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SOCIAL RATING

PART I – Progress Towards the Development of Social Rating

The four microfinance rating agencies – M-CRIL, Microfinanza Rating, Planet Rating and MicroRate – are currently developing and piloting social rating products. The following progress brief aims to build understanding of what these social ratings are and how they may contribute to more transparency and better practice for social performance in microfinance. As a credit rating does for financial risk assessment, a social rating will be an independent assessment of an organization's social performance using a standardized rating scale – in terms of the 'risk of not achieving social mission' or 'the likelihood of contributing social value'. Drawing on current understanding of social performance, social performance management and social responsibility, the rating process will involve evaluating practices, measuring a set of indicators and then scoring them against benchmark levels, best practices, or internationally accepted standards. The process in some ways will resemble an audit in that the rater will assess the quality and credibility of systems including available data for social performance ('social accounts'), identify areas for improvement, and through the evaluation help the MFI build capacity. While achievement of social impact is the ultimate goal of social performance, impact assessment is a separate – more costly – exercise. A social rating is not an impact study. Proving that a given intervention has caused a certain social outcome is a complex econometric exercise which would not be possible within the quicker process envisaged for social rating. Instead, what a social rating can achieve is an analysis of the steps towards achieving impact: the processes undertaken by an MFI towards achieving their desired goals, and the results to the extent of analyzing outreach and quality of services provided.

With substantive testing of social rating over the past 3-5 years, and drawing upon different tools or approaches (*Imp-Act* social performance management, CERISE Social Indicators Initiative, USAID – AMAP Social Performance Assessment¹) all the rating agencies follow the same conceptual framework for social rating, (a major achievement coordinated through the Social Performance Task Force²). There are broadly two different products that are likely to be available: a 'comprehensive' rating and a 'thin' rating. Both kinds of rating include meetings with program management and review of internal information to assess operational capacity to achieve social goals. The difference between the two rating approaches lies in the fact that the comprehensive rating includes client level information to assess outreach and quality services, and collects this information as part of the rating exercise if it is not available

with the MFI, while the thin rating relies on available information which may consist of outputs (in terms of for example, number of products, average loan size.)

The current phase of piloting involves comparing the two approaches in terms of the value added by the comprehensive approach, at an additional cost compared to the thin rating. Two of the rating agencies – M-CRIL and Microfinanza Rating – are testing both approaches, and will be able to offer both a comprehensive and thin rating. Planet Rating and MicroRate currently plan to offer the thin rating product. Product decisions will depend on evidence that client level information may be essential to making a robust assessment of social performance in practice, and that this justifies the additional cost involved (for field level data collection).

The costs of social rating vary by rating agency. The prices can vary a lot depending on the dimension of the MFI, its geographical coverage (dispersion of clients); the quality of the information available at the institutional level and whether or not the social rating is done together with a credit rating which reduces the cost. Generally, a thin social rating (without field survey) may cost between 30% and 60% of a credit rating, while a comprehensive social rating (with survey) between 90% and 150% of a credit rating.

A social rating does not judge the worthiness of an MFI's mission, but seeks to convey to investors how effective the MFI has been in translating that mission into practice, in line with general social goals. In microfinance today, accepted social goals and MFI social missions take a variety of forms, but in general include: extending financial services to under-served areas, offering financial services to persons previously excluded from the banking sector, supporting micro and small enterprises, social responsibility issues, contributing to gender equity, reducing poverty, reducing vulnerability among the poor, bringing marginal groups into mainstream society, and facilitating job creation. Ideally, a social rating will complement a credit rating, which focuses on profitability and institutional capacity. The combination of financial and social analyses should enable potential – especially 'social' – investors to place funds in organizations that best serve the double bottom line of meeting an altruistic mission while demonstrating sound financial management.

As in the case of credit ratings, social rating will serve several functions. Both ultimately aim to facilitate the flow of capital into the microfinance industry. Social rating is ideally placed to facilitate social investment. By participating in the rating process, MFIs develop an understanding of key data and issues that affect their social performance and aspects to address to improve further. If an MFI has already conducted internal studies on the efficacy of its services, the independent social rating will validate those studies (or highlight weaknesses) and assess how the findings of such studies

1. For more information on these initiatives, see Social Performance Progress Brief vol. 1 no. 1 available at www.seepnetwork.org

2. For more information on the Social Performance Task Force visit www.microfinancegateway.org/resource_centers/socialperformance/article/28257

are useful for the MFI. In the long term, being subject to formal evaluations should also decrease the risk that MFIs deviate from their social missions and values. The expectation, in fact, is that social ratings will lead to development and improvement in social performance management practices to achieve deeper outreach, quality of services, client protection and socially responsible behaviors in general, just as credit ratings have led MFIs to adjust their financial practices to better achieve sustainability. The data generated through social ratings will also contribute to better social reporting and transparency in the industry informing wider stakeholders including policymakers.

PART II – Description of Social Rating Products

Four microfinance rating agencies provide social ratings: M-CRIL and Microfinanza Rating offer both comprehensive and thin ratings; Planet Rating and MicroRate provide thin ratings. The text below provides more detail on each company and its rating system:

M-CRIL (offers “comprehensive” and “thin” social ratings)

Micro-Credit Ratings and Guarantees India Ltd (M-CRIL) was the first of the microfinance rating agencies to pioneer a social rating product. It launched its social ratings product in 2005, conducting seven social ratings in the 2005-6 period and 8 audits. In addition, 11 social ratings for 2007 are nearing completion. M-CRIL's flagship social rating product is the comprehensive social rating which includes analysis of country development context, MFI model, products and services, mission, systems, portfolio data and a small statistical field sample to analyze outreach and appropriate services. If an MFI does have robust client level information, M-CRIL will assign a social rating based on verification and analysis of that data.

The comprehensive social rating is undertaken at around the same level of cost as a full credit rating, and is intended to provide complete, evidence based, information about social performance to discerning investors with strong social motivation, donors, and interested MFIs.

The M-CRIL social rating report provides information about the context in which the MFI operates, details the steps the MFI uses to translate its social mission into practice, and discusses the ways in which the MFI complies with social responsibility mandates. If the client chooses the field survey option, the report will also cover depth of outreach and client feedback on products and services. This field data can serve as baseline information for future follow up – which could be included as part of a later social rating exercise which would include an assessment of change at the client level on key development indicators. The six dimensions covered in an M-CRIL social rating are thus Context (country development indicators and MFI profile), Mission and Systems Alignment to mission*, Social Responsibility (SR)*, Social Goal Outreach (SGO)*, Social Goal Services (SGS)*, and – if data is available – Social Goal Change (SGC). The full rating report provides a graded assessment

based on four dimensions (as starred in the list). The grades mirror those for credit rating ranging from ²α++ (Excellent adherence to social mission and values) to ²γ (Weak adherence to social mission and values/no social mission or values).

M-CRIL also provides ‘thinner’ (less costly) social rating products if these seem relevant and appropriate. For more information on M-CRIL social ratings visit www.m-cril.com or email Frances Sinha at francesinha@edarural.com.

Microfinanza Rating (offers “enhanced/comprehensive” and “simple/thin” rating)

Microfinanza Rating has so far conducted 10 social ratings: 2 simple social rating tests (methodology without survey) in the Europe/Central Asia region; 1 enhanced social rating test in Africa; 4 enhanced social ratings (SR with survey) in Latin America (Nicaragua, Mexico, Peru); 1 additional enhanced social rating (SR with survey) in Nicaragua; and 2 enhanced social ratings (SR with survey) in Romania. Several other social ratings are already planned for 2008 (commissioned by social investors/MFIs/donors).

Microfinanza Rating offers two main types of social ratings: simple social rating (also called social rating without survey) and enhanced social rating (also called social rating with survey). Both versions address four areas of analysis:

1. Social mission, strategy, and systems (SPM System)
2. Social responsibility
3. SG1: Outreach
4. SG2: Quality of services³

Based on quantitative and qualitative elements of analysis, the social rating report includes:

- a. The description of the socio-economic context of the MFI operations;
- b. For each of the four areas of assessment: a detailed analysis of the MFI performance, a summarized assessment of strengths and weaknesses and an overall judgment;
- c. A final opinion of the MFI's overall social performance; once the piloting phase is completed, social rating scores will begin to be assigned as well.

The two social ratings differ mostly in terms of sources of information used. The simple rating (SR without survey) is largely based on information that the MFI can provide itself, such as data captured in the MIS and information provided in staff interviews (i.e., proxies to estimate client poverty such as loan size, gender, lending methodology, sectors financed). The enhanced rating methodology integrates these sources of information with firsthand client data (such as the % of households living below national and international poverty lines⁴, the % of clients without access to financial services, % of clients without access to basic services, household members educational level and occupation) gathered through field work-surveys to a representative sample of clients, individual interviews and

3. As far as SG 3 (Creating Change) is concerned: if up-dated and reliable information is available from the MFI or external sources (impact studies, etc), the results in terms of outcomes are described. Moreover, the systems and strategy relevant to track and achieve the impact/change goals included in the mission are deeply analyzed in the process part, and some aspects of change are addressed with respect to gender empowerment and employment issues (where relevant).

4. The 'Progress Out of Poverty Index' (PPI) is applied to measure the poverty levels of clients. For more information on the PPI contact Nigel Biggar at nbiggar@grameenfoundation.org.

focus groups. Measuring clients' socio-economic profile and getting their direct feedback results is a significant enrichment of the analysis of outreach and of service quality.

More details available at www.microfinanzarating.com and contact Micol Guarneri at micol.guarneri@microfinanzarating.com to receive an example of an enhanced social rating report).

Planet Rating (offers "thin" rating)

Planet Rating has developed a Social Performance Rating that provides an opinion on the capacity of an MFI to achieve its social goals. It is based on an audit of Social Performance Management systems and relies on social accounts available at the MFI level and secondary data about the country social and economic environment. Social performance outcome measurements, when available at the MFI level, are checked for reliability and integrated in the rating report. The evaluation covers four dimensions (1) Institutionalization of the social mission (2) Outreach (3) Service Offering (4) Social Responsibility.

Planet Rating's Social Performance Ratings are conducted with a transparent methodology and in an interactive mode and can be preceded by a training to ensure an optimal appropriation of the conclusions of the audit.

The four areas of SPR are scored from "1" (lowest) to "5" (highest). For each of them, they evaluate the intentions (clarity and consistency), implementation (efficiency) and results (comparison with benchmarks). A weighing system is then applied in order to obtain a global rating from the scores assigned to each area.

- 5. ADVANCED:** Long-lasting commitment to social goals; efficient management of social performance and social responsibility risks; institution very likely to achieve a positive social impact.
- 4. CONVINCING:** Clear commitment to social goals; reasonable management of social performance and social responsibility risks; institution likely to achieve a positive social impact
- 3. IN PROGRESS:** Clear intent to reach social goals; social performance management systems being implemented
- 2. INCIPIENT:** Clear intent to reach social goals; low capacity to manage social performance
- 1. INTANGIBLE:** Intention to reach social goals is non tangible; low level of management of social performance

As Planet Rating considers institutional sustainability to be a key element of social performance, Social Performance Ratings are only conducted for MFIs that have already undergone an institutional rating by a reputable microfinance rating agency. Missions can be conducted at the same time as GIRAFE rating missions or within the 6 consecutive months. The specialized social rating analyst spends 2-4 days on-site. Social Performance Rating fees are approximately half of GIRAFE rating fees. Combining GIRAFE and Social Performance processes provides efficiency gains that are reflected in the prices.

Planet Rating's methodology has been refined through on-site testing and collection of feedback from actors within the sector (MFIs, investors, donors, social performance specialists) during 2005 and 2006. Testing and probing has been conducted with 8 MFIs from different regions, legal status and stages of development. In 2006, the draft methodology was used for 6 MFIs in Mali.

The final methodology was used for 4 ratings in Ethiopia in July 2007 (3 reports already available upon request at rating@planetrating.com: Buusaa Gonofaa, AVFS, SFPI). Others are planned for Q4 2007 and Q1 2008 in Africa and Latin America. More details and social rating reports available on www.planetrating.com (contact Emmanuelle Javoy at ejavoy@planetrating.com).

MicroRate (offers "thin" rating)

MicroRate offers investors and interested parties a way of evaluating a MFIs social performance through an independent assessment of an organization's social performance and social risk. The objective is to allow social investors an easy way to compare different types of MFIs from different regions on an objective scale in the two general areas that matter most to investors in addition to financial sustainability.

The first part of MicroRate's social rating - social performance - measures the effective translation of an institution's social mission into practice. The second part of the social rating - social risk - measures the risk that the MFI deviates from its social mission and fails to produce forward looking outcomes.

Component of Social Rating	Factors Used to Measure
Social Performance	Institutional Outputs 1. Outreach 2. Depth and Variety of Services 3. Cost and Sustainability 4. Social Responsibility
Social Risk	Internal Processes 1. Mission, Communication and Management Leadership 2. Strategic Planning 3. Customer Service 4. Monitoring 5. Recruitment and Training 6. Incentive System

MicroRate uses this analysis to assign a social rating score and a social risk score to the MFI. The social rating score ranges from "excellent" (*Very good likelihood of social impact with outstanding service outreach and depth. MFIs whose operations are exceptionally well-aligned with their social mission*) to "poor" (*Weak likelihood of social impact with limited service outreach and depth. MFIs whose operations are poorly aligned with their social mission*). The social risk score value can be high, medium, or low, representing the probability of deviation from the social mission.

MicroRate has performed 3 Social Ratings in Latin America in 2007 and has plans to unroll the methodology throughout Africa in 2008. More details available from Sebastian von Stauffenberg at sebastian@microrate.com).

[Note – that M-CRIL and MicroRate plan to work towards complementarity in the social ratings they offer, within their new global alliance, MicroRating International.]

PART III – From the Field - Feedback from Practitioners

A Social Rating and Performance workshop was organized by EDA Rural Systems in August 2006 in Gurgaon, India, with the support of Friends of Women's World Banking (FWWB). The purpose of the workshop was to share the method and experience of social ratings being developed by M-CRIL as a new product alongside credit rating. The participants were the executive heads or senior management staff of 15 MFIs from different regions of India, all institutional partners of FWWB, and staff from FWWB. Four of the MFIs represented had obtained a social rating from M-CRIL in the past year.

The MFIs who participated in this workshop gave generally positive feedback on the practice of social ratings. They agreed that social ratings reflected how well they were staying on track to achieve their mission and identified areas where they had room for improvement. After the rating process, some MFIs revised their mission statements, implemented a new focus on strong governance, and revised the structure of various loan products based on guidance from client feedback. One of lessons that emerged from the social rating experience was that an MFI will do a better job of meeting its social performance goals if it has a strategic plan to do so. Many MFIs also noted that a significant benefit of social ratings was the credibility that the MFI gained in the eyes of investors thanks to the rating.

MFIs also discussed areas for improvement in the social rating process. One challenge was that, due to the newness of the social rating concept, MFIs had not been familiar with the rating process and therefore entered into it unprepared. The result was that they were sometimes not able to provide the requisite information for the rating system indicators. Some MFIs simply did not have the data in

their MIS for the type of portfolio analysis that the raters wanted to do, while others had the capacity to generate that data but had not previously done so. Another concern was the difficulty in balancing commitment to social goals with the ever-present pressure to perform well financially in order to gain greater access to funds and expand. It is unclear whether donors and/or investors will value social performance as much as financial performance when deciding where to place their money.

The MFIs listed several areas of interest for continued implementation of social performance monitoring. An important initial step would be to collect information on the different dimensions of social performance, particularly concerning outreach (e.g. those who are actually served in terms of poverty level, whether they or members of their families already have access to financial services, some social indicators such as children are attending school) and social responsibility to clients (e.g. effective communication to clients of the terms of financial services – interest rate on credit, interest rate for savings, cost and coverage of insurance; monitoring indebtedness of poor clients). Those who already had such information expressed the need for a clearer system of collection and computerization of social performance data, the ability to evaluate rural and urban area performance separately, and an operational structure to keep such information up-to-date. This would probably involve orientation and training in social performance management. Participant MFIs also declared a goal of having a social rating within 6 to 12 months from the time of the workshop.

The workshop concluded with the development of five key suggestions. The first was for MFIs to include social indicators within their program evaluations. The second was to create awareness among MFIs about social ratings, notably the areas of study and the methodologies used in the ratings. The third was to prepare a strategic plan to be sure more social ratings occur. This would involve giving time for MFIs to learn about and prepare for the social rating process. The fourth was for FWWB to support the promotion and training of social performance management. The final suggestion was for FWWB to help MFIs develop their MIS and other relevant systems for social reporting.

Social Performance Briefing Series

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Argidius Foundation was founded in 1956. Its mission is to support business based development approaches that focus on the creation of sustainable employment "plus" for the poor in developing countries. The 'plus' refers to the leverage of employment creation on social areas such as education, health, nutritional status and environment.

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The SEEP Network is a membership association of more than 75 international organizations that support microfinance

and enterprise development programs around the world. SEEP's mission is to connect microfinance and enterprise development practitioners in a global learning community.

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