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## Re-Positioning Microfinance with Impact Investors: Codes of Conduct and “Social First” MFIs

*Keywords: Microfinance, Social impact, Impact investing, Codes of Conduct, Social First*

### **Abstract**

Investor interest in microfinance continues despite questions raised by recent repayment issues and by more sceptical assessments of social impact, but investor scrutiny has intensified. The industry can take the opportunity to more clearly articulate its social and financial objectives and how it will achieve them. An important part of this clarification will be to acknowledge that not all investors or microfinance institutions (MFIs) share the identical mix of social and financial objectives and on occasion choices among objectives will have to be made. Tools are becoming available that can make these priorities more transparent and predictable so as to more closely match the objectives and expectations of MFIs and investors. Codes of corporate conduct and minimum standards can provide a starting point for double bottom line investors. A differentiation between “financial first” (FF), and “social first” (SF) companies can give investors greater confidence that coinvestors, directors and managers are fully aligned in pursuit of the same set of priorities. With this clarity, enhanced FF capital flows can have a major impact in achieving MF’s social objectives through expanding scale and outreach in total numbers, while enhanced SF MF will push the envelope and set the evolving standard on improving MF’s effectiveness in achieving its social objectives.

## 1. INTRODUCTION

Over the past few years, MF has matured, facing new challenges and engaging with new associates. In many respects, these challenges and changes reflect the culmination of a decades-long effort to position microfinance as an investment-worthy endeavor, moving decisively out from under the wing of official institutions and philanthropies and engaging with the full range of private capital sources.

With the engagement of the full spectrum of private investors has come anxiety about the ability of microfinance to preserve its essential character, and retain its focus on benefiting the poor and the traditionally excluded. These anxieties have played out against a broader theoretical and ideological context of different theories of social change, poverty elimination and development.

In its seminal 2009 report on Impact Investing, the Monitor Institute proposed a segmentation of the impact investing industry into Social First (SF) and Financial First (FF). Social first prioritizes social outputs with a floor on financial returns while financial first does the reverse. For whatever reason, this segmentation has largely failed to take hold in the microfinance industry to date, with much of the MF industry holding to the notion that priorities need not be set as trade offs are rare and insignificant.

This note suggests that microfinance has reached a level of maturity where it must and can accommodate multiple theories of how it generates social impact so as to comfortably and legitimately access capital from sources across the spectrum of the capital markets. To do so honestly and reliably, however, requires that the industry move beyond the idea that there is a single model of commercial microfinance in which social and financial objectives can generally be achieved without trade offs, and that a conventional shareholder corporation is always the best vehicle for commercial MFIs. Instead MFI managers, investment managers and investors must all articulate more clearly where their priorities lie, what their financial and social return requirements and expectations are, and be prepared to act on these priorities at times at the expense of other, explicitly lesser goals.

The differentiation referred to here is entirely within what has traditionally been called the “commercial” segment of the microfinance sector. It involves investors and managers who are all dedicated to the proposition that MFIs must be sustainable, meaning they must be sufficiently profitable to (1) survive, and (2) attract the necessary funding to grow, increasingly if not entirely from market-based sources. In many cases, this means both debt and equity funding, although there are many prominent non-shareholder institutions in this category as well. Within the commercial category, the discussion seems to boil down to two issues:

- whether there are trade offs between social and financial outcomes;
- whether there is an “appropriate” ROE for MFIs and IRR to investors in MFIs.

Behind these core issues lie different theories of impact, and different views of the responsibilities of investors for the social outcomes and impacts of the companies in which they invest. In other industries,

there has been a gradually evolution of the concept of socially responsible investing, such that there is now a well established sector which combines negative screens and shareholder advocacy within a conventional shareholder structure. The experience is fully consistent with a “financial first” investor objective and is supported by a well developed infrastructure of reporting and benchmarking. The motivating theory of impact for this sector might be summarized that profit maximizing private businesses are the best instruments for achieving social advancement and alleviating social ills, so long as their behavior is monitored and constrained by codes of conduct and activist shareholders that hold management to account for social externalities and corporate behavior.

Parallel to this but less well established are efforts to create and mobilize capital for businesses that prioritize social outputs. These companies turn the conventional corporation on its head: they are not in business to earn profits, but rather they earn profits to enable them to pursue specific social goals. This theory of impact holds that for all its unequalled power as a productive force, a conventional profit maximizing company will always be at best an imperfect instrument for achieving social goals, and only by elevating social goals and dethroning profits will corporations achieve their full potential as agents of social improvement.

This note focuses on microfinance in emerging markets, where explicit discussion of these issues has perhaps been less developed than in some other sectors notwithstanding the fact that the distinct theories of impact have been roiling the microfinance world for some time. The paper offers a suggestion for how more aggressive adoption of codes of conduct and some of the approaches and distinctions being developed in other sectors by initiatives such “B Corp” or the “Common Good Corp” movements might help the microfinance industry move beyond the debate to a framework which can comfortably accommodate the full range of investors and entrepreneurs.

## **2. DO INVESTORS FACE TRADE OFFS BETWEEN FINANCIAL AND SOCIAL PERFORMANCE?**

Any discussion of priorities presupposes that choices may have to be made between objectives. The necessity may arise seldom, or it may arise often, but if we believe that the need to choose will never arise, then we don’t have to bother setting priorities.

The view of the no trade off camp in microfinance has been recently rearticulated in the November 2010 J.P. Morgan paper on impact investing: “Increasingly, entrants to the impact investment market believe they need not sacrifice financial return in exchange for social impact” (J.P. Morgan Global Research 2010, p6). And in a discussion between Mohammad Yunus and Michael Chu at the World Microfinance Forum Geneva in 2008, Chu drew a related conclusion: in order for microfinance to achieve true impact by reaching scale, microfinance needs to be transformed into an industry, and that in order to create an industry “you need not substandard, not average -- but above average – returns” (WMFG 2008, p2).

At its most simple and intuitive level, the “no trade off” argument rests on several compelling points: (1) Good client treatment equals good business, and MFIs that abuse clients, or provide them with

substandard products will ultimately be driven out by MFIs that provide to clients a more attractive value proposition. (2) The goal first and foremost is access to financial services, and once access is established, market forces will drive the industry to offer better value to clients. (3) Because access is so low, the best way to maximize impact at this stage is increasing the number of clients rather than increasing the value per client.

All these arguments receive some support from recent studies. Microfinanza Rating finds that “social and financial performance are compatible” and that more financially successful MFIs also register higher social performance scores (Guarneri 2010 (1), p2). The study also finds “evidence of specific mechanisms mutually reinforcing social and financial performance”, including positive correlations between breadth of outreach (measured by clients, portfolio and savings relative to a benchmark), social responsibility towards staff, and clients below the poverty line with stronger financial performance. Mix Data Brief #7 finds that training of staff on social performance and progressive human resource policies are associated with increased staff productivity and better portfolio quality and that higher dropout rates reduce MFI efficiency (Gonzalez 2010, p1).

But the same studies also confirm the intuition and logic behind the trade off argument. Careful unpacking of the operations of MFIs document both trade-offs between financial and social objectives. MiX Data Brief #7 identifies a number of trade-offs offsetting the synergies noted above. These include a number of policies that reduce efficiency in terms of operating expense as a percentage of gross loan portfolio, including targeting poor or very poor borrowers, and incentivizing staff for social performance. Overall, the study notes that “investments in human capital go hand in hand with higher staff productivity and better portfolio quality, but lower efficiency; that social performance training and HR policies have stronger synergies and weaker trade-offs with financial performance; and that serving the very poor and poor comes at a cost in terms of efficiency, but not in terms of risk or productivity.” (Gonzalez 2010, p1)

The Microfinanza studies echo this result, finding many of the same synergies, but also finding that poverty outreach comes at a cost in terms of financial performance. The study concludes that “the desired levels of poverty outreach cost and benefit should be intentionally set in order to balance the social and financial performance in the overall strategy.” (Guarneri 2010 (1), p 4)

To be fair, from the time when private investor participation in MF began to take off in 2004 until the onset of the financial crisis in 2008, it was not unreasonable to argue that both social and financial goals could be achieved to everyone’s satisfaction, and that while on some level of trade offs might exist, the opportunity for financial and social performance seemed so promising that there was no need to prioritize, and in any case, hard evidence on trade offs or financial returns was not available.

This happy confluence reflected a period in the development of MF that is probably gone for good in most or all parts of the world: competition was limited, growth rates were high, portfolios were extraordinarily solid, entry prices were low and multiple expansion could often be expected.

Thus, the “no trade off” argument is more accurately characterized as an “acceptable trade off” argument: so long as the performance of leading MFIs was such that financial performance expectations seemed achievable, some sacrifice of financial performance to pursue social objectives, if and when necessary,

was acceptable. But in any case, the research did not yet exist to argue strongly that trade offs were unavoidable and there was insufficient track record for investors to judge whether targeted returns would be achieved.

This discussion also ignores the non-financial services that many microfinance practitioners feel are essential if enhanced access to financial services is to be used well and have the desired impact. These can range from financial literacy programs to health and gender interventions, or marketing and agricultural extension services. What these non-financial products typically have in common is that they do not fully cover costs. While it can be argued that they indirectly improve financial performance by cementing client loyalty or decreasing portfolio risk, it is generally the social rather than the financial agenda that drives these initiatives.

Overall, recent research seems to support a conclusion that trade offs between financial and social objectives do exist, as do synergies. In some cases the net effect will be positive, with financial return actually enhanced. In others it may be negative, however, so that to the extent an investor places the priority on social outputs, they should be prepared to accept a lower return although they may not always -- indeed may never -- need to.

## **TEXT BOX: DEFINITIONS**

*Impact Investing:* Actively placing capital in business and funds that generate social and/or environmental good and at least return nominal principal to investors. (Monitor Institute, 2009) Investments intended to create positive impact beyond financial return. Impact investments provide capital, expecting financial return, to businesses (fund managers or companies) designed with the intent to generate positive social and/or environmental impact. (J.P. Morgan Global Research 2011)

*Impact First or Social First Investors* seek to optimize social or environmental impact with a floor for financial returns. They primarily aim to generate social or environmental good and are often willing to give up some financial return if they need to. (Freireich 2009, p31)

*Financial First Investors* seek to optimize financial returns with a floor for environmental or social impact. These investors may be driven by fiduciary requirements as in the case of pension plans. (Freireich 2009, p 31)

*Social Business:* A business designed to meet a social goal that pays no dividends but rather sells products at prices that make it self-sustaining. The owners get back the amount they've invested in the company over a period of time, but no profit is paid to investors. Any profit made stays in the business – to finance expansion, to create new products or services, and to do more good for the world. (Yunus 2007, p xvi)

*Common Good Corporation:* There is much that is already assumed to be behaviors that give priority to the common good. Some of the obvious ones are to not kill, steal, or have slaves. Some of the recently emerging ones are a livable wage as the minimum wage, a responsible relationship with the environment, and fair trade. It now seems likely that a new one to soon emerge will be a cap on the return to equity investors (not necessarily an ungenerous one), with each year's excess net profit being permanently set aside and solely invested in common good companies and funds that also place a cap on the return to equity investors and invest the excess in the same way. . . . The goal of the common good capitalism movement is to self-finance its growth through more and more companies becoming . . . Cap Club companies and investing this capital in common good funds that solely buy companies and convert them to Cap Club companies. (Mollner 2012, p 285)

*Benefit Corporation:* Certified B Corporations are a new type of corporation which uses the power of business to solve social and environmental problems. B Corporations' legal structure expands corporate accountability so they are required to make decisions that are good for society, not just their shareholders. B Corporations' performance standards enable consumers to support businesses that align with their values, investors to drive capital to higher impact investments, and governments and multinational corporations to implement sustainable procurement policies. ([www.bcorporation.net](http://www.bcorporation.net))

### **3. FAILURE TO ARTICULATE PRIORITIES: WHY IT MATTERS**

If trade-offs do exist, how are they navigated in a conventional shareholder corporate structure? In the past, the issue could be conveniently ignored so long as the investor base for the full range of institutions was basically the same group of philanthropic and official donors and investors, or given the absence of clear data demonstrating synergies and trade offs. With new, conventional private investors entering and becoming increasingly important sources of capital and active participants in governance, the differences are coming into sharper relief.

As might be expected and is appropriate given the conventional shareholder corporate structure of most commercial MFIs, to date the tensions have been resolved largely to prioritize financial performance. A 2011 Imp-Act / MicroSave study found little board level focus or resources on the social side of the microfinance double bottom line.

Such lack of focus in governance translates directly to the operations of the MFIs. A Microfinanza Rating report on Poverty Outreach reveals that many MFIs have fewer clients below the poverty line than the national average, and that larger MFIs tend to have a lower proportion of poor clients by number than smaller MFIs (Guarneri 2010 (2) p2). While there are many factors that can affect these results, such as the age of the MFI, the proportion of the population in the lowest (<\$1 / day) versus the somewhat higher (<\$2 / day) income categories, all other things being equal it is reasonable to expect that Financial First MFIs would generate this result.

Similarly, the performance of MFIs with respect to most of the six original Client Protection Principles verges on the dismal according to another Microfinanza study (Guarneri 2010 (3)):

- Principal 1, Overindebtedness: by a conservative estimate, at least a quarter of MFI clients were carrying loans from other sources and 15% of MFI clients had repaid a loan with a loan from a different source.
- Principal 2, Transparency: only 37% of MFI clients know the interest rate they are charged;
- Principle 4, Ethical Treatment: 66% of MFIs have never conducted a staff satisfaction survey;
- Principle 5, Grievances: 63% of MFIs have no complaint or grievance procedure.

The Imp-Act / MicroSave study recommends multiple steps that can be taken to address such issues based on Social Performance Management Principles ([www.spmresourcecentre.net](http://www.spmresourcecentre.net)). These principles articulate a common sense approach to achieving social objectives:

- Translate mission and values into clear, measurable objectives to capture intentional social benefits.
- Design and implement systems for social responsibility, including client protection.
- Track, understand and report on whether the MFI is achieving its social objectives.
- Align business processes to achieve both social and financial objectives.
- Ensure that decision-making considers both social and financial outcomes.

But it would seem that the failure of MFIs to place a high priority on implementing such steps and more effectively incorporating social considerations into their operations is to be expected: MFI governance and operations are appropriately following the financial first priority of the conventional corporate form.

Therefore the key question for microfinance is: what should double bottom line investors require to ensure that MFIs do no harm and achieve the social outputs targeted?

While until now codes of conduct for microfinance were lacking, or insufficiently concrete to be meaningful, various initiatives such as the SMART Campaign ([www.smartcampaign.org](http://www.smartcampaign.org)) and MF Transparency ([www.mftransparency.org](http://www.mftransparency.org)) can now enable managers and investors to meaningfully define minimally acceptable standards of corporate behavior. Furthermore, the risks of not implementing robust codes and the need to engage the public and the authorities in assessment of their success in preventing abuses seem more pressing in the aftermath of the Andhra Pradesh crisis of 2010.

For their part, Social First MFIs can also benefit from the tools and standards developed in these codes. But they will also require structural changes to institutionalize a social first priority that ensures that social outputs are and will remain the focus of governance and management.

Rather than a single model, a differentiation between Social First and Financial First MFIs, and an acknowledgment that circumstances will arise in which they will behave differently, would remove confusion and uncertainty from management and boards. Financial First MFIs would clearly focus on achieving the financial returns expected by investors, particularly institutional investors sensitive to their fiduciary responsibilities, while using codes of conduct and active governance to avoid destructive corporate behaviors. Social First MFIs can genuinely implement a more structured framework for disciplined social performance management such as that outlined by Imp-Act / MicroSave to ensure that social outputs are effectively prioritized.

#### **4. HOW TO DIFFERENTIATE “SOCIAL FIRST” MICROFINANCE**

In anticipation of the tensions facing board and management, Monitor Institute proposed to differentiate double bottom line investments between “Impact First”, called Social First (SF) here, and “Financial First” (FF) investments. While FF microfinance can utilize the traditional shareholder model, it is not clear that SF MF fits comfortably or at all within such a model. This misfit reflects a number of observations drawn above and their implications:

- There are both synergies and trade offs between financial and social objectives. Sometimes the synergies will outweigh the trade offs, in other cases the opposite will be true.
- When the necessity of a trade off arises, MFI managers and investors must be clear on which objective to prioritize: social or financial. This priority needs to be set at the outset, not adopted on an ad hoc basis as an issue arises.
- For those that prioritize social objectives, a minimum ROE and IRR can be set which will logically be lower than expected or minimum acceptable ROE / IRRs for conventional shareholder or FF double bottom line companies with a similar risk profile. Managers and investors are prepared to accept reduced ROE / IRR when conflicts arise, although financial performance may well *exceed* that of conventional businesses;

The goal of this differentiation is to acknowledge and ensure support systems for two different models of microfinance based on distinct theories of impact which both provide benefits to the “client population”, taken as the entire low income population.

The financial first model is consistent with the Bottom of the Pyramid (BOP) opportunity popularized by Prahalad. This model is entirely consistent with profit maximization and is based on the notion that the poor have substantial resources and economic activity and that properly designed and distributed products can at a minimum increase consumer choice and be profitably delivered and in some cases provide stunning improvements in access to critical health, energy, communications services accessibly and affordably. It also recognizes that the scale and scope of MF today, for all its success, falls seriously short of the need: according to Chu (2011), less than one third of potential clients are currently reached, and product offerings fall short of what is required.

The BOP business model espoused by Prahalad, and the MFIs that utilize it, work with a theory of impact whereby scaling up of activities of BOP businesses positively affect the poverty status or economic security of the poor. But there is ample evidence that his principles of adapting products or delivery systems to tap the purchasing power of the poor can cause harm as well as good.

In a study which might be considered the evil twin of Prahalad’s, Gary Rivlin paints a picture of “mercenary entrepreneurs [taking] advantage of an era of deregulation to devise high priced products to sell to the . . . working poor” (Rivlin 2010, p i). While this is clearly the antithesis of the virtuous process that Prahalad envisions, the commercial logic seems unassailable. For a traditional shareholder company, in fact, there is nothing in Prahalad’s arguments that would make Rivlin’s vicious outcomes any less likely than Prahalad’s virtuous ones.

Rivlin’s examples are drawn from the US financial sector and took place with the active participation of prominent and respected listed companies, under the scrutiny of a sophisticated regulatory system, in an environment of high literacy and ample sources of information, and despite the determined efforts of a developed network of consumer advocates.

Initiatives such as MF Transparency or the SMART Campaign might have helped stymie some of the most egregious practices in the US. These codes of conduct, once they have stabilized and been widely adopted, provide FF microfinance investors with an opportunity to promote and select for MFIs that “do no harm”, much as socially responsible investors use negative screens and shareholder advocacy to encourage companies to avoid damaging practices and products while continuing to maximize shareholder value. Such an approach fully respects the fiduciary responsibilities of conventional shareholder companies and investors.

In contrast to conventional, Financial First corporations, Social First companies are motivated by a different theory of impact. In this view, social outputs will only be reliably and consistently achieved if they are enshrined as the priority of the company, rather than relying on market forces, albeit constrained by codes of conduct, to achieve social justice and sustainable outcomes. These companies go beyond the “do no harm” threshold for socially responsible Financial First companies and set as priorities specific social outcomes or outputs such that the purpose of such companies is not to create shareholder value, or

even to deliver a specific product or service. Their purpose rather is to mobilize and deploy resources – financial and human – to relieve deprivation, comfort the afflicted, and give hope to parents for the future facing their children.

While many MFIs do espouse such goals, what is lacking are structural features that can ensure that investors, directors and managers are fully aligned and focused on prioritizing their achievement. Social First MFIs can address this flaw by drawing on efforts to create new corporate forms that use for profit structures with priorities other than maximizing shareholder value. These emerging forms are variously called Social Businesses, Benefit Corporations or Common Good Corps.

The objective of field managers and staff of such companies, as one manager put it, “is to improve the quality of life of clients, not to provide financial products.” Or, in an example drawn from another industry, a bakery certified as a B Corp defines itself as follows: “we don’t hire people to make brownies, we make brownies to hire people.” In his World Microfinance Forum appearance in 2008, Yunus insisted that “The goal of microcredit is not to provide money. . . . The goal of microcredit is to dramatically transform the life of a family in its totality, by providing education loans, health insurance, etc. . . .”

This distinction first and foremost brings microfinance back to intentions. But in contrast to the past, where intentions began and ended with mission or values statements on websites, it is now better understood that there are concrete decision points and structural features that can clearly differentiate companies which exist as first and foremost as profit oriented enterprises and those that are defined by their social and environmental objectives.

Building on the work of B Corp, Yunus and Mollner, defining features of a SF MFI might include some or all of:

- Explicit commitment to multi stakeholder value proposition; no priority to shareholders
- Self perpetuating board so long as minimum ROE achieved
- Minimum rating by GIIRS ([www.giirs.org](http://www.giirs.org)), B Corp or equivalent
- Commitment to specified minimum ROE for a defined period
- Board responsible for maximizing social / environmental impact once minimum ROE achieved

To the extent that FF and SF investors can meet their goals and provide sufficient capital so that the SF and FF sectors can remain segregated in the context of enhanced transparency and self selection, great. It appears that for the foreseeable future, though, the volume of SF capital is insufficient to fully meet the SF appetite. Under this circumstance, the tensions between the requirements of SF and FF investors can best be managed in a context of enhanced transparency of objectives and careful segregation of FF and SF capital in different tranches of a company’s capital structure. This would be a form of hybrid or “yin-yang” deals (Freireich 2009, p 33). However, care needs to be taken in such hybrid structures to ensure that the various tranches fulfill the objectives of different types of investors, and avoid giving inconsistent guidance to management. FF shareholders can fruitfully participate in the governance of SF

MFIs, but only if they have clearly endorsed the SF priorities, and if SF shareholders dominate governance.

## **Figure 1. Commercial MFI Investment Landscape**

### **5. WHAT RETURNS CAN MF INVESTORS EXPECT? WHAT RETURN SHOULD SF INVESTORS EXPECT?**

Even during the halcyon 2004-2008 period, many things had to go right for funds to achieve the IRRs to investors that were targeted, but such a scenario was not out of the question. A numbers of features of the landscape made strong financial performance plausible: low competition, high repayment, high growth. The conjunction of these features, particularly in the period from 2006 to late 2010, enabled prospects for MFIs to seem consistent with the “acceptable trade off” argument.

The window during which these stars were aligned appears to have been brief, however. In the past two years, a bit of the air has escaped and microfinance seems to have settled back towards earth. Growth has slowed, portfolio quality has ticked down; MiX data shows that ROA for the top quartile of MFIs has ranged around 4-5% in recent years (Gonzalez 2011 (2)), and returns have steadily declined. As documented in the July 2011 JP Morgan / CGAP Valuation Survey, multiples have also dropped back a bit.

Very roughly speaking, investors would not be unrealistic to expect returns somewhere around the 15% level, without providing for any foreign exchange gain or loss. This would apply to conventional, Financial First MFIs. Using this as a benchmark, and assuming that Social First MFIs would face more or less frequent occasions when a choice might be made that would prioritize social outcomes at the expense of financial performance, one might arbitrarily suggest that Social First investors should be prepared to accept returns a few points lower than those for Financial First investors, for example, 8-12%.

These ranges are generally consistent with what has been found with respect to the expectations of both conventional and social investors. The November 2010 JP Morgan report on impact investing finds that mainstream emerging market private equity managers target net returns of 15-20%. The same report finds inconsistent evidence of whether social investors expect lower returns than conventional investors, depending on the asset class and whether it is a developed or emerging market asset. But in at least some cases, social investors clearly expect to trade off return: in developed market debt and equity, social investors expected returns 30-50% below the conventional benchmarks. The report also notes that “average realized returns . . . almost always lag the expected, forecast or projected returns when the investment is made.”

## **CONCLUSION**

Microfinance has matured to the point that it can access the full range of capital providers. However, as an impact investment, microfinance offers a more complex investment proposition and attracts investors with very different motivations, expectations and requirements with respect to financial and social outcomes. A clear understanding of how these goals may be mutually reinforcing or at cross purposes, and a differentiation of MFIs that prioritize one or another among these goals can help MFI managers, directors and investors self select and ensure that companies are held to an internally consistent set of expectations. The Financial First and Social First differentiation among double bottom line investors and MFIs recognizes the two objectives that dominate and shape MFI and investor expectations, and the explicit adoption of these categories will help investors and MFIs better build the sector and achieve its financial and social objectives.

Along with the increasing heterogeneity of the investor base, the industry has assumed greater importance and visibility in national financial systems. Together, these trends make rigorous implementation of codes of conduct and minimum standards essential. New capital flows hold the potential for the sector to accelerate its growth and outreach, increase its penetration, broaden its range of products, and increase efficiencies. Without rigorous implementation of strict codes of conduct, however, this acceleration risks harming the vulnerable target populations and generating political backlash as it seeks to achieve the “market” rates of return required by conventional investors. To reduce these risks, all double bottom line investors should insist on adherence to strengthened codes of conduct by MFIs, use their influence in governance to support management in implementing these codes, and insist that conventional co-investors do the same.

The challenge for microfinance is to create a framework where both SF and FF can flourish, and provide investment opportunities consistent with different theories of impact, different return requirements and commitments, and different requirements for social outputs.

For all investors, as data on returns and social outcomes from microfinance become available they should be carefully reviewed, and expectations and targets adjusted to reflect them. Early indications are that some of the more ambitious financial scenarios are less frequently achieved than originally thought. Similarly, new studies and debate continues to refine our view of what social impact microfinance can realistically be expected to achieve. Steady and reliable capital flows to the sector are more likely if investors enter with the most up to date and comprehensive understanding of the range of possible outcomes and probabilities available.

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