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The double bottom line debate in microfinance: Is it possible for the industry to keep financial sustainability and social performance in balance?

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List of Acronyms

CARD MRI	Center for Agriculture and Rural Development Mutually Reinforcing Institutions Leadership
CERISE	Comite d'Echange, de Réflexion et d'Information sur les Systèmes d'Epargne-crédit
CGAP	Consultative Group to Assist the Poor
ECA	Eastern & Central Asia
CRS	Catholic Relief Services
FFH	Freedom From Hunger
FINCA	Foundation for International Community Assistance
FCAT	Finca's Client Assessment Tool
IDS	Institute of Development Studies
IFAD	International Fund for Agricultural Development
IFIs	International Financial Institutions
IM	Impact Management
LAC	Latin America & the Caribbean
MENA	Middle East & North Africa
MIX	Microfinance Exchange
MFC	The Microfinance Centre for Central and Eastern Europe and the New Independent States
MFIs	Microfinance Institutions
MIVs	Microfinance Investment Vehicles
NGOs	Non-Governmental Organizations
OSS	Operational Self-Sufficiency
PAT	Poverty Assessment Tool
PPI	Progress out of Poverty Index
ROA	Return on Assets
SEF	Small Enterprise Foundation
SEEP	Small Enterprise Education and Promotion Network
SP	Social Performance
SPA	Social Performance Assessment
SPM	Social Performance Management
SPTF	Social Performance Task Force
SF MFIs	Socially Focused MFIs
TCP	Tshomisano Credit Programme
USAID	United States Agency for International Development

Introduction

This paper aims to primarily investigate qualitatively and quantitatively if within the debate of “double bottom line” it is possible to have a balance between financial and social performance. Therefore the hypothesis chosen is: “*Socially Focused MFIs (SF MFIs) are reaching a balance between financial sustainability and social performance with respect to the industry as a whole*”. Also, as framed within this research, the paper seeks to explore how the industry of microfinance is moving towards different initiatives to provide better services and continue to serve the poor.

In Chapter 1, the first section presents microfinance as a poverty alleviation tool. Section 2 defines the scope of the paper and the next parts aim to present a complete overview of this industry. They cover the evolution and achievements of microfinance, provide a literature review of impact evaluations of microfinance programs, and analyze some criticisms of the industry.

In addition, Chapter 2 explains the challenges the industry faces, notably how difficult it is for MFIs to be profitable and to maintain a business when resources are scarce and the competition is growing every day. It centers on the “mission drift” some MFIs are suffering due to business commercialization. Moreover, it introduces the “double bottom line” debate, namely the need to balance financial sustainability and social performance to truly have an impact on the poorest of the poor. Finally the chapter analyzes how cost-effective it is for the industry to assess social performance and presents two case studies.

Chapter 3 describes the main efforts undertaken by the microfinance sector to measure social performance. It compares the main actors and organizations within the social performance process and some of the main poverty alleviation tools and social indicators proposed.

Chapter 4 presents the data sources and statistical work, and the methodology undertaken to combine the theoretical and empirical parts of the research. The core of this chapter is devoted to presenting a comparison of financial indicators from a sample of "socially focused" MFIs (SF MFIs) with the same indicators from a bigger sample of 310 MFIs (Global MFIs). The goal is to determine whether it is possible for the SF MFIs to find an efficient balance between financial sustainability and social performance.

Finally, the last chapter draws general conclusions and future research proposals.

Chapter I. Microfinance impact on poverty alleviation

1. Microfinance as poverty alleviation tool

In many development countries capital markets are still rudimentary and formal banking in its daily operations is subject to regulations which may disadvantage poor clients or even exclude them. Under this scenario, the poor face difficulties mainly related to their lack of collateral and high transaction costs involved. Indeed, the poor tend to borrow small amounts but the costs of processing plus assuring their repayment are very high. Those are fixed costs which are not proportional to the amounts lent. This is when microfinance comes in. It provides the poor with relatively small loans and short repayment periods. The destination of the funds varies from basic consumption smoothing, to production oriented activities such as handcrafts, agriculture, and trading industries, etc.

Microfinance as an economic tool for development dates back to the mid 1970s. The idea arose from the need to assist low-income women and men by providing them access to financial services. According to Ledgerwood, J., 2000, these services include financial intermediation products which are mainly credit and savings. These grant the ability to build assets (for example obtain land, build their own home, and purchase animals), stabilize consumption, protect themselves against shocks and run their businesses.

By offering credit and savings microfinance empowers people to diversify, and in turn increase their income sources. This helps them to save and manage cash flows and it reduces the need to sell assets in cases of crisis. Also it allows beneficiaries to shift their focus away from daily surviving. They can plan for their future and direct their spending towards investing in education and nutrition among other needs.[1]

Some microfinance institutions (MFIs), as organizations that provide financial

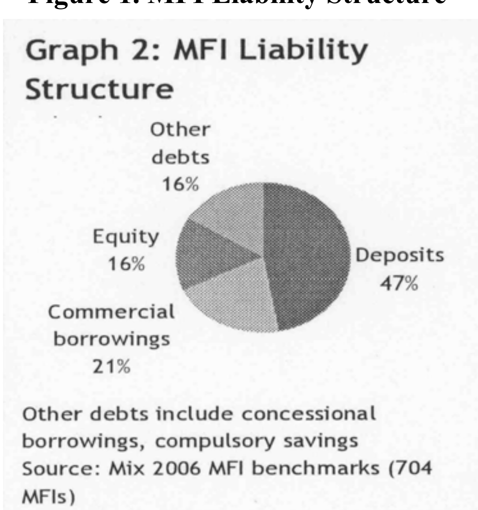
[1] (http://www.cgap.org/p/site/c/template.rc/1.26.1305. Accessed Nov. 4, 2008)

intermediation for the poor regardless of being regulated or not and financial or not financial in nature, complement this by providing insurance and other payment services (as remittances). In addition, many MFIs provide also social intermediation services to support their financial operations such as group formation, development of self confidence, and training in management capabilities between group members. For this reason the definition of microfinance usually includes both financial and social intermediation. (Ledgerwood, J. 2000: 1-7).

Taking into account the above definition of microfinance, MFIs may vary not only in the kind of products and services they offer but as well in their organizational and legal structure. These institutions could be: credit unions, nongovernmental organizations (NGOs), nonbank financial institutions, or even government and commercial banks. All have the same goal (in principle): serving the poor. However, each MFI has its own social mission. The wide array of differences between MFIs, whether logistical or ideological, implies that the quantity and quality of the products and services provided will differ significantly between institutions.

An additional reason why the MFIs industry is considered to be heterogeneous is because it includes both financial and non-financial institutions together. Many well known MFIs have their origins in local grass-roots NGOs (for example Grameen Bank in Bangladesh) or started as partners of international non-profit microfinance networks (for example FINCA International), which are funded by donations or government aid budgets. Others were created as specialized microfinance banks funded by capital from multilateral development banks or international financial institutions (IFIs).

Figure 1. MFI Liability Structure



However, MFIs are increasingly funding themselves through private sources outside of donations and grants that would make them profitable enough in order to survive and be self-sustainable in the long run. “MFIs have sought to diversify away from aid-driven funding, and have turned their focus to attracting third-party commercial sources of debt funding, such as domestic savings, microfinance investment vehicles (MIVs) or even accessing the local and international capital markets". (Fitch Ratings, 2008: 6). Figure 1 illustrates the percentages of recent liability structure of MFIs from a benchmark conducted by the Mix among 704 MFIs in 2006.

Therefore, despite their differences, as a general rule, MFIs struggle to maintain financial sustainability, and to continue to provide services to the poor. As a result this trend has created a special profile of MFIs based on the way they are trying to combine public and private sector players for funding, and on the relative weights they attached to financial return and the achievement of their social mission.

2. Justification and Scope of the microfinance topic within the paper

In order to understand better the scope of the paper regarding microfinance and MFIs' operations, I will use a typology to classify them that I found useful from (Ledgerwood, J., 2000: 65). As we can see in Annex 1 MFIs are classified according to the type of products and services offered to their beneficiaries taking into account two approaches: the *minimalist* and the *integrated*.

The *minimalist approach* is based on the idea that the lack of short-term credit is the cause of under-development, hence these MFIs generally provide by definition financial services as credit is considered to be "the missing piece". But *financial intermediation* alone is usually not enough for the poor to overcome the barriers they face. Therefore, *social intermediation* is used often to help these clients to make a better use of financial products and services by encouraging cooperative groups or associations among clients. These usually generate trust and social capital, which facilitate financial intermediation.

On the other hand, the MFIs with an *integrated approach* offer both financial and nonfinancial services on the basis of a more holistic view of its clients. These are divided in a) *enterprise development services* for their clients to receive training in: business and production, skills development, marketing and technology services; and b) *social services* which include improvements in the well-being of their clients such as: education, health, nutrition and literacy training. Within this approach it is said the MFIs tend to get closer to its clients and therefore supply those services which are most needed.

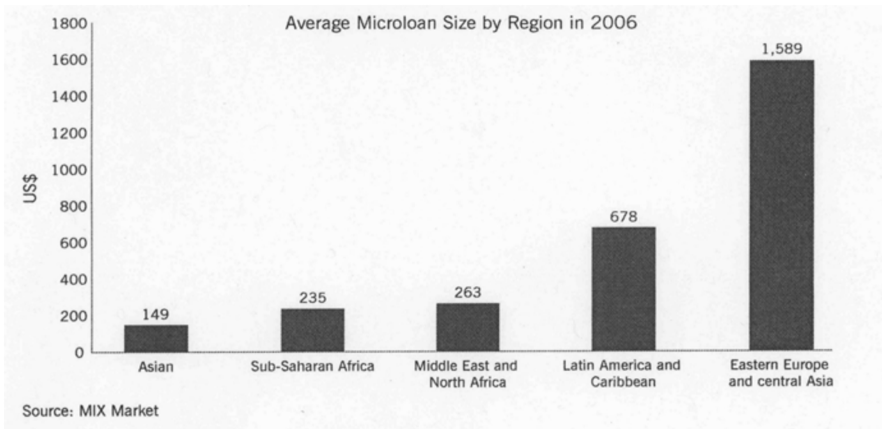
The extent to which MFIs offer one approach or the other is difficult to generalize and depends not only on their own corporate or social mission. It also depends on how the institution wants to diversify its products and services and how it is willing or able to pay to provide them. Nonfinancial services are usually expensive in the long run, and when it comes to covering the costs of providing them each institution may have a different perspective and capacity to do it.

Now that MFIs were here classified under a certain frame, it is important to state that the present paper concentrates mainly on MFIs taking a minimalist approach by providing financial and social intermediation products and services. For the empirical part of the paper I am assuming that a certain group of MFIs, due to certain qualitative and quantitative characteristics may be taking a more integrated approach. So, in Chapter 4 my purpose is to use the last approach to compare a sample of MFIs called "SF MFIs" (assuming they are more "socially focused") with a bigger sample called "Global MFIs" that represent MFIs with or without an integrated approach.

3. Evolution and achievements of microfinance

Since its origins, microfinance industry has expanded throughout developing countries as well as the variety of products offered that are now available. According to an article by Morgan Stanley, 2007 microfinance is considered today as an important component of "the effort to alleviate world poverty and an effective tool to improve human development through economic empowerment" (Morgan Stanley, 2007: 1). Their research suggests the microfinance business model is successful, scalable and with a high propensity to grow over the next decade. "MFIs serve roughly 100 million low-income entrepreneurs, and have an estimated total microloan volume of US$ 25 billion”[2].

Even though the volume of loans and borrowers are heterogeneous as the average loan size of microloans varies on average in each world region, –as seen in this graph of the Mix Market, 2006[3]- many MFIs all over the world share to have achieved reaching the poor people by developing the same strategies. For example, group lending. The organization of borrowers in groups reduces the risk of default as each group member is liable for the payment of principal and interest for the entire group. Also, in this way information is disseminated on how to improve areas under risk of the poor such as: sanitation, health, legal rights and education. Even if some groups tend to exclude the poorer people, peer pressure replaces the need for collateral. This method encourages cooperation because groups serve as collaterals for one another.



Moreover, microfinance products and services have proven to be effective when targeted to women as they are not only poorer than men but also more responsible for repaying and they tend to invest in the household.[4] Many women have been benefited from microfinance as they have been provided with opportunities for small-scale self-employment, access to knowledge and thus, they have increased their security, autonomy and status within the household.

[2] Dieckmann, Raimar, “Microfinance: An emerging investment opportunity,” *Deutche Bank*, December 2007. Cited by Morgan Stanley 2007, p. 3.

[3] http://www.mixmarket.org/ Accessed October, 2008.

[4] Urban Poverty Alleviation Course (4323). Session 11: Microcredit for distinct firm groups. Professor: Peter Knorringa. Institute of Social Studies. May 2008.

Microfinance programs bring about many benefits for the poor like increase in consumption of certain basic needs, reduction of their vulnerability, as well as their income poverty. The increase in household’s consumption is relevant to be mentioned because even a tiny increase in regular consumption leads to better nutrition and health. This in turn, increases the micro borrower’s possibilities to access education, gain skills that will ensure a better access to the job market.

Taking into account the reduction of the poor’s vulnerabilities, the small loans provided to the poor let them protect themselves against idiosyncratic shocks as well as to cover emergencies like natural disasters and other aggregated shocks. Microcredit is just one of the many ways used by the poor in developing countries to manage their money by converting these funds into savings. According to Rutherford, S., it is not true that they are too poor to save. Saving is important for them to cover lifecycle events, emergencies and for investment opportunities (in case they are setting up a business or trying to expand and existing one). (Rutherford, S. 2001: 7-10)

While income poverty reduction is usually attained in the long run, it can also be listed as a benefit for the poor when they have a certain degree of stability derived from increasing their savings’ capacity. In this situation, the poor will be able to invest in profitable businesses in order to grow -if that is their logic-. If not, they will save for the future necessities and lifecycle events such as weddings, funerals, etc.

One can say that as microfinance has evolved in the past 4 decades it has had a positive impact “on enterprise and household income and asset accumulation, household consumption, women’s empowerment, and in helping poor households to manage and cope with risk”. (Woller, G. 2002: 305-306) And not only that, but the industry’s strong financial performance has begun to attract private-sector investors which are making it more solid as an effort to fight world poverty.

4. Impact of microfinance

The United Nations named 2005: “The International Year of Microcredit” and during that year many MFIs were assessed about the social impact derived from their work in the sense of ensuring that people accessing microfinance were able to improve their socio-economic well-being. In other words, the question was if the goal of microfinance was the reduction of poverty and how was this attained.

As most of the studies up to the time (2005) suggested little evidence to respond this question, Nathanael Goldberg of Grameen Foundation USA made some research and compilation of studies that used empirical data to prove microfinance's impact. These showed interesting findings. For example, that there is strong evidence that female clients are empowered, though the data on increased adoption of family planning is less clear. Other studies show how society-wide benefits can go beyond clients. In some other cases it was reported that when women take loans, even if they don't directly use the loan, they and their families benefit more than if the loan had gone directly to their husbands. (Goldberg, N. 2005: 1-45)

Economists Shahidur Khandker and Mark Pitt from Brown University wrote a paper in 1998 called *"The Impact of Group-Based Credit Programs on Poor Households in Bangladesh: Does the Gender of Participants Matter?"* using statistical methods to assess three Bangladeshi programs: Grameen Bank, BRAC and RD-12. They found that every additional taka lent to a woman adds an additional 0.18 taka to annual household expenditures (an 18% return to income from borrowing).

However, other economists such as Jonathan Morduch replied to this study expressing concerns with the statistical data and model used by the authors. Thus, Khandker improved their model and in 2005 presented an updated version of the paper called: *"Micro-finance and Poverty: Evidence Using Panel Data from Bangladesh"*. The new findings showed each additional 100 taka of credit to women increased total annual household expenditures by more than 20 taka and that there were no returns to male borrowers at all. Also he found that between years 1991-92 and 1998-99 moderate poverty in all villages decline by 17 percentage points. (Goldberg, N. 2005: 5-6)[5].

Other studies launched in 1995 by the United States Agency for International Development (USAID) used longitudinal data and non-client comparison groups:

- *Managing Resources, Activities, and Risk in Urban India: The Impact of SEWA bank" (2001)*, by Martha Chen and Donald Snodgrass; compared the impact of clients who borrowed for self-employment to those who saved with SEWA Bank without borrowing, and compared both groups to non-clients. Borrowers' income was over 25% greater than that of savers, and 56% percent higher than non-participants. Savers also had an income 24% higher than income of non-participants.
- *Microfinance Program Clients and Impact: An Assessment of Zambuko Trust, Zimbabwe" (2001)*, by Carolyn Barnes; found that while clients income was significantly higher in 1997 than the incomes of other groups, by 1999 the difference was no longer statistically significant, but continuing clients still earned the most.
- *The Impacts of Microcredit: A Case Study from Peru" (2001)*, by Elizabeth Dunn and J. Gordon, found Mibanco clients earned $266 pesos more per household member per year than non-participants. (Goldberg, N., 2005: 16-28)

Some additional examples of wider impact studies are:

- *Rural Credit Programs and Women's Empowerment in Bangladesh (1996)* by Hashemi Schuler; used a measure of the length of program participation among Grameen Bank and BRAC clients to show how each year of membership increased the likelihood of a female client was empowered by 16%.
- *Poverty Alleviation and Empowerment: The Second Impact Assessment Study of BRAC's Rural Development Programme" (1998)* by A. M. Husain; reported that participants of BRAC's programs who had been members the longest had significantly higher rates of contraceptive use.
- *Credit Programs for the Poor and the Health Status of Children in Rural Bangladesh" (2003)* by Pitt, Khandker, Chowdhury and Millmet; found substantial impact on

[5] Original papers found at: www.gfusa.org. Accessed in July, 2008.

children's health (measured by height and arm circumference) from women's borrowing. (Goldberg, N., 2005: 29-41)

After reviewing most of the literature of the studies assessed by Goldberg, N. 2005, we found evidence that microfinance programs can increase incomes, help families to get out of poverty and have several positive spillover effects. However these facts prove specific cases over time providing just part of the story. Therefore, the effectiveness of a program in a certain year and in a certain country does not tell us if microfinance globally works for the reduction of poverty. In addition, despite of all the resources spent to carry out these studies which are expensive in nature, it is difficult to come to strong conclusions with respect to their impact. One of the biggest issues of measuring impact is that the process is technically difficult and expensive. (Copestake, J. 2007)

5. Assessment of microfinance

As we got an idea on how microfinance programs have brought benefits to the poor not only directly but also spillover effects in the lives of many, we also can figure out that microfinance services for the poor as a useful tool, if not well implemented could even be harmful for development. Microfinance is not a panacea which turns all loans into profit for all the poor and helps them suddenly to get out of poverty. This can take years and it depends on the logic of the borrower and client.

Some critics of microcredit programs like Woller, G., blame the market's orientation many providers have adopted leading not only to supply ineffective services but also to not reach the very poor. This exclusion, whether by self-selection, loan officers, or peer pressure of the groups, seems to be the prevalent tendency. Also, microfinance institutions (MFIs) seem to be "focusing in the products and services they *could* produce rather than the products and services costumers *want* them to produce; on *institutional* needs rather than on *customer* needs" (Woller, G. 2002: 306).

In the same line of thought, reviewing the achievements of the so called "microfinance revolution", Matin, I., Hulme, D. and S. Rutherford, concentrate on the necessity to design and deliver better financial products focusing on the poor and most poor. For this they took into account the debate about how finance and poverty reduction are determined by the different meanings of who the poor are and the origins of poverty. They state that microfinance certainly serves as a platform used by the poor to raise their own possibilities to come out of poverty. Emphasis is given to the relevance for MFIs to supply financial services that increase the depth of outreach serving the poorest people. This is the degree to which the products offered meets the poor's specific needs by designing the products to their real needs. (Matin, I., Hulme, D. and Rutherford, S. 2002)

Microfinance programs are usually judged for being too dependent on subsidies and not self-sustainable. According to Morduch, J., there are also reasons to suspect of microfinance as a "too good to be true story". Poverty alleviation by giving loans apparently is an old idea (1950s to 60s), which has been tested as a failure because loan-repayment rates in some cases often dropped more than 50%, the subsidies costs were too high and not always resources reached the targeted groups but others. As well, many programs continue to be subsidized directly through grants and indirectly though soft terms from donors, thus creating dependency. On the other hand some programs that are financially sustainable are not precisely the ones characterized to serve the poorest of the poor. (Morduch, J. 1999)

Other reviews of microfinance are based on the idea that even though very poor people have been able to achieve significant loan impact, they are the exception rather than the rule. This is because when lenders supply their credits to the poorest there is a relatively low total impact on household income, whereas if they focus on the not so poor higher impact is achieved. For many lender institutions the tradeoff can often be moved by appropriate innovations in institutional design, in particular modifications to savings, loan collection, and incentive arrangements for borrowers and staff. However, there are few institutions which do this adequately and sustainably (Mosley, P. and Hulme, D. 1998).

To conclude, I believe that despite of the critics and the difficulties to measure the impact of microfinance on poverty alleviation there are a lot of benefits derived from this industry. My argument is that more than specific quantitative results are changing the lives of many poor who maintain an industry which has been rapidly developing and is growing. Part of the issue may be that those qualitative impacts are not evident enough as they don't occur from night to day.

Most of the critics are based on the common believe on evaluating social impact as a finite result and not as a process, like it should be. The analysis should take into account a combination of qualitative and quantitative facts that structure a progression of efforts which will eventually lead to a major common goal: poverty alleviation. For this, one should expect different degrees of benefits as we found various types and qualities of poverty in the world. It could not be different as microfinance is a global tool which in principle aims to battle poverty doing its transformation depending on the context.

Chapter II. The "double bottom line" in microfinance: Financial sustainability and social performance

1. Microfinance commercialization and "mission drift" of MFIs

The microfinance industry has increasingly grown in the past decades as more capital sources have increased. According to Morgan Stanley, MFIs have expanded their customer base by approximately 25% annually (Morgan Stanley, 2008: 4). Even though supporters of this sector are usually IFIs, multilateral development banks and socially motivated donors and investors, also diverse investors from the private sector are injecting commercial capital. These include: insurance companies, pension funds, commercial banks and private equity firms which have scaled up microfinance due to its potential for high social impacts and its possibilities to attract market-based returns.

As this growth assumes an increase of assets within MFIs it also creates some constraints which are worth mentioning. When MFIs develop in size some of them face difficulties as not having the capacity to manage themselves accordingly (for example to attend the increasing number of transactions and to expand their products and services). And not only that, but it is not an easy or an inexpensive task to be profitable and at the same time struggle to provide more integrated products and services -if the aim is to continue to benefit the poor-.

Another probable consequence of growth is that some non-for-profit MFIs could decide to change their status to for-profit institutions, diversify their funding sources away from donors or development banks and even search for regulation (Fitch Ratings, 2008: 14-15). Some MFIs in this case drive away from their target low-income customer base and tend to measure their activities based only on financial indicators, such as loan repayment rates, financial sustainability and efficiency. It should be taken into account that efforts towards poverty reduction may not be necessarily part of the social mission of all MFIs and other microcredit providers, which interest is just to be financially sustainable.

In other words, some MFIs in the race for commercialization and financial status will tend to suffer from “mission drift” or will be working hard to accomplish financial viability at the expense of their initial social mission. This in turn, can seriously affect their “*raison d’ être* as institutions and therefore affect its beneficiaries. With such scenario the microfinance sector is looking for more transparency and accountability regarding the operations of MFIs, who despite of their growth needs still want to maintain their social principles and responsibility towards the poor.

On the other hand, microfinance commercialization is considered by some to be positive and essential for MFIs nowadays. With more profitability and loan volume derived from the increase of financial and social intermediation not only more clients are benefited, but also some MFIs will be willing to provide more social services as: education, health and training on business development. “Commercialization can thus maximize MFIs’ impact on poverty alleviation” (Morgan Stanley, 2008: 3).

Seen like this, the long-term success of the industry would depend not only on profitability but also on the achievement of social goals. In this line of thought, microfinance commercialization could be an opportunity for many financially sustainable MFIS to be more competitive by providing more integrated services to the poor. Since many of these MFIs successfully work in developing countries, the twofold goals of financial viability and social impact should not be mutually exclusive, as they could more easily earn the trust of microloan borrowers and of policymakers in those countries.

2. Double bottom line in microfinance: Trade-off or balance between financial sustainability and social performance

2.1 Definitions and justification of social performance assessment

We can say that MFIs interested in avoiding “mission drift” are aiming not only to maintain a strong financial sustainability as any profitable business would do, but also to complete this by undertaking a constant social performance assessment (SPA) in order to accomplish their social mission. This subject is well touched within the debate on the "double bottom line" in microfinance. But in order to address this debate, some main concepts regarding social performance will be introduced.

Social performance (SP) is understood as the process by which an MFI transforms its social goals into achievements -in terms of benefits for its clients-. Thus, in general, if an MFI's social objective is to serve poor and excluded people, and to improve their quality of life, this should be reflected as a result of the services this MFI has offered to its clients. In turn, the MFI becomes socially accountable to its clientele and hence, socially responsible.

Definitions of social performance vary slightly depending on the authors and organizations that use them. But there has been consensus within the microfinance industry regarding one definition: *"The effective translation of an institution's mission into practice in line with accepted social values that relate to reaching larger numbers of poor and excluded people; improving the quality and appropriateness of financial services; creating benefits for clients…"*[6]

BOX 1. SOCIAL PERFORMANCE FRAMEWORK

INTENT AND DESIGN
What is the mission of the MFI?
Does it have clear social objectives, and are systems designed to achieve those objectives?

▼

ACTIVITIES
What activities will the MFI undertake to achieve the mission?

▼

OUTPUT
Does the MFI serve poor and very poor people?
Are the products designed to meet their needs?

▼

OUTCOME / IMPACT
Have MFI clients experienced social and economic improvement?

Source: http://www.microfinancegateway.org/resource_centers/socialperformance/definition

Therefore, when we talk about social performance assessment (SPA), we refer to the evaluation of the level at which MFIs meet their social goals. Normally such evaluation focuses on impact but this is just one element of social performance. SPA looks at the whole process by which impact is created. It includes an analysis of the declared objectives of institutions, the effectiveness of their systems, and services in meeting these objectives, related outputs and its benefit effects in the lives of clients.[7]

[6] http//www.microfinancegateway.org/resource_centers/socialperformance/definition. Accessed date: 25/01/2008.
[7] http//www.microfinancegateway.org/resource_centers/socialperformance/definition. Accessed date: 25/01/2008.

The SP framework in Box 1 above has been accepted by the industry to describe how social performance is about many different dimensions. Different SP initiatives choose to assess social performance through focusing on specific dimensions and not necessarily on the whole. Some organizations like the Consultative Group to Assist the Poor (CGAP) and the Ford Foundation assess SP through looking at outcomes whereas the *Comite d'Echange, de Réflexion et d'Information sur les Systèmes d'Epargne- crédit* (CERISE) focuses on intent, activities and output -but not on outcomes and impact-[8].

The practice of SPA by the different stakeholders within the microfinance industry stems from the necessity to address the "double bottom line" debate and the so called "mission drift" of many MFIs. In this process MFIs search to define for themselves or with the help from other stakeholders which social indicators might best demonstrate that social goals are taken into consideration within the normal MFIs' operations.

In addition, evaluation of SP is important to improve MFIs' programs in order to achieve the social goals set in their mission statements, to be accountable towards clients and increase transparency and many practical benefits to industry stakeholders: it creates more client-centered organizations; demonstrate blended returns to donors and investors; permits social performance benchmarking; and facilitates better financial performance.

Another concept which is relevant to define is "outreach". It points out the extent to which MFIs and their services reach the poor directly, increasing their participation in the market process and empowering large number of poor people. It is the final goal of MFIs in poverty reduction (Yaron, 1994: 49-70). It can be measured in terms of the number of clients, average loan size, percentage of women clients, range of financial and non-financial services offered to the poor, etc. Therefore, not only financial sustainability can be measured but also SP can be determined in terms of outreach indicators.

Only by measuring SP an institution would be able to know how well it is

[8] http://www.microfinancegateway.org. Accessed in Nov. 1, 2008.

providing products and services, and moreover if the targeted clients are reaching these and in which level. According to (Matin, I., D. Hulme and S. Rutherford S., 2002) the depth of outreach problem of MFIs can be seen in terms of demand and supply forces. Most studies focus on the demand side (for example concluding that not all the poor use the services adequately). But it is fair to say that those demand constraints are caused by certain supply side factors like the nature of the service provision. Thus, it can be said that an improvement in the institutional side services (such as better products design and incentive arrangements for borrowers and staff) can make an impact in the client's lives deepening the outreach.

2.2 Double bottom line debate: the need of balance

Currently the debate about MFIs efficiency and sustainability is being centered on "the double bottom line" referring to two different and relevant approaches for the microfinance industry: financial sustainability and SP. Some authors like Greeley, M. 2003 talk about both perspectives for MFIs in terms of financial sustainability and poverty reduction (regarding financial and social values). Despite the fact that both perspectives acknowledge that supply-led approaches to products and services of MFIs are not sustainable or enough, they reflect differences in which this industry should evolve.

The main discussion remains on how to be financially or socially sustainable (or both). This debate is making strain on MFIs to justify their existence by making emphasis on reaching the demands of poor people and maintain financial sustainability. Moreover to obtain a dual target of profit and social mission poses reputational risks, associated with operating in the low-income market segment which is *perse* a challenge for this industry. In other words, MFIs face increasing demands from social or "double bottom line" investors to document and quantify their financial and social performances (Fitch Ratings, 2008: 1-19). These demands expose the industry to outside scrutiny and additional regulatory risks.

Nowadays the majority of MFIs' funding sources are mainly "socially" motivated, rather than purely profit driven. According to Fitch Ratings, 2008, microfinance investments have been "in fashion" over the last years, in part due to the increased interest of socially responsible investments. "The 80 or so MIVs attract primarily investors motivated by the double bottom line returns of microfinance" (Fitch Ratings, 2008: 17). Hence, in case of an MFI not behaving responsibly or ethically as expected, or because of the lack of consistent tools for SPA the MFIs' funding is susceptible of being affected.

Additionally, to assess the SP of an MFI is becoming necessary in terms of reviewing that the ultimate beneficiaries are in fact positively impacted. Not only because an MFI has "faithful" clients, this means their life conditions are better. They could be returning because they are indebted and need to acquire new debts to pay and not because the MFI is providing them with the kind of products and services they need. Thus, SPA plays a key role to review the quality of services, client satisfaction and the actual improvements in the clients' lives.

Also, while acknowledging that demonstrating impact is not only expensive but difficult, including SPA into the regular activities of an institution or by performing social performance management (SPM), the MFI can create the practices needed to show its operations do create change. SPM refers to "the systematic assessment of performance relative to social objectives and the use of this information to improve practice".[9] In other words, SPM process is used by MFIs to assure their social mission is accomplished through their work at all levels.

For these reasons, MFIs are expected to be pursuing the double bottom line objectives in order to get funding to be able to operate and keep on serving the poor –if that is their social mission-. But this challenge represents costs that arise when engaged in a process that involves measuring the many aspects of "being social".

[9] http://communities.seepnetwork.org/edexchange/node/622 - Accessed date: April 28, 2008. P. 64.

3. Cost-effectiveness of maintaining a double bottom line

One of the concerns of taking into account SP with the same weight as financial sustainability is that the later could be harmed. It might be argued that social aspects are financially costly for an institution to be focused while trying to carry on its operations. Moreover, to be able to measure and report on social indicators, MFIs would need not only to be reporting already on their financial status (not all are doing it), but at least to agree on which indicators would be the most significant to report on according to a defined criteria.

The struggle posed by the double bottom line debate states many repercussions to be faced by the microfinance industry's stakeholders. These are translated in terms of costs and reputation when taking into account the trade-off costs: the costs of reaching certain poverty outreach will have implications for achieving financial sustainability according to the context (depending on the type of poverty). Any type of targeting involves that the cost recovery interest rate will be higher (identification and operational costs). Other costs accounted are the direct financial market costs (because of smaller loan sizes and riskier portfolio). Thus, "quantifying these costs and the associated welfare benefits is a key industry challenge" (Greeley, M. 2003: 10).

When in this paper reference is made to cost-effectiveness, it is used as criterion to define how able an MFI is of maintaining social and financial objectives throughout its normal operations. Accordingly, an MFI will be cost-effective if it is self-sustainable and gainful not only in profit terms but in the quality and quantity of social outcomes derived from its operations.

It is important to recognize that each type of MFI will have a different perspective to cover the costs of providing services. For most formal financial institutions this effort is paramount since financial sustainability is vital. For most NGOs, even though they are expected to operate efficiently (covering their costs as much as possible) they are not expected to generate a profit as it is not usually an objective of their mission. However, there is a breed of NGOs popularly called "business NGOs" which are tending to transform into financial institutions since their involvement in financial intermediation activities is high and thus, for them it is relevant being able to recover their costs. (Ledgerwood, J., 2000: 64)

Another aspect to consider when weighting the costs of providing further than financial intermediation services to the poor is that depending on how financially sustainable the MFI is, it will be more or less dependent on subsidies to cover these costs. This taking into account that social intermediation services may require subsidies for a longer period than financial intermediation but these are eventually removed; enterprise development services may or may not require subsidies depending on the capacity of the clients to pay for them; and social services commonly require ongoing subsidies (Ledgerwood, J., 2000: 63-82).

Accordingly, if to offer certain services means higher costs for the institutions this will certainly represent a high dependency on subsidies for institutions not so financially viable. These costs need to be recovered –if that is the logic- or at least be acknowledged by the MFI in order to provide the services with or without subsidies. Hence, if MFIs decide to provide social services should be aware of the costs involved either to assume them or to inform their investors and/or donors about the implications this causes.

Many critics of microfinance’s integrated approach argue that if social services are more expensive these should be accounted separately from financial activities, or provided by other agencies different than MFIs as the cost of recovery may not be possible in the long run. But on the other hand, many MFIs seem to be cost-effective as they have shown capacity of being self-sustainable and being able to provide social services at the same time (Ledgerwood, J., 2000: 79-80). These are attracting more investments and subsidies needed from their donors and investors.

Moreover, some MFIs defend the provision of additional services to the poor considering their clients need more than just credit. Therefore they provide social intermediation and/or social services to help their beneficiaries to overcome their lack of entrepreneurial experience, social exclusion, limited self confidence, etc. An example of this is the case of the NGO Freedom from Hunger (FFH). They have a program called "credit with education" based on group lending, where in a cost-effective way they use the regular group meetings to give learning sessions at the same time.

As a result, the members of the group identify poverty-related problems they face and are encouraged to find common solutions appropriate to the location. Practitioners of this program believe that there might be costs of not providing education for their clients, such as epidemic outbreaks, loan growth stagnation and member dropout due to illness of children (Ledgerwood, J., 2000: 81).

The issue with this approach is that the gains of further services for the poor are difficult to measure. For example the value of knowledge, skills or education a person gains from training is difficult to assess. Most important, organizations as FFH differ in their attitudes towards covering the costs of education with the profits of their operations. Some consider education as a social service which should be subsidized by grants. Others believe that the "marginal cost of education can be charged to the village banks, because it makes the members better financial service clients by improving their family survival skills, productivity and management skills". (Ledgerwood, J., 2000: 82).

An important aspect of SPA is that it represents additional costs for the institutions regardless of the products and services it is providing. To better understand this, it is necessary to do a case by case analysis reviewing whether the MFI is financial sustainability enough to cover the costs derived from conducting SPA (for example monitoring of operations to follow-up their clients and get satisfaction rates). Nonetheless, many institutions consciously doing SPA and SPM are being cost-efficient regarding their double bottom line. The next session will take account of some of these cases.

3.1 Cost-effectiveness of social performance assessment: Case studies

This section refers to two case studies from a list of six organizations which have included SPA and SPM in their operations. The organizations not mentioned here are: The Covelo Network, Honduras; Finrural, Bolivia; PRADAN, India; Vola Mahasoa, Madagascar. For each case it was observed that MFIs can develop and implement cost-effectively their own tool to assess their performance in line with their financial status. The results vary depending on the context and the organization's needs.

- *Prizma in Bosnia-Herzegovina*

Prizma is an MFI based in Mostar, Bosnia-Herzegovina which by 2001 had reached full financial self-sufficiency. Its mission is to improve the quality of life of poor women by providing long-term access to quality financial services. So as to assess if it was achieving its social goals this MFI created three tools: a poverty scorecard, an exit monitoring system and market research focus group discussions. A study published on September 2004 by Gary Woller explains the cost-effectiveness of these tools.

The study analyzed client retention rate as indicator for benefit and demonstrated how increases in client retention would increase profitability of Prizma's joint enterprise loan, based on figures for average loan cycle profits. Reductions in the client drop-out rate of 50%, 25% and 10% were modeled, concluding that even smallest improvements in client retention have significant effects of profits that would cover the costs of the SPA tools (Woller, G., 2004: 41-42). Analyzing the three activities separately, Prizma would need to retain 78 clients (1.1% of clients) for one loan cycle to cover the costs of the poverty scorecard; 24 clients (0.4% of clients) for one loan cycle to cover the costs of the exit monitoring system; and 50 clients (0.7% of clients) for one loan cycle to cover the costs of the market research focus group discussions. Table 1 bellow shows details on break-even analysis.

Table 1. Summary of break-even analysis (Prizma)

Assessment activity	Cost	Break-even increase in client retention	Equivalent percentage point drop in weighted average drop-out rate
Poverty scorecard	$21 692	78	1.1
Exit monitoring	$6 605	24	0.4
Focus groups	$13 759	50	0.7
Total	$42 056	152	2.2

Source: (Woller, G. 2004: 50)

The study verifies the assumption that undertaking SPA activities as client evaluation and monitoring can be costly as observed (US$42.056 are the costs of conducting the three tools). But although the costs were high, the benefits were higher. For only a small incremental increase in client retention, this MFI was able to cover the costs of the SPA tools and generate significantly higher profits.

Nowadays Prizma has integrated these assessment tools into its operational processes. For instance, the poverty scorecard plays an important role as it became a goal-setting for new and active clients to measure the poverty outreach and the poverty impact. Hence, significant long-term gains from SPA are expected. (Woller, G., 2004: 49-51).

- *Small Enterprise Foundation in South Africa*

The Small Enterprise Foundation (SEF) is an MFI located in the Limpopo Province of South Africa. It runs a program called “The Tshomisano Credit Programme” (TCP) which only targets women who live below half of the poverty line. For this, SEF developed an institutional system for monitoring social performance: “Impact Management” (IM).

This system is based on a constant monitoring system of the trends in the well-being of its clientele. As ongoing tools to monitor changes in the livelihoods of clients, SEF uses: client-level indicators, dropout monitoring, vulnerable groups and centers, and management information systems (MIS). The basic tool is an interview that questions on subjective (for example satisfaction with food) and objective indicators (as household income and expenses) about the client status (Baumann, T., 2004: 28-40).

From 2002 to 2004, SEF's TCP went through a crisis of massive client dropouts. As a result, they conducted a study where they interviewed SEF's clients and staff to understand their different motivations. It was disclosed that the high dropouts were a consequence of staff field workers' incentive system which preferred portfolio growth over quality of services –apparently due to pressure from donors on SEF to be financially sustainable-. The MFI was able to correct this issue and dropouts started to fell rapidly.

Moreover, SEF attributes the improvement of its social performance to its monitoring system to identify the issues and verify the causes. This tool ensures that the MFI keeps serving very poor clients sustainably as seen in Table 2 bellow:

Table 2. Return to SEF impact management investment, 06/02-12/03

TCP Interest income/ IM costs	*Amount*	*Rate of return to IM investment*
Cost of IM during the period	$32 029	
Income above hypothetical May 2002 'stagnation' level	$369 350	1153%
Income from improved client retention	$118 333	369%
Imputed income from programme growth	$251 017	784%

Source: (Baumann, T., 2004: 39)

Here we can observe that an additional income is earned during the period that SEF invested in IM and also that improved client retention is caused by IM. Thus, SEF has proven to cost-effectively manage its double bottom line. And not only that, but also has demonstrated that impact can be better measured over time than at any set moment. (Baumann, T., 2004: 39-40)

As we could appreciate both cases demonstrate that despite of the assumed costs that SPA and/or SPM could cause, also it is possible to achieve a double bottom line. This might be a long-term process but could bring many benefits for the MFIs interested in avoiding "mission drift". Moreover, even if the cases are isolated examples of successful stories, they constitute proves that it is possible to be cost-effective in microfinance.

In sum, SPA and SPM are becoming more popular as the industry commercializes. These provide different stakeholders with regular information about SP of MFIs, which is increasingly growing in practice. Apart form the studies cited above, many different cost-effectiveness studies funded by the *Imp-Act* Consortium show that implementing assessment tools can improve the overall effectiveness of the MFIs in terms of social goals and increased financial efficiency (IFAD, 2006: 32).

Chapter III. Social Performance Assessment (SPA): The process

1. How is the microfinance industry assessing social performance and to what extent?

The purpose of this Chapter is to describe what measures have the microfinance industry been undertaking to assess SP. Also it illustrates who are the stakeholders involved in this process and how they are working to define social indicators to reach balance between financial and social sustainability. Whether the stakeholder is a practitioner organization, donor or social investor, network, rating agency, etc. she/he will focus on certain social indicators or poverty alleviation assessment methods according to specific criteria.

MFIs as practitioners within the "SPA movement" are starting to use different strategies and mechanisms that help them to reach these objectives. For these institutions the process of SPA allows them to demonstrate in a continuous basis that their operations can be cost-effective. It also aids them to show socially motivated investors that they have used well their money as the MFIs might have responsibly used it. "Some MFIs have even self-imposed standards on information provision…More than 1,100 institutions are reporting financial indicators on the MixMarket[10]…" (Fitch Ratings, 2008: 18).

From the perspective of donors and investors of microfinance, they are interested in SPA because they can get more information from MFIs activities and choose one to invest in according to its priorities. In order to do this they consider the positive and negative, social and environmental consequences of investing as well as do an exhaustive financial analysis. Also, they relay on the information given by the MFI or get it with the support of other institutions like rating agencies and audit firms. These stakeholders help in the SPA process not only by providing funds but also by: setting requirements for MFIs to get access to funds; participating in the planning process of an MFI; influencing

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[10] The MixMarket: Microfinance Information Exchange, Inc. is an online information marketplace that promotes knowledge sharing and collaboration between MFIs and prospective investors and clients. (http://www.mixmarket.org/)

the MFI to ensure strong management committed to improve double bottom line; making sure that the MFI reports on certain specific social indicators.[11]

Other important actors for SPA are the rating agencies which seek to evaluate social risk: risk of not achieving a social mission; and social performance: likelihood of contributing social value. There are four main specialized rating agencies: M-CRIL, Planet Rating, MiroFinanza Rating and MicroRate. Each one has a framework or rating scale to do SPA by evaluating practices and scoring SP indicators against benchmarks or best practices.

The kind of products that social ratings agencies offer to its clients (MFIs) are two types of rating: *comprehensive* and *standard.* Both review the MFIs internal information and capacity to accomplish its social objectives. The difference between them is that the comprehensive or enhanced rating collects client-level information -in case the MFI does not count with this information- to evaluate its depth of outreach and the quality of services supplied. MFIs will take one approach or the other depending on its needs or the price it is willing to pay (SP Map, 2008: 111-127). See Annex 2 for an example of the social rating of Buusaa Gonofaa, an MFI in Ethiopia done by Planet Rating in 2007.

With respect to other players within the microfinance industry, we can also name the network associations, whose main interest is to facilitate investments in the sector. The role they play varies from transfer of knowledge to capacity building of stakeholders. Also they support the industry by disseminating and promoting best practices, serving as a bridge between MFIs and other developmental organizations, advocating for an enabling policy environment, attracting and encouraging cooperation among donors, etc. Some of these organizations are: SEEP Network[12], the CGAP, SPTF[13], CERISE[14], and

[11] http://communities.seepnetwork.org/edexchange/node/622. Accessed April 2008).
[12] SEEP Network: Small Enterprise Education and Promotion Network
[13] SPTF: Social Performance Task Force. Crated in 2005 by the Ford Foundation, the Argidius Foundation and the CGAP. It is in charge of learning sharing, dissemination of findings, building industry support, and moreover to defining social performance as well as tackling issues about SPA and SPM. It also organizes the industry annual meetings between the member stakeholders interested in these topics.
[14] CERISE is a network of four French microfinance support network with partners throughout Africa, Asia and South America.

Imp-Act Consortium[15] among others.

2. Tools for SPA

As mentioned before, currently the microfinance industry is heading to achieve more transparency and thus, making sure that information is flowing between the different actors involved. Within this frame many initiatives have born not only towards exchange of knowledge among them but also to promote accountability to beneficiaries of microfinance.

One of the most relevant efforts from the industry regarding SPA is the design of a Social Performance Map which was created by the SEEP Network's SP Working Group and presented publicly online in April 2008. It is a compilation of different SPA topics and initiatives, which brings together the different tools available in the industry to evaluate poverty and client conditions, to rate social performance and to perform SPM among others.

The SP Map's main objective is to make the process of assessing SP more transparent showing especially practitioners are doing the "right thing" by providing microfinance services to the poor in line with their social mission. Also, within the global movement towards Corporate Social Responsibility (CSR), the SP Map seeks to promote institutional accountability of MFIs towards its clientele. The SP Map targets all stakeholders in the industry providing the most recent information and experience for these to be able to make decisions regarding SPA and SPM.

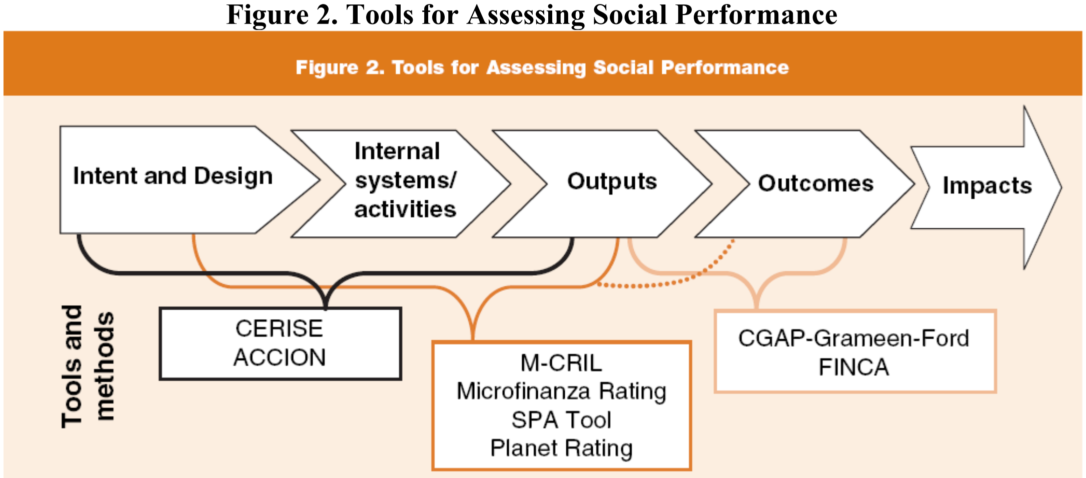
In addition, it is important to mention that the *Imp-Act* Consortium published recently their latest guidelines for SPM called: *Putting the "Social" into Performance Management: A practice based-guide.* This practice guide is based upon the experience and lessons learned of 45 MFIs with the aim to help practitioners of microfinance to manage and achieve their social mission through strengthening their operative systems

[15] The *Imp-Act* Consortium's partners include: CARD MRI, EDA Rural Systems, Freedom from Hunger, CRS Project MISION, MFC, Grameen Foundation-USA, IDS, and the Microfinance Council of the Philippines.

and maintain a double bottom line.[16]

This "global movement" promoting SP is very heterogeneous not only for the variety of stakeholders involved, but also for the tools each one uses to assess SP at the different dimensions of the process. Figure 2 shows how different stakeholders participate within the framework of the SPA process (See Box 1 in Chapter 2) and the tools they have develop to undertake it. It just gives an idea on where these specific organizations fit in the process, but the amount of organizations that have developed their own tool has not yet been quantified (over 180 at least). And many more tools are still in process to be developed-

Figure 2. Tools for Assessing Social Performance



Source: CGAP Focus Note No. 41. http://www.cgap.org. Accessed on June 2007. Also found in (SP Map: 2008: 133)

Table 3 below describes in more detail how the eight stakeholders from the diagram above work using their tools within SPA. It was prepared based on: Box 1. Social Performance Framework (on page 22) and on Figure 2.

[16] http://www2.ids.ac.uk/impact/ Accessed in October, 2008.

Table 3. Eight Stakeholders and their SPA Tools

Stakeholder	Organization	Tool Name	Description of assessment tool	SPA Dimension
Network	**CERISE**	Social Performance Indicators Initiative (SPI)	Evaluates intentions and actions: (1) outreach to the poor and excluded populations, (2) adaptation of products and services for target clients, (3) improvement in social and political capital, and (4) corporate social responsibility	Intent and Design, Internal systems/activities, Outputs
MFI	**ACCION**	ACCION SOCIAL Tool	Seeks to capture: social mission, outreach, client service, information transparency, association with the community, and labor climate.	Intent and Design, Internal systems/activities, Outputs
Network	**CGAP-Grameen Bank-Ford Foundation**	Progress Out of Poverty Index (PPI)	Poverty scorecards based on statistical analysis of national household expenditure surveys.	Outputs, Outcomes
MFI	**FINCA**	FINCA's Client Assessment Tool (FCAT)	Questionnaire on: demographic information, loan information, household expenditures, asset accumulation, social metrics (health, housing, and education), business metrics, and client satisfaction and exit interview questions.	Outputs, Outcomes
Government Agency	**USAID**	SPA Tool	Includes a scorecard evaluating six dimensions of outreach: breadth of outreach, depth of outreach, length of outreach, scope of outreach	Intent and Design, Internal systems/activities, Outputs, Outcomes
Rating Agency	**M-CRIL**	Social Rating Tool	Covers both organizational systems and results, including client-level, indicators. It analyzes mission statements, policies, and internal systems of the organization	Intent and Design, Internal systems/activities, Outputs, Outcomes
Rating Agency	**Microfinanza Rating**	Social Rating Tool	1st tool: Social Rating Survey - social performance dimensions: social and economic context in which the institution works; its mission, strategy, and systems; the quality of its services; its social responsibility; and client-level information 2nd Tool: Social Rating - simplified version of the first tool and excludes client surveys	Intent and Design, Internal systems/activities, Outputs, Outcomes
Rating Agency	**Planet Rating**	Social Rating Tool	Relies completely on available data at the MFI level.	Intent and Design, Internal systems/activities, Outputs, Outcomes

Furthermore, an updated version of the SPA tools available in the industry can be found in (SP Map, 2008: 142-179). The guide, called Consumer's Guide to SPA Tools in Microfinance, serves to find information on any specific tool and on the online resources, contact information to get it, etc. With this purpose it constitutes a 22 page summary tables.

In terms of social rating the industry has proposed as well a common framework. It is presented here in Box 2 and it reflects the heterogeneity of the practitioners involved in the process. To be able to rate an MFI not only its social objectives and mission are evaluated. There is an established framework that includes three components (context, process and results) including its own dimensions, which should position an MFI with respect to the others allowing to a better understanding of how it operates. This common framework should ideally be the basis for rating MFIs, in the sense that even though they have unique social missions and characteristic they all share general developmental values. Among these values the industry emphasizes corporate social responsibility (CSR) and environmental sustainability as seen in Box 2.

Box 2. Proposed Common Social Rating Framework

Component	Dimensions
Context	Country and regional development indicators (from secondary sources) MFI profile and financial services
Process: Governance, Policies, and Systems	SPM: Social performance management—mission clarity, alignment of systems, decision making SR-CL: Responsibility to clients—client protection SR-Cm: Responsibility to community SR-St: Responsibility to staff SR-Env: Responsibility to environment GA: Gender approach MG: Member governance (if member-owned institution) NFS: Nonfinancial services
Results or Achievement of Social Goals: Client and Community Levels	SG-Or: Social goal—outreach SG-Sv: Social goal—services SG-Ch: Social goal—change

Source: (SP Map, 2008: 134).

3. Poverty Assessment Tools

In terms of poverty assessment tools used by the industry, some of the latest are: a) Progress out of Poverty Index (PPI), developed by the Grameen Bank, The Ford Foundation and CGAP; and b) Poverty Assessment Tool (PAT), created by IRIS Center at the University of Maryland for the USAID.

Table 4. Comparative description of PPI and PAT

	Progress out of Poverty Index (PPI)	**Poverty Assessment Tool (PAT)**
Purpose	Provide low-cost and accurate estimate of poverty incidence; targeting; measure change in poverty incidence	Provide low-cost and accurate estimate of poverty incidence
Method	Estimate percentage of population bellow absolute poverty line using a short set of proxy indicators	Estimate percentage of population bellow absolute poverty line using a short set of proxy indicators
Source of Information	Existing data from recent national households survey	Existing data from recent national households survey; primary data collection by IRIS on nationally representative sample
Derivation Method	Unique process based in part on Logit regression	Selects the most accurate model for each country from a pool of 8 potential regression methods.
Poverty Lines	Extreme poverty: US$1 DPCE[17] adjusted for PPPs[18]	Extreme poverty: US$1 DPCE adjusted for PPPs
Types of Indicators	Simple, objective, practical, and objectively verifiable that show variation over time	Simple and practical that show variation over time

Source: (SP Map, 2008: 183-184).

The reason why these are more described here instead of other conventional mechanisms to evaluate poverty levels is that these ones are derived from actual poverty lines and thus their precision is known. Some of the standard methods are: a) poverty scorecards, which are not always user friendly; b) outcome indicators: housing conditions, access to services, children's education, etc., tend to be difficult to collect and interpret; c) poverty proxies: housing index, food security, wealth ranking, etc., are complicated or not linked to poverty lines (SP Map, 2008: 180-184).

Despite of the efforts done by the industry, the existence of so many choices of indicators and tools could be confusing for inexperienced practitioners of SPA.

[17] DPCE: daily per capita household expenditures
[18] PPPs: purchasing power parities

Moreover, in the pursuit to establish defined SPA tools and social indicators for the whole industry, they might be putting barriers to the local needs of each practitioner. This could be harmful if priority is not given to the context and other intrinsic characteristics of every stakeholder.

On the other hand, the definition of common social tools and indicators would facilitate the performance of benchmarks useful for more accurate comparisons between practitioner's operations. Indeed, it also can contribute to evaluate better the quality of services delivered to beneficiaries of the industry in a more "friendly user way".

To sum up, as mentioned also on Chapter 2 there is a sector of the microfinance industry currently running a race to achieve the double bottom line. Furthermore, as stated on the present chapter this sector is working to reach consensus regarding social indicators in order to report on them in the long run. However, there is not yet an agreement or a "developed culture" where most of the MFIs are willing to define and report their social indicators. Not even all of the MFIs report on their financial structures as a common practice, although it is getting more common every year.

An important part of these mentioned efforts of the industry towards social SPA was the creation of a pilot survey regarding social reporting in microfinance. The survey was created by the SPTF in 2007 as a pilot test aiming to minimize a list of 185 potential SP indicators into a shorter one. It asked respondents to answer "yes or no" if each one of the proposed indicators was: easy to be obtained; easy to be verified; if the indicator was relevant for the institution and will yield quality results; and if the institution was willing to publish the data of such indicator on the MixMarket. (SP Map, 2008: 189).

The main purposes of the exercise were: (1) better understand and document the process of gathering and inputting the data from the SP indicators, and (2) finalize the set of social performance indicators. Also, to promote SPA by MFIs and microfinance networks, and make them report on social data in the long-run in a common space.

The survey was undertaken through the SPTF during February-May 2008 and included the participation from over 50 MFIs, which responded fully the questionnaire giving their feedback and posting their data on the MixMarket by June 2008. The survey was launched as a pilot to make sure those institutions reported their answers within a process where they felt confident. In this way, institutions could give honest feedback regarding their own stage in the process as well as in their comments about SP indicators.

The acknowledgment of the mentioned survey is used to make a point in the present research. I am assuming that the organizations that responded the survey are more socially focused. Thus, I will use the list of respondents[19] to evaluate how their "social orientation" affects their financial sustainability. This is explained in detail in Chapter 4.

Annex 3 (pp. 3-7) provides the draft list of tentative social performance indicators agreed so far by the industry at the SPTF annual meeting in Paris, June 2008.

[19] I took this list from the qualitative and quantitative assessment of the pilot survey during the SPTF annual meeting in Paris, June 16-20, 2008.

Chapter IV. Data Sources, Methodology and Analysis

1. Data Sources

For the theoretical part of this research paper I used secondary data. These have been collected by different microfinance stakeholders and are public on the Internet. These data have been gathered from document sources such as economic papers and articles I have found in different academic magazines, as well as from virtual sources like mass media outputs publicly available on the Internet. Some of these are official virtual documents such as the SP MAP (mentioned in Chapter 3).

Regarding the empirical part of the paper, I am using secondary data from information previously gathered by the Microfinance Information Exchange, Inc. (Mix Market). These data are publicly available at: http://www.mixmarket.org/.

2. Methodology

2.1 Analysis of Secondary Data: Descriptive statistics

The methodology I used to statistically describe and analyze financial indicators gathered from my data sources was the following. For each indicator I calculated means, maximum and minimum values, as well as the standard deviation and variance. Moreover, I computed a significance test to reinforce my hypothesis that: *Socially Focused MFIs (SF MFIs) are reaching a balance between financial sustainability and social performance with respect to the industry as a whole"*, as will be observed further on. See Annex 4.

In this part my aim was to compare the financial performance of a sample of 49 MFIs (called from now on "socially focused or SF MFIs") and a global sample of 340 MFIs (called "Global MFIs"). 30 of the Global MFIs were also socially focused. The descriptive statistics of Global MFIs were taken directly from the MicroBanking Bulletin of Spring 2008, available on-line. For the SF MFIs I calculated those statistics myself using data from each of the 49 individual companies.

Through this comparative analysis, the aim is to determine whether there is a positive or a negative relationship between social performance and financial performance. The financial indicators of each group, the SF MFIs and the Global MFIs, are compared to assess whether socially focused MFIs do significantly differently from other MFIs in their financial performance. This would also allow observing to what extent SP is in balance with the MFIs' financial performance.

It is important to note at this point that when I did the preliminary analysis of the data, there was a bias in my results. I was comparing data of 340 MFIs against the group of 49 MFIs but soon discovered that 30 of this 49 were already included in the 340 MFIs. Hence, I had to recalculate my data excluding the 30 repeated in the 340 MFIs sample to find the mean, maximum and minimum values, standard deviations, and variance, of the revised sample of 310 MFIs. Annex 4 of the paper shows calculations for 340 MFIs and for 310 MFIs. Ultimately, I compare the 49 SF MFIs to the group of 310 Global MFIs and hence remove the bias.

Therefore, I needed to calculate all the descriptive statistics for the group of 310 companies. Not being able to gather individual information for each of the 310 companies, I used various methods to deduce the statistics from the information I had on the 340 group and the 30 individual SF MFIs. Those methods are described bellow.

To find out the mean of each indicator for the 310 MFIs (which are now the revised "Global MFIs" sample) I used the following equation:

[340 (MEAN of 340 MFIs)] – (Sum of 30 SF MFIs to be removed) / 310 MFIs = 23,198,380.

To calculate the standard deviation of the 310 Global MFIs sample, I had to follow a linear approximation because the information I had was not sufficient.

If we account for all the number of MFIs in this research we are talking about a total of 359 companies, which are 340 (310 + 30) plus the 19 MFIs not included in the 340. Therefore, we could have calculated the mean using a linear approximation through the following equation:

340/359 (MEAN of 340 MFIs) + 19/359 (MEAN of 19 MFIs) = 49/359 (MEAN of 49 MFIs) + 310/359 (MEAN of 310 MFIs)

So that Mean of 310 MFIs = 359/310 [340/359 (22,060,645) + 19/359 (5,862,464) - 49/359 (8,581,802)]

The calculation of the sum of the 19 MFIs can be seen in Annex 4.

I used the same kind of linear approximation to find the standard deviation since I did not have all the data for all indicators of the 310 MFIs. Indeed, the information on the 340 MFIs was aggregated data found in an on-line report as previously stated, and because of time constraints I could not go to each of the websites of the 310 companies individually to gather the necessary data. The linear approximation for the standard deviation (SD) is as follows:

{[340/359 (SD of the 340)] + [19/359 (SD of the 19)]} = {[49/359 (SD of the 49)] + [310/359 (SD of the 310)]}

Replacing the standard deviation's values in the equation:

[340/359 (119,665,277)] + [19/359 (12,477,051)] – [49/359 (18,930,232)] / [310/359] = **111,000,165.**

Unfortunately, as could be expected, the linear approximation of the standard deviation is not an accurate method. A quadratic approximation should be used but that method is too complex for the data I have. Therefore, I had to abandon the linear approximation for the standard deviation for the 310 MFIs. However, in order to perform the Z-Test I conducted below, I still needed a standard deviation. Therefore, since the 310 sample can be considered as a "sub-sample" of the 340 sample and their sizes are similar, I make the assumption that the standard deviation for the 340 sample and the 310 sample are more or less the same. Thus, we will now assume that the standard deviation of the 310 MFIs is equal to the standard deviation of the 340 sample: **119,665,277.** See Annex 4 for details of calculations.

For the maximum and minimum values I calculated the values for the 49 MFIs, and the data for the 340 from aggregated data came from the (MicroBanking Bulletin, 2008). Here also I had to estimate the maximum and minimum values for the group of 310 MFIs. See Annex 4.

To fix the data I observed that the maximum values of the 49 SF MFIs sample indicators were strictly inferior to the maximum values of the Global MFIs sample indicators. Therefore, the maximum of the Global MFIs is not included in the 30 MFIs' I removed. Consequently, taking out the 30 MFIs from the sample, will not affect the maximum values of the Global MFIs sample indicators. The maximum values are the same for the 340 MFIs indicators and the 310 MFIs indicators.

For the case of the minimum values, a similar logic would apply in reverse. If the minimum value of the 49 SF MFIs is strictly superior to the minimum value of the Global MFIs indicators, then removing the 30 companies included in the 340 sample would not change the minimum value. However, not all the minimum values of the SF MFIs sample indicators were strictly superior to the minimum values of the Global MFIs sample indicators. There were four cases where the relation was the opposite. But it could be that it is one of the 19 companies not included in the 340 sample that is biasing down the minimum of the group. Therefore, it is important to restrict the calculations only to the 30 companies we are removing. I calculated de minimum values for the 30 SF MFIs to check that their values for these indicators were strictly higher than the minimum values of the Global MFIs sample. This was the case. Therefore, removing the 30 MFIs does not affect the minimum value of the Global MFIs sample. The minimum values of the 310 MFIs will thus remain the same as those of the 340 sample. See Annex 4.

With the calculation of the standard deviation for the Global sample, I was able to compute a significance test, which reinforced the qualitative analysis that will be seen in Section 3.6. This test was useful in discussing the original assumption: how are the 49 SF MFIs handling the process of balancing their double bottom line objectives and thus, make my research more robust.

The test I chose to do this is the Z Test as it appropriately compares the means of both samples for each financial indicator of each sample and determines whether or not the means are significantly different. If the test estimates that the means are significantly different, then the conclusion will be that the socially focused MFIs perform differently than other MFIs. By this, the present research attempts not only to confirm that nowadays the microfinance industry is trying to reach consensus in its practices towards being more socially accountable and transparent. It also might demonstrate that this movement of MFIs is in the process of working towards balancing financial sustainability and SP.

<u>Test Statistic Z:</u>

$$\frac{(\bar{x}_1 - \bar{x}_2) - (\mu_1 - \mu_2)}{\sqrt{\frac{\hat{\delta}_1^{\,2}}{n_1} + \frac{\hat{\delta}_2^{\,2}}{n_2}}}$$

In the formula $\mathbf{x_1}$ and $\mathbf{x_2}$ represent the means of each sample: **$\mathbf{x_1}$= Mean of the 310 MFIs sample and $\mathbf{x_2}$= Mean of the 49 MFIs sample.**

μ_1 and **μ_2** represent the means of each population. In this case their difference is zero as the samples are from the same population.
δ_1 represents the standard deviation of the 310 MFIs sample
δ_2 represents the standard deviation of the 49 MFIs sample
n_1 = 310, representing the number of MFIs in that sample
n_2 = 49, representing the number if MFIs in that sample

The null hypothesis (H_0) and the complementary hypothesis (H_1) for this test are:
$H_{0:}$ Mean of Global MFIs – Mean of SF MFIs = 0

H_1: Mean of Global MFIs – Mean of SF MFIs ≠ 0

To do the Z Test I used the formula above to compare the means of each financial indicator of the “SF MFIs’ sample” towards the same indicators of the “Global MFIs’ sample”. In other words, the Z Test was applied to each of the 10 indicators in each of the 3 years (or 30 times).

Once the formula was applied replacing the numbers, the value obtained was compared to the critical value of the Z-distribution table to estimate it.

In order to find the critical value, I also required knowing the degrees of freedom (k) in my model. To do so, I applied the formula: **n1 + n2 -2= k,** which yields 357. For values higher than 120 degrees of freedom, the Z-distribution dictates we take the infinite □ number with a 95% confidence level. Therefore the critical value we will use to compare our results, according to the table is: **1,645**.

2.2 Justification of Data

My main goal with analyzing these data was to determine whether being more socially oriented makes an MFI financially better or worse off -on average- compared to the industry. Furthermore, this contrast will let us know how proficient the industry currently is and hopefully how will it be the in the long run by measuring its SP.

This research states the importance for MFIs to maintain a strong financial performance as any business would do, but this should be complemented by undertaking a constant social performance assessment in order to accomplish their social mission.

3. Comparison of selected indicators of “SF MFIs” sample and “Global MFIs” sample

3.1 General characteristics of data

- Number of SF MFIs invited to answer the “social reporting” pilot survey: 107

- Number of SF MFIs who participated: 57 (responded online); 54 completed the survey fully; the available list of actual participants who completed the survey shows a total of 50 known MFIs. From these 50, only **49** were considered since one of them (Cordial Microfinanzas, Argentina) has not yet reported its financial indicators on the MixMarket.

There are various reasons why only 50 MFIs fully responded the survey, which are stated in detail in (Sihna, F., 2008: 1-105). Among these, there was a consideration of the time consumed to answer the survey online. The average time was 114 minutes but it could take longer depending on who responded within the institution. Regardless of who did it (director, research manager, etc) no single department could have completed the range of questions included by themselves without consultation with other departments.

Also, there were some issues of interpretation of the survey as respondents had to answer "yes" or "no" if they agree or disagree. But for many cases if they did not know what to say because probably they were not aware of current outcomes of certain processes but will know in the future, there was no option to express it. Another point is that some questions and terms were understood in different ways among respondents such as: women's empowerment, member governance, hired employment, etc.

Moreover there were a few technical issues as answering a survey on-line is not easy for all locations in the world, so the reach of the survey was limited. Also, it was not possible to download one's responses, and there was, for some cases, a lack of consistency in the dates for which data was requested. (Sihna, F., 2008: 2-4) Most importantly, respondents knew that responses would be assessed and shown publicly, which would be a strong dissuasive factor for some participants. As this is a new process not all organizations might have started to include these practices into their operational systems and therefore, they would be exposed if responding.

It is relevant to mention that a lot of MFIs do not yet report on their financial indicators, therefore they might not be "there yet" in reporting social indicators. Social reporting is a relatively new process within the industry and there is not yet a general consensus on what, how and where to report. In any case, there were 50 respondents from a sample of roughly 100 invitees. This is almost 50% and I consider this number as fairly representative of what the industry is facing currently.

- Legal organizational type of respondents: NGOs, Non Banking Finance Companies (NBFC), Cooperatives or Credit Unions, and Banks. For the qualitative and quantitative analysis of the survey (Sihna, F., 2008: 1) all are considered to be MFIs because they provide banking services to the poor. See Annex 6 for details on organization structure of these MFIs.

- The percentage of MFIs per region (Africa, Asia, ECA, LAC, MENA) can be seen on Table 5 (See Annex 5 for bar graph):

Table 5. World REGIONS represented	**Number of SF MFIs**	**% of the Sample**
Africa	5	10%
Asia	17	35%
ECA. Eastern & Central Asia	5	10%
LAC. Latin America & the Caribbean	15	31%
MENA. Middle East & North Africa	7	14%
Total SF MFIs Sample	**49**	100%

Source: Data taken from Excel sheet calculations and the MixMarket (http//www.mixmarket.org/).

- The descriptive analysis was done using three years of data (2004–2006): the 49 chosen SF MFIs have been reporting financial indicators for at least three consecutive years (2004-2006). It is important to clarify most of the MFIs being assessed have not reported on previous or future years within this trend. Also there are cases of missing data as seen in Annex 4. Some MFIs did not report all data for all years.

- Other aspects of the data:

It is important to underline that the MFIs considered as “socially focused” constitute a small sample with respect to the “global sample”. And as mentioned before 30 of the SF MFIs’ sample are included in the Global MFIs’ sample.

3.2 Qualitative observations

One of the challenges of this research is to demonstrate that the SF MFIs have special characteristics which might motivate them to mainly work for the public good or on behalf of the poor's. As I have explained at the end of Chapter 3, I consider them to be "socially focused" because of their expressed interest and participation in a public pilot survey regarding SP. But this reason might seem a little light as a standalone explanation.

However, we know as a fact these 49 organizations decided to respond to a social reporting survey from a group of 107 organizations from all over the world who were invited. And we also know that they chose to answer because they believed it was important for this information to be gathered, which shows their social consciousness. We also know that they took action despite the fact that their information was going to be shared publicly and assessed at the annual meeting of the SPTF -one of the most important and attended events of the industry in the past 3 years-. This fact alone proves that these 49 institutions are involved in a process for strengthening their double bottom line at the expense of being benchmarked and compared within their peers. Moreover, this shows there is a commitment from the SF MFIs with the SPA movement and therefore, there might be a correlation with the industry's effort of providing tailored products and services for the poor.

Moreover, with the intention of acknowledging the SF MFIs' intentions and trying to give more weight to the fundamental assumption that these institutions are socially oriented, I attempted to catalog them starting from an analysis of their own characteristics. Also, it is important to take into account that the 49 institutions themselves are heterogeneous from many points of view: they represent over 30 countries from 4 regions of the world which makes it more difficult to put them in the same basket (see Table 5 and Annex 5 for detailed percentages of world region represented by this sample). Another point is their financial and social structures are dissimilar not only because of their cultural differences but also because their aims and social mission might be divergent since their *raison d'être* varies from one another.

Nevertheless in order to continue to classify these MFIs I went to the profile of each one of them to see in detail which of these mentioned characteristics makes them evidently more “social” than only profit-led MFIs. A profile showing each of these MFIs’ profile can be observed in Annex 6. This description includes: current legal status of the MFI, type of regulation, products offered, percentage of the MFI’s operations comprised by microfinance, other services provided by these institutions if any, their main founding sources, and largest funders.

Many MFIs’ profiles gave information on the types of services which some of these institutions are providing additionally from financial intermediation. But in some cases as the information is presented, it is not necessarily clear if these services take into account mere complementary social intermediation or if they go beyond providing social services and enterprise development services, and at which level. Also we don’t have the necessary information to know the degree of dependency on subsidies from each institution because most of them did not report on it. Consequently, we assume the 49 institutions listed are taking mainly a minimalist approach (since the percentage of their activities are mainly dedicated to microfinance activities with very few exceptions), but also some of them provide services within an integrated approach if we account for some MFIs which reported on these types of services.

After learning a bit about the nature of the “SF MFIs”, we can say that these are socially oriented by their structure and by the type of services they offer to the poor, although the profiles’ descriptions do not lead us to establish that these -due to their characteristics- are in fact more socially oriented than the industry or that they are remarkably differentiated from the called Global MFIs. But, we can still say these MFIs are doing an effort to provide products and services for the poor. In most cases these go beyond credit and cover health services, education, training and consulting, and others such as business development services. These services entail a number of building capacity elements so that the poor can complement the services and make a good use of the loans they are provided with, and at the same time aim to improve their quality of life and raise their living standards. See Annex 6.

To better assess the type of approach taken by the 49 sample of MFIs it would be necessary to evaluate each one of them to know more details about what they do. But not only that: a complete analysis of the quality of these services should be done in order to comprehend the degree to which these institutions are aiming to sustain a “double bottom line” or if it is not the case. Unfortunately, this is not within the scope of this paper.

Even though the qualitatively analysis sheds much light on the social nature of the products and services offered by the SF MFIs sample, it was completed with a quantitative analysis of the data following the methodology explained before. The next sections present the statistical results.

3.3 Indicators selected for the comparison

In Table 6 we find the indicators assessed per MFI, per year (2004-2006) for SF MFIs and Global MFIs.

Table 6

Indicators Assessed (2004 – 2006)	
Gross Loan Portfolio (US$)	Return on Assets (%)
Capital/Assets Ratio (%)	Operational Self-Sufficiency (%)
Number of Active Borrowers	Financial Revenue Ratio (%)
Women Borrowers (%)	Operating Expense/Loan Portfolio (%)
Average Loan Balance per Borrower (US$)	Portfolio at Risk>30 days Ratio (%)

The chosen indicators measure financial sustainability with five basic criteria: a) financing structure and size; b) outreach; c) overall financial performance and profitability; d) efficiency and productivity; e) portfolio quality and risk. From these indicators it is relevant to take into consideration that the outreach criterion although it is expressed in financial (percentage and monetary) terms it is referring to indicators which aim to account for social characteristics or measure at some point the extent of social performance of the institutions in question.

I will try to define these indicators in simple words to explain a bit more what I mean with being financially sustainable and efficient:

a) Financing structure and size indicators: These measure the financial composition of an institution which shows how it is capable to be sustainable through a period of time.

- Gross Loan Portfolio (US$): It measures the amount of money handled by the MFI that is in the hands of clients (loans).

- Capital/Asset Ratio (%): This indicator measures how much of the money handled is actually from the MFI. In other words it shows if an MFI performs by sufficiently managing its own capital resources (overall capital sufficiency). It includes earnings, liabilities, equity, and debt. It does not include donations and grants.

b) Outreach indicators: These measure qualitatively and quantitatively the type of clients reached by an institution and their level of poverty.

- Number of Active Borrowers: Presents the actual number of borrowers with loans outstanding.

- Women Borrowers (%): Presents the percentage of active women borrowers over the adjusted number of Active Borrowers.

- Average Loan Balance per Borrower (%): Presents the Adjusted Gross Loan Portfolio over the Adjusted Number of Active Borrowers. For this research this indicator is taken as to show how poor are the borrowers. So, the lowest this indicator appears, the poorer the borrower will likely be.

c) Overall financial performance and profitability indicators: These measure the institution's income in relation to the structure of its balance sheet. "Profitability ratios help investors and managers determine whether they are earning an adequate return on the funds invested in the MFI" (Ledgerwood, J., 2000:220)

- Return on Assets (ROA) (%): It is an overall measure of profitability that reflects both the profit margin and the institution's efficiency. In other words, it measures how well the institution uses all its assets.

- Operational Self-Sufficiency (OSS) (%): It indicates the MFIs' ability to cover all its costs with its financial revenues. If the OSS is less than 100% the MFI is not financially sustainable in the long run. "Some MFIs define operational self-sufficiency as generating enough operating revenue to cover operating expenses, financing costs, and the provision for loan loses." The problem is that not all institutions account for financing costs into their OSS because not all earn financing costs in the same way, which makes it difficult to generalize (Ledgerwood, J., 2000: 217).

- Financial Revenue Ratio (%): It is a measure of profitability and financial sustainability as it shows the total amount of revenues from the MFIs' loan portfolio and other financial assets over the total assets of the MFIs.

d) Efficiency and productivity indicators: These provide information on the volume of business that is generated (output) for a given resource or asset, and on the cost per unit of output. They are used to compare performance over time and improvements in the MFIs' operations. (Ledgerwood, J., 2000: 212)

- Operating Expenses/Loan Portfolio (%): It is an indicator of the overall efficiency of a lending institution measuring the costs for the institution of delivering loan services. The lower the operating expense ratio is, the higher the efficiency will be. It should be said that the outcomes of these indicators might be affected by the fact that MFIs are not homogeneous in the nature of their activities. Thus expenses will vary differently within MFIs.

e) Portfolio quality and risk indicators: These ratios measure the quality of the institution's portfolio as their name indicates. Among these indicators we find: arrears rate, ratio of delinquent borrowers and portfolio at risk (Ledgerwood, J., 2000: 207) among others.

- Portfolio at Risk 30 > days Ratio (%): It shows the proportion of the MFIs' portfolio that after 30 days of not being repaid is in risk. The lower the portfolio at risk ratio is, the higher the quality of portfolio will be.

3.4. Comparison of selected indicator's "on average" for year 2006: Analysis

In Table 7 below, a comparison between SF MFIs and Global MFIs can be seen showing the means of the indicators analyzed for year 2006, which is the most recent financial activity reported on "The MicroBanking Bulletin, Spring 2008"[20] as a document available at the MixMarket web page (http://www.mixmarket.org/ accessed several times to gather data through July to October, 2008). The fourth column represents the mean reported for the Target Market Peer Group[21], which are the MFIs observed by being under the low end or poorest category (average loan size of less than US$150).

Table 7[22]

Indicators for 2006 MEANS	Socially Focused MFIs (49)	Global MFIs (310)	Target Market (low end)
Gross Loan Portfolio (US$)	18,890,636	41,193,058	26,607,542
Capital/Assets Ratio (%)	36.10%	32.66%	36.89%
Number of Active Borrowers	45,571	91,555	164,828
Women Borrowers (%)	70.14%	65.01%	83.93%
Average Loan Balance per Borrower (US$)	583	1,011	234
Return on Assets (%)	4.02%	0.76%	0.14%
Operational Self-Sufficiency (%)	111.95%	123.83%	117.51%
Financial Revenue Ratio (%)	27.69%	29.51%	32.73%
Operating Expense/Loan Portfolio (%)	26.45%	24.16%	31.44%
Portfolio at Risk>30 days Ratio (%)	2.25%	4.96%	4.11%

Financing Structure and Size Indicators

- **Gross Loan Portfolio:**

The table numbers tell us that the Gross Loan Portfolio of the Global MFIs (US$ 41,193,058) is on average double the Gross Loan Portfolio of the SF MFIs (US$ 18,890,636). This means that the Global MFIs disburse larger loan, which can be seen as well in the Average Loan Balance per Borrower (US$) indicator.

[20] Microfinance Information Exchange, Inc. "The MicroBanking Bulletin". Issue No.16 Spring 2008. Pp. 1-72.
[21] The bulletin Tables classify MFIs into three categories –low end, broad, and high end- according to the average balance of loans served. For international comparison, this balance is stated as a percentage of local income levels (GNI per capita).
[22] Summary Table using data from Annex 4 and the MixMarket (http//www.mixmarket.org/).

When comparing the Average Loan Balance per Borrower of the SFI MFI sample with the same indicator of the Target Market lower end benchmarks we observe:

-For the Means: SF MFIs = US$583 vs. low en Target Market MFIs = US$234

This shows that the SF MFIs might be targeting a slightly higher clientele than expected. It may be that some SF MFIs may be really trying to target the low end portion of the population, but some other SF MFIs might be trying to serve different types of clientele due to other reasons. For example, trying to improve their profitability by targeting less poor beneficiaries.

Maximum value for 2006	Minimum value for 2006
SF MFIs: US$ 219,047,933	SF MFIs: US$ 3,646
Global MFIs: US$ 3,024,872,608	Global MFIs: US$ 159,569

- **Capital/Assets Ratio (%):**

Comparing the ratios we can see that they are quite close but Global MFIs have on average a lower ratio than the SF MFIs, which could be explained by the fact that Global MFIs might be financing their assets with debt -since they are larger in size and have more access to debt financing-.

Here also the SF MFIs can be compared more closely to a low end population Target Market. The average ratio is 37.63% for SF MFIs and 36.89% for Target Market (low end), which means both groups are quite similar.

Maximum value for 2006	Minimum value for 2006
SF MFIs: 93.18%	SF MFIs: 5.05%
Global MFIs: 105.40%	Global MFIs: -111.00%

<u>Outreach Indicators</u>

- **Number of Active Borrowers:**

We can observe from the comparison that the Global MFIs reach out on average to the double the number of borrowers as the SF MFIs. This was to be expected since

Global MFIs generally have a larger network of branches; their clientele is aware of their existence and the products they offer. It seems SF MFIs still need to do more advertising and build a reputation.

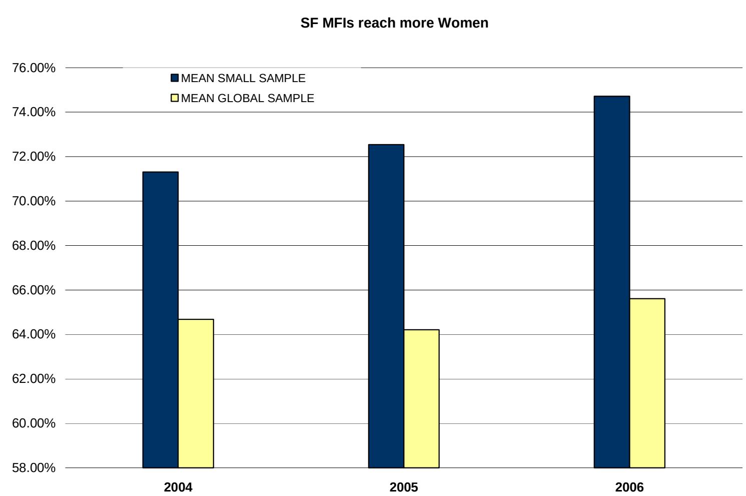
Maximum value for 2006	Minimum value for 2006
SF MFIs: 405,558	SF MFIs: 17
Global MFIs: 5,121,561	Global MFIs: 161:

- **Women Borrowers (%):**

In both samples the mean is over 50%, which shows the SF MFIs are more focused on lending to women on average than Global MFIs. I would like to underline that this indicator may be showing that the industry in general is still inclined to try to serve women as main borrowers, which is one of the principles with which microfinance idea started over three decades ago. Graph 1 shows trends of this indicator.

This indicator for the SF MFIs is comparable to the poorest category of peer group, which confirms that women tend to be poorer than men.

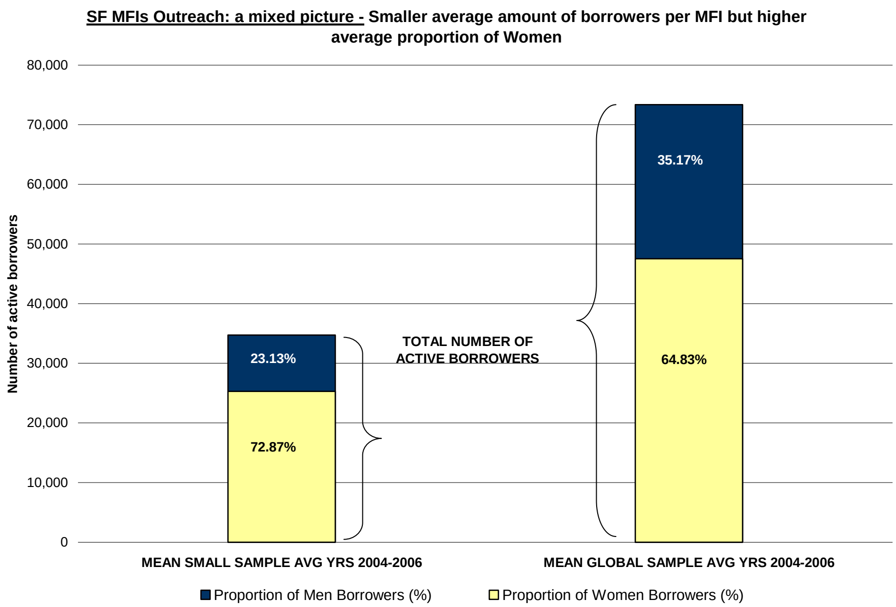
Graph 1



Maximum value for 2006	Minimum value for 2006
SF MFIs: 100.00%	SF MFIs: 8.00%
Global MFIs: 100.00%	Global MFIs: 16.10%

Graph 2 below shows that even though SF MFIs have on average less number of active borrowers than Global MFIs, they have on average higher percentage of women borrowers.

Graph 2



- **Average Loan Balance per Borrower (US$):**

The mean of their Average Loan Balance is lower for SF MFIs (US$ 583) than the mean presented for Global MFIs (US$ 1,011). This could mean that SF MFIs target the poorer population, who will generally ask for smaller loans. It could also mean that the SF MFIs themselves do not have access to the financing needed for larger loans, or that they are not able to cover the risks and guarantee larger loans.

Maximum value for 2006	Minimum value for 2006
SF MFIs: 4,660	SF MFIs: 37
Global MFIs: 8,490	Global MFIs: 45

Overall Financial Performance and Profitability

- **Return on Assets (ROA) (%):**

For the ROA, we can see that SF MFIs are on average as four times as high as

Global MFIs. So, we can say that for SF MFIs there might be correlation between their financial and SP, since these MFIs are more profitable on average than the Global sample MFIs.

Maximum value for 2006	Minimum value for 2006
SF MFIs: 19.17%	SF MFIs: -53.89%
Global MFIs: 24.20%	Global MFIs: -68.50%

- **Operational Self-Sufficiency (OSS) (%):**

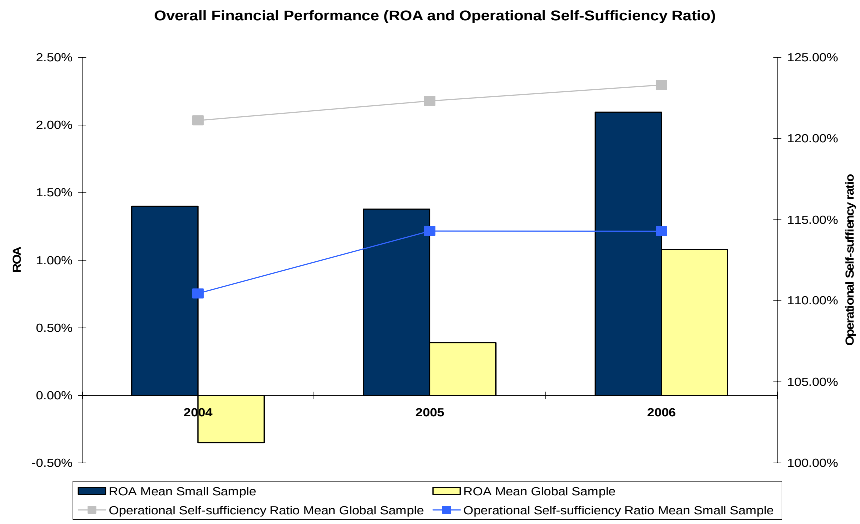
Even though for both samples of MFIs their ratio on average is above 100%, for Global MFIs is relatively better on average than for SF MFIs. This finding may be due to the fact that SF MFIs present on average higher Operational Expenses. For some of them, being more socially oriented could mean that more time and resources would be spent to be able to provide additional services to their clients (like education or training). This could also mean that some SF MFIs are closer to clients and invest more on personal relationships to best meet the needs of each client.

The OSS ratio for SF MFIs can be closely compared to the ratio of the Target Market low end as they are not too far apart.

Maximum value for 2006	Minimum value for 2006
SF MFIs: 198.41%	SF MFIs: 2.16%
Global MFIs: 275.40%	Global MFIs: n/a

See Graph 3 for trend of OSS and ROA indicators.

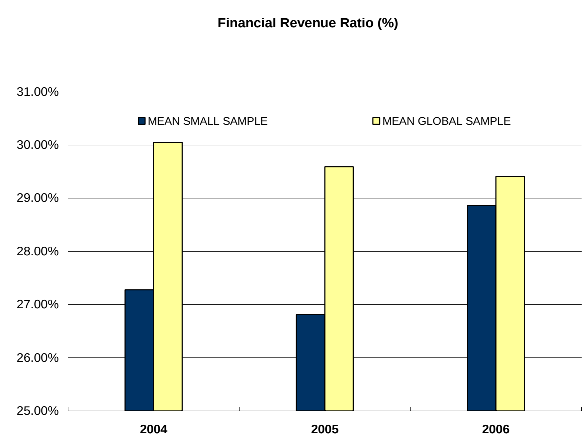
Graph 3



- **Financial Revenue Ratio (%):**

As we observe this ratio indicates SF MFIs and Global MFIs are on average similar, since their Financial Revenue Ratios are not very far from each other, but SF MFIs are relatively less profitable than Global MFIs. This could be in part because the sample of SF MFIs might be trying to lower the interest rates for their clients, whereas the Global MFIs might be charging higher interest rates. See Graph 4 for indicator trend.

Graph 4



Maximum value for 2006	Minimum value for 2006
SF MFIs: 56.30%	SF MFIs: 7.92%
Global MFIs: 79.90%	Global MFIs: 8.80%

Efficiency and Productivity

- **Operating Expense/Loan Portfolio (%):**

The Operating Expenses are on average a bit higher for SF MFIs (26.45%) than for Global MFIs (24.16%), which means the sample of SF MFIs are less efficient than the sample of Global MFIs, since it seems to be more costly (per dollar) for SF MFIs to lend money to their borrowers, to pay salaries to their staff and to maintain the general systems of the institutions. Also as said before, SF MFIs seem to be spending more by providing further services to their clients.

Maximum value for 2006	Minimum value for 2006
SF MFIs: 108.57%	SF MFIs: 4.28%
Global MFIs: 112.80%	Global MFI: 2.50%

Portfolio Quality and Risk

- **Portfolio at Risk>30 days Ratio (%):**

Observing the means in the table, we find SF MFIs have on average a lower Portfolio at Risk Ratio than Global MFIs, which tells that the repayment of their rates in a month period is on average higher. This could be explained as the tendency of some socially oriented MFIs to be more client-led by focusing on their client satisfaction and maybe they are monitoring them through more efficient information systems.

Maximum value for 2006	Minimum value for 2006
SF MFIs: 30.43%	SF MFIs: 0.00%
Global MFIs: 78.60	Global MFIs: n/a

3.5 Comparison of average of percentage changes of means from 2004 to 2006: Analysis

In order to complete the proposed quantitative analysis, I computed annual percentage changes from years 2004 to 2006 and obtained the average among them per indicator, to see how much percentage points these varied throughout the selected years.

See Annex 4.

Financial Structure and Size (2004-2006)

Gross Loan Portfolio (US$)		**Capital/Assets Ratio (%)**	
SAMPLE	Average % Change	SAMPLE	Average % Change
SF MFIs	**48.85%**	SF MFIs	**-3.80%**
Global MFIs	**33.30%**	Global MFIs	**-9.30%**

The gross loan portfolio indicator has increased more on average percentage points for the SF MFIs sample than for the Global MFIs sample, although is clearly increasing on average for both samples. This means the SF MFIs are growing more in size on average with respect of the Global MFIs, which had by 2006 a gross loan portfolio on average as twice as big as the gross loan portfolio of the SF MFIs.

The average percentage change for the capital/asset ratio indicator shows a tendency to decrease less for the SF MFIs than for the Global MFIs, even though both decrease on average percentage points for the period 04-06. The Global MFIs sample could be financing part of their assets with debt than SF MFIs, which in the long run is better for SF MFIs independence on investors' loans.

Outreach (2004-2006)

Number of Active Borrowers		**Women Borrowers (%)**		**Average Loan Balance per Borrower (US$)**	
SAMPLE	Average % Change	SAMPLE	Average % Change	SAMPLE	Average % Change
SF MFIs	**42.73%**	SF MFIs	**5.87%**	SF MFIs	**13.49%**
Global MFIs	**21.81%**	Global MFIs	**0.99%**	Global MFIs	**12.41%**

The number of active borrower's indicator presents an increase in average percentage change for both samples but this increase is higher for the SF MFIs. Although for year 2006 the amount of active borrowers in the Global MFIs was double what of the SF MFIs, this number has not tended to increase for these as much as for the SF MFIs during the period of analysis.

Regarding the percentage of women borrowers' indicator, we can observe how on average the percentage change for the SF MFIs has increased five times compared with the same indicator's percentage change for the Global MFIs. This could indicate that the SF MFIs may have a special interest of wanting to serve more women as borrowers.

The average loan balance per borrower indicator seems to have increased annually on average percentage points for both samples, but less for the Global MFIs sample than for the SF MFIs sample. Therefore, the SF MFIs sample shows a propensity to increase the average loans per borrower closer than the Global MFIs.

Overall Financial Performance and Profitability (2004-2006)

Return on Assets (%)		**Operational Self-Sufficiency (%)**		**Financial Revenue Ratio (%)**	
SAMPLE	Average % Change	SAMPLE	Average % Change	SAMPLE	Average % Change
SF MFIs	**21.11%**	SF MFIs	**5.07%**	SF MFIs	**12.93%**
Global MFIs	**138.80%**	Global MFIs	**0.89%**	Global MFIs	**-1.41%**

With respect to the return on assets indicator, we can observe a higher annual percentage change increase on average for the Global MFIs than for the SF MFIs. This shows that even though for each individual year, the average ROA for SF MFIs was more than the double for Global MFIs, Global MFIs could be increasing their efficiency on average because their profit margin tend to get stronger.

For the OSS indicator we observe that the SF MFIs sample are on average more prone to change in percentage points than the Global MFIs sample. This could be connected to the fact that the SF MFIs seem to be decreasing their expenses as seem in the next indicator below and hence, could be working towards better covering their costs with their financial revenues.

The financial revenue ratio presents an increasing average percentage change for the period (04-06) for the SF MFIs sample of 12.93%, and a decreasing average percentage change for the Global MFIs sample (-1.41%). The latter sample has shown each year a tendency to decrease on average in the proportion revenues over their total assets contrary to the SF MFIs which have a tendency of increasing their revenues.

Efficiency and Productivity (2004-2006)

Operating Expenses/Loan Portfolio (%)	
SAMPLE	Average % Change
SF MFIs	**-4.18%**
Global MFIs	**-9.69%**

For the SF MFIs sample the percentage change through years 2004 to 2006 is negative as well as for the Global MFIs sample, but we can observe that for Global MFIs was lower than for SF MFIs. This shows that in terms of financial efficiency the Global MFIs could be better-off than the SF MFIs as on average the industry seems to be decreasing more their expenses and thus, being more productive in their processes.

Portfolio Quality and Risk (2004-2006

Portfolio at Risk > 30 days Ratio (%)	
SAMPLE	Average % Change
SF MFIs	**-7.09%**
Global MFIs	**10.96%**

The average percentage change for this indicator shows that the SF MFIs have a tendency to decrease their risk of non-repayment of their loans in comparison to the SF MFIs which are increasing it by 10.96%. Thus, one could say that on average during that period the "socially focused" MFIs in general were working towards a better relationship and follow-up of their clients.

3.6 Results of the Statistic Z-Test

As mentioned and explained in the methodology, I computed a Z-Test to compare the means of the two samples. See Annex 4 for details on calculations.

The Z-Test's results confirmed that for 6 out of 10 indicators (these include 2 of the 3 outreach indicators) the means obtained for the "SF MFIs" prove to be statistically significantly different from the means obtained for the "Global MFIs". For these 6 indicators: Gross Loan Portfolio (US$); Operational Self-Sufficiency (%); Financial Revenue Ratio (%) –for years 2004 and 2005-; Portfolio at Risk 30 > days Ratio (%); Number of Active Borrowers; Average Loan Balance per Borrower (%), we can observe their values are higher than the critical value (1.645). Thus for these cases I reject the null hypothesis and can conclude that there is a statistically significant difference between the two samples.

On the other hand I accepted the null hypothesis for: Capital/Assets Ratio (%); Return on Assets (%); Operating Expense/Loan Portfolio (%); and Women Borrower (%) as outreach indicator. Hence one could say that for these indicators there is not a statistically significant difference between the two samples.

It is important to mention the fact that after the test was conducted I noticed that for year 2006, the Financial Revenue Ratio (%) value obtained is lower than the critical value. Therefore I accept the null hypothesis for this year only.

In sum, I can say that the 49 "SF" MFIs are on average more likely to be and have certain characteristics that make them worth being catalogued as "socially focused" compared to the "Global" sample of 310 MFIs. For that reason, we can say the values obtained by applying the formula are statistically significant in 6 of the cases and hence for the majority of the Z Tests performed (17 of 30).

In other words, after computing the test statistic chosen, we can confirm in good part of this research the assumption that the SF MFIs are trying to balance their financial sustainability towards their SP. Moreover, this fact let us say that having participated and responded the mentioned social indicators survey was a strong indication of the key role that SPA is playing throughout their operational processes.

Conclusions

In conclusion, even though SPA is a relatively new practice within the microfinance industry it has proven that poverty alleviation is a possible goal to achieve if there is transparency on the complexity of the process. Therefore to measure the magnitude of social impacts, practitioners have to account the relevant role of their internal systems combined with ongoing monitoring of their beneficiaries. This assumes MFIs have to invest in resources to cover the costs derived from the process. And not only that, but stakeholders have to acknowledge that it takes time to quantify outcomes and thus, to demonstrate evidence.

The SPA process is challenging for MFIs interested in sustaining a double bottom line because more than assuming the institutions have a social goal, they are also supposed to follow an organizational culture. This is a set of developmental values which the MFI has to put into practice inside the institution and for the benefit of the ultimate beneficiaries: the poor. Otherwise it does not make sense to spend resources and time on for example, training their staff to deliver better services, as well as on adopting and adapting a particular poverty assessment tool among their clients.

Nonetheless, there are many cases (some reported in this paper) where MFIs demonstrate to be cost-effective when performing social practices into their operations (or undertaking SPM). Moreover, after conducting the statistical comparisons and Z-Test we observed that SF MFIs were financially viable and profitable despite of the additional costs they face by being more social. Thus, we can say that SP is driver of financial sustainability.

Nowadays due to the commercialization of microfinance, this industry is going through high pressure from different stakeholders such as donors and investors. Therefore, SP comes to justify the distribution of subsidies and grants in this sector as it shows improvements in the financial sustainability of institutions and in the clientele’s lives in the long run.

Furthermore, the process of SPA has shown that MFIs are more engaged to promote transparency and accountability towards the industry's supporters and clientele. This method will be strengthened once the last version of agreed SP indicators is released. Then, MFIs are expected to be assessed quantitatively and qualitatively using the established indicators. Hence, data to conduct comparisons and benchmarks of SP indicators will be more complete and more year trends could be taken into account. As a result, the industry would be able to improve the quality of products and services delivered and the outreach of poverty alleviation would be larger.

Given the results of the statistics calculations carried out we can confirm the hypothesis that *"Socially Focused MFIs (SF MFIs) are reaching a balance between financial sustainability and social performance with respect to the industry as a whole"*. This hypothesis is supported by the fact that SF MFIs seem to be committed with the SP process as being involved in the different networks and new initiatives promoted by the industry.

Lastly, the microfinance double bottom line debate has much more to be written about as it will be evolving. Hence, there will be many challenges and issues to be addressed and to be resolved in the future. One of them, to what extent the current financial crisis will affect microfinance. Certainly the current financial crisis represents higher risks for any type of investing including microfinance. It would be interesting to see how social investing will behave in the long run and how financially sustainable MFIs will respond to the crisis. Indeed, this could be the topic of future research proposals.

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