Social Rating and Social Performance Reporting in Microfinance

Towards a Common Framework

by

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for the

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Abbreviations and Acronyms

AMAP	Accelerated Microenterprise Advancement Project (of USAID)
CERISE	Comité d'Echanges, de Réflection et d'Information sur les Systèmes d'épargne-crédit
GRI	Global Reporting Initiative
M-CRIL	Micro-Credit Ratings International Ltd. (Gurgaon, India)
MDG	Millennium Development Goals
MFI	microfinance institution
MIS	management information system
MSE	micro- and small enterprises
PPP	purchasing power parity (basis for comparing income- and expenditure-linked poverty lines to reflect differentials in costs of living between and within countries)
SME	small and medium enterprises
SP	social performance
SPII	Social Performance Indicators Initiative
SPM	social performance management
SR	social responsibility

The following abbreviations are introduced in this report as a suggested notation for social performance reporting and rating:

GA	gender approach
MG	member governance in member-owned institutions
NFS	non-financial services
SG	social goal
SG-Or	social goal—outreach
SG-Sv	social goal—appropriate services
SG-Ch	social goal—change
SR-CL	social responsibility to clients
SR-Cm	social responsibility to community
SR-St	social responsibility to staff
SR-Env	social responsibility to the environment

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Preface and Acknowledgments

This paper arises from the work and shared experiences of different initiatives and agencies that over the past few years have directed attention to the social aspects of microfinance. Representatives from these initiatives sit on a sub-committee for social rating and reporting, appointed by the Social Performance Task Force. I was asked to act as sub-committee chair, representing M-CRIL (Micro-Credit Ratings International Ltd.), the first specialised microfinance rating agency to develop a tool for social rating. Others on the sub-committee represent the other three main specialised rating agencies: Micol Guarneri of Microfinanza, Emanuelle Javoy of Planet Rating, Sebastian von Stauffenberg of MicroRate; also Rekha Reddy of ACCION International, Anton Simanowitz of the *Imp*-Act Consortium, Cécile Lapenu of CERISE, Gary Woller of Chemonics, Allan Bussard of Integra, and Marc Berger of SIDI.

All members of the sub-committee contributed substantially to the content of this paper. Others, too, made significant contributions, especially Koenraad Verhagen of the Argidius Foundation and Geert Jan Schuite of Triodos/FACET BV.

The sub-committee was set up to see if a common framework could be drawn up, inspired by the different initiatives available, that was relevant to social reporting and rating, but adaptable enough to work with varying frameworks, foci, and methods. These initiatives are primarily the *Imp-Act* project for Social Performance Management, the CERISE Social Performance Indicators Initiative, USAID's Social Performance Tool, and M-CRIL's initial social rating tool.

Consultations have been mainly by e-mail, with presentations on behalf of the sub-committee at two meetings of the Social Performance Task Force during The SEEP Network's Annual Conference in Washington, DC, November 2005, and at International Fund for Agricultural Development (IFAD) in Rome, April 2006.

The main agencies for rating in microfinance are the specialised rating agencies that emerged independently and developed frameworks and tools for financial risk assessment. These agencies have gradually converged around objective indicators and agreed ratios—though the style of reporting or grading may differ. For social rating, assessment is challenging and, if anything, is more complex than financial rating. Because of this, we were asked to converge from the start—to agree on the scope and parameters of a social rating, the key indicators, and the assessment approach—and then to link social rating to an agreed framework for social reporting by MFIs.

This paper represents a 'work in progress'—as far as we have got. It represents an attempt to coordinate our different initiatives and perspectives. Much work remains to be done, but I hope that this is a fair representation of the experience so far, and that it provides a sound basis for developing further the transparent measurement of social performance in microfinance.

I thank the Argidius Foundation for supporting my involvement, with special thanks to Koenraad Verhagen for his encouragement and valuable perspective.

—Frances Sinha
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Social Rating and Social Performance Reporting in Microfinance

Toward a Common Framework

Executive Summary

This paper draws upon a number of on-going initiatives working on social performance to develop a common framework for social rating and an indicative list of dimensions and indicators for social performance reporting in microfinance. The framework follows the *Imp-Act* pathway that emphasizes social performance, not only as an end result (the 'impact'), but also as the steps to get there, including the social and development values widely associated with microfinance. It reflects the following definition of social performance:

The translation of mission into practice,
in line with accepted social values

The framework is divided into context, process, and results, with the key dimensions as follows (including a suggested notation as a counterpart to the notation now familiar in financial performance):

Context
• Country and regional development indicators (from secondary sources)
• Microfinance institution profile and financial services
Process: Policies and Strategies
• Social performance management **(SPM)**—mission clarity; alignment of systems
• Social responsibility—to clients **(SR-CL)**, including, where applicable, gender approach **(GA)**, member governance **(MG)**, non-financial services **(NFS)**
– to community **(SR-Cm)**;
– to staff **(SR-St)**; and
– to environment **(SR-Env)**, from lenders to small enterprises
Results: Achievement of Social Goals (SG)
• Outreach **(SG-Or):** Depth and breadth, may include hired (non-family) employment
• Financial services **(SG-Sv):** Variety, appropriateness, and transparency
• Change **(SG-Ch):** Outcomes and impact

SPM (social performance management) has reference to the mission and model of each MFI. The other dimensions assume generic social values, though specific indicators may be adjusted (or omitted) depending on the MFI model. For example, **MG** (member governance) is applicable to member-owned institutions; indirect indicators of outreach (for example, hired employment in credit-supported enterprises) are applicable to MFIs that do not focus on the poor, but aim to provide finance to micro- and small enterprises.

Within this framework, several indicators are already available from most MFIs (microfinance institutions), from their existing documents and portfolio databases. Very few MFIs, however, have client-level information on results. Portfolio information can be used to generate proxy (supply-side) indicators, but more robust information depends on client-level data. Such data may be collected as part of a social rating or by the MFI as part of its own **SPM** system.

The collection of such information represents a substantial investment of resources and in new skills, both for rating agencies and for MFIs. The justification for such an investment lies in the need to substantiate the double bottom line in microfinance, so that there is evidence for the claims (the 'hype') about microfinance, leading both to greater transparency and to constructive efforts to improve. But, the substantial investment may pay off through greater loyalty of clients (and even staff motivation).

Rating agencies are trying out different approaches (a 'thin' approach that uses proxy indicators and a more comprehensive collection of additional client-level information). If an MFI is collecting client-level information, this can then be validated ('audited') and used for social rating, reducing the need for a sample survey as part of the rating exercise.

The scoring and weighting options, which are a part of rating, are also being tested as more data are collected and can be benchmarked. The basic data can be presented so that different users may apply their own weights. Weighting will have to take into account not only the relative significance of a particular dimension but the robustness of the information collected. If a higher weight is given to results, this is an argument for investing in client-level information.

The framework and the list of indicators currently being considered for social rating provides a foundation for selecting a set of key indicators for social reporting that may be used by MFIs in their annual reports (complementing the financial information and accounts already being presented), and to fill in the blanks for social performance in the Microfinance Information eXchange (MIX) Market.

Further consultation and experimentation will be required within the microfinance sector, and will involve different stakeholders—MFIs (different models and regions), investors, raters, donors, the MIX Market—to select the core indicators for social reporting, with appropriate and clear definitions.

The task is analogous to the process that established the parameters and indicators for financial reporting. These must have seemed, early on, relatively complex and difficult. Financial indicators are now established and accepted as 'basic' and straightforward, and are integrated within information systems and reporting. However, their acceptance has taken several years with adjustments to MFI data systems to enable systematic and robust monitoring. The same may apply to social reporting.

Objectives and Scope

The aim of this assignment was to develop a systematic format for social rating and social performance reporting in microfinance which:

- covers key elements of social performance (**SP**), with clearly defined terms and indicators;
- reflects certain accepted development values as well as the specific social mission of an MFI;
- can be adapted to different contexts and organisational models of microfinance;
- is obtainable in terms of requiring a 'reasonable' amount of resources (time and effort);
- is applicable for both internal self-assessment (by an MFI) and external reporting (with external validation or auditing); and
- facilitates benchmarking of social performance across MFIs and across countries.

The assignment has involved consultations among the different specialised rating agencies (especially M-CRIL, Microfinanza, and Planet Rating) and with other related organisations or initiatives, in particular the *Imp-Act Consortium*, CERISE (Social Performance Indicators Initiative), ACCION, USAID (Social Performance Assessment Tool), the Triodos Bank/Global Reporting Initiative project (Transparency in Sustainability and Finance), and the Grameen Foundation ('Progress out of Poverty Index').

This report draws on these consultations and the experience so far to present a common framework for social rating and social performance reporting. This common framework sets out the key dimensions of social performance and the indicators that are relevant to each dimension. The framework for **SP** reporting by the MFI and **SP** rating by an external agency is the same, though a rating is likely to cover a larger number of indicators. The different initiatives agree on the key dimensions, but there is some divergence on which indicators to apply. Nevertheless, it has been possible to draw up a complete list of indicators from which core indicators may be selected for social reporting by MFIs. An indicative 'short' list is presented here.

Context—Understanding 'Social Performance'

Initial Focus on Financial Performance

The power of the microfinance ideal lies in its potential to combine financial sustainability with meeting social goals, achieving the 'double bottom line' of financial and social performance. Until recently, however, the main emphasis of training, research, and reporting has been on financial performance. Perhaps this was not surprising, given that microfinance was introduced mainly within development organisations ('welfare' organisations, such as NGOs and societies), which were now being encouraged to be more 'business-like' so they could access investment funds rather than continue being dependent upon donor grants. This brought in new dimensions of accounting, management, and reporting which, over several years, led to the establishment of standard definitions and terms for reporting on financial performance. These are now almost routinely included in the annual reports of MFIs; nearly 700 MFIs report them to the Microfinance Information eXchange (the MIX).[1] Specialised rating agencies apply these indicators to the credit ratings of MFIs.

What happened to social performance? MFIs include social goals in their mission statement, but few report on their achievement. Part of the reason for this disinclination lies in the conception of social performance primarily in terms of impact. Impact, technically, is defined as 'change that can be attributed to the intervention'. As such, impact assessment requires very careful research and involves substantial resources and time and quite complex analysis (which is not disputed). It is not surprising, then, that this sort of research and reporting was left to the specialists, while the microfinance sector concentrated on more practical tasks.

Unpacking the Concept of 'Social Performance'

Some important new initiatives, however, have explored social aspects with a new definition of social performance that includes impact as the end-goal, but specifically unpacks the steps and practices taken to get there. The focus shifts from proving an end result to managing and reporting on those steps that are likely to lead to positive social outcomes. Social performance is seen not only as a result but as the process of achieving that result—and this can be reported on.

The two main initiatives behind this shift are the *Imp-Act* program and the CERISE Social Performance Indicators Initiative (SPII). The *Imp-Act* program set out to establish what MFIs could do to improve (and prove) their impact. Social performance

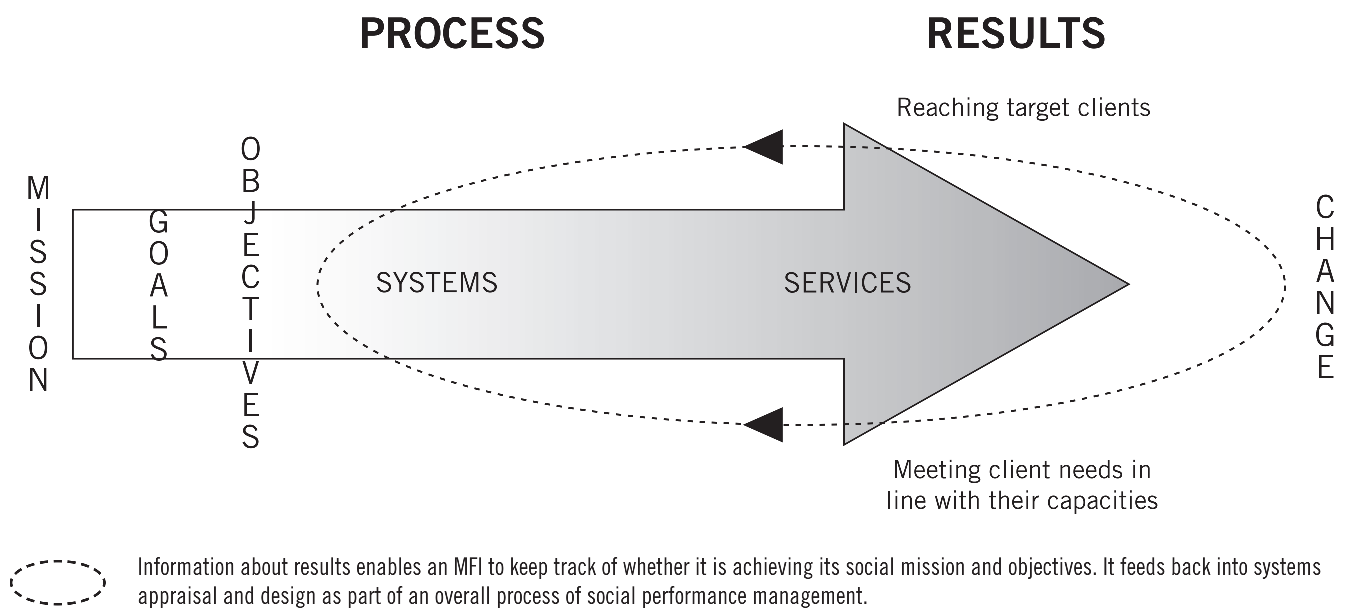
1. The MIX Market is the global microfinance information marketplace, providing financial data and profiles on microfinance institutions and the microfinance sector on the Internet, at http://www.themix.org.

was defined as *the effective translation of an institution's mission into practice*. This definition emphasizes that social performance is not only the end result (the impact) but a deliberate process of getting there. It reflects the concept of an impact *pathway*_ (derived from the conceptual framework for impact assessment research), anchored in mission and leading to change, but contains several steps to work through so as to achieve change systematically (i.e., 'put into practice').

The impact pathway can be represented as an arrow, with the main shaft representing the MFI's governance, management, and strategic systems—the process; the arrow head represents the results: reaching target clients, meeting clients' needs in line with their capacities, and ultimately achieving impact (see figure 1). The arrow points in one direction, but there is an iterative flow of information about the results (represented by the dotted line in the figure) feeding back into decision making. This enables an MFI to keep track of whether it is achieving its social mission and objectives, and contributes to an overall process of social performance management.

The CERISE approach adopts the same MFI-centered definition of social performance, but adds objective concepts of social value (improving the lives of poor and excluded clients and their families and widening the range of opportunities for communities) and social responsibility (to clients, communities, staff). These may not be explicitly spelled out in an MFI's objectives, but are assumed to be implicit and to have broad applicability, whatever the MFI's stated goals.

Figure 1: **The Imp-Act Pathway**



Source: Adapted from *Imp-Act* Guidelines, http://www.ids.ac.uk/impact/publications/guidelines/Guidelines_Text.pdf

Whose Values?

One of the biggest challenges for social rating and reporting is whether it is possible to agree on certain generic values that apply to all MFIs, to enable direct comparison and 'benchmarking' across different contexts and models. Rating necessarily implies that there are certain standards or values that provide the benchmarks against which to assess an organisation. In credit rating, measurements and ratios for efficiency and sustainability have become clear; indicators for good governance, management systems, and control have also developed as information about them has been collected. These standards apply whatever the mission of an MFI. Whether explicit or not, most MFIs do aim to be efficient and sustainable, and it is now accepted as reasonable to assume so, whether or not this is clearly spelled out by the MFI.

In contrast to the application of uniform financial objectives, some would argue that social issues are too complex and too varied ('every MFI is different') to allow generic social values to emerge and be valid. In this view, each MFI is a unique organisation with its own specific objectives, model, institutional structure, and environment and should therefore be assessed primarily in terms of its own stated objectives. There are MFIs that target women and those that work with men, MFIs that target the poor and those that target the larger population excluded from formal financial services (of which 'the poor', however defined, are a sub-set), and MFIs that apply a group model based on social collateral and those that apply an individual model—and some that do both. Some MFIs have a cooperative institutional structure in which client representation in governance is a core element, but this may not be an issue in other organisational forms; some MFIs offer a range of financial services, some are prohibited by law from offering savings. The list can go on.

This, then, is the challenge. If reporting only reflects each MFI's specific circumstances, then comparability and benchmarking are ruled out, and both rating and common reporting are non-starters. Rating and reporting, if they are to be undertaken at all, have to involve some comparability and 'generic' value, but at the same time, they have to take into account an MFIs' specific circumstances and choices, otherwise they are not valid.[2] The framework presented in the following section shows a way to balance both.

A Common Framework

Reporting on social performance is not just about measuring the results but is also about the systems in place, and the actions and corrective measures that are taken to bring about those results. Social rating and reporting must therefore look at both—both process and results—a feature which mirrors the working hypothesis of credit rating: that an MFI's financial performance is critically affected by its managerial capabilities and governance.

In addition, while each MFI has its own mission and model, there are certain generic values that apply to the 'manner of doing business' in general, reflecting concepts of social responsibility and certain development values which are widely associated with microfinance. These are captured in the definition of social value in microfinance, and articulated by the Social Performance Task Force, in box 1.

Accordingly, social performance may be redefined as:

The translation of mission into practice, in line with accepted social values

Box 1. **Social Value in Microfinance**

The social value of microfinance relates to:

- improving the lives of poor and excluded clients and their families; and
- widening the range of opportunities for communities.

To create this value, the social objectives of an MFI may include:

- serving an increasing number of the poor (and people excluded from financial and other services) sustainably, and expanding and deepening outreach to poorer people;
- improving the quality and appropriateness of financial services available to the target clients through a systematic assessment of their specific needs;
- delivering such services in a cost-effective way that offers low fees and fair interest rates on loans and deposits;
- creating benefits for the clients of microfinance, their families, and communities, that relate to social capital and social links, assets, reduction in vulnerability, employment creation, income, access to services, and fulfillment of basic needs;
- improving the social responsibility of the MFI towards its employees, its clients, and the community it serves; and
- monitoring and acting upon unintended negative side-effects of microfinance, such as over-indebtedness and multiple loans.

Source: Part of the common definition (and social value language) of social performance agreed upon by the Social Performance Task Force at the March 2005 meeting in Paris.

The key elements of social performance reflect this definition and provide a framework for social rating and reporting, as set out in table 1. Two elements relate to organisational process in terms of an MFI's policies: strategies and systems put in place (1 to manage its social performance and (2 to ensure social responsibility—to clients, community, staff, as well as to the environment. Three elements relate to the achievement of goals or results at client and community levels: outreach, appropriateness of services with effective communication, and [achieving] change.

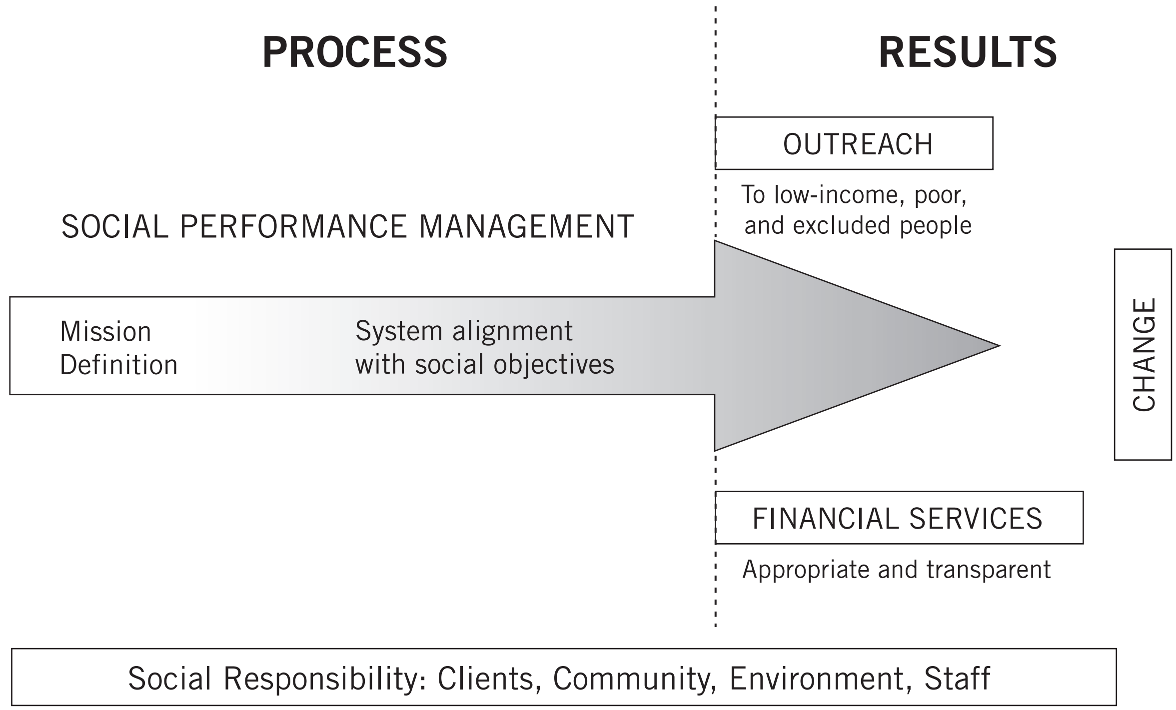
Table 1. **Key Elements of Social Performance**

Process: Governance, policies, and systems	
1	Social performance management: Mission definition and strategic systems
2	Social responsibility: Policy and mechanisms for compliance
Results or Achievement of Social Goals: Client and community	
1	Outreach—depth and width
2	Financial services—appropriateness and transparency
3	Achievement of change

There is a clear—and intended—overlap with the *Imp-Act* pathway, as shown in figure 2.

2. This is the drawback with the scoring methodology for some indicators of the CERISE tool and the AMAP tool. They build in certain assumptions about models of microfinance or products, for example, which are not applicable to all MFIs.

Figure 2: **Social Reporting and the *Imp-Act* Pathway**



In financial performance reporting, there are agreed notations to identify the key indicators and ratios, such as, for example, ROA (return on assets), FSS (financial self-sufficiency), OSS (operational self-sufficiency), OER (operational expense ratio), and PAR (portfolio at risk). These acronyms and their meanings are well established and widely used. Social performance reporting needs its own notation. Suggested acronyms for the key social dimensions are shown in box 2.

Box 2 also sets out the balance between an MFI's own mission and mandate and generic social value. SPM has reference to the individual MFI, and assesses mission clarity and systems alignment with reference to the MFI's articulated mission and model. For example, it should not be assumed that each MFI targets poor clients (though most say they do, including banks in this sector). Some may target areas, but not particular households within areas (for example, cooperatives, which should follow the principle of open membership). Strategic systems, human resource policies, and information systems should support the mandate of each organisation, which is the reference for assessment.

Some dimensions are applicable to certain MFI models and not to others: under social responsibility to clients, there are issues of gender approach (GA), member governance (MG), and non-financial services (NFS)—which are applicable to MFIs that target women, or are member-owned institutions, or aim to provide (or link clients with) non-financial services. These dimensions are not assumed to be applicable to all (though there is a case for gender equity as a universal value).

Other dimensions, also shown in box 2, may be assumed to have generic social value: client protection (as the key element of social responsibility to clients—**SR-CL**) and the other social responsibilities (**SR-Cm**, **SR-St**, **SR-Env**). Two social goals—outreach (**SG-Or**) and appropriate financial services (**SG-Sv**)—reflect social values associated with microfinance: reaching substantial numbers of the poor and excluded, and providing appropriate financial services in line with client needs and capacities. The third social goal, achieving change (**SG-Ch**), reflects wider development objectives (such as the Millennium Development Goals) and may also be linked to an MFI's specific objectives.

This will become clearer as the details of parameters and indicators relevant to each dimension are discussed in the next section.

Parameters and Indicators of Social Performance

Social performance relates to process and results; it also relates to context. This section sets out the main parameters and indicators for these three aspects and the different dimensions. The indicators listed are currently in use or being considered by the specialised rating agencies. They also reflect related initiatives, as listed in the 'Objectives and Scope' section above. Some of the more commonly used indicators are listed in box 3 below. The list may not be complete, but it reflects current thinking and application.

Box 2. **Social Dimensions: Acronyms and Reference**

	TENTATIVE ACRONYMS *	DIMENSIONS	REFERENCE	
			MFI Mission/ Model	Social Value
Process: Governance, policies, and systems				
1	**SPM**	Social performance management	•	
2	**SR-CL**	Responsibility to clients—client protection	•	•
	GA	Gender approach	•	•
	MG	Member governance—if a member-owned institution		•
	NFS	Non-financial services (direct provision or linkage)	•	
	SR-Cm	Responsibility to community		•
	SR-St	Responsibility to staff		•
	SR-Env	Responsibility to environment		•
Results or Achievement of Social Goals: Client and community levels				
1	**SG-Or**	Social goal—outreach		•
2	**SG-Sv**	Social goal—services		•
3	**SG-Ch**	Social goal—change	•	•

* This is a first attempt at developing a notation for social performance to be the counterpart of the notation for financial performance (FSS financial self-sufficiency, OSS—operational self-sufficiency, OER—operating expense ratio, PAR—portfolio at risk, etc.).

Context

Context information is important for describing key features of an MFI and the environment in which it operates. The main features and indicators of context are:

- socio-economic data from secondary sources about the country and region(s) where the MFI operates, including GDP/GNI per capita, national poverty line, percent of population below the national poverty line, percent of population with access to banking services, HDI (human development index) indicators, and marginal communities/population;
- the regulatory environment;
- the MFI—evolution, institutional form, model, and mission;
- the MFI—portfolio size, total savings (if applicable), number of clients (borrowers and savers), percent of women and men, percent from rural, town, or city; and
- the MFI's financial services and products and client access (by type of product, by how accounts are distributed during different cycles and by years [in percents], and by mean/median amounts).

Process—Organisation Level

Key elements of process at the organisation level are social performance management and social responsibility. Indicators of these dimensions are based on information and data available from the MFI.

SPM—Social performance management refers to clarity of mission and the alignment of an organisation's strategies and systems to its social mission. This dimension includes:

- clarity and communication of mission;
- establishment of specific social objectives;
- alignment of organisational systems (human resources, incentives, and management information systems) with objectives;
- monitoring and reporting of the achievement of these objectives (through, for example, poverty scoring of clients, conducting market research, tracking drop-outs, setting up impact studies); and
- use of such information for strategic decision making.

SR—Social responsibility has four dimensions which are applicable at the organisational level in terms of policies and mechanisms for compliance.

SR-CL—Responsibility to clients is a fundamental dimension and is increasingly being recognised as such, especially to the extent that MFIs are catering more to poorer clients who may be illiterate and lack financial skills. It refers primarily to client protection and includes issues of:

- fair and transparent pricing;
- effective communication (including teaching financial literacy to clients and adapting communication methods to include illiterate clients);
- sensitivity to over-indebting clients (effective credit appraisal and monitoring)
- ethical behaviour of staff, including appropriate debt repayment practices;
- provision for loan insurance; and
- pro-active mechanisms for client complaint and redress.

Other dimensions, detailed below, also relate to client responsibility (where applicable).

GA—Gender approach is applicable to MFIs that have women clients (if not, as some argue, applicable to all organisations). This dimension includes:

- the number and percent of women and men on the organisation's board, management, and staff; and
- whether the MFI strategically tries to address the social and economic constraints that women face in its local area (for example, low literacy and limited access to markets).

MG—Member governance incorporates strategies for effective member governance in organisations that are member-owned (e.g., cooperatives and credit unions), such as:

- board elections in compliance with by-laws;
- training and capacity building of representatives to help them perform their governance role effectively;
- regular all-member meetings and attendance; and
- effective strategies to communicate policy decisions to ordinary members.

NFS—Non-financial services: it is not assumed that an MFI, which is primarily a financial intermediary, will also provide non-financial services (enterprise skills development, business development services, and other social services) or ensure linkages to NFS for clients. But, some MFIs have decided to offer direct or linked provision as part of their mandate. For those that do, the issues include:

- what non-financial services are provided/available to clients;
- what non-financial services are offered to how many clients in previous year—by service; and
- whether there is evidence of how effective such services are. (Is it tracked by the MFI?)

SR-Cm—Responsibility to community is a rather broad notion, but its reference to microfinance may cover:

- a policy for the type of activities for which credit is provided, such as those activities promoting positive community value (e.g., start-up enterprises and job creation) and those avoiding negative community value (e.g., enterprises employing full-time child labour and liquor vending);
- other support to the community (investment and donations, as a percent of revenues);
- funding in event of collective disasters (as percent of revenues); and
- positive action to improve local culture, e.g., governance, anti-corruption, and other social values.

SR-S—Responsibility to staff includes:

- staff training—percent of staff trained and number of days of staff training (excluding new hires);
- salary structure (and benefits) in line with comparable sectors;
- security of working conditions;
- fairness and transparency of incentive schemes as perceived by staff; and
- feedback mechanisms for staff and their involvement in decision making.

SR-Env—Responsibility to environment is likely to be most applicable to financial institutions lending to small and medium enterprises, though it seems less relevant at the level of microenterprises and livelihoods usually supported by microfinance. Where applicable, it includes:

- environmental policies applied to core business lines;
- processes for assessing and screening environmental risks in core business lines;
- processes for monitoring client compliance; and
- processes for improving staff competency to address environmental risks and opportunities.

Results—Client and Community Levels

The results of microfinance are of prime importance and ultimately depend on good information at the client level. Such information is not necessarily available to an MFI, and until recently, the reporting of results has depended on 'proxy' indicators, based on portfolio information that MFIs maintain as part of their financial management. These proxy indicators are included here, along with the direct (client/community level) indicators that can provide a more robust picture.

SG-Or—Outreach—depth and width refers to overall number of households served, their location in more remote or under-developed areas, and their socio-economic profiles related to poverty and exclusion. This dimension may refer to the targeting approach of the MFI, but is not limited by it. In other words, the indicators apply to all MFIs, whatever their target or approach. This enables comparison within the industry on a fundamental issue of social value—depth of outreach, or how many clients of microfinance are poor when they join an MFI.

Depth of outreach may be indirect, including expanded market opportunities and employment (those hired from outside the client household) in credit-supported enterprises. These indicators are particularly relevant to MFIs that target SMEs and do not specifically focus on the poor. (Indirect employment is especially relevant here; expanded market opportunities are more difficult to assess.) Relevant indicators, therefore, include:

Proxy indicators of outreach

- Minimum amount required to open a savings account (if savings offered)
- Average loan size (of new clients) as a percentage of per-capita GDP/GNI
- Average loan/per-capita GDP (in correlation with GINI index)
- Percentage of loans less than (a) US $300 in Asia, Africa, and Middle East; (b) $400 in Latin America and the Caribbean; and (c) $1,000 in Europe and Central Asia
- Calculated loan installment amount, relative to per-capita GDP

Direct outreach[3]

- Percent of clients in areas with lower than average–socio-economic development (poverty levels, illiteracy, HDI, infrastructure determined by using secondary data)
- Percent of clients belonging to marginal communities or with marginal characteristics relative to share in local population (as recognised in different countries, e.g., the illiterate, casual labourers, female-headed households with no adult male earner)
- Percent of recent client households without a savings account (bank, post office)
- Percent of recent client households without access to formal credit (bank, cooperative)
- Percent of recent clients from households living below international poverty line (less than US $1/day, less than $2/day purchasing power parity—PPP), and below national poverty line
- Percent of recent clients from households who are very poor (less than $0.50/day PPP; more than half over the national poverty line or any other index of quality of life, including, for example, poor living conditions, owning minimal assets)
- Estimated total clients from households existing on less than 1$/day PPP when they joined the program
- Number of family members (men, women, and children) working in credit-supported enterprises (full time and part time)

3. Poverty outreach in terms of key indicators of poverty and financial exclusion should ideally be assessed for new clients or those just recently joined to capture their status (or rather the status of their households) at the time they join the MFI. This is because the poverty status (for example, ownership of assets, income) of client households may change as a result of use of microfinance services.

Indirect outreach

- Number of hired (non-client household) employees; men, women, and children in credit-supported enterprises (full time and part time)
- Profile of hired employees: their household poverty level, what percent belong to marginal communities

SG-Sv—Financial services—appropriateness and transparency—refer to the extent to which an organisation is meeting its clients' financial needs (with different types of services and products), in relation to their capacities (cash flows and opportunities). It also includes a check on **SR-CL** at the field level, to confirm whether clients are fully aware of the terms and conditions of MFI products, and their views on and experience with services offered.

Proxy indicators—range of products and services (with reference to the regulatory environment)

- Voluntary savings (if legally allowed), designed for specific purposes
- Distinct loan products (for enterprises, housing, education, emergencies)
- Variety of collateral accepted
- Flexible terms
- Portfolio distribution in use of loan
- Insurance products (life, health, asset), directly provided or linked to insurance companies

Direct indicators

- Effective interest rates, compared to alternative, accessible credit options
- Percent of client households with a member in another MFI
- Percent of client households borrowing from informal moneylender in previous year
- Client household indebtedness (all sources), as a proportion of household income
- Client exit: drop-out rate (method of calculation defined)
- Client awareness:
  - Savings (if applicable), terms, interest payable, own total deposit
  - Credit—range of products and terms, including fees, interest rates, and distribution of loan installment amount between principal and interest
  - Insurance availability and terms
  - Passbooks up to date and kept by clients
  - Procedure in case of complaint
- Client feedback:
  - Meetings and frequency of transactions
  - Savings terms
  - Credit products, amounts, timeliness
  - Insurance utility, experience
  - Non-financial services (if applicable)
- Reasons for drop-out

SG-Ch—Change is not defined in terms of the 'impact' that can be attributed to a microfinance program. Impact assessments are interesting and can be useful to 'prove' what microfinance services achieve. If there is an impact assessment of a microfinance program, then the findings should be included. Even without research on full impact (research, for example, without a non-client comparison group), it is possible to document or track changes at the client household level, which may plausibly represent at least some contribution from accessing microfinance services. Such findings may be included under this dimension, provided they appear valid. Indicators include findings of any recent (within past two years) studies of changes at the client and community level, as well as these below:

Change indicators that may be linked to the MFI's specific objectives, for example:

- Diversification of livelihoods and new enterprises
- Increase in household income
- Management of enterprises by women
- increase in employment (self-employment and hired employment, men and women) and earnings; other benefits to hired employees
- Reduced household dependency on moneylenders
- Sustainability of livelihoods and greater financial inclusion: percent of loan clients who have evolved from taking loans to making deposits.

Change indicators that may be linked to wider development objectives, as reflected in the Millennium Development Goals (MDGs):

- Poverty reduction (percent of client households moved out of poverty)
- Universal primary education (percent of school-age boys and girls, in client households, that go to school)
- Women's equality and empowerment
- Improved health (and access to medical care)

A couple of initiatives are developing indicators and tools to enable MFIs (with their own staff) to collect information about their clients themselves in a relatively trouble-free and roughly accurate manner. Indicators relevant to the MDGs are currently being tested under the Ford Foundation-CGAP Social Indicators Project. As part of this initiative, Grameen Foundation USA is piloting a 'Progress out of Poverty Index' for different countries with its MFI partners in different countries. The index has a set of indicators which are simple and easy to measure: it takes a loan officer just 4–5 minutes to collect the information from a client as part of standard loan appraisal. The indicators are statistically correlated with the US $1/day-poverty line, based on national data sets. This results in a quick yet robust assessment of the likelihood of client poverty, whether by MFI staff or by an external agency, that enables an MFI to track its depth of outreach (through the poverty score of client households when joining the MFI) and the changes in the poverty score of client households over time.

Social Rating—Initiatives in Progress

The specialised microfinance rating agencies are experimenting with social rating as a crucial, additional assessment of an MFI that will complement the financial, organisational appraisal of a credit rating. It provides a balanced assessment of the double bottom line (if not the 'triple bottom line', where environmental aspects are also relevant), rather than just the 'one-sided assessment' of financial risk.

Many of the questions on the process of social performance (**SPM**, **SR**) can be easily incorporated into the MFI-level discussions that are already a part of credit ratings. A social rating can cover all the dimensions, using a range of indicators, as listed in box 3.

In social rating, there remain perhaps two main challenges: scoring and weighting, and the method of collecting data. Both of these are likely to be influenced by the potential users of a social rating: investors, donors, and MFIs themselves.

How—and Whether—to Score?

On the question of scoring, 'rating' implies an assessment of performance and applying measures and indicators, which are scored against benchmark standards. Benchmark standards are yet to be developed that can compare many of the indicators across different regions. Some standards are available for some regions. For example, in south Asia, there are studies that show the average depth of outreach of MFIs (the percent of clients who have recently joined, who are poor defined as living below the international US $1/day poverty line) to be in the range of 25–35 percent on average.[4] This level is similar to or slightly above the poverty ratio reported for different countries in the region, but not so much above as apparently assumed in statements about

4. Studies conducted by EDA Rural Systems in India (2002–2005, 21 MFIs), Bangladesh (2004–2005, 12 MFIs) and Myanmar (2005). Poverty assessment of clients who had recently joined MFIs was based on a triangulated methodology for poverty assessment: participatory wealth ranking, index scoring, and per-capita income (cash and in kind) benchmarked to the national poverty line and the international US $1/day poverty line at purchasing power parity (PPP). Similar poverty levels amongst MFI clients are reported in USAID, 'Developing and Testing Poverty Assessment Tools: Results from Accuracy Tests in Bangladesh', IRIS Center, University of Maryland-College Park (Washington, DC: USAID, 2005); and James Copestake et al., *Money with a Mission*, vol 1, 'Microfinance and Poverty Reduction' (Bourton-on-Dunsmore/Rugby/Warwickshire, UK: ITDG Publishing, 2005).

the (100 percent) poverty outreach of microfinance. Based on this, M-CRIL has set its 'optimal' score for depth of outreach at less than 60 percent of recent clients living below $1/day. This seems the appropriate bench-mark in countries of South Asia and Africa. In regions where the cost of living is higher, the $2/day poverty line would be the relevant standard, as applied by ACCION and its network partners in Latin America and the Caribbean.[5]

For some indicators, it is relatively easy to figure out the cut-offs for 'optimal', 'average', and 'weak'—e.g., for operations in extremely poor areas, member governance, or even gender ratios (though there are cultural variations). In the present early phase of social rating, rating agencies will present the 'base data', with or without scores, as they gradually build up their data base.

Similarly, on the question of weights between—and within—the dimensions, one approach currently in favour is to present rating results in such a way that users can apply their own weighting to the rating findings. For example, more results-oriented social investors might give more weight to outreach, appropriateness of services, and change, than to managerial systems leading to these results.

Data Available + Additional Data?

The second issue is to what extent ratings should rely on data available from an MFI. Ideally, ratings should be based on an MFI's own data, but available data in the MIS is usually geared toward financial analysis and reporting (and that, of course, is what raters as financial analysts are trained to use).

There is nevertheless a choice to be made in social rating—between a 'thin' approach and a comprehensive approach. A 'thin' methodology relies on existing data and uses proxy indicators to reflect 'results'—for example, using average loan outstanding as a proportion of country GNP for depth of outreach or number of financial products for appropriateness of services. This is the approach employed by USAID Social Performance Assessment Tool and to some extent by Cerise too. A more comprehensive approach uses available data, but in the absence of field level information, prefers not to rely on portfolio-based (supply-side) proxies, which provide a very limited picture of the demand side (since, for example, small loan sizes do not exclude the non-poor, and number of products is not necessarily the critical factor in meeting the financial needs and capacities of different client segments).[6] A comprehensive approach, therefore, involves the additional task of carrying out a field survey to obtain information directly from clients for **SG-Or** and **SG-Sv**.

The rating survey does not include **SG-Ch** (which is more complex), but the data obtained to assess the poverty level of recent clients (including household per-capita incomes and other socio-economic indicators of poverty) can serve as a baseline for a later follow-up survey of the same sample. Such a follow-up survey (which could be part of a social rating update) would provide evidence for change over time. Though, if an impact assessment of the MFI has been undertaken by any agency, and the impact findings are well researched (valid/robust) and up to date (fresh), such findings would be included as part of the social rating for SG-Ch.

If the user of a social rating is interested in the results of microfinance, as reflected in the idea of a strong weighting of the results dimensions, this suggests the need for having more robust information such as would be available from a client level survey. This does however imply a new skill set for raters, and entails a higher cost because of the additional time involved. M-CRIL uses a minimum sample size (127 client questionnaires) for statistical confidence in quantitative findings.[7]

5. Poverty assessment is complex—both in definition and measurement. The international poverty line (US $1/day at purchasing power parity) provides a broadly accepted and internationally comparable bench-mark, but its direct application requires very strong skills both in data collection and analysis. In response, there are some interesting initiatives to develop tools for poverty assessment which are benchmarked against the $1/day poverty line, using indicators that are much easier to record than income or expenditure estimates. The 'country poverty score cards' being developed by the Grameen Foundation, following the work of the IRIS/USAID project, have already been mentioned. Once tested, such score cards will provide a simple methodology for assessing the depth of outreach of an MFI, and possibly too client shifts out of poverty over time. The cards will be a useful tool for MFIs themselves to apply as part of their social performance management and reporting. The cards could also be used as part of a social rating.

   Until such tools are available for different countries, direct measurement remains the option, as has been applied by ACCION and by M-CRIL. M-CRIL's assessment of poverty level at the household level involves a questionnaire covering details of household income (cash and in kind) and other indicators of quality of life. From this, data for household per capita incomes can be benchmarked against the $1/day poverty line at PPP, adjusted for each country. The expenditure measure (which is the basis of the $1/day poverty line) is usually preferred as more accurate than incomes (since households are more likely to understate incomes), but it requires a more complex questionnaire and assumes ability for detailed recall. In either case (expenditure or income), while the $1/day poverty line is a useful measure because it enables objective benchmarking, the possibility of benchmarking should not blind one to its shortcomings: its measurement is bound to contain some degree of error; there is, after all, not much poverty difference between households within a few cents of the PPP cut-off, and it represents just one dimension of poverty understood as a more complex situation of deprivation.

6. See, for example, Chris Dunford, 'What's Wrong with Loan Size?' Freedom from Hunger, Davis, CA, 2002 ; and M-CRIL, 'Can MFIs Achieve the Double Bottom Line?' Technical Note 4 (Gurgaon, India: M-CRIL, 2005).

7. The M-CRIL assessment of poverty level in households employs a questionnaire that asks for details of household income (cash and in kind) and other indicators of quality of life. From this, data for household per-capita incomes can be benchmarked against the US $1/day-poverty line at PPP, adjusted for each country. The expenditure measure (which is the basis of the $1/day-poverty line) is usually preferred because it is more accurate than incomes (since households are more likely to understate incomes), but it requires a more complex questionnaire and assumes ability for detailed recall. In either case (expenditure or income), while the $1/day-poverty line is a useful measure, since it enables objective benchmarking, the possibility of benchmarking should not blind one to its shortcomings: its measurement is bound to contain some degree of error. In practice, there is not much difference in poverty among households within a few cents or more of the PPP cut off. It represents just one dimension of poverty, which is understood to be a complex situation of deprivation.

SPM by MFIs Will Improve the Data Available

Potentially useful client profile data may already be collected by some MFIs, as part of a targeting approach in MFIs with a group lending methodology, for example, or as part of credit appraisals in MFIs providing individual loans. However, this information is not usually part of the MIS and may not in fact be collated at all—and there are issues of reliability related to the context in which loan officers collect information.

As MFIs themselves undertake SPM, including the use of tools for client level profiling (reviewing and improving their existing data collection or applying a poverty score card benchmarked to the international poverty line—see footnote 4), market research, and monitoring change at the client level (household, enterprise, local community), such reports would become part of the material for a social rating.

Their methods and findings would need to be audited (validated) as part of the process of rating, with perhaps some cross-checking at field level (but this would reduce the additional work load—and costs—of a comprehensive social rating). Such information would strengthen social reporting by MFIs.

Social Reporting by MFIs—A 'Short' List of Indicators

Based on the framework presented here, that is beginning to be applied by specialised raters, some suggestions can be made for social reporting by MFIs—that make use of the spaces currently left blank in the MIX reporting format and that balance the organisational and financial information provided in annual reports.

A short list of relevant indicators (but still too many) is outlined in box 3. They are drawn from the long list of indicators collected by the sub-committee for social rating and reporting of the Social Performance Task Force and should be seen as a step forward in the process of defining the key indicators for MFI reporting. Further consultation and experimentation will be required within the microfinance sector, involving different stakeholders, such as MFIs (different models and regions), investors, raters, donors, the MIX Market, to select the core indicators for social reporting and develop appropriate and clear definitions.

The indicators in Box 3 are partly those that are likely to be available in a typical MIS. Some may require adjustment (as indicated by this symbol, ◘) to focus on client level information rather than loan information or to include reference to secondary information. Other indicators (those marked with a '#') will depend on client-level information. This may be collected by the MFI (as part of its SPM system) or, in part, could be obtained through a comprehensive social rating.

The task is analogous to the process that established the parameters and indicators for financial reporting. These must have seemed, in early days, relatively complex and difficult. Financial indicators are now established and accepted as 'basic' and straightforward, and are integrated within information systems and reporting. However, their acceptance took several years, with adjustments to MFI data systems, to enable systematic and robust monitoring. The same may apply to social reporting.

Going Forward

This paper has drawn on current initiatives around social performance analysis and measurement in microfinance to set out a common framework for rating and reporting on social performance. The framework defines the key dimensions and their conceptual basis and linkages. Possible indicators are also listed under each dimension. The list is a comprehensive one and is intended to provide a basis for further experimentation and refinement, which should ultimately lead to indicator selection, definition, and specification of tools for data collection.

For social rating, the specialised rating agencies are well placed to start building data comparisons and to test benchmarks and scoring across different models and contexts. For social reporting by MFIs, there needs to be a process of engagement across the industry to build consensus on key measures that are both robust and practical, and would ideally be part of an organisational system for social performance management.

Initiatives for both are already under way.

Box 3. **Suggested 'Short' List of Indicators for Social Reporting by MFIs**

◘ : Indicators likely to be available in the MIS; may be adjusted to provide client level information rather than loan information or to include reference to secondary information.
: Indicators that depend on client-level information.

1	**CONTEXT**
	Organisational Profile
	Legal form; years of microfinance operations; model of microfinance (group type, individual)
	Total portfolio and total loan accounts
	Total savings and total savings accounts
◘	Total client households
◘	Percent of rural and urban clients (separating semi-rural and urban if possible); percent of women and men
	Financial Services and Access
	Product information: savings products (compulsory and voluntary), deposit amounts, interest payable, withdrawability
	Loan products, first loan sizes, costs (fees, declining interest, term)
	Insurance services—and whether they are the MFI's own or are linked to an insurance company
	Type of savings: total savings amount, number of accounts, average deposit outstanding
	Type of loan product: total portfolio, number of accounts, average amount outstanding
◘	Number and percent of accounts in different loan cycles (or percent of clients by loan cycle or years with MFI
	Number and terms of insurance policies; percent of clients who applied for, or received, pay-out in previous year
	Effective interest rate on different loan products (EIR)

2	**PROCESS**
SPM	**Social Performance Management**
	Mission statement and date of formulation
	Target group(s)—how defined or how criteria applied
	Main parameters on which staff incentives are based
	Whether MFI uses information about clients to track outreach
	Whether MFI has conducted, commissioned, or used market research in past 2 years
	How MFI defines drop-outs; whether it tracks drop-out rate and reasons for exit
SR	**Social Responsibility**
SR-CL	Whether MFI has a written formalised code of conduct for client protection
	What measures MFI has in place to ensure client protection (board review, operational manual, staff training, staff appraisals)
	Whether MFI provides written statement of repayments to clients that distinguishes principal, interest, and other payments; adapts communication strategy to capabilities of (poorer) clients
	Average time between approval and disbursal of loan
	Time between application for insurance pay out and payment
	Whether MFI monitors client indebtedness (at time of loan appraisal for possible default)
GA	Women and men on board of directors, in management, field staff, and support staff
	Specific strategies to address gender constraints in the local cultural/market environment
NFS	Any non-financial services provided (directly or through linkages with other NFS providers) and description ,
	Percent of clients who have accessed these services in each of previous 2 years
SR-Cm	Percent of operating revenues reinvested in the community during previous year
SR-St	Written, formal code of conduct governing actions towards staff
	Career and training opportunities: number of days/year per staff category
SR-Env	Organisational practices in line with environmental conservation (energy, paper, etc)
	Description of environmental policies applied to core business lines (where applicable, as for SME finance)

3	**RESULTS**
SG-Or	**Social Goal—Outreach**
◘	Operational areas ranked—with distribution of clients across areas
#	Percent of clients belonging to marginal communities (as applicable in different countries)
#	Percent of [recent] client households with no savings accounts or loans from other sources (bank, cooperative, other)
#	Percent of recent clients living below US $1/day and $2/day at PPP
#	Percent of clients according to other poverty levels defined by the MFI (with details of how defined)
# ◘	Number of financial services-supported enterprises by number of hired (non-household) employees (0, 1–2, 3–5,6–9, 10–30, < 30)
	Proxies if direct information not available:
	Average loan size as a percentage of GNI/GDP per capita for new loan clients
	Percentage of loans (a) > $300 in Asia, Africa, and the Middle East; (b)> $400 in Latin America and the Caribbean; and (c) > $1,000 in Europe and Central Asia
SG-Sv	**Social Goal: Appropriate Services**
#	Findings of any market research (in past 2 years with sample details), including if possible:
	Percent of clients aware of interest payable on savings
	Percent of clients aware of full costs of borrowing (fees, declining interest)
	Percent of clients from households with member in another MFI
	Percent of clients from households borrowing from informal moneylender in previous year
	Drop-out rate in previous years (and how defined)
#	Results of any drop-out tracking or survey, if available, including if possible: exit rates within different client categories (poverty level, loan cycle), and reasons for drop-out
SG-Ch	**Social Goal: Change—Effects or Impact**
#	Findings of any recent (within past 2 years) impact studies of MFI (design details, methodology for, size of sample, method for poverty assessment)
#	Contribution toward achieving MDGs (indicators being developed by C-GAP Ford Social Indicators Project), for example, percent of clients who have moved out of poverty after 5 years, percent of school-aged children (girls and boys separately) of clients who attend primary school (compared to children of non-clients)
	Sustainability of livelihoods and greater financial inclusion: percent of loan clients who have evolved after 5 years from taking loans to making deposits
#	Contribution to employment generation
	Total number of credit-supported enterprises, percent of new enterprises started with microcredit and continuing for at least 2 years
	Increase in number of clients employed in credit-supported enterprises, separately for family and hired: men, women, boys, girls (children defined as younger than 15 years), and for full time and part time (full-time defined as working more than 8 months of the year, and at least 6 hours/day; part-time is less than this, including both seasonal and irregular work)

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Web Sites

ACCION: http://www.accion.org/products.asp

CERISE Social Performance Indicators Initiative: http://www.cerise-microfinance.org/publication/impact.htm;

http://www.cerise-microfinance.org/publication/pdf/impact/spi2/spi2_reportno3_result_ve_june05.pdf#search=%22CERISE%20Social%20Performance%20Indicators%20Initiative%22

CGAP-Ford Foundations Social Indicators Initiative: http://www.microfinancegateway.org/content/general/detail/35402?PHPSESSID=9f7bae42a5c13ea37ead4d4e183474ad

Grameen Foundation ('Progress out of Poverty Index'): http://www.gfusa.org/programs/social_performance/ http://www.microfinance.com/#Poverty_Scoring (Web site developed by Mark Schreiner)

Imp-Act: http://www.ids.ac.uk/impact/resources/SPM_index.html

M-Cril: http://www.m-cril.com/social-rating-microfinance-institutions.html

Millennium Development Goals: http://www.un.org/millenniumgoals/

Microfinance Information eXchange-MIX Market: http://www.mixmarket.org/

Microfinanza: http://www.microfinanza.com/

MicroRate: http://www.microrate.com/

Planet Rating: http://www.planetrating.com/

Triodos-GRI 'Transparency in Sustainability and Finance': http://www.triodos.com/com/static/pdf/coen_gri3.pdf#search=%22transparency%20in%20sustainability%20and%20finance%22

USAID Social Performance Assessment Tool: http://www.povertytools.org/

USAID-AMAP: http://www.microlinks.org/ev_en.php?ID=1222_201&ID2=DO_TOPIC

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