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Building Vibrant and Inclusive Financial Sectors: Success Indicators for Microfinance Associations

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Building Vibrant and Inclusive Financial Sectors: Success Indicators for Microfinance Associations

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The mission of the Citi Network Strengthening Program, the largest global grant program to be implemented in support of the Citi Foundation's microfinance strategy, is to increase the capacity and scale of the microfinance sector by strengthening the operational, technical, and financial capacity of twelve national and regional microfinance associations.

Special appreciation is owed to Patrick McAllister who led this global effort as well as to William Tucker, SEEP's Executive Director, who challenged us to embark on this ambitious initiative and provided us with guidance along the way. Sharon D'Onofrio and Deena Burjorjee provided substantial support in refining the indicators and finalizing this publication.

Additionally, we owe special thanks to all the association representatives who participated in the development and review process and especially to the following regional working group leaders who led the development and pilot initiatives in their respective regions:

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Jamie Bedson, Banking with the Poor (BWTP)
Francisco de Hoyos, ProDesarrollo
Dr. Wolday Amha, Association of Ethiopian Microfinance Institutions (AEMFI)

ABBREVIATIONS

AEMFI	Association of Ethiopian Microfinance Institutions
AMFA	Azerbaijan Microfinance Association
BWTP	Banking with the Poor
CGAP	Consultative Group to Assist the Poor
MFI	Microfinance Institution
MIX	Microfinance Information Exchange
NGO	Nongovernmental Organization
PAR	Portfolio at Risk
ROA	Return on Assets

Introduction

Microfinance associations operate at the meso level of the microfinance industry: between retail services providers and their customers on one side; and government, regulators, and investors on the other. Today, 70 microfinance associations in over 80 countries represent a client base of over 60 million microentrepreneurs.[1] These associations promote financial access through the development of **vibrant and inclusive financial sectors that provide appropriate services to poor and low-income people.** This access is realized through:

- strong, sustainable associations that provide demand-driven products to their respective member bases;
- a range of healthy, sustainable microfinance institutions that offer a wide range of quality services to clients at competitive prices; and
- a transparent business environment that ensures fair competition and protection for consumers.

Given the role that associations play in strengthening the microfinance sector, it is important that they clearly **identify their development goals and measure the impact of their efforts on the industry as a whole**. Progress has been made toward a consensus definition of success for microfinance *institutions,* one that combines financial and social performance. However, this publication is the first attempt to define and measure the success of microfinance *associations* in a clear, quantifiable way.

The SEEP Network, in partnership with the Citi Foundation, engaged a wide range of associations and other key industry stakeholders in a global effort to define metrics of success for the industry. Over 50 associations from all over the world contributed to this consultative process via in-person regional meetings, online conferences, Web-based seminars, email feedback, and initial piloting of indicators.[2]

The resulting consensus indicators measure the success of associations at three distinct levels: **performance** of the association itself; **results** of the association's member MFIs; and industry **quality**. Together, these measurements provide a snapshot of the success that an association has had in promoting financial inclusion.

Table 1. Microfinance Associations Success Indicators

Association performance
Member satisfaction results
Member ratio (%)
Member coverage
Core cost recovery ratio
Overhead ratio
Member Results
No. of deposit-taking members
Deposit-taking members (%)
Gross deposits
Gross loan portfolio ($)
% members with PAR over 30 days <5%
Total assets ($)
% members with positive ROA
Total equity ($)
No. active borrowers
No. active depositors
No. active insured
% women
Rural penetration
Industry Quality
Interest rate disclosure
Consumer protection
Financial transparency

1. SEEP defines microfinance associations as national and regional associations that represent the microfinance industry in a given country or region.

2. The effort to develop and pilot these indicators was led by the following associations, which volunteered to coordinate the initiative in their respective regions: AMFA (Europe and Central Asia); Sanabel (Middle East); BWTP (Asia); Prodesarrollo (Latin America); and AEMFI (Africa).

Association Performance

Goal Strong sustainable associations that provide demand-driven products and services to their member base.

Membership and Representation

Member satisfaction

Associations are member-based organizations, so it is critical that they satisfy the needs of their members. By regularly measuring member satisfaction, associations are able to better tailor their services to meet market gaps, thereby building their credibility with and support among members. An association can then leverage this confidence to engage in larger, more complex activities with greater success.

Member ratio

This indicator measures the number of microfinance service providers that are members of the association, compared with the total number of providers on the market. It is a critical measure of success, because it answers the question: are MFIs joining the association? If not, the association cannot consider itself truly successful and representative of the market that it strives to represent.

Before calculating this ratio, an association must define the market that it seeks to serve. In some markets this data may be difficult to find; the exact number of service providers may be disputed or unknown. However, an association should always attempt to ascertain the number. All associations should have this basic information about microfinance in the country or region where they operate. An association can then segment the total number of MFIs to establish the total number of MFIs *in their market* in order to calculate this ratio. Until there is agreement on the exact number of MFIs in the market, an association will have to estimate based on the best available data.

Member coverage

Equally as important as the preceding indicator is the market share represented by an associations' members, which is defined by the number of customers that they serve. In many markets, the top five to 10 MFIs can serve 80–90 percent of total customers using microfinance services. If these five to ten institutions are not members of the association, it is not as successful and representative as it could be. Stakeholders will be more receptive to messages coming from institutions that speak for a large number of customers. Thus it is important for an association to have a very high member coverage ratio. Here again, good data about the number of microfinance customers may not be readily available, but an association must take the lead in collecting this data.

Association Financial Performance

Core cost recovery ratio

Measures the relative ability of an association to cover core costs (direct expenses related to core services and the associated overhead) from its earned revenues. A cost recovery ratio allows an association to assess its ability to cover its most essential costs in the absence of outside funding. Note that how an association defines core costs will be based on its own characteristics. Core costs are comprised of: (i) core overhead, defined as the minimum administrative expenses required for the association to deliver its core services, and (ii) the costs of core activities, defined as the direct costs associated with core services. For most associations this would include, at a minimum, costs associated with holding an annual conference, advocacy activities, information exchange activities, and other activities considered integral to achieving their missions. However, core costs may be limited to core overhead only.

Overhead ratio

Measures the percentage of total operating expenses used for overhead. This indicator measures how efficiently an association manages its resources—the smaller the ratio, the more efficient the association. The ratio will fluctuate over time, increasing as associations add new products and services, and decreasing as new economies of scale are reached. However, this ratio should show a decreasing trend over time and stabilize at an acceptable level.

Member Results

Goal Associations represents a range of healthy, sustainable microfinance institutions that offer a wide range of quality services to clients at competitive prices.

Member Performance

Number of deposit-taking members

Savings is an important financial service, with an increasing number of MFIs seeking to meet the regulatory requirements for accepting deposits. This indicator is a proxy for the variety of services offered to microfinance customers, as well as for the ability of MFIs to fund growth with local capital, that is, with customer deposits. A successful association will have an increasing number of deposit-taking members, signaling its ability to represent institutions that provide a range of services to customers. In markets where MFIs are not allowed to accept deposits, this indicator will be zero; however, associations may work on changing the legal framework so as to enable them to do so.

Gross loan portfolio

Access to credit products is a fundamental element of financial inclusion. A successful association should be focused on helping its members expand their loan portfolios to ensure a greater supply of credit in the market. Where microfinance is only one part of a lender's total portfolio of loans, the gross microfinance loan portfolio may need to be disaggregated. By analyzing this figure, along with the number of borrowers, associations can assess the impact of average loan balances on portfolio growth.

Gross deposits

The volume of savings in the market reflects total deposits held by MFIs in both individual and corporate accounts. This indicator reveals client accessibility to safe places to save, as well as the availability of capital to fund portfolio growth and spur economic development. This indicator should be relatively easy to collect, as deposit-taking MFIs generally report this information to the local regulatory body. Where microfinance is only one part of an institution's financial operations, the figure may need to be disaggregated from consolidated portfolio data.

Percentage of members with PAR over 30 days < 5%

Portfolio risk management is an essential part of ensuring the long-term sustainability of microfinance institutions. Portfolio at risk measures the percentage of a lender's loan portfolio that is at risk of not being repaid. This standard indicator should be readily available from MFIs. To calculate it, divide the number of an association's MFI members with PAR over 30 days less than 5 percent by the total number of member MFIs.

Member Sustainability

Total assets

MFIs use their assets to grow and serve more customers. A growing microfinance sector can be most easily measured by growth in assets. Total assets can also be used as part of other ratios.

Percentage of members with positive ROA

Profitable institutions ensure that clients have stable, permanent access to financial services. This indicator measures the percentage of an association's members that are profitable. Return on Assets (ROA) is common broad calculation. To calculate it, divide the number of an association's MFI members with positive ROA by the total number of member MFIs.

Total equity

MFIs need equity in order to leverage additional capital for growth. The more equity that is invested in the microfinance sector, the greater its potential to meet demand for services. Successful associations recognize the importance of investment in a strong, stable industry and support members to build healthy balance sheets with sufficient equity.

Member Outreach

The goal of financial inclusion is to ensure universal access to financial services. While most official statistics are based on volume, it is important that microfinance associations seek to reach all members of the community who are excluded from formal financial services.

Number of active borrowers

By measuring the number of its members' active borrowers, an association can get a better sense of total industry outreach and how well members are closing the financing gap. While number of borrowers is a commonly collected indicator, some MFIs count the number of loans. However, borrowers often have more than one loan from the same institution. Therefore, associations should help MFIs differentiate between loans and borrowers in their reporting, and only use the latter figure.

Number of active depositors

Like the number of borrowers, this indicator is crucial for measuring MFIs progress in offering a range of financial services, among which savings is considered the most valued by poorer clients.

Number of active insured

Insurance is a fast-growing part of the microfinance landscape. It's not easy to capture the number of people benefiting from insurance with a single indicator, particularly since the benefit of insurance products more often accrue to the financial institution than the insured or named beneficiaries (e.g., credit life insurance). Therefore, while it may be easier to collect information on the number of policies, to capture the number of clients that benefit directly from insurance, the number of insured lives must be measured. A life insurance policy that insures a husband and wife, for example, represents two insured lives. A health insurance policy that insures a family of five represents five insured lives.

Microinsurance is a relatively new service and the data on insured lives may not be readily available. An additional difficulty may arise because insurance regulators are not generally familiar with microfinance or microfinance associations. Successful microfinance associations build relationships with insurers and insurance regulators, as well as help members that offer insurance collect and report on this important indicator.

Percent of women clients

Historically, women have been one of the largest groups without access to safe and sound financial services. Successful associations measure the percentage of women who are active clients as an important indicator of gender equality, as well as a proxy for reaching more marginalized customers.

Rural penetration

In many parts of the world, rural areas have the lowest penetration rates for financial services. Successful associations help members by monitoring this indicator and encouraging greater rural outreach. ***The calculation for this indicator does not compare rural clients to all clients, as may be expected***. Instead, the calculation compares the percentage of active clients from rural areas with the percentage of the country's adult population living in rural areas. The indicator allows the microfinance industry to see how equitably financial services are distributed. Thus, between countries with vastly different rural populations (e.g., 20 percent of the population compared with 80 percent), the calculation for each will show how well the industry is reaching rural areas in that specific context.

There is no standard definition for "rural" in financial services, but many governments have developed policies specific to rural areas and have thus developed a definition. When possible, it is best for an association to use the government definition for consistency. If no definition exists for rural, or if the definition is not well-suited to financial services, successful associations develop a consensus definition to track this indicator.

Industry Quality

Goal An association that supports a transparent business environment with fair competition and consumer protection.

Interest Rate Disclosure

Measures the percentage of members that uniformly disclose interest rates to customers. Leveling the playing field so that customers can compare the costs of similar products between institutions helps improve competition, as MFIs then compete on product quality rather than hidden costs. An important part of the disclosure discussion has been about how to uniformly disclose interest rate information, particularly to unsophisticated and vulnerable borrowers. Recent studies suggest that these borrowers may not understand or value an annual percentage rate–type calculation, preferring that costs be disclosed as the payment amount. Successful associations help ensure that their members uniformly disclose interest rates in ways that are most useful to customers.

Consumer Protection

Complaint resolution is used as a proxy for determining how well consumers are protected against unscrupulous or deceptive practices. Existence of a complaint resolution process indicates that consumers have some protection. Opinions differ on whether protecting consumers is a government function or an industry function, or whether consumers should organize themselves to avoid harmful practices. Ultimately, all three players have a role to play.

Where a government has established a complaint resolution process, successful associations work with that body to ensure that it is working smoothly and that complaints are resolved in a fair and timely manner. Where such a mechanism does not exist, successful associations help establish a complaint resolution process for their members, producing goodwill among customers and avoiding negative publicity generated by unscrupulous actors in the market. Finally, successful associations develop relationships with consumer advocates to ensure that they understand financial service issues, so that customers who seek out impartial, third-party information are well informed.

Financial Transparency

Financial transparency is essential for the legitimacy of the microfinance industry. This indicator measures the percentage of association members that provide regular financial and social performance reports to the association and institutions such as The MIX Market and other local prudential or self-regulatory bodies. Associations should ensure members' compliance with international reporting standards and build on local initiatives to provide meaningful, relevant reporting to local stakeholders. By providing accurate and up-to-date information on their members, associations build confidence among donors, regulators, and investors, and promote the development of standards and performance benchmarking in the industry.

Calculations, Benchmarking, and Targets

The opportunity to monitor performance over time and compare an association's performance to those of its peers is an important reason why many of these organizations are collecting and reporting on success indicators. In an effort to help set standards for the industry, SEEP has established certain basic success targets, based on industry trends to date. The targets presented below will continue to be revised and refined as available data accumulates and benchmarking for microfinance associations becomes more sophisticated. In addition, peer groups may be established to refine benchmarks, making them more valuable tools of analysis and drivers of change.

Table 2. Initial Indicator Targets

	Indicator	Target	Formula
ASSOCIATION PERFORMANCE	**Membership and Representation**		
	Member satisfaction results	Increasing	Score
	Member ratio (%)	100%	No. MFI members/Total no. MFIs in the market
	Member coverage (%)	100%	Total active clients of association members/Total active clients in the market
	Association Financial Performance		
	Cost recovery ratio	100%	Adjusted earned income/Core costs
	Overhead ratio	15%-20%	Overhead cost/Total operating expenses
MEMBER RESULTS	**Member Performance**		
	No. of deposit-taking members	Increasing	Number
	Deposit-taking members (%)	100%	No. deposit-taking members/Total deposit-taking institutions in the market
	Gross deposits ($)	Increasing	Total deposits
	Gross loan portfolio ($)	Increasing	Total loan portfolio at end of period
	% members with PAR over 30 days <5%	Increasing	No. of MFI members with PAR over 30 days <5%/No. MFI members
	Member Sustainability		
	Total assets ($)	Increasing	Total assets
	% members with positive ROA	100%	No. MFI members with ROA>0/No. MFI members
	Total equity ($)	Increasing	Total Equity
	Member Outreach		
	No. active borrowers	Increasing	Number of active borrowers
	No. active depositors	Increasing	Number of depositors
	No. active insured	Increasing	Number of insured lives
	% women	> 50%	Number of active clients who are women/Number of active clients
	Rural penetration	Increasing	% active clients who are from rural areas/% adult rural population
INDUSTRY QUALITY	Interest rate disclosure	100%	No. members who uniformly disclose interest rates/Total no. members
	Consumer protection	100%	No. of complaints resolved
	Financial Transparency	100%	No. member MFIs reporting financial and social performance info/ No. MFI members

Frequently Asked Questions

What are the benefits for associations reporting on these indicators?

An important benefit for associations that report on these indicators is the opportunity to benchmark their performance against other microfinance associations around the world. Reporting on internationally recognized standards also increases the reputation of associations with their stakeholders. Finally, these standards assist associations in setting goals and measuring their impact of their work.

Why these indicators? Most of them concern member MFIs, not the association.

The indicators described in this note are designed to measure the success of national and regional microfinance associations. They are based on the explicit role of associations in developing and improving the microfinance sector in their respective markets. It is therefore important that associations measure their results using indicators that reflect this role.

How were these indicators developed?

As part of the Citi Network Strengthening Program, SEEP engaged associations around the world and other key industry stakeholders in a global effort to define specific indicators of success for microfinance associations. It also helped develop the metrics to track them. Over 50 associations from all over the world have engaged in this consultative process.

Why aren't there more qualitative indicators?

To establish benchmarks, metrics must be standardized and quantifiable.

Will additional indicators be added?

Stakeholders agree that the number of indicators should be limited. For this reason, most indicators can be used as a proxy for other, similar indicators. While new indicators may be added through consensus, any new indicator would need to be subjected to a consultative process.

Indicator Development Process

- 2008 SEEP Global Network Summit: 45 associations agree to develop indicators of success
- 5 regional coordinators lead global initiative
- 18 associations participate in initial round of feedback
- Regional consultation meetings held in Addis Ababa, Belgrade, Beirut, Singapore, Arequipa: 56 associations
- Online conference: 182 participants
- Consultations with other industry stakeholders: CGAP, MIX, IRIS Center, Citi Foundation, BlueOrchard, MicroRate
- Initial Pilot: 8 associations

Glossary

Active clients are the total number of clients of all association members who have an active deposit account, an outstanding loan, or an insurance policy, or some combination thereof. Customers with multiple accounts are counted only once.

Adjusted Earned Income is all earned income, adjusted to account for the expenses associated with non-core services. It includes total gross revenue from core activities, including fees paid for membership services, sponsorships, foreign exchange gains and/or losses, interest, and other sources of self-generated income, plus net earned revenues from non-core activities.

Assets are the cumulative value of assets from the balance sheets of all MFI members of an association.

Borrowers are the individuals or entities that currently have an outstanding loan balance with an MFI. Individuals who have multiple loans are counted as a single borrower.

Complaint resolution refers to complaints that are recorded and tracked as part of a redress system. This system may not be connected with an association (such as a government ombudsman scheme), but should be a formal system that produces statistics on complaints resolved.

Core costs are the essential expenses that an association must cover in order to operate in the absence of outside funding. Depending on the business model of the association, these costs may be a subset of overhead costs or may be larger than simple overhead. Calculation of these costs should be defined in an association's accounting policy and tracked in the accounting system.

Earned income all revenue derived from fees paid for membership services, sponsorships, foreign exchange gains and/or losses, interest, and other activities for both core and non-core services. This sum includes all direct revenue generated by products and services..

Deposits are customer savings placed with an MFI. Generally, deposits are readily accessible by a depositor. In some cases (such as time deposits, or when used as collateral), savings access may be restricted. So long as the customer has control over his or her savings, they can be considered deposits. Savings that are contractually connected with credit (where a client must save a certain amount periodically to continue to be in good standing with a credit account) are generally not considered deposits. Contractual savings not tied to credit (where interest is tied to periodic saving) are generally considered deposits.

Depositors are customers with savings deposits.

Equity is the cumulative value of equity from the balance sheets of all MFI members of an association.

Insured lives are the number of individuals covered by all voluntary insurance policies where an association member is the insurer, agent, or broker. This indicator does not include compulsory insurance or insurance that offers no residual benefit to the insured.

Gross loan portfolio is the outstanding principal on all loans of an MFI. The figure includes current, delinquent, and renegotiated loans, but not loans that have been written off. Neither does it include interest receivable.

Market is self-defined by an association. It may be a geographic market (e.g., an association that seeks members from a specific country); a type of institution (e.g., an association that seeks only NGO MFIs as members), or a combination thereof.

Operating expenses may also be called program expenses or direct costs. These are expenses that are specifically attributable to a program area or a cost center.

Overhead refers to central administrative costs that are essential for successful program management, but cannot be identified with a specific program activity. This category of expense is often distributed among programs.

Principal at risk over 30 days is the outstanding amount of all MFI loans that have one or more installments of principal past due 30 days or more.

ROA (return on assets) signifies the amount of profit per unit of capital deployed. It is calculated by dividing after-tax profits by average assets.

Rural areas are defined by a government or other civic authority. Where no such definition exists, MFIs may use their own definition.

Uniform disclosure means that interest rates are calculated using a common formula (including but not limited to the annual percentage rate, so that customers can compare rates among institutions.

About SEEP

The SEEP Network is a global network of microenterprise development practitioners. Its 80+ institutional members are active in 180 countries and reach over 35 million microentrepreneurs and their families. SEEP's mission is to connect these practitioners in a global learning environment so that they may reduce poverty through the power of enterprise. For 25 years, SEEP has engaged with practitioners from all over the globe to discuss challenges and innovative approaches to microenterprise development. As a member-driven organization, our members drive our agenda while SEEP provides the neutral platform to share their experiences and engage in new learning on innovative practices. The SEEP Network helps strengthen our members collective global efforts to improve the lives of the world's most vulnerable people.

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