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Social audits in microfinance: what have we learned about social performance?

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In a nutshell

Social performance assessment has dramatically evolved during the past few years, with the development of social audits, social ratings and reporting standards. With the results of 287 SPI audits from 223 institutions in 53 countries, the database gathered by CERISE presents a huge potential for taking stock of the social dimension of microfinance practices worldwide. Following up on a study on the links between social and financial performance published in a previous MBB issue (December 2009), this article deepens the analysis of the social performance trends by MFI peer groups (size, age, continent, etc.) with a larger sample of audits. It shows for example that Asian MFIs tend to target more actively the vulnerable people, while African ones are generally more participative. Among other findings, we observe in this study that not for profit institutions score generally better than for profit, while bigger MFIs are generally less oriented towards the poor and the excluded but score better on the other social performance aspects. On the financial side, we see that direct/individual targeting of the poor is correlated with higher operating expense ratio. However indirect methodological or geographical strategies of targeting, as well as other social performance aspects, such as participation, social responsibility and service adaptation, are linked with better results in productivity, costs and portfolio quality.

Introduction

Social performance assessment has evolved a lot in recent years, with the development of social audits, social ratings and reporting standards. CERISE has been a key force behind these developments, as pioneer of the Social Performance Indicators (SPI) tool. Developed in 2004 in collaboration with a wide range of practitioners (now members of the ProsperA¹ network), the SPI is an open access tool² that assesses the principles, actions and corrective measures implemented by an MFI to achieve its social objectives. The indicators are used to score the MFI's social performance based on four key dimensions divided into three criteria (see table). The SPI includes all of the core SPTF/Mix Social Performance Standards and most of the optional indicators of this reporting format³, making it easy for MFIs to enhance transparency through MIX.

Dimensions	Criteria
Dim 1. Targeting and outreach	C1.1 Geographic targeting C1.2 Individual targeting C1.3 Pro-poor methodology
Dim 2. Products and services	C2.1 Range of traditional services C2.1 Quality of services C2.3 Innovative and non-financial services
Dim 3. Benefits to clients	C3.1 Economic benefits to clients C3.2 Client participation C3.3 Social capital/Client empowerment
Dim 4. Social responsibility	C4.1 SR to employees C4.2 Consumer protection C4.3 SR to the community and the environment

The SPI tool assesses and analyzes MFIs' practices, thus helping them to manage social performance and improve social impact.

¹ <http://www.cerise-microfinance.org/-prospera-network->

² Available in English, French and Spanish at www.cerise-microfinance.org

³ Only questions 18-22 on Outcomes are not included, as they do not fit into the SPI framework which focuses on the other stages of social performance: intent and design, internal systems and activities, and outputs.

1. The increasing popularity of social audits

As of March 31, 2010, CERISE had received the results of 287 SPI audits⁴ from 223 institutions in 53 countries worldwide.

Profile of the MFIs using SPI											
	Peers	SPI Base		MBB 09			Peers	SPI Base		MBB 09	
Continent	Africa	66	30%	195	18%	Charter type	Bank	7	3%	82	8%
	Asia	19	9%	283	26%		Credit U	54	24%	182	17%
	ECA	5	2%	217	20%		NBFI	33	15%	338	31%
	LAC	123	55%	333	31%		NGO	87	39%	389	36%
	MENA	10	4%	56	5%		Rural B	4	2%	84	8%
Age	New	23	11%	191	18%	Scale	Small	75	37%	428	36%
	Young	33	16%	203	19%		Medium	49	24%	394	34%
	Mature	134	66%	657	63%		Large	48	24%	351	30%
	N/A	14	7%	0	0%		N/A	32	16%		

Latin American and African institutions dominate the sample (55% and 30% respectively) due to the active involvement of MFIs' apexes and socially responsible investment funds in these regions. Compared to MIX data, the sample present similar distribution in terms of age and scale. Only in the charter type category are NBFIs slightly under-represented.

SPI audit by year and type of review

		Audits	%	MFI	%
Year of the SPI review	2004	45	15,7	19	8,5
	2005	1	0,3	1	0,4
	2006	16	5,6	6	2,7
	2007	44	15,3	34	15,2
	2008	96	33,4	78	35,0
	2009	85	29,6	85	38,1
Assessment type	External	173	60,3	148	66,4
	Internal	98	34,1	64	28,7
	Test	16	5,6	11	4,9
SPI Version	SPI1	45	15,7	19	8,5
	SPI2	177	61,7	144	64,6
	SPI3	65	22,6	60	26,9
Source of the SPIs	MIV	82	28,6	76	34,1
	Network	80	27,9	70	31,4
	TA	77	26,8	49	22,0
	Other	48	16,7	28	12,6

In fourteen countries, more than five MFIs have been audited. We estimate that the vast majority of MFIs in Bolivia, Benin, Ecuador, El Salvador, Guatemala, Mali and Nicaragua have used the SPI tool. In other words, the first countries to adopt widespread use of the SPI are countries where microfinance has been called into question by governments and where willful default movements have emerged. In these countries, social audits have been used to dialogue with governments, justify changes to regulatory frameworks and public policies, and occasionally create distance from the irresponsible practices of "black sheep" MFIs.

The first version of SPI was pilot tested by 25 MFIs in 2004, and a wider public started using the tool after it was finalized in 2005. Our analysis only looks at data from 2006 (versions 2 and 3). External auditors validated most of the audits. Up until 2008, mostly networks and technical assistance providers administered the tool, either accompanying MFIs in the audit process or verifying results. Starting in 2009, several MIVs (Microfinance Investment Vehicles) started to use SPI, which has helped to diversify the profile of MFIs using the tool by attracting first-time users. The current widespread use of the SPI tool suggests it meets the expectations of practitioners, investors, apex institutions, support organizations, researchers, governments, regulators and donors alike.

⁴ The CERISE database had 320 audits as of 05/31/2010.

2. Social performance results

Distribution of SPI scores			
	N	%	Cumul.
< 35%	14	6,9	6,9
35-40%	11	5,4	12,4
40-45%	11	5,4	17,8
45-50%	22	10,8	28,7
50-55%	30	14,7	43,6
55-60%	19	9,3	53,0
60-65%	29	14,2	67,3
65-70%	28	13,7	81,2
70-75%	22	10,8	92,1
> 75%	16	7,8	100
Total	202	99,0	

Fewer than one in eight MFIs obtain very low results (less than 40%). Similarly, fewer than one in twelve score over 75%. Indeed, if we exclude the bottom and top quartiles, half of the MFIs score between 49% and 68%. The median is 57% and the average 58%.

This distribution is due to the fact that the SPI tool is standardized. It aims to be a relatively comprehensive assessment of the different dimensions of social performance. As such, we do not expect MFIs to score full points in every aspect; rather, results should reflect the institution's self-defined mission and strategy. For example, urban banks may prioritize a diverse product mix and social responsibility, while a rural cooperative will focus on targeting and participation. This is why it is so

important to refine analysis beyond the aggregated score; each dimension should be analyzed against the institution's strategic priorities. Moreover, comparing scores is only useful when institutions are part of the same peer group.

Social performance scores according to MFI peer groups

	Tous (N=204)	Africa (60)	Asia (14)	ECA (4)	LAC (116)	MENA (10)	Mixed (N=79)	Rural (N=62)	Urban (N=55)	Mature (N=134)	New (N=23)	Young (N=33)	Large (N=48)	Medium (N=49)	Small (N=75)	For Profit (44)	Not For Profit (N=141)	Bank (N=7)	Credit Union (N=54)	NBFI (N=33)	NGO (N=87)
Total SPI score	58%	54%	66%	47%	59%	54%	57%	62%	53%	58%	54%	56%	60%	61%	54%	54%	59%	59%	56%	53%	60%
Dim1-Targeting	63%	53%	77%	48%	67%	70%	61%	73%	54%	61%	66%	65%	57%	67%	62%	57%	65%	59%	53%	56%	72%
C1-1 Geog targeting	55%	48%	66%	52%	57%	66%	54%	72%	39%	53%	57%	57%	49%	62%	52%	47%	57%	48%	48%	44%	63%
C1-2 Indiv targeting	52%	40%	67%	30%	58%	49%	50%	56%	51%	52%	58%	49%	50%	53%	51%	53%	52%	60%	37%	51%	62%
C1-3 Methodol targeting	57%	51%	67%	44%	58%	68%	56%	63%	52%	55%	57%	65%	50%	60%	59%	50%	59%	44%	53%	52%	62%
Dim2-Services	62%	55%	68%	51%	65%	55%	63%	62%	60%	63%	56%	59%	69%	65%	56%	63%	61%	70%	59%	60%	63%
C2-1 Range of services	62%	58%	67%	51%	65%	40%	63%	61%	62%	64%	55%	56%	67%	70%	56%	62%	62%	77%	68%	57%	58%
C2-2 Quality of services	71%	62%	76%	56%	75%	70%	73%	68%	71%	72%	65%	67%	80%	76%	62%	72%	70%	78%	65%	72%	73%
C2-3 Innovative non fin services	54%	46%	62%	47%	57%	53%	53%	57%	49%	54%	50%	53%	60%	51%	50%	54%	53%	57%	47%	53%	56%
Dim3-Benefits	49%	54%	55%	38%	48%	35%	47%	59%	42%	50%	44%	48%	52%	49%	47%	41%	52%	39%	60%	42%	47%
C3-1 Eco Benefits for clients	50%	48%	56%	34%	52%	34%	47%	55%	47%	51%	48%	46%	53%	52%	46%	50%	49%	63%	54%	48%	46%
C3-2 Participation	48%	64%	50%	33%	42%	31%	44%	65%	37%	49%	43%	48%	50%	46%	49%	34%	53%	16%	71%	37%	42%
C3-3 Empowerment	50%	50%	60%	47%	51%	40%	50%	56%	44%	52%	42%	49%	52%	48%	47%	41%	53%	43%	53%	42%	53%
Dim4-Responsibility	56%	52%	62%	50%	58%	57%	57%	55%	56%	58%	51%	52%	63%	62%	51%	57%	56%	67%	53%	55%	59%
C4-1 SR to staff	64%	60%	67%	65%	65%	65%	66%	59%	66%	66%	65%	59%	71%	72%	57%	67%	64%	76%	59%	65%	68%
C4-2 Client protection	64%	59%	71%	61%	65%	73%	66%	60%	65%	67%	55%	61%	72%	72%	58%	66%	64%	85%	59%	62%	67%
C4-3 SR to community environ	40%	33%	49%	23%	44%	32%	37%	45%	37%	41%	34%	36%	44%	41%	36%	37%	40%	43%	38%	37%	42%

MFIs generally score highest on dimension 1, targeting and outreach (63% on average). This is indeed microfinance's main objective, one that has underpinned the creation of most MFIs. Next highest is dimension 2, products and services adaptation (62%), and dimension 4, social responsibility (56%). Dimension 3, which measures the economic and social benefits MFIs provide their clients, generates the lowest scores (49%). Indeed, this dimension implies that the MFI regularly monitors and evaluates its clients' situation, or involves them in governance—two aspects that tend to be neglected in the microfinance sector.

In terms of criteria, most MFIs score high on quality of service (C2-2). This is because it is hard to establish objective indicators that are also standardized and verifiable. Nonetheless, even if this criteria is slightly over-rated, the result suggests that MFIs pay a close attention to their clients' needs. The criteria that produces the lowest scores focuses on social responsibility vis-à-vis the community and environment (C4-3). It attempts to measure the

complex dynamics of local development, and account for environmental protection as it relates to MFIs, a relatively new concept.

From a **geographic** standpoint, the best scores have been recorded in Asia, particularly in dimension 1 (targeting), but fewer audits have been done on the continent than elsewhere (due to fewer trade associations and a less developed ProsperA membership base). Latin American institutions also score well, especially for dimension 2 (products and services). Africa tends to score high in criteria on participation (dimension 3).

Rural MFIs tend to score higher than **urban** or mixed institutions. This advantage is reflected especially in dimension 1 (targeting) and dimension 3 (benefits to clients), namely the criteria on participation and innovative/non-financial services.

Analyzing the **size** of MFIs allows us to assess the trend toward mission drift. Findings suggest that large MFIs generally target less the poor and excluded than medium and small MFIs. However, they tend to score well in the other dimensions of social performance.

Charter type appears to have an impact social performance: overall, for profit institutions score lower than non-profits. That said, if we analyze performance by governance type, banks and NGOs stand out as having similar overall scores. Banks score well in products and services and social responsibility while the NGOs emerge as targeting “champions.” NBFIs score the lowest, appearing to be caught in the middle, having left targeting strategies to NGOs, but with no clear policy concerning services or social responsibility.

3. The relationship between social and financial performance in microfinance

The most recent study on the relationship between social and financial performance was conducted in 2009 on a smaller data set⁵.

Correlation (Spearman) between social and financial performance

	Borrowers/Staff		Portfolio at Risk (30 days)		Operating expense ratio		Operational self sufficiency		Return on assets		Total Portfolio	
	All MFIs	NGOs	All MFIs	NGOs	All MFIs	NGOs	All MFIs	NGOs	All MFIs	NGOs	All MFIs	NGOs
Type of MFIs												
Number of MFIs included	167	76	162	78	166	76	159	72	172	77	175	79
Total Social Performance Score	.212**	.176	-.016	-.079	-.058	-.034	-.002	-.057	.066	-.041	.285**	.174
Dim 1. Targeting and outreach	.270**	.185	.014	.016	.091	.115	-.083	-.186	.090	-.104	-.017	-.056
C1.1 Geographic targeting	.317**	.162	-.087	-.121	-.033	-.176	-.057	-.105	.054	-.173	.057	.093
C1.2 Individual targeting	.108	-.045	.082	.154	.187*	.239*	-.084	-.244*	.053	-.103	-.022	-.073
C1.3 Pro-poor methodology	.235**	.298**	-.023	-.126	.024	.129	-.064	-.079	.098	.044	-.071	-.174
Dim 2. Products and services	-.069	-.279*	.034	.071	-.136	-.081	.066	-.069	.008	-.106	.450**	.190
C2.1 Range of traditional services	-.134	-.216	.084	-.008	-.188*	-.246*	.056	-.046	-.088	-.171	.281**	.169
C2.1 Quality of services	.094	-.072	-.037	-.096	-.130	-.059	.151	-.014	-.012	-.146	.481**	.291**
C2.3 Innovative and non-financial services	-.024	-.189	.010	.161	.053	.150	-.031	-.114	.109	.056	.219**	-.009
Dim 3. Benefits to clients	.175*	.229*	.060	-.009	-.063	.010	-.046	.008	.038	.102	.118	.000
C3.1 Economic benefits to clients	.055	.127	.054	.051	-.142	-.049	-.102	-.069	-.049	.088	.206**	.055
C3.2 Client participation	.163*	.273*	.035	-.135	-.033	.016	-.047	-.029	-.008	.015	-.003	-.077
C3.3 Social capital/Client empowerment	.142	.151	.073	.107	.008	.033	-.002	.074	.144	.170	.135	.050
Dim 4. Social responsibility	.153*	.173	-.215**	-.270*	-.104	-.166	.113	.028	.034	-.092	.459**	.476**
C4.1 SR to employees	.108	.095	-.146	-.120	-.093	-.139	.108	.021	.069	-.054	.380**	.199
C4.2 Client protection	.041	.192	-.152	-.325**	.002	-.149	.111	-.051	-.049	-.160	.304**	.409**
C4.3 SR to the community and the environment	.163*	.029	-.126	-.162	-.122	-.112	.054	.184	.078	.097	.259**	.319**
**	Correlation significant at 0.01 level		Significant convergence between social and financial performance									
*	Correlation significant at 0.05 level		Significant divergence between social and financial performance									

⁵ Bédécarrats, Lapenu and Angora (2009). *Is Social Performance Profitable*, “MicroBanking Bulletin”, n°19, December 2009.

At first glance, the dominance of green/blue cells indicates that good social performance is generally associated with good financial results. Beyond this preliminary comment observation, it is necessary to look at these results per dimension and criteria.

Our analysis confirms what many studies have found focusing on the depth of outreach, measured through proxies such as average loan size: institutions that target directly, selecting clients based on poverty levels or exclusion tend to have higher operational expenses. Such trade-off is classically explained by several key factors: the cost is proportionally higher with smaller amounts, this clientele presents higher risks, lacks of guarantees, is more reluctant to join microfinance programs and therefore requires stronger marketing, follow up as well as non-financial support.

However, this divergence of social and financial performance seems limited to individual targeting and we see that other targeting strategies to reach the poor and excluded, namely geographic or methodological, are correlated with higher productivity. In particular, we observe that more clients are deserved per staff member in MFIs that decided to operate in deprived areas where no other financial services are available, or when their services are designed specifically to reach the poor or excluded. This is intertwined with the participatory models these institutions combine with their targeting models. More client participation allows them to rely on grass root commitment to overcome the operational difficulty implied by their focus on vulnerable population.

Our analysis emphasises the importance of economies of scale for improved social performance. MFIs with the largest loan portfolios score highest in range and quality of services and social responsibility. We find that these same institutions have the best repayment rates as well as lower operating cost, but it is still unclear how far this is due to size and how far it is due to responsible practices.

Current SPI data allows us to refine these findings by peer group. For example, the observation regarding the cost of individual targeting applies particularly to NGOs, and is even associated with low OSS. For NGOs, a diverse product mix is correlated with lower staff productivity. On the other hand, those with well-developed consumer protection measures have a lower portfolio at risk.

Further analysis is needed to clarify the relationship between social performance and more complex financial performance indicators like OSS, ROE and ROA. Nonetheless, our analysis echoes the call to go “back to the basics”: the pillars of microfinance’s social utility (include the excluded, offer appropriate services, benefit clients) clearly impact the fundamentals of financial sustainability: productivity, efficiency and portfolio quality. It also shows the risks of an interest ceiling agenda, as observed in several countries, which can affect primarily the institutions that are the most active in selecting vulnerable clients, and in particular the NGOs, due to their higher operating expense ratios. Finally, it may reopen the debate of possible smart subsidies for the most pro-poor NGOs.

Conclusion

Active stakeholder involvement has made the SPI a standardized social audit tool that effectively addresses social performance assessment and management needs. With more and more institutions using the tool, we now have a critical mass of data, making it possible to characterize the social performance of MFIs according to context and type: rural MFIs tend to overcome the inherent difficulties of their operating areas by developing participatory governance models but also strong adaptation of services, and efforts towards social responsibility; NGOs tend to have strong targeting strategies and while banks appear to focus on diverse product mix and solid social responsibility policies. For the NGOs, the measures in favor of consumer protection are linked with lower portfolio at risk.

The attention being given to social performance is paying off: our analysis confirms that social performance and financial performance are compatible. It is indeed possible to have a clear strategy for sustainable microfinance—one that aligns financial, social and environmental objectives.