feedback from beneficiaries to donors therefore; helps the entire stakeholders better understand what works and what doesn't. In terms of funding coming from the donor communities, it helps reduce the opportunities for fraud and corruption by addressing the most pressing priorities. Therefore the information published should be comprehensive, accessible, comparable, accurate and timely.

7.2 HOW SPM IS CURRENTLY BEING COMMUNICATED TO THE PUBLIC

The heart of SPM is information use. An SPM system needs to both collect relevant and timely information and communicate it effectively to interested stakeholders. The means of disseminating social performance information can range from selected case studies to analytical reports or combination of both. Although there are infinite ways to collect and report information it will be of little benefit unless the data is used in a systematic way to assess and improve operations, services, products, and customer relations. Therefore the way information is used requires planning and attention (Imp-Act 2005).

❖ **The Feedback Loop**

Figure 3



Source: Impact 2003 cited from IFAD - Assessing and Managing Social Performance

7.2.1 The feedback loop – From MIV perspective

The feedback loop provides a practical framework for thinking about how to ensure that the information gathered with the SPM system will get used (Impact 2003). Although the use of the feedback loop is more apparent for MFI operations, it can also represent an important analytical lens for understanding how to integrate certain aspects of social performance management into MIV's internal and external operational procedures.

All of its ten components are highly relevant and can be refined for application on MIVs. For example, in order for MIVs to take social performance seriously they need to align it with staff training; budgeting to ensure that enough money have been allocated to ensure timely collection, and analyzing and reporting of performance information. In the event that an MIV wishes to outsource the process of social performance (as in the case with European fund of South East Europe) then they need to develop procedures outlining when, and for what purpose, outsourcing will occur. Furthermore, it is crucial to establish a longer term cooperation with external consultants to develop better understanding of system requirements and needs, and to avoid unnecessary delays (Imp-Act 2003).

Since MIVs cannot act alone in the pursuit to measure social performance, the Feedback Loop can also serve as an important angle for discussion to not only understand but to map out imperative institutional arrangements between MIVs and their partner MFIs to reinforce and better co-ordinate the communication pathway between the two entities, to ensure the exchange of timely and credible information. All this is grouped under the banner of governance of which its consideration can shed light on the communication flow across various stakeholders ranging from the CEO of the MIV to the field staff and clients of the MFI. The outcome from this endeavour can surely yield the type of benefits asserted by Roy Mersland (mentioned earlier), when he argued about the need to search for governance mechanisms which can bring benefits to both the MFI and customers (Roy Mersland).

7.2.2 Methods of communication

7.2.2.1 Internal communication

Social performance results are used first and foremost internally by the institution to inform its board or management team of its social performance. For example the SPI audit offers an objective, concise and visual description of the systems in place to achieve institution's social mission, and how the latter affects operational and financial performance. In addition, indicators can be monitored over time by management, to help inform strategic planning (*Source: Cerise SPI guide on what to do with social performance results)*

7.2.2.2 External communication

7.2.2.3 The annual reports of the MIV

Social performance report can be disseminated through the organisation's website. The report can also be mailed to shareholders electronically or by post upon request. An important benefit highlighted by CERISE is that the complete report can be used to enhance an organisation's general reporting (in annual reports, performance reports or public relations material, for instance).

7.2.2.3.1 MIX Market database

Like MFIs, MIVs can report the Social Performance Standards (SPS) on the MIX Market. To ensure credibility of information, external auditors are often used to help certify the information. This drive for transparency is important for improving dialogue on social performance within the microfinance sector, consolidating relationships between the sector and government authorities and improving microfinance's image in public opinion (Operational Guide to the SPI questionnaire, version 3.1). Reporting through the MIX Market is also widely regarded as an important initiative towards standardization of reporting tools and format as well as being instrumental in spreading good practices.

7.2.2.3.2 Presentation and Road shows

The social performance report is an important tool to help organisations showcase their social achievement in various stakeholder meetings and networking events. Method of communication can be in the form of Power Point or video or combination of both. Video for example is a powerful method to convey client stories reaching wider audients.

7.2.3 Conclusion

Social performance communication is characterised by the wide mixture of disclosure styles which is hugely problematic not only for investors and researchers but also to civil society at large including the very clients of microfinance. Comparability of information is another important element associated with successful industry reporting standard. While there are some advances in this, the situation can be improved. The task of acquiring common reporting standard is well beyond an individual company's responsibility. It requires a common framework that reflects a wider industry initiative.

The Microfinance Information Exchange (MIX) is already pursuing a laudable initiative which can act as a springboard for further development. According to the MIX, it is worthwhile noting that some companies are making significant efforts to consider stakeholder interest in the contents and formats of their report. With honest feedback from stakeholders or external reviewing bodies, this trend is set to continue markedly. I therefore suggest for the communication loop to be extended to the actual clients of microfinance. Clients may spend the money they borrowed productively if peer pressure is exerted on them through emulative and inspiring client stories. Success stories can be very inspiring and motivating especially to close-knit communities.

7.3 Social Performance Monitoring Tools for MIVs

Stocktaking and analysis

Social audit tools for MFIs have multiplied in recent years helping numerous MFIs to improve their social performance. This phenomenon is better described by Imp-Act Consortium as: There are so many social audit and poverty assessment tools available in the sector to the extend that MFIs are sometimes confused or overwhelmed by the different choices and often unsure about when to use one over another, which ones are complementary and which ones overlap. They further assert that some MFIs have used a number of these tools in succession, only to find themselves with too much data that is similar, but not consistent enough to analyse and act upon (Anita Campion & Chris Linder and Katherine E. Knotts-Imp-Act Consortium 2008).

By contrast, investors/MIVs have been somewhat forgotten in the ongoing innovation and experimentation. It was noted from CERISE that while some of these tools available can be refined to accommodate the social performance measurement requirements of MIVs, they evidently deserve an audit methodology tailored to their own concern (CERISE SPI-Investor). As investors' standpoint on the social performance debate is very diverse, identifying universally accepted social performance indicators is one of the most difficult challenges facing the microfinance industry.

In its discussions on social metrics with investors, IAMFI has uncovered a spectrum of opinions that reflects the diversity of the investor population itself. Some investors believe that the social outreach aspect of microfinance is sufficient to infer social benefits and they don't need further proof. Others want some sort of metrics – but measured at the MFI, not the client, level for greater efficiency. Still others feel that social metrics unnecessarily distract management and that scarce resources are better spent on product development, client outreach and loan portfolio administration (IAMFI 2008).

In this section I intend to take stock of some of the SPM tools available including those designed specifically for MIVs. Where possible, I will describe and analyse them in terms of both their functionality and suitability for meeting investor's and industry expectations. Therefore any noticeable shortcomings will be flagged up.

7.3.1 CERISE Social Performance Indicators (SPI) Initiative (CERISE)

Assesses MFIs' social performance by using a series of questions to evaluate their intentions and actions, as well as their systems and processes, along the following four dimensions:

1. Outreach to the poor and excluded populations
2. Adaptations for products and services per target market
3. Improvements in social and political capital (i.e. empowerment);
4. Social responsibility (toward clients, employees & communities)

Source: http://www.cerise-microfinance.org/pdf/En/spi_quest.pdf (cited from the report of Imp-Act Consortium 2008)

7.3.2 The SPI-Investor Tool (CERISE)

This is a questionnaire based tool designed to be administered internally by MIVs.

➢ **Please refer to the case study section of this report for more information on this tool.**

Source: CERISE SPI-Investor V1-2-3

7.3.3 The GRI (Global reporting Initiative)[3]

An independent institution started in 1997 whose mission is to develop and disseminate globally applicable, sustainability reporting guidelines, comprising 158 indicators. These are for voluntary use by companies and governmental and non-governmental organizations to report on the economic, environmental, and social dimensions of their activities, products, and services. The concept of this tool is embedded on what is commonly referred as the triple bottom line, being People Profit and the Planet. The GRI initiative was endorsed by the United Nations Environmental Programme in 1999, providing funding for further development as well helping to publicise it to the wider investment community. More than 30,000 stakeholders from 80 different countries have contributed to formulating the GRI criteria (Microfinance for bankers).

7.3.3.1 Who is using the GRI

GRI claims over 1500 businesses and other organisations as users. The GRI reporting standard was adopted by Triodos bank in 2001. Triodos bank is major financial institutions with assets of around 3.7 billion. It manages three funds that provide finance to more than 80 microfinance institutions. In short, Triodos regards the GRI as the most well-known and the widely accepted of all social performance reporting and recommend it to its equity investees engage in inclusive finance.

The GRI is applicable to wide range of industries and reflect the following areas: Labour practices, use and disposal of natural resources and economic foot print. For smaller organisations, GRI offers user-friendly guidelines to help ease the reporting process.

7.3.3.2 Specific shortcomings

According to significant body of literature many investors find the emphasis on environmental performance more relevant to chemical, energy and transportation and less relevant to inclusive finance. " As the GRI is designed to be broadly applicable across

[3] Much of the contents relating to the GRI is derived from the book Microfinance for Bankers- Elizabeth Rhyne

sectors, it does not address some of the information important to the inclusive finance community particularly data on the socio-economic characteristics (Elizabeth Rhyne, 2009).

7.3.3.3 The Incremental nature of GRI

The incremental nature of GRI means infinite reporting burden as the more institutions grows the more they have activities to report.

7.3.4 Progress out of poverty Index (PPI) [4]

The PPI was developed by Mark Schreiner for Grameen Foundation, CGAP, and the Ford Foundation. The tool is composed of a set of 10 questions that measures family's poverty level. The assessment begins immediately when clients are on board and periodically thereafter. At any point of time the tool is applied to determine whether if the family has moved out of poverty over time. Among its indicators are welfare and education of children, housing, energy use, consumer goods and employment. The indicators are culturally sensitive, in that questions are tailored to reflect the culture of each country.

7.3.4.1 Specific Shortcomings

Indicators are culturally sensitive, so need refining before showcasing in other countries.

They can be expensive to develop and validate

They make no distinction between urban and rural households, which will likely have different poverty characteristics.

7.3.5 PAT IRIS Poverty Assessment Tool [5]

The Poverty Assessment Tool was developed by the IRIS centre at the University of Maryland, USA in response to amendment to the U.S Microenterprise funding on the "very poor". The amendment requires USAID to develop, field test, and certify poverty assessment tools for use by microenterprise practitioners.

The tool is composed of short household questionnaires with 16 to 33 questions on topics ranging from consumer durables ownership to educational attainment. The tool is based on simple, low-cost quantitative tools for measuring extreme poverty among clients of microfinance and microenterprise programs.

7.3.5.1 Specific Shortcomings

1) The PAT does not measure the impact of financial services on clients.

[4] [4] Imp-Act consortium and the IRIS centre.
[5] Imp-Act consortium and the IRIS centre.

2) Clients might use loan to buy consumer goods instead of investing it, there by causing biased assessment results.
3) Because the PAT is analyzed only at the aggregate level, it cannot be used in its present form for admitting or denying admittance of clients into the program based on their poverty status. With very slight modification, this is possible.

4) It has another drawback of increasing the incentive and opportunity for manipulation by loan officers and clients, particularly when it is used for poverty targeting (accepting or reject client in the program based on their poverty status).

More information: www.iris.umd.edu or http://www.povertytools.org/

7.3.6 Quality Audit Tool (QAT)6

Developed by Anton Simanowitz for the Microfinance Centre (MFC), the Quality Audit Tool is a diagnostic tool designed to review and improve the effectiveness of management processes for achieving social goals. The QAT reviews three main aspects of microfinance social performance in order to identify the actions needed to improve performance:

1. Process management
2. Internal systems
3. The status and effectiveness of the systems for managing social performance.

MFIs can conduct the QAT with internal resources, often with just the help of a facilitator.

7.3.6.1 Specific shortcomings

QAT focuses on an organisation's specific objectives and the effectiveness of its systems for achieving them, as opposed to social ratings, which tend to examine procedural compliance or benchmark against common social indicators or practices.

7.3.7 USAID Social Audit Tool (SAT)7

The US AID Social Audit Tool (SAT) uses a process auditing approach to assess social performance in relation to the MFI's stated social mission. It attempts to answer the following questions: To what degree do the internal processes promote fulfilment, or
Lack of fulfilment, of the MFI's stated social mission?

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[6] Cited from the Imp-Act Consortium Report- putting social into Performance Management- a practice-based guide
[7] Cited from the Imp-Act Consortium Report- putting social into Performance Management- a practice-based guide

Process auditing involves an in-depth assessment of six internal processes critical to
The MFI's social performance:

1. Mission statement and management leadership
2. Strategic planning
3. Customer service
4. Monitoring systems
5. Recruitment and training
6. Incentive systems.

The SAT also assesses the MFI's performance in relation to its social responsibility (SR).

7.3.7.1 Specific Shortcomings of SAT

1) Audit is carried out by external party, thereby allocating less responsibility to internal staff
2) Focuses solely on performance quality and revenues
3) Collects a lot of data on loan application form, but does not put it into the MIS of the organisation or use it to make management decisions related to SPM.

7.3.8 The ECHOS of Incofin

Developed by Incofin internally to assess its own social performance and that of their investees abroad.

- **Please refer to the case study section of this report for more on Incofin's tool, ECHOS**

7.3.9 IFAD Decision Tools for Rural Finance[8]

As I am writing the final part of this report in mid-June 2010, the launch of another tool was announced. The IFAD decision tool for Rural Finance is the direct result of an intensive consultation process with researchers and practitioners. Building on the content provided by Enterprising Solutions Global Consulting, the decision tools were discussed and reviewed with the IFAD Thematic Group on Rural Finance and with key leaders from a number of partner institutions and centres of excellence in microfinance.

This knowledge management tool is designed to help identify and answer the questions that arise in each rural finance project, provide background on key issues, define common terms, highlight risks and opportunities, and provide references for further investigations. IFAD

[8] IFAD 2010

describes this tool as a ‘living document’ that will be continuously updated and improved to reflect the development of the industry and innovations. The tool is divided into four main sections, each with a specific objective:

1) **Assessing the market.**
   Analyse the status of a financial sector and identify the gaps

2) **Designing a project.**
   Define the interventions in a rural finance project

3) **Assessing and selecting project implementation partners**
   Assess and select project implementation partners through a transparent, competitive process

4) **Conducting performance monitoring and evaluation**
   Effectively conduct ongoing and annual performance monitoring

7.3.9.1 Specific shortcomings

1) While the tool is applicable to microfinance institutions, its functionality is specific to rural development through agricultural activities, leaving other aspects of development from the equations. In recognition of this gap IFAD asserts that: rural finance is not the only answer in rural poverty reduction, but it is a key part of the response.
2) Its supporting mechanism is centred more on agricultural projects of significant scale.
3) It seems to focus more on donor organisations rather than private financing

7.3.10 External Social Audits[9]

The main purpose of an external social audit or rating is to provide an objective assessment of the social performance of organisations, both in general and compared to its peers, in a way that is more credible than an internal audit report would be. This information is also often shared with (and paid for by) investors and donors to serve their own performance requirements. Although there are many social rating agencies, most of them seem to tailor

[9] Cited from the Imp-Act Consortium Report- putting social into Performance Management- a practice-based guide

their services at MFI level and not at MIV level. Below is an example of a rating Agency and the areas that they address:

7.3.10.1 Microfinanza Rating's

Microfinanza Rating addresses the following areas:

1. Social mission, strategy and systems (SPM framework)
2. Social responsibility
3. Outreach
4. Quality of services

Source: www.microfinanzarating.com (cited from the Imp-Act Consortium, 2008.)

M-CRIL, PlanetRating and **MicroRate** are all important players in the microfinance rating industry.

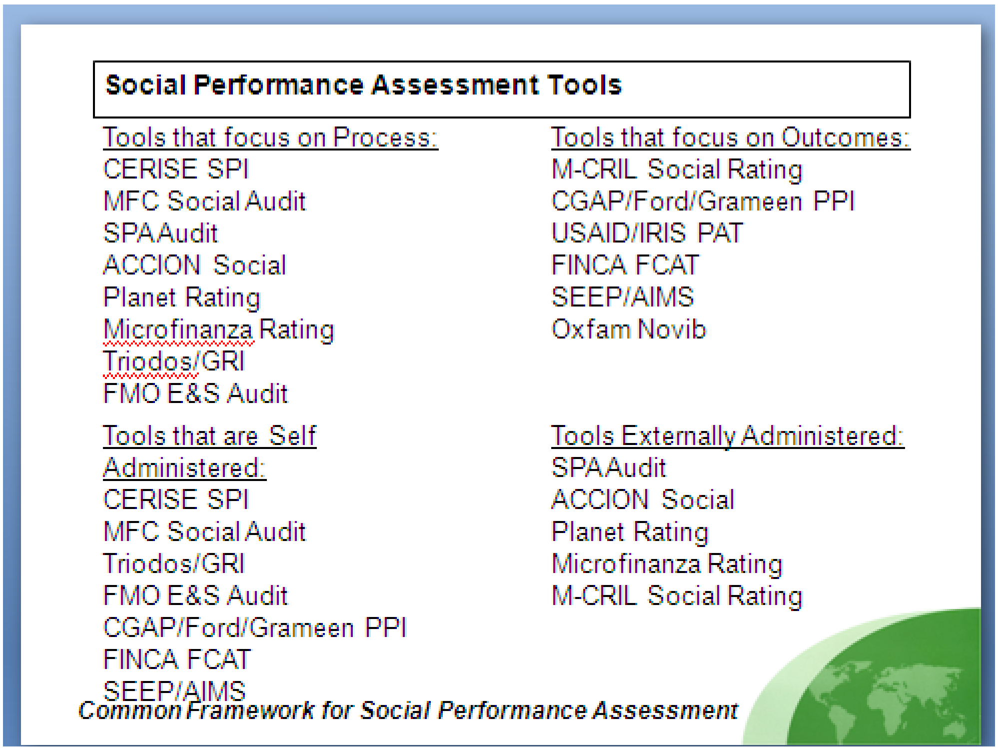
7.3.10.2 Specific short comings of Rating Agencies

1) Service is more tailored to address the social performance measurement at MFI level.

2) Service can be expensive.

3) Services offered is limited to identification of weaknesses in terms of social performance rather than offering suggestion on how to improve social performance.

Figure 4



Source: IMP-ACT

7.3.11 Conclusion

There are a number of different users of social performance management tools, at both MFI and MIV levels, each with their own specific needs and requirements that reflect their different objectives. The inclusion of the social rating agencies in the above list suggests that some institutions outsource their social performance management. While these variations shape their priorities, they also confirm that microfinance practitioners have different concept and means of addressing poverty. For example, some institutions focus on women's empowerment through inclusive finance while others concentrate on measures to support small and medium enterprises, irrespective of their ownership in terms of gender. Some funding institutions may also favour and support rural development initiatives while others may choose to help urban slum-dwellers to attain a better living standard by addressing their housing needs.

This contradiction in the way institutions perceive poverty is clearly an indication that the industry is far from adopting a common social metric. However, a way round this baffling situation, as suggested by one scholar is to ensure that social metrics for internal use is tailored to each company's unique pursuit of comparative advantage (Elizabeth Rhyne, 2009).

Elizabeth Rhyne further argues that these inherent difficulties do not suggest that the effort that is being channelled towards social performance management should be abandoned.

To ensure that MIVs are included in this development phenomenon, it is paramount for practitioners to build upon the existing tools with utmost considerations for MIVs. There is no need to start from zero as some of the tools like the SPI, PAT and GRI are all characterised by an important level of flexibility for further development and enhancement to accommodate new measurement functionality specific to the activities of MIVs. In support of this argument, the SPI-Investor tools is already being piloted and the results is so far encouraging, indeed for investors. The ECHOS of Incofin is another tool developed specifically to accommodate the needs of MIVs. The need for better measurement tools is far too great, rather the task should be approached with flexibility and realism (Elizabeth Rhyne, 2009). This flexibility characterises some of the existing tools and should be taken onboard throughout the process of standardization.

Regarding the GRI, more specialised indicators have been called for to make it more suitable for inclusive finance. On the other hand, the endorsement of the GRI tool by Triodos bank means that it has a great potential to meet the needs of MIVs. Its inherent feature to support good environmental practices makes it highly relevant to MIVs considering adopting, the ESG (Environment, Social and Governance) principle. Whilst I find the PPI, PAT and SPI highly relevant to MFIs, they can be utilised directly by MIVs if their social performance measurement is done by means of aggregating their investment portfolio. With such tools they can collect and analyse data of their partner MFIs which make up their overall investment portfolio.

I notice that most of the tools including those of the rating agencies have these common four dimensions: “Social Mission and vision” “Access & outreach” “Quality of customer services” and “Responsibility and contribution to community”. Of course these similarities are crucial to ensure reporting on the MIX database, but also represent a positive and welcome approach towards greater mainstreaming and standardization.

As new MIVs continue to mushroom in the inclusive finance sector, we are likely to see more new tools emerging to reflect such growth. In view of the current reputational risk cloud hanging over the microfinance sector, the IAMFI has indicated its preference for indicators measured at the MFI level that improve customer protection and service while fostering industry sustainability (IAMF 2008). Therefore tools that support such preference among other important priorities are set to earn the favour of investors. **Please refer to the recommendation section for further details regarding investor concerns and expectation**.

If there is any practice that the MIVs should avoid emulating from the MFIs, it would the lack of joint effort or universal approach in the process of developing social performance measurement tools. Therefore if experience is any guide, such mistakes can be avoided.

CHAPTER 4

8 Case study: The experiences of Incofin and Oikocredit

This study is based on practical experiences of both Incofin and Oikocredit in measuring their own social performance and that of their partner MFIs. Therefore the study seeks to gain an interesting insight into their tools, indicators, methodological approaches and the challenges that confronted them, from the outset to implementation.

Thanks to key industry practitioners like Incofin and Oikocredit whose advanced creativity and capability to explore beyond established pathways represents clear evidence that MIVs are now beginning to measure their social performance. The Incofin and the Oikocredit methodologies represent a few rational ways by which to measure social performance of MIVs where effective and standardized methodology does not exist. I will first dwell into their common methodological approach before studying separately each organisation.

8.1 COMMON METHODOLOGICAL APPROACH

How performance is data collected?

The cheapest and most common approach is to have MFIs periodically provide data to the investor on pre-formatted templates. This approach requires few resources from MIVs, other than time spent enforcing template submission and contacting investees to fill in incomplete data. As for Incofin and Oikocredit, the following methodology is observed.

- **First, a visit is made to the MFI abroad**

  This gives the Investment Officer an opportunity to have access to first-hand information and to build rapport with the dedicated team of the MFI responsible for providing the requested information. In order to complete the evaluation form properly and incorporate it into their social performance system, the investment officer may also conduct series of interview during the visit.

- **Presentation of data to the investment officer**

  In response to the investment officer's request, data is presented, in the form of manuals or statistics for computation. The investment officer checks and verifies data to ensure accuracy. Any incomplete field is checked with the data supplier. It is advisable to complete this checks on the field. These checks can be done in the field or upon the Investment's Officer's return.

Cleaning the data

- Upon the Investment Officer's return, information will be subjected to further verification and amendment if necessary prior processing. This process may take place under the supervision of the MIV's internal auditor.

Computation of data and results

- The data will then be fed into the company's system (in to ECHOS in the case of Incofin) for computation to finalise the process. Once data is fed into the system, all the necessary computation is finalised, and results produced. A successful completion of an evaluation should detail a total social performance result for each of the given dimension analyzed by the social performance system/software.

8.2 The experience of Incofin[10]

8.2.1 Company introduction

A Belgian cooperative company founded in 1992, Incofin manages four microfinance investments funds with a global geographical reach. In December 2007 Incofin managed an investment portfolio of nearly 65 millions, spread across 18 countries and 49 MFIs. Today Incofin position itself as Belgium's leading microfinance Investment Company and one of the biggest players in the industry.

8.2.2 Introduction of Tool- The ECHOS

With inspiration from tools developed by CERISE and ACCION International, ECHOS was developed in-house by Incofin to address their urgent need to measure their activities. It was later revised in 2007 with more generic indicators and dimensions to help them undertake their due diligence responsibilities. ECHOS is a small software with several modules that includes a questionnaire with 43 social performance measurement indicators. The tool is applied directly via an investment officer; therefore the collating and documenting first-hand information from MFIs is possible.

[10] The data relating to the Incofin case studies is obtained from Incofin's various documents in the public domain including their annual reports and studies on social performance management. To ensure richness of data, I also have conducted and interview with their social performance representative, David Dewez.

8.2.3 Dimensions incorporated in this tool

Table 1

Dimensions	Weight	# indicators per examined dimension
Mission and Vision	10%	5
Scale and outreach	30%	11
Quality of service	25%	8
Human resources	25%	7
Environment and social contribution to the community	10%	5
Total	**100%**	**36**

Source: Incofin

Each dimension above is measured by a series of both quantitative and qualitative indicators totalling 36 as shown above.

8.2.4 A study conducted by Incofin using their social performance management system, ECHOS

The examples presented in the tables below represent an aggregated results based on 23 social performance analysis Incofin had carried out since the launch of their new tool in 2007 up to 2008 using the methodology described above. Incofin argues that while the sample does not represent the global picture of the microfinance industry, its variable mixture of different institutions from different geographical locations makes the study less bias. The scale of the sample diversity is described as follows***: "There is information from entities located in 27 countries of four continents (Africa, Asia, America and Eurasia) and 9 geographical regions"*** (David Dewez and Sandra Neisa, 2009).

Summary of results between 2007 and 2008

DIMENSIONS	AVERAGE SCORES OF THE INCOFIN PORTFOLIO	
Mission and Vision	8,2/10	**82%**
Scale and outreach	24/30	**80%**
Customer service	17/25	**68%**
Human resources	21/25	**84%**
Environment and Contribution to the community	5,2/10	**52%**
AVERAGE TOTAL SCORE	**74.2%**	

Table 2

Aggregated results based on the 23 social performance analysis Incofin has carried since their new tool was rolled out in 2007. Source: Incofin

EXPLANATION OF RESULTS OBTAINED

	Grade Ranges
91-100	Excellent Performance
81-90	Very Good Performance
71-80	Good Performance
55-70	Low Performance
0-54	Inadequate Performance

Score <50 percent = MFI with inadequate social performance**: File is rejected**

Source: Incofin - August 2008

8.2.5 The social performance of Incofin's Investment portfolio

- The average social performance score of the MFIs included in Incofin's portfolio is 74.2%. Although this is a very good score according to the above explanatory table, Incofin is less complacent with the results and noted that there are certain gaps that need addressing.

- The higher scores are centred around the "Human Resources", "Mission and Vision" and "Scale and Outreach" dimensions.

- The remaining dimensions,” Customer Service” and “Environment and Contribution to the Community” show lower score. Incofin noted this gap and believes that with time, these dimensions will come to the fore.

- **Social performance by geographical location**

  Key findings

Africa	64.2 percent
Asia	70.8 percent
Eurasia	71.8 percent
Latin America	71.9 percent

Source: Incofin

- Latin America with 71.9 percent displays the highest score. According to Incofin the underlying reason for this high score is attributed to high degree of maturity of the microfinance sector in Latin America.

- Africa shows the lowest score of 64.2 percent. The reason for such a score is due to the fact that the microfinance sector is relatively young and inexperienced.

- The difference between the score in Latin America (71.9 percent) and Eurasia 71.8) is very marginal. This is a clear indication that the microfinance sector in Eurasia is rapidly catching up with that of Latin America and for that matter taking social performance seriously.

Table 3

8.2.6 Key Advantages of Incofin tool
Quality of information is assured, as information is collected from the MFI by an Investment Officer
Effective in capturing data
Investees display greater responsibility in respect of the data they submit
It is easy to use and allows the MFI to conduct internal self-assessment.
Low operational cost. However one must invest time and money at the beginning
Based on data which is easily available and checked by an external auditor
Clear and comparable results at country and regional level
Compatible with the MIX database

Table 4

8.2.7 Some specific shortcomings
Can be costly in terms of time and any travel expenditure
Quality time is spent on data validation and amendment
Limited scope.

8.3 The experience of Oikocredit[11]

Oikocredit is an International Development Finance Institution established in 1975 at the initiative of the World Council of Churches. Oikocredit's mission is to promote global justice by challenging people, churches and others to share their resources through socially responsible investments and to empower people with credit. At the end of December 2007, investment capital from members exceeded €318 million (Oikocredit, 2008).

Oikocredit's core business is development financing to SMEs, fair trade enterprises, micro-finance and community based enterprises in over 60 countries. A network of 11 Regional Offices and 29 country offices is involved in project identification, evaluation, monitoring and

[11] The data relating to the Oikocredit case study is obtained from Oikocredit's various social performance documents including their annual social performance reports and CERISE's SPI and the investors Brief DP N°6.

administration. During the last years, the increase of the Microfinance projects in Oikocredit's portfolio has been significant (SPI and the investors Brief DP N°6).

8.3.1 Introduction of Tool - THE SPI-Investor

Based on the original SPI tools designed for the assessment of microfinance institutions, the SPI-investor was developed to evaluate the social performance of Investors like Oikocredit. It is specifically refined to assess the MIV's operations including strategy, products and any social benefits.

Its role in social performance management is summarised in the following words by CERISE: ***"It is a transparent reporting tool with benchmarking potential, a welcome addition to a field that is mostly self-regulated".*** The overall objective is to measure MIV's efforts to invest effectively and responsibly.

8.3.1.1 Questionnaires of the tool (source: CERISE)

The questionnaire that forms the basis of the SPI-Investor tool is divided into 3 sections:

Section 1 MIV's Strategy

The tool assesses the social performance against MIV's own objectives. Therefore the first section is to focus upon the investor's strategy and social mission.

Section 2 – Social performance of Investees (MFIs)

This section focuses on the aggregated social performance of MIV's investees, an indicator of the quality of an MIV's investment decision and level of exposure. This data also helps MIVs make investment choices on which MFIs to support.

Section 3 –Social Responsibility of the MIV-

This final section analyses the MIV's practices using social responsibility criteria. CERISE has adapted the environmental, social governance aspects, crossing them with issues specific to microfinance based on the four dimensions and related indicators.

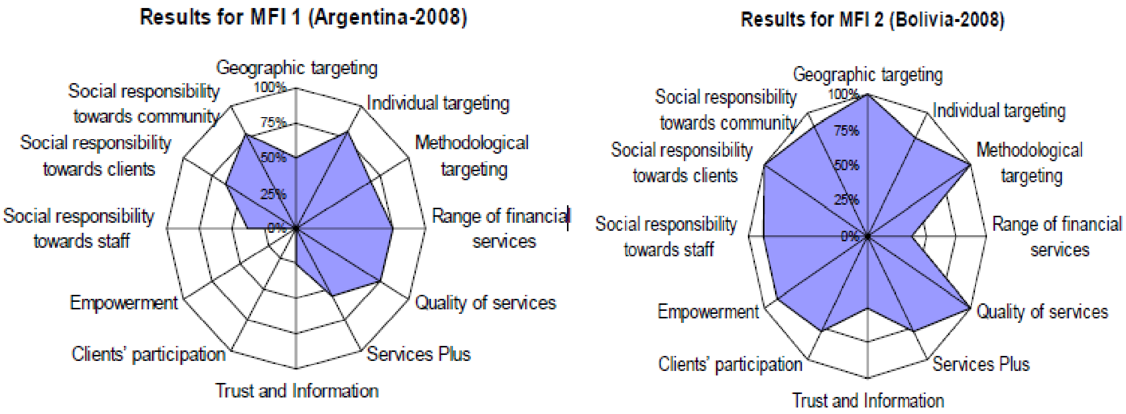
8.3.1.2 Application of tool at regional level

This experience is based on a study in which Oikocredit collaborated with the Uruguayan Regional Centre and conducted a Social performance exercise. This pilot program was an opportunity for Oikocredit to assess various MFIs in Latin America, using the SPI tools developed by CERISE. "With the SPI assessments, in Bolivia, Brazil and Paraguay, Oikocredit exchanges with its partner MFIs in order to analyse to analyse and discuss their commitment to achieve a good social performance" (Oikocredit -2008).

Summary of key findings across various geographical locations

Figure 5

These diagrams show key results in Argentina and Bolivia



Source: Oikocredit 2008

- The area with lower score is the third dimension which assesses the action of the MFI to improve its client's social, political capital. The sub-dimension on CSR towards community is also low.

- Although institutions in Brazil and Argentina have reached a moderate social performance, gaps have been highlighted.

- The fourth dimension which assesses the social responsibility towards staff shows a good score

- Oikocredit noted that any low or moderate score in respect of the MFIs in Brazil and Argentina is attributed to the fact that MFIs in these regions are quite young, therefore still developing. On the other hand the good performance cited in MFIs in Bolivia is credited to the maturity of MFIs in this region.

8.3.1.3 General application of tool – on all four dimensions of Oikocredit's SPM

Summary of key findings across all four dimensions

Dimension 1 - Targeting MFIs most in need

The tool was able to show that Oikocredit has a large geographical exposure, hence their presence in numerous countries in Africa, and Asia and Latin America. Another important finding is the revelation that about 30 percent of Oikocredit's portfolio reaches MFIs serving clients who are at the bottom of the economic pyramid in their countries. To reassure the company that women client benefit most, the tools was able to show that among its MFI partners, on average, women constitutes 80 percent of total clients.

Dimension 2 - Adaptation of services to the needs of MFIs

An interesting finding here is the combination of loans with capacity building funds offered to clients. This clearly demonstrates the fact that while loans are important, their intervention alone cannot lift the poor out of poverty. A strong field involvement was also noticed, Oikocredit believes this is crucial for ensuring long-term partnership.

Dimension 3 - Capacity building of MFI

The results show increased participation in governance by MFIs, clients and other partners. This is manifested in the numerous cooperative and professional member-based organisations that Oikocredit support. In short this dimension shows that microfinance and their clients are now being involved in the decision-making process.

Dimension 4 - Demonstration of social responsibility to the microfinance sector

Oikocredit has an active member of various international initiatives including the client Protection Principles, CGAP, the Microfinance and Transparency campaign, to name but just a few. Furthermore the results in this dimension show that Oikocredit is able to maintain a close relation with its regional offices around the globe.

Table 5

8.3.1.4 ADVANTAGES OF OIKOCREDIT TOOL
It is adaptable to the variety of MFIs and their local contexts
It allows MIVs to evaluate their overall investment portfolio across diverse geography
They are based on data which is easily available and which can be easily checked by an external auditor
Comparison of results is possible
It provides systematic and qualitative information
Capacity to capture a wide range of information
Compatibility with MIX indicators of social performance
SPI system is available free of charge from CERISE

Source of content: CERISE

Table 6

8.3.1.5 Specific Short comings
The system is excel-based and requires a proficient excel user to handle data
Methodology can be costly, hence the cost of travelling to the field as well as the cost of external auditors.
The SPI-Invest is still being tested, so full capacity is to be determined

8.3.2 Analysis of the experiences of Incofin and Oikocredit

This case study epitomizes the tremendous efforts being channelled towards greater transparency and accountability in the way that funds are being used to help address the socio-economic problems that bedevil the lives of many poor people of the world. Although it is easy to see that we have a long way to go before reaching a better and improved methodology to assess the social benefits of microfinance, the twin endeavours of Oikocredit and Incofin and the support of CERISE represent an angle of comfort and optimism in this ongoing debate. Both social performance measurements systems are characterized with a degree of flexibility to ease integration with internal procedures, to feed into external database for benchmarking and to allow the incorporation of any future dimension and indicators. In fact this is why, both organizations managed to add the client Protection Principles to their existing dimensions with less difficulty.

Although the ECHOS of Incofin might be a small tool, it is capable of capturing and managing significant data across different investees from different countries just as the SPI-Investor tool. The obvious similarities between these tools stems from the fact that ECHOS gained its inspiration from the SPI, among other tools.

In both studies, Scale and Outreach represent the highest score while the Environment and Contribution to the Community represent the lowest score. The high score of the later can be attributed to the fact that MIVs are preoccupied by their growth strategy and trying to expand their level of clientele. The satisfactory scores on Customer Care and Human Resources clearly show the strong commitment that MFIs and MIVs place on these dimensions. Many MFIs have left this issue "to be dealt with later", believing their primary mission is to provide access to financial services (The experience of INCOFIN, David Dewez April, 2008).

My findings also revealed that companies are actively promoting the value of social performance within the industry. These activities are manifested in the form of road shows and workshops to offer cognitive skills to practitioners particularly MFIs. The idea behind this is to help practitioners not only embrace and implement social performance, but to successfully integrate it into their operations. Knowledge is also imparted with stakeholders through participating in industry dialogue by joining certain groups and schemes. Both tools were able to show clearly that Incofin and Oikocredit have signed to the Client Protection Principle, a global initiatives for the promotion and protection of client's rights and other important initiatives, thus adding a significant weight to their social performance overall rating. While it is good to join and participate in many industry initiatives, one must be cautious as keeping up with the pace of these initiatives may require both time and resources.

8.3.3 Concluding remarks of Case Study

After venturing into the experiences of Oikocredit and Incofins, it transpires that genuine and meaningful effort is being made towards standardization of social performance management. The initiatives of these organisations represent an embodiment of such effort. Another important development is that both Incofin and Oikocredit have successfully integrated social performance management into their internal procedures, demonstrating to other MIVs that this no more a daunting task. ***"I can confirm that we have already integrated our social performance management into our internal procedures. This is something we are very pleased with"*** (My interview with David Dewez, June 2010). As for Oikocredit, their commitment in pushing forward social performance to the forefront is clearly demonstrated by the company through creating a Department of Social Performance and Financial Analysis. ***"The creation of Social performance department and Financial Analysis has enabled Oikocredit to more easily set clear social objectives and monitor progress towards achieving those goals"*** (Ben Simmes, Deputy Managing Director, Jan 2010).

In spite of all these efforts, the industry should not be complacent. Instead, practitioners particularly MIVs and research institutions should team up to build upon existing initiatives. This cannot be done with "back to back approach". Therefore constant consultation and sharing of information should be the driving force of any future development. On a positive note, with the support of various institutions and initiatives such as SPTF, CERISE and CGAP, the quest to attain effective and standardized social performance management seems achievable.

It is important for the reader to note that the purpose of this study was not to compare and contrast Oikocredit and Incofin. The idea behind the conception of such methodology was to demonstrate that the problems of social performance may not be confronted alone. It requires holistic approach that can only be achieved through coordinating joint efforts as we have seen in the case of SPI-Investor initiatives.

The study also shows that the diverse nature of the structure of microfinance is not a hindrance to its success. In fact, if managed properly with the correct tools and expertise, MIVs based in Western Europe can zoom into their activities well beyond their territories to monitor, control and measure and most importantly, replicate successfully, initiatives across the countries of their partner MFIs.

9 Challenges facing MIVs

Various literature and industry leaders including investors, researchers hold that socially oriented investors are interested in microfinance's social impact, good image and relatively good return/risk profile. The low default rate of borrowers is also a much appreciated factor. At the same time, some problems and obstacles threaten increased investment in microfinance. The challenges identified here reflect the priority concerns and issues arising from the deliberations of the International Association of Microfinance Investors and other important bodies representing investors. Many of the challenges identified below are relevant to the holistic view of social performance. More broadly, I seek to relate these challenges to pressing questions that need urgent attention to ensure that the measuring and reporting of social performance is of great significance and relevant in this rapidly growing microfinance industry. Based on this context, this section seeks to convey only what I consider to be key challenges.

9.1 Reputation risk associated with lending to the poor threatens the sector

In view of the recent negative press surrounding microfinance, the well-earned reputation of the industry is threatened. There have been reports of sexual harassment and commitment of suicide, all linked to malicious collection practices. In India for example, the sexual harassment of female microfinance borrowers has been a problem in this part of the world. Press reports in the Indian State of Andhra Pradesh alleged that a wave of women's suicides was the result of microfinance institutions using "barbaric" recovery methods, including the physical and sexual harassment of the MFI's female clients by hired youths. (Bell and Clemenz – 2006, cited from Catherine S.M. Duggan 2009).

According to another report, it was not uncommon for field officers who are in charge of granting and collecting weekly payments or 'instalments' to resort to violence in collecting loans. Physical and sexual abuse were common" (Cons and Paprocki, 2008 cited from Catherine S.M. Duggan 2009). The IPO (Initial Public Offering) conducted by Compartamos Bank, Mexico, have raised various unanswered questions and does very little to enhance the industry's reputation.

These unsolicited practices, means that trust is now waning among various stakeholder groups including investors, civil society and microfinance clients. To that effect, in Uganda for example, there is some evidence that borrowers avoid taking microfinance loans for fear of abuse. In 2003, a focus-group study of Ugandan borrowers noted that respondents "were generally very scared of micro finance institutions' procedures on default," and that many avoided microfinance borrowing as a result (Catherine S.M. Duggan 2009).

In today's investment environment with increasingly ethically conscious investors, an MFI's success should take both its repayment rates and collection policies into account, particularly as relationships with international donors and organizations to provide something of a 'seal of approval' for borrowers. This is especially true for MIVs that use local partners to administer their loans, and often have relatively little idea about their partners' policies on collection. In an attempt to uphold the good name of microfinance and in view of the lack of strong market regulation, various scholarly literature point to the need for Investors and donors to take integral part in supervising microfinance institutions. This means that their social performance in place should take the need to protect clients seriously. To this end, a noticeable progress has been the introduction of the client protection principles which are being endorsed by many MIVs and MFIs.

9.2 Non-standardised social performance metrics and Disparity in social performance metrics

Currently, social indicators are being applied quite unevenly; many MFIs and microfinance investment vehicles (MIVs) have no process in place. Some MFIs networks have implemented proprietary or third party social performance measurement tools, some MIVs measure social performance using array of basic to comprehensive metrics, and many donors are funding various initiatives to define and implement indicators in partner MFIs (IAMFI). In order to ensure long term sustainability of the microfinance industry and to develop best practices a standardized approach must be developed. There is already a good start on this as some MIVs are now reporting both their financial and social activities into the MIX database. Lack of standardized indicators can sometimes inhibit funding from investors since they will not be able to make informed investment decision.

9.3 Complex and qualitative metrics can cause shift from financial performance

While there is a common stand for the need for MIVs to report their social performance of their investment portfolio, there has been consensus amongst stakeholders, particularly investors, to lower administrative burdens stemming from using complicated social performance metrics.

Variable opinions have been noted in respect of using complex social performance metrics. Some group of investors have voiced concerns that some of the more complex and qualitative metrics will overburden MFI and investors, divert attention from financial management, and add complexity in tools and information management, thereby increasing operating costs. Other stakeholders (investors) hold that social metrics unnecessarily distract management and that scarce resources are better spent on product development, client outreach and loan portfolio administration (IAMFI). This point is simply a re-iteration that MIVs social performance cannot be meaningful and comprehensive unless it fairly integrate the variable opinions of all those who have vested interest in it.

9.4 Selection of relevant indicators out of a large pool

Given the large pool of indicators designed to measure the social performance of MFIs, Microfinance Investment Vehicles face a very difficult task of selecting what might be and might not be suitable for them. The problem is exacerbated because most of these tools are not designed for direct applications by MIVs. According to CGAP, the challenge is to select indicators that are simple and low cost, yet, at the same time, sufficiently robust and globally applicable (CGAP-2007). Although most of the indicators available today are specifically designed to meet the needs of MFIs, MIV may still find some of these indicators useful. MIVs may want to roll out their social performance programme by starting at the micro level. That is measuring the social performance of their partner MFIs, before proceeding to the second phase (macro level) i.e. looking at their own social performance. In either case they should consider gathering data readily available and sufficiently representative of their overall portfolio. At this early stage of gathering information MIVs may want to know how to collaborate with their partners in obtaining data with the possibility of offering them support to fetch the requested data.

Jumping too quickly to selecting and implementing social performance indicators, without thinking through your specific information needs, will cost more time and money in the long run. ***"When starting out, we recommend that you identify just a few critical information gaps to focus on: those that are essential to understanding your social performance"*** (Anita Campion & Chris Linder and Katherine E. Knotts-Imp-Act Consortium 2008). More light is shed on this in my "recommendation section".

9.5 Fungibility and additionality

Money is fungible and borrowed funds can be used for many purposes so it is difficult to determine how funds were actually used and what benefits were realised (Thomas Dichter and Malcolm Harper, 2007). For example part of a loan can be used by a borrower to pay for the school fees of their children or even to pay for a health bill instead of investing it in a business as previously foreseen. Social performance indicators do not always take these kinds of situations into considerations thereby producing bias results at the end. This kind of situation is a reminder of the need to address poverty with holistic approach. For example where viable, MIVs and their partner MFIs may consider offering complementary products such as micro insurance to mitigate problems resulting from a failed harvests or ill health.

9.6 Contrasting mission of MFIs and diversity and in the services that MFI provide

MIV and their partner MFIs differ in the services offered. Some are minimalist and only supply with limited orientation to borrowers on matters such as disbursement and repayment procedures. Others provide obligatory or voluntary savings services. Some lend for any purpose while others attempt to direct loan to product purposes (Thomas Dichter and Malcolm Harper 2007). For example ResponsAbility Social Investments AG focuses on small businesses and independent media (among other activities) while other companies focus on rural development. These contrasting missions means that clients receive different treatments, thereby making any benchmarking of organisations very difficult, also many social performance metrics do not always take these variable features into considerations.

9.7 Collecting and analysing the data

Collecting and analysing data can be a very a demanding task. Where MIVs staff are deployed to collect data from MFIs in the field, data is expected to be of high quality. Unfortunately these expectations are not always met. One proponent highlights a major concern: Apart from having a limited time to collect data, MFI staff may introduce distortion to the results because they may have a vested interest in reporting favourable impact. Their clients may also want to please them by giving them desired responses, thereby skewing the results (Thomas Dichter and Malcolm Harper 2007).

To minimise such problems, it is paramount that partner MFIs are involved in the social performance process at the very beginning of the implementation process. A communication process characterised by" top-down" and "bottom-up" should be established, allowing the MIV, MFI and the client to raise and address their concerns. This process can be very effective in the long run as stakeholder involvement revolves around a strong pillar of trust and understanding.

9.8 Geographical constellation of MIV partners and activities

The wide array of MIV partners and activities spread across different countries, continent, countries, regions and sectors can be very problematic. Such diverse features are often associated with the following problems which are often in the centre of blame if anything goes wrong.

- Contrasting administrative frameworks and political systems
- Different regulatory and legal settings
- Variable professional practices
- Multi-lingual and cultural environment

Therefore, in order for MIVs to pursue their business interest successfully, their strategy should consider all these different circumstances. While this task remains complex it can also slow down process of co-ordination, service delivery and social performance monitoring. Such processes can be very time-consuming because the pattern of decision making is not universal. For example what might be appropriate and accepted in one country or region might be contested and often rejected in another.

In a world often characterised by growing corruption, embezzlement of funds, nepotism and bribery, immature rule of law, bureaucratisation of certain procedures, operating in developing countries can remain highly challenging.

On the other hand, if these circumstances are well managed it can yield positive experience through spreading and showcasing good practices. Such practices are manifested in the added value of networking, learning and sharing experiences and the tendency to develop future benefits.

CHAPTER 5

10 Recommendations

The recommendations aim at LMDF and similar MIVs considering the implementation of social performance management. The recommendation section is divided into four sub-sections: First, the proposed assessment tools and indicators based on the tools that I have analysed. The second part deals with the approach of ResponsAbility Social Investments AG which I believe best reflects the tools and set of indicators proposed to LMDF. The third section represents the conclusion of all these themes. The fourth section represents carefully selected suite of recommendations of which if followed, MIVs can implement social performance management successfully.

10.1 PROPOSED INDICATORS FOR NEWLY ESTABLISHED MIVS OR THOSE CONSIDERING THE IMPLEMENTATION OF SOCIAL PERFORMANCE MANAGEMENT.

The overwhelming majority of microfinance investors are motivated by social objectives and do not approach microfinance with a pure profit motive, but rather with the dual goal to foster social advancement among the marginalized while also obtaining a profit that may range from below-market to fully risk-adjusted returns (IAMFI 2008). One investor also asserts: ***"We do not invest into microfinance thinking that we would lose. Therefore, a reasonable investment return would be welcome. The microfinance debt repayment rate is very good and we hope that LMDF can replicate this in their investment portfolio" (Gregory Claudy May, 2010).*** Thanks to these kinds of perceptions, the evolution of the industry towards profit-driven and ethically conscious investors is on the increase.

After extensive research, the observation of media comments, as well as conducting interviews with both investors and practitioners, three areas of concern have been identified: Reputational risk (IAMF 2008), consumer exploitation and lack of transparency. Based on this context and in accordance with the MIX reporting standards, the following indicators are proposed to newly established MIVs and those considering implementing social performance management. I believe that it is only by adopting the proposed metrics, that MIVs can promote best practices, protect their customers, uphold the integrity of the industry, thereby contributing to the long-term sustainability of the industry.

The proposed indicators take four dimensions into consideration and characterised with a structure and format that comply with the MIX reporting standard. To keep the initial phase of social performance implementation simple and manageable, only a handful of indicators should be used to track these dimensions with the hope of extending them as the MIV grows. I believe that three dimensions reflect the aforementioned areas of concern and can surely put new MIVs in the social milieu. The underlying reasons for selecting each dimension are also explained:

1. Mission and Vision

With over 150 million clients worldwide and growing strong, microfinance is increasingly in the public eye. The enthusiasm has boosted capital flows, especially in recent years. The sector's dynamic growth has not been without pitfalls, however. There is a need for prudence, especially in today's financial context. It's time to go back to the basics: client proximity, simple and well-designed services, risk accountability and the double bottom line (CERISE SPI-Investor 2009). Adopting this dimension, MIVs should be able to rekindle connection with reputable past trajectories, and to understand and gain control of their mission.

Inspired by the SPI-Investor framework, this first section focuses on the investor's strategy and social mission as well as the vision of the different stakeholders. The below suite of questions represent sample of indicators designed to guide MIVs in pursuing their social performance goal. MIVs will need to reflect on their strategy occasionally as a pre-emptive measure to prevent inadvertent mission drift.

Table 7

Examples of Questions
What is your investment strategy and social mission?
What are your reasons for investing in Microfinance?
What kind of MFIs do you target?
What products do you offer?
How do you choose where to invest?
Do you have investment criteria to select MFI?
Do you have a policy for reinforcing the social performance of investees?
Is environmental impact a criteria for selecting MFIs?

Source: CERISE SPI-Investor

2. Access and outreach

When assessing an MIV, investors might want to analyse the MIVs underlying MFI partners in a given portfolio to familiarise themselves with key issues central to them. For example average loan size provided by the MFIs, how borrowed funds are being applied by the MFI's clients, (e.g. Agricultural production or entrepreneurship). The term "empowerment of women" is universally popular particular in the development agenda. As a result, investors might want to see a break down of loan portfolio in terms of gender. Many MFIs are already reporting on this. Some investors show particular interest in the geographical diversification of MFI market and for that matter might want to understand the breakdown of rural and urban borrowers in a given portfolio. Based on this context, chosen indicators should be able to measure the following concerns:

a. Depth of outreach
b. Accessibility of services
c. Flexibility and adaptability of products

Below are examples of indicators suitable for addressing these areas of concern:

Table 8

Indicator	Calculations	Source
Total number of borrowers (millions)	MFIs	MFIs' quarterly declarations
Average outstanding credit per borrower (USD)	Unweighted average of all credits per borrower across all MFIs	MFIs' quarterly declarations
Microfinance clients by gender	Percentage of MFI clients made up by men, women, and legal entities respectively (unweighted average across all MFIs)	MFIs' annual declarations
Microfinance clients by place of residence	Percentage of MFI clients living in urban and rural environments respectively (unweighted average across all MFIs)	MFIs' annual declarations

Source: ResponsAbilty Social Investment AG

3. Quality of Customer Service or Client Protection

As confirmed by IAMFI, many investors prefer the focus to be on consumer protection and responsible finance principles. Therefore in an attempt to address investors' key concern under this dimension, the following areas should be addressed:

- Transparency in product terms and conditions
- Transparency in interest rate policies and disclosure of full product costs (Annual Percentage Rate including all fees)
- Prevention of customer over-indebtedness
- Policies and procedures for customer grievance resolution
- Abusive collections practices

Table 9

Indicators	Calculations	Source
Average interest rate	The portfolio yield is taken as a proxy for interest rates charged by MFIs and simply averaged across all MFIs.	MFIs' annual declarations
Average outstanding credit per borrower (USD)	Unweighted average of all credits per borrower across all MFIs	MFIs' quarterly declarations

Source: ResponsAbilty Social Investment AG

4. Responsibility to the Community

This can be adopted through following the principles of corporate social responsibility. At their worse corporate social responsibility programmes may be a mere window dressing exercise. At best these initiatives represent genuine attempts by companies working with stakeholders to address the great environment, social and ethical challenges of our times (Transparency International, 2010).

MIVs should consider embracing such initiatives. It doesn't have to be big, it can be as small as buying Christmas gifts for a group of orphans or any vulnerable group in society. It doesn't also have to be taken place in the field- India or Africa. For example MIVs domiciled in Luxembourg can begin what would be an exemplary practice here in Luxembourg in the eyes of various investors and potential investors. The idea is to demonstrate and confirm the ethical values that should underpin an MIV's business module and to dismiss any myth that MIVs are money making machine at the expense of the poor. Among the MIVs who already have meaningful CSR are Oikocredit, ResponsAbility, Incofin and European Fund for South East Europe.

While reporting a company's social responsibility is voluntary in many countries, an emerging trend in corporate social responsibility has been the use of legislation by some countries. Denmark and France for instance, have adopted laws which mandate companies to include information on their social responsibility in their annual reports. In the United Kingdom, trustees of pension programmes must now disclose how they have taken into account corporate social responsibility issues in their decisions (Transparency International January, 2010). Therefore, indicators chosen should be able to address most of these recent and urgent claims by demonstrating MIVs' efforts to invest responsibly.

Example of indicators that Investors might consider:[12]

a. Adaptation to local culture, traditions and values (Cerise)
b. Number of CSR programmes
c. Geography of CSR programmes
d. Linkages with other businesses, NGOs etc

10.2 Social Performance Management of ResponsAbility Social Investments AG[13]

An approach to emulate

After having identified the aforementioned dimensions and giving examples of pertinent indicators to match with, I am inclined to propose to newly established MIVs like LMDF to consider embracing and emulating the indicators of ResponsAbility Social Investments AG, a Swiss based social investment company that uphold the maxim that private and institutional investors can contribute to positive social development and at the same time aim for a financial return in a professional manner.

ResponsAbility Social Investments AG is one of the world's leading providers of social investments. At the end of December 2009, the volume of the social investments managed by ResponsAbility across all investment themes stood at around USD 900 million, an increase of 27 % year-on-year. ResponsAbility is present in 60 developing and transition countries via its financing activities that span across many countries and regions including Latin America, Eastern Europe, and Central Asia. Through its investment products, ResponsAbility enables people in developing countries and emerging markets to have access to markets, information and other services important for their development in areas such as microfinance, SME financing, fair trade, and independent media (ResponsAbility, 2009).

Like other industry trendsetters, ResponsAbility has developed their own social performance tool: The ResponsAbility Development Effectiveness Rating (rADER). They use rADER to assess the development relevance of what an MFI does, by asking – among other things –

[12] CERISE SPI
[13] Most of this data is obtained from the annual Social Performance Report of ResponsAbility-2009. CERISE is also an important source of information.

whether it is focused on poorer groups of clients, what proportion of clients in rural areas it serves, and how it goes about checking to see whether clients may be overindebted.

rADER covers 19 indicators in five categories (ResponsAbility, 2009 report).

1. Mission and objectives: Alignment of MFI's mission and strategy to the social dimension; use of analytical systems to capture level of poverty among clients

2. Products and services: Variety of financial products and services offered; fair pricing

3. Operational systems and processes: Appropriateness of Internal systems and workflows in terms of enabling responsible management of employees, clients and the Environment

4. Access to financial services: Number and type of microenterprises reached; access to savings facilities

5. Contribution to local economic development: Level of Poverty in the country; economic sectors financed; proportion of rural population and women in MFI's clientele

Although ResponsAbility will report on rADER's results for the first time in the Social Performance Report of 2010 (ResponsAbility, 2009 report), I find their current indicators and methodology highly adoptive and relevant to any MIV on the verge of implementing such programmes particularly newcomers. My reasons for this proposal are detailed below:

10.2.1 Cost-effective methodology

Some social performance management methodologies require designated investment officer to visit the partner MFIs and collect data during their visit. While this method can be beneficial in terms of producing rich and quality data as well as reinforcing understanding between MIV and MFI officials, it can be very expensive hence travelling and lodging cost among other expenses.

Having examined their sources of data, it transpires that the Swiss based company, ResponsAbility obtains most of their social performance data from existing MIS such as MFIs quarterly and annual declarations. Whilst it might be expensive to put in place such system, once implemented, data will become easily accessible, thereby trimming down cost significantly.

10.2.2 Highly desirable reporting format that guarantees clarity, thoroughness and simplicity

Disparities in reporting styles and formats characterise the microfinance industry. Arguably most institutions use narrative reporting style while others use tabular reporting method. The former (narrative style) is often criticized for creating a greater volume of reporting and makes it difficult to ascertain whether all relevant information has been disclosed (Transparency International, 2008). Therefore when establishing a reporting template, it is important to consider one through which the information can be imparted to stakeholders in the most efficient and effective manner. One way of doing this is by using a tabular approach ideal for combining both brevity and clarity, thereby increasing transparency and at the same time making the message disclosed in a more user-friendly for all stakeholders. ResponsAbility offers exemplary practice in this direction by combining tables, charts and succinct explanatory notes. Where necessary, client stories or case studies are added for complementary purpose, but in their briefest forms.

10.2.3 Quantitatively measurable indicators with less complicated calculations

Researchers usually use two types of investigation processes. First is quantitative research, which employs numerical indicators to ascertain the relative size of a particular communication phenomenon. The second type of investigation process is qualitative research, which employs symbols and words to indicate the presence or absence of phenomena or categorize them into different types (Matveev Alexei 2002). While responsibility recognizes the fact that both methods can be mutually reinforcing, their social performance reporting focuses on quantitatively measurable indicators (ResponsAbility, 2009).

In order to reflect their large geographical spread and to ensure a greater level of detail, Information disclosed in charts and tables is usually aggregated by country, region, social groups and overall investment portfolio applying rigorous and yet simple statistical calculations/formulae. As one scholar asserts, this type of approach is crucial to eliminating or minimizing subjectivity of judgment (Kealey & Protheroe, 1996 cited from Matveev Alexei 2002). Since impact of microfinance is plagued by its subjective judgement and normative underpinning, focusing on quantitatively measurable indicators can help minimise potential bias thereby increasing reliability of gathered data paramount for decision making. It also makes cross-checking of information by an independent body less complicated.

10.3 Conclusion

Building social performance initiatives that address investor and public concerns requires MIVs to communicate and be more transparent about their efforts with all stakeholders. This is something the industry is very good at doing. The launch of ECHOS of Incofin, the recent introduction of rADER of ResponsAbility represents interesting initiatives for the social investment sector. In that it characterises a new trend of in-house tools to address the diverse array of MIVs' objectives. These developments clearly point to the needs for individual MIVs to design their own tools tailored to their specific objectives rather than using off-the shelf tools. On the other hand, the development of the SPI-Investor tool, a joint initiative of Cerise and Oikocredit demonstrates the importance of a collaborative approach between investors and the academic community using research programs.

In view of the growing trend in Corporate Social Responsibility, it is vital for new MIVs and their partner MFIs abroad to seriously start considering it now. It is better to embrace it now and gain experience from it while it is still voluntary. Amongst the benefits of corporate social responsibility is that it helps to minimise corruption, a practice that bedevils many communities in the developing world.

While monitoring against some indicators can be undertaken by direct observation of the MIVs' internal Management Information Systems (MIS) through quarterly and annual returns, a number of indicators, particularly those measuring client protection require direct feedback from clients and local communities. This can be undertaken through field surveys by investment officers or external agents. To ensure quality of data regarding indebtedness and bad recovery practices, it is important to seek engagement directly with microfinance clients. Such engagement should not only be directed to existing clients but also to client who already left the scheme or prospective clients. Quality data can be obtained from both groups as to why they have left the scheme or why they are hesitant to join.

Although basic indicators are suggested here, the relevance of these indicators, and others not presented, will vary between MIVs. The final selection of indicators should be determined in consultation with all pertinent departments starting with the social performance committee and externally with partner MFIs.

10.4 Selected Recommendations

In addition to the proposed indicators and best practices derived from the approach of ResponsAbility and other industry leaders, this section represent a carefully selected recommendations which if followed can help ease difficulties that MIVs may encounter when implementing social performance management.

10.4.1 Establish clear performance targets and a baseline

Those investors who measure socio-economic and environmental returns stress the importance of developing a "baseline" against which to measure net impact at the end of the investment period. The baseline is simply an assessment of the relevant performance indicators before the investment is made (Elizabeth Rhyne, 2009).

10.4.2 Concentrate on only a few simple performance indicators

Most of the literature I came across warn strictly about the danger of collecting too much of data and overloading both investees and their staff with extensive measurement task. As the performance measurement process becomes more burdensome, it inevitably becomes more costly, less timely, and more likely to fail altogether if processes are not kept to a minimum. Each indicator should be clearly defined, and a common format for their collection should be developed. Only information that can be easily gathered, tabulated and used to draw simple, meaningful conclusions should be used for social performance monitoring purposes Extraneous information and non-standard formats should be avoided (Rosenberg 2009; IFAD 2002a).

This view was echoed by Mr Gregory Claudy during my interview with him*: **"Collecting data can be a very expensive and time-consuming task. While social performance measurement is mandatory, it should be kept to minimal by using readily available or easily accessible data. It is also vital to develop a relationship, characterised by trust and transparency with partner MFIs. One way of achieving this is by conducting evaluation prior to investing"*** (My interview with Mr Gregory Claudy, May, 2010). I totally share this view as it clearly reflects the 'Know your client principle', an important guiding principle within mainstream banking, often applied when conducting due diligence.

10.4.3 Allocate sufficient resources to ensure ongoing management

Social performance management is not a one-off process. Instead, it should be embedded in the core strategy of MIVs and integrated in their regular internal procedures. Therefore an

MIV serious about performance measurement must allocate sufficient resources in terms of time, headcount (technical assistance or MIV's own human resources) and finance to ensure progressive management.

10.4.4 Report financial, socio-economic, and social/environmental benefits separately

It transpires that some MIVs are keeping these types of reporting separately. ResponsAbility of Switzerland reports its social performance separately. Oikocredit is another example of an MIV that have dedicated social performance report. While this is a good practice as it demonstrates a strong commitment, it is also a welcome practice.

10.4.5 Do not outsource your social performance management

It was revealed in one of my interviews with one MIV representative that it is imperative for MIVs to maintain at least some aspects of their social performance management internally instead of outsourcing everything. Among the MIVs tied to such good practice are Oikocredit, Incofin and ResponsAbility. In fact, these MIVs manage their social performance processes. I therefore recommend any MIV considering putting in place social performance management to show great responsibility.

10.4.6 Be a trend setter and not just a "trend sitter"

When I asked David Dewez of Incofin if he can share with me their major breakthrough in pushing social performance to the forefront, his answer was the creation of their very own social performance software, ECHOS. This innovative approach does not only give them an edge in an industry where those who can demonstrate their social values set to win the hearts and minds of socially conscious investors but also allows them to become part of a group that genuinely offers exemplary practices to emulate.

MIVs can be innovative in their social performance approach. There are various ways of doing this. For example, an MIV can choose to measure certain social or environmental dimensions ignored by the others. For example, some MIVs may wish to support MFIs in riskier tiers or territories instead of focusing only on less riskier ones.

10.4.7 Be daring and venturous

Given the required capacity and the necessary technical know-how, geographical diversification is undoubtedly a clever move for businesses to consider if they want to exploit unsaturated markets as well as new market niches in other parts of the world. Therefore venturing out in notoriously risky countries like Haiti may not only demonstrate an MIVs geographical outreach by trying to rich forgotten countries blight by political or geological vulnerability but also demonstrates their shrewd business strategy if the underlying risk is mitigated properly, thereby making such business venture fruitful. A social performance dimension that shows the support of MFIs in Haiti or Darfur in Sudan will certainly carry a heavy weight crucial in contributing to the overall results of an MIV's rating when it comes to outreach.

10.5 How to start the implementation process[14]

10.5.1 A proposed methodology - a practical guide for action

1) The research team and/or social performance committee to team up and agree on sets of social performance dimensions and indicators. Interdepartmental consultation might be necessary to ensure general consensus.

2) To send letter to partner MFIs to gather their reactions. This letter should clearly articulate the reason for embarking on such a project and most importantly the benefits that can be derived from implementing effective social performance measurement and reporting. MFIs managers should be asked to comment on each of the dimensions, sub-dimensions, and indicators in terms of relevancy, data availability and accessibility and general practicality.

3) The introductory letter would yield better feedback if it contains the following questionnaire:

a. From a general point of view, do you think this framework is relevant? Can it be useful for your organisation?

b. Would you have incentive to use this framework?

c. Would you have the time and information to fill in the necessary questionnaire (a sample questionnaire might be attached at this stage?)

d. Indicator by indicator, how would you rate the relevance of each of them in terms of availability of the information, reliability, and quality for measuring social performance?

e. Would you suggest alternative or additional indicators?

4) Allow at least one month to receive feedback from partner MFIs

[14] Most the information relating to the implementation process is obtained from CERISE - Manfred Zeller, Cécile Lapenu Martin Greeley -2003

5) Upon receipt of the feedback from partner MFIs, the research team would collaborate with the internal Social Performance Committee to assess the opportunities and any constraints for developing a cost effective and reliable of assessment of social performance of its partner MFIs

6) The committee and the research team to produce a summary report of the proposed dimension and indicators.

7) The final stage in this process is to organise field-testing. This can be conducted by a member of the research team or an Investment Officer by means of a visit to the partner MFIs.

11 CONCLUSION OF STUDY

While MIVs have common mission to take crucial role of lifting the poor people out of poverty, they are all different in terms of operational structure, market segments and geographical outreach. These varying features make it very difficult for the industry to reach a common approach towards measuring, monitoring and managing social performance. However, in recent years, the microfinance industry is preoccupied trying to perfect and standardize effective tools for measuring social performances. While there are still numerous challenges ahead, significant progress has been achieved in this endeavour. This is manifested more at MFI level, hence the countless social performance tools that are now available for practitioners to pick and choose from.

These positive results demonstrate that there is an efficient structure within the microfinance industry where different stakeholders groups can work together successfully to achieve their varying goals. The experience gained at micro level (microfinance Institutions) so far will not go in vain; it can be used as a catalyst to address the social performance of MIVs.

Most of the literature I came across firmly emphasise the urgency of developing more appropriate tools for MIVs in respond to increasing call from investors for transparency. As an ever-increasing number and diversity of governments, funders, and institutions with various motivations become interested in microfinance, it is more urgent than ever to have more transparency on social performance (CGAP 2007). Such transparency will not necessarily force everyone into having the same social objectives, but will ensure that all actors are accountable for what they promise to investors among other stakeholders.

Although being transparent to investors is crucial, one must understand that investors' perception cannot be changed over night. Certain groups of socially conscious investors may always wish to continue with their investment activities irrespective of changes in market or social conditions. However, this may prove to the contrary for profit oriented investors whose goal is for profit maximization.

As clarified by Kramer and Cooch, the extent to which people care about certain issues is what motivates them to invest. Some investors put great emphasis on the financial return, others on another aspect of social or environmental impact. Therefore even if every aspect of social impact could be quantified, each component would have to be weighted differently for different investors. It is extremely difficult to quantify or monetize many social and environmental impacts; and even if a formula for valuing these impacts is developed, the methodology is likely to be complex, tied to subjective assumptions, and therefore open to questions (Mark Kramer and Sarah Cooch, 2006). These assertions suggest that MIVs should keep social reporting minimal, relevant and realistic. By doing so, both MIVs and MFIs can allocate fairly their resources and time to other issues deemed necessary in the quest to satisfy shareholder interest.

Credibility of information is a key towards achieving a satisfactory social performance reporting. Therefore a modest measurement, based on few assumptions and an ironclad methodology, is likely to carry more weight than the claim of a larger impact supported by complex or unstated assumptions (Mark Kramer and Sarah Cooch, 2006).The more visible the results, the more likely funders are to learn from successes and failures, and to take corrective actions when needed. Clarity of goal at the onset is a key to successful implementation of social performance reporting. Therefore MIVs should decide from the beginning what exactly they want to accomplish and what to measure. While such a task might be shouldered by the internal social performance committee of the organization, it is important to involve all the departments of the MIV in order to ensure successful integration of the new social performance procedures and processes with the existing ones in other departments.

One social performance advocate suggests that social and financial performance may never share equal footings and each should be valued separately, using conventional quantitative measures for financial performance and the combination of both qualitative and quantitative measures for social and environmental benefits. If this assertion holds firmly, qualitative reporting through documenting and reporting client stories for Microfinance institution’s annual reporting will continue to be an important part of social performance reporting.

The concept of social performance is still in its earliest stages, thus we are yet to see more and more new methodologies. While some might be different, most of them are expected to be similar in practice since they share common source of inspiration, notable the SPI tools of Cerise and CGAP-Grameen-Ford Progress out of Poverty Index. This development process need to be accompanied with a periodic review/study, similar to this one, as information relating to progress will always need to be collected to show the current state of practice, to inform and reassure new entrants to this field whether they are practitioners or investors.

Dissemination of project results or any relevant information can help bring successful outcomes to the doorstep of industry practitioners, and most importantly it can pave the way towards standardization. Improvements in social performance measurement and reporting will become necessary, and ultimately more standardized, especially in anticipation that social investors will become more educated and will no longer take for granted the positive development impact of micro credit (European Fund of Southeast Europe, 2009).

Behind the enigmatic concept of social performance lies the idea that with so many good ideas in the industry there is no need to reinvent the wheel. By working together and sharing experience, surely the entire microfinance community can embrace, nurture and integrate social performance in their core internal procedures more quickly. Therefore if carried out efficiently and effectively, dissemination of results, can bring not only challenges encountered by a certain group of MIVs to the attention of others within the industry, but also the type of approaches that have been adopted to deal with them.

I believe that the ethical promise that underpins the social performance of MIVs cannot be fully realised without the commitment of MIVs to closely collaborate with their partner MFIs to eschew malicious practices of certain loan officers in the field. Although the reputation of microfinance may not be subverted because of the repugnant behaviour of a tiny group of so called practitioners, it can cast a shadow of concern over its credibility in the long-run, as those who genuinely care for the poor will start to raise awkward questions.

In an attempt to address these unwelcome practices that take place miles away from the MIVs' head offices, the industry should consider creating a watchdog committee entrusted with the sole responsibility of addressing such malicious practices. The industry should commit the watchdog committee to publish full information on such practices as well as measures taken to deal with them. The proposed watchdog is achievable and can be situated well within the framework of the Client Protection Principles. Since MIVs hold significant stake in their partner MFIs, they can use this influential position as a muscle to not only penalise MFIs accused of such heinous act but also help prevent it from occurring in the first place.

Although the growth of microfinance shows no sign of abating despite the current global economic crises, however, an important cautionary note is that the vagary nature of the economic conditions in the developing world makes the vulnerability of microfinance unparalleled to any industry. Failed harvests due to drought, natural and man made disasters, widespread corruption practices are all too familiar. Therefore it is paramount for MIVs to take all these factors on board when considering venturing abroad. Operating successfully under these kinds of circumstances requires a strong business acumen that is deeply rooted in a pre-emptive risk strategy capable of mitigating different eventualities. Information relating to the social and financial performance of their partner MFIs abroad is central to such strategy.

MIVs with partners in countries where corruption is rampant must be careful in the way they advocate their ethical policies. While considering local conditions, they should always maintain their original values of integrity and assist their partners to adapt gradually to their company's cultural settings and core mission. On the other hand, an important lesson for many MFIs in the field is that they should not take advantage of their weak local, political, legal and socio-economic situations to conceal all the values associated with transparency. To this end, I point to the need for extending the feedback loop to the microfinance institutions in the field and their clients through seminars and workshops.

Social performance management is more than the indicators or information technology you use. It's about how you use the available tools and information to effect change throughout your organisation, operations and staff, and how those changes translate your social mission into practice (Anita Campion, Chris Linder and Katherine E. Knotts, 2008). Furthermore, poverty manifests itself in different forms, thus making it very difficult to measure with tools and systems. While such devices are useful and can play an important role towards documenting and reporting the effectiveness of poverty alleviation measures, they cannot be compared with the emotion and empathy that should guide practitioners to understand the daily plight of poverty.

The increasing commercialisation of microfinance comes with a very high social price tag, therefore causing a major concern to the industry and its reputation. Such concerns are illustrated by the Compartamos issue in Mexico. When this microfinance NGO became a private sector financial institution, its directors became multi-millionaires overnight. For many observers this was distasteful, as people who had negotiated public grants to establish an MFI, and who charged high rates of interest on loans to low-income people (under the banner of poverty reduction), converted the resources generated by grants and high charges into private fortunes (Thankom Arun and David Hulme 2008).

The over indebtedness is a major concern and can only be tackled at it its roots. If allowed to permeate in communities, it can seriously hinder development and mask any social performance. For example the developing world's chronic reliance on donor finances is a major contributor to various unsuccessful business ventures. Such funds often fall into the hands of either corrupt individuals or those who lack the necessary skills to utilise the funds in a sustainable way. A remedy to this fruitless approach of distribution of capital would be a comprehensive intervention packaged with relevant technical assistance for capacity building and training. For MIVs to make a difference in the lives of the poor, they should supply more than just a capital. Any breakthrough in this proposed approach will depend on their innovativeness and their willingness to learn from the experiences of donor organisation and other reputable microfinance practitioners.

11.1 Suggestion for further research

11.1.1 The spatial constellation of microfinance investment vehicle

The spatial constellation of Microfinance Investment Vehicle that spans across various international boundaries deserves more attention. The immense opportunities and constraints that characterise the structure of Microfinance Investment Vehicle should be examined in detail.

11.1.2 Feedback from microfinance clients

Despite the launch of the Client Protection Principles in recent years, there is barely a forum where microfinance clients (the underlying clients of MFIs) can participate in decisions that affect their livelihoods. An in-depth research into understanding clients' concerns and how these very clients can be drawn closer to the decision-making table can be beneficial to the industry. The study should look into how the views, ideas and experiences expressed by this vulnerable stakeholder group can be taken into consideration in the development of an MIV's strategy.

12 Appendix

Appendix 1

Social Performance Indicators of

ResponsAbility Social Investments AG, Switzerland

Microfinance

Indicator	Calculation	Source
Total number of borrowers (millions)	Total number of all borrowers across all MFIs	MFIs' quarterly declarations
Total number of savers (millions)	Total number of all savers across all MFIs	MFIs' annual declarations
Total outstanding MFI credit portfolio (USD millions)	Sum of outstanding credit portfolio across all MFIs	MFIs' quarterly declarations
Total client savings managed by MFIs (USD millions)	Sum of clients' savings across all MFIs	MFIs' annual declarations
Average outstanding credit per borrower (USD)	Unweighted average of all credits per borrower across all MFIs	MFIs' quarterly declarations
Average savings per saver (USD)	Unweighted average of all savings per saving account across all MFIs	MFIs' annual declarations
Microfinance clients by gender	Percentage of MFI clients made up by men, women, and legal entities respectively (unweighted average across all MFIs)	MFIs' annual declarations
Microfinance clients by place of residence	Percentage of MFI clients living in urban and rural environments respectively (unweighted average across all MFIs)	MFIs' annual declarations
Number of employees of MFIs	Number of employees across all MFIs	MFIs' annual declarations
Number of microfinance clients reached	Fraction of MFI's credit portfolio refinanced by responsAbility, multiplied by MFI's total number of borrowers (aggregated across all MFIs)	MFIs' quarterly declarations
Number of family members reached (millions)	Number of borrowers of an MFI multiplied by average number of people per household in country of investment	Extrapolation based on number of microfinance clients reached, demographic data supplied by World Bank and UNDP, and proprietary data
Scale of MFIs by gross loan portfolio	Institutional scale is measured by the size of an institution's loan portfolio in US dollars (USD). The measure of scale is regionalized to reflect differences in income levels across regions. Large: Africa, Asia, ECA, MENA: >8 million LAC: >15 million Medium: Africa, Asia, ECA, MENA: 2 million - 8 million LAC: 4 million - 15 million Small: Africa, Asia, ECA, MENA: <2 million LAC: <4 million	Classification as per MicroBanking Bulletin, MFIs' quarterly declarations
MFI's target clients	MFIs are split into four categories based on the average balance of loans served in relation to GNI per capita (Depth = average loan balance per borrower/GNI per capita). Low end: Depth <20% OR average loan size <USD 150 Broad: Depth between 20% and 149% High end: Depth between 150% and 250% Small business: Depth above 250%	Classification as per MicroBanking Bulletin, MFIs' quarterly declarations

Economic sectors financed	Credit portfolios are spread among the following sectors: agriculture, manufacturing/industrial production, commerce, services, other sectors. The percentage by volume is calculated.	Classification as per MicroBanking Bulletin, MFIs' quarterly declarations
Lending methodology	Credit portfolios are spread among following lending methodologies: individuals, small solidarity groups (up to 10 people), large solidarity groups/village banking (more than 10 people). The percentage by volume is calculated.	MFIs' annual declarations
Loan products	Credit portfolios are spread among the following loan products: micro/small enterprise loans, consumer loans, housing loans, other loan products.	MFIs' annual declarations
Average interest rate	The portfolio yield is taken as a proxy for interest rates charged by MFIs and simply averaged across all MFIs.	MFIs' annual declarations

SME Financing

Indicator	Calculation	Source
Indicators in development		

Fair Trade

Indicator	Calculation	Source
Total number of members of cooperatives	Sum of members of all cooperatives	Annual declaration
Number of farmers reached through rA investments	responsAbility investment as a percentage of cooperative's total sales, multiplied by number of cooperative members (aggregated across all cooperatives)	Annual declaration

Independent Media

Indicator	Calculation	Source
Media users reached in millions	Fraction of Media Development Loan Fund (MDLF) credits arranged by responsAbility, multiplied by number of media users reached through MDLF	Social Dashboard, MDLF. Annual Update

Appendix 2

Over the past several years, consensus has emerged that providers of financial services to low income clients should adhere to the following six core principles:

1. Avoidance of overindebtedness
2. Transparent pricing. The pricing, terms and conditions of financial products (including interest charges, insurance premiums and all fees) will be transparent and will be adequately disclosed in a form understandable to clients.
3. Appropriate collection practices. Debt-collection practices of providers will not be abusive or coercive.
4. Ethical staff behaviour. Staff of financial service providers will comply with high ethical standards in their interaction with microfinance clients, and such providers will ensure that adequate safeguards are in place to detect and correct corruption or mistreatment of clients.
5. Mechanisms for redress of grievances. Providers will have timely and responsive mechanisms in place for complaints and problem resolution for their clients.
6. Privacy of client data. The privacy of individual client data will be respected, and such data cannot be used for other purposes without the express permission of the client.

(Source: Cited from ACCION International 2008).

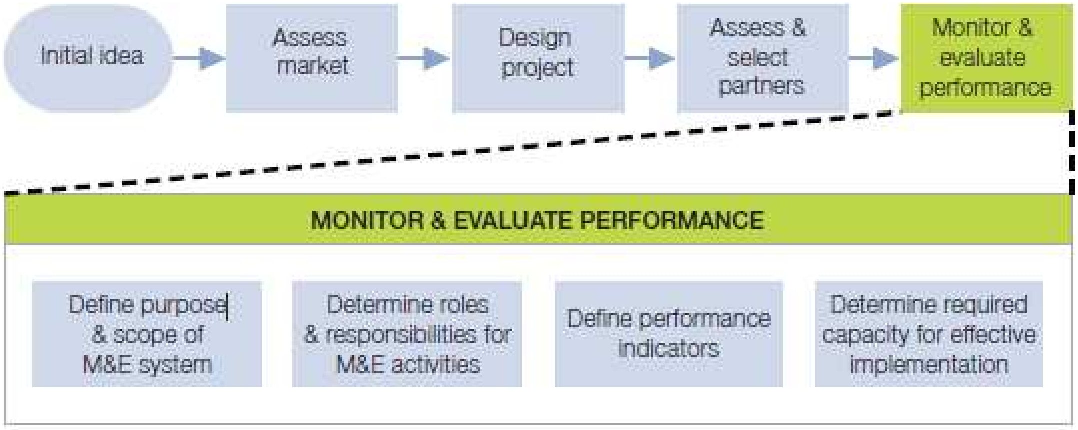
Appendix 3

Given the complexity of social performance management, it is advisable to approach such endeavour with some core beliefs embedded in the centre of the MIVs social strategy.

1.	Hear the constituent voice
2.	Exercise rigor within reason
3.	Assess not for assessment's sake
4.	Design assessment and strategy together
5.	Don't let assessment sit on a shelf
6.	Collaborate, don't dictate
7.	Build off and build up
8.	Borrow, don't reinvent
9.	Foster learning culture

Source: http://www.iamfi.com/documents/MaximizingREV.pdf

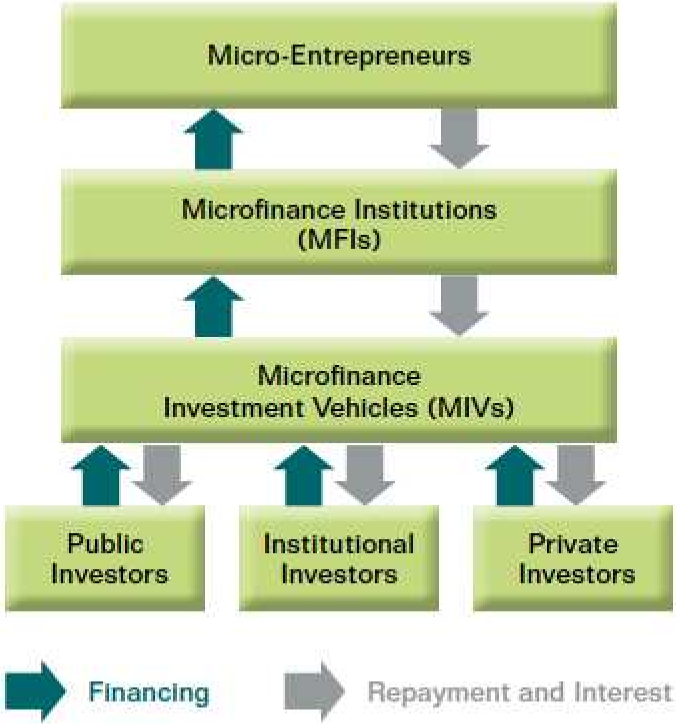
Appendix 4



Source: IFAD 2010

Appendix 5

Funding framework of MIV



Source: *ALFI, MicroRate and Symbiotics, December 2008.*

Appendix 6A

Name and position of Interviewees

- All interviews took place in Luxembourg between 04. 05.2010 & 30.06.2010

NAME	PLACE OF WORK	POSITION	TYPE OF Interview
Gregory CLAUDY	Bank of Fortuna, Luxembourg	Director	Formal - open ended
David DEWEZ	Incofin Investment Management	Senior Investment Manager	Formal - open ended

- Informal consultation (panel discussion) with ADA and LMDF staff to ensure better understanding of topic and expectations from an MIV's perspective.

Between February 2010 and June 2010

NAME	PLACE OF WORK	POSITION
Axel De Ville	ADA, Luxembourg	Executive Director
Ming-Yee Hsu	ADA, Luxembourg	Investment Officer
Marilene OBERLIN	ADA, Luxembourg	Programme Assistant
Quentin LECUYER	ADA, Luxembourg	Investment Officer
Kaspar WANSLEBEN	LMDF, Luxembourg	Executive Director

Appendix 6B

Interview Questionnaire – Targeting MIVs

Interviewer: Mustapha Choi, student at the University of Luxembourg

Subject: Social Performance Management of MIVs

1. Could you please introduce yourself and your organisation?
2. What does the term Social Performance mean to you?
3. What are your social performance objectives and how does your organisation seek to achieve them?
4. How do you communicate your social performance to stakeholders? Is this process satisfactory? If no, what measures are you taking to improve it?
5. Which stakeholder group is more important for you and why when it comes to Social performance? Please rank in order of importance:
   a. Investor
   b. The industry/public
   c. Client
6. How should MIVs promote their social performance to gain investor interest?
7. Could you please explain how Social Performance research/initiatives are being coordinated and disseminated within your organisation and between your partner MFIs. Do such initiatives interact with your other procedures particularly your financial performance procedures?
8. What would you say are the major achievements in respect of Social Performance for your organisation so far?
9. What Indicators do you currently use and why? Do you find them reliable and effective? How do they defer from others?
10. Is there any gap between these tools and public expectation? If any, what steps is your organisation taking to address such gaps?
11. Do you consult these indicators when making investment decisions? If yes, how instrumental are they in your decision making process?

12. What are the major challenges in the development, adoption and implementation of Indicators within your organisation?

13. Have you ever received any feedback from investors or any stakeholder group regarding your current Social Performance reporting? If yes, what kind of feedback and what did you learn from it?

14. What will happen in the future in respect of Social Performance concept development? Will it become standardised as financial performance? Can you detail any progress made by your organisation in an attempt to realise such undertaking?

Interview Questionnaire – Targeting Investors

Interviewer: Mustapha Choi, student at the University of Luxembourg

Subject: The Importance of Social Performance Management from Investors' perspective

1. Could you please introduce yourself and the organisation that your are representing?

2. What does the term Social Performance mean to you? How important is it for you why?

3. In order of importance, where would you exercise the concept of social performance in respect of the following stakeholder groups?

    - Investor
    - MIV
    - Client

4. Why did your institution invest in LMDF? How would you differentiate these types of funds with conventional ones?

5. Does your institution invest in similar funds with social objectives? If yes, did you receive a report on social performance and were you happy with it and why?

6. What benefits would your organisation obtain from Social Performance reporting?

7. Would you use such reports to determine any future investment and why?

8. Would you give any feedback to LMDF in future once their social performance reporting had been implemented?

9. How should MIVs promote their social performance to gain investor interest?

10. Is Social Performance monitoring important for you and why? If yes, what information would you consider satisfactory to determine if your investment will contribute to the socio-economic development of microfinance beneficiaries?

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