

# NMI'S SOCIAL PERFORMANCE FRAMEWORK



Center meeting in the Microfinance Institution NESFB - an hour's drive from Guwahati, Assam, India. The main source of income for these women is pig rearing.

3<sup>rd</sup> April 2018

# NMI's Social Performance Framework

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# 1 NMI's approach to social performance

Nordic Microfinance Initiative (NMI) invests in financial inclusion. As a double-bottom-line investor, we incorporate our social mission into everything we do - from the policies and guiding principles we apply, to the processes and tools we use when evaluating investment opportunities - and in our active engagement during the investment period. This document explains how NMI works with its social mission.

The terms social mission and social goals should be understood broadly. The microfinance institutions (MFIs) we invest in are typically businesses that apply commercial means to achieve a mission that incorporates both financial and social goals. These social goals include reaching out to large numbers of poor and excluded people, improving the quality and appropriateness of financial services, and creating benefits for specific client groups.

NMI's mission and guiding principles direct the investments we make. We invest only when the MFI's mission and social goals are aligned with NMI's mission and guiding principles. For each of our investments we have a social ownership agenda, and we establish social goals together with the MFI. During the investment period we work to support the MFI in fulfilling their mission and achieving their social goals.

## 1.1 Definitions

Social performance together with financial performance constitutes a double bottom line approach that is characteristic of MFIs. Specifically, social performance refers to the MFI's effectiveness in achieving its stated social goals. Social performance management (SPM) refers to the systems used to achieve stated social goals.

## 1.2 NMI's mission

The mission of NMI is to contribute to the empowerment of poor people and to the creation of jobs, wealth, and economic and social sustainability in developing countries. We accomplish this by investing in and building up microfinance institutions, which particularly target poor women in developing countries. NMI combines existing experience in the field of microfinance and international development cooperation, with the capital strength and financial experience of institutional investors.

## 1.3 NMI's six guiding principles

1. We aim to create sustainable long-term impact with the investments we do. We do not invest where it is easiest or where risk is lowest. We invest where we believe we can achieve the biggest social impact alongside financial return.
2. We believe that responsible<sup>[1]</sup> microfinance has a positive impact through the provision of financial services in general. However, we prefer to invest in MFIs that have a clearly stated social mission that describes the positive impact the MFI aims to have on society. Therefore, we evaluate the MFI's social ambition and its capacity to fulfil this mission prior to investing.
3. We believe the best way to create sustainable long-term impact is by helping to develop well-managed, financially healthy, scalable financial institutions. Therefore, we invest in MFIs that have reached financial sustainability or have good prospects for attaining financial sustainability within the next few years.

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<sup>[1]</sup> By "responsible microfinance" we mean microfinance that adhere to the Client Protection Principles (CPPs)

4. We wish to ensure that we and our investees do everything we can to treat clients well and protect them from harm. Therefore, we endorse the client protection principles and require all investees to do the same. We also apply and require investees to adhere to standard policies on AML, business exclusion and business integrity as well as relevant national legislation.
5. We strive to be fair and transparent in all dealings with investees and partners. Also, we strive to deliver appropriate financing that meets demand, clear and balanced contracts, and fair processes for resolving disputes.
6. We seek to be an active investor and, when possible, take up governance positions in the board of the MFI or committees under the board. When investing in emerging MFIs, we carefully evaluate if the MFI would benefit from professional or other technical assistance that is available through NMI's Technical Assistance Facility.

## NMI'S COMPARATIVE ADVANTAGE

*93 MIVs managed by 44 fund managers reported to the 2017 Symbiotic Survey. In total they manage \$12,6 billion invested in financial inclusion, 76% of which is invested in microfinance.*

- ✓ **NMI makes primarily equity investments**, whereas only 15% of direct investments in the industry are equity investments.
- ✓ **NMI's debt investments are offered in local currency**, whereas only 31% of direct debt investments in the industry are made in local currency.
- ✓ **NMI invests in Sub-Saharan Africa, South Asia and South East Asia**, whereas only 10% of the direct investments in the industry are made in Africa and 15% in South Asia. 60% are placed in Latin America and Easter Europe & Central Asia.
- ✓ **NMI invests primarily in medium sized MFIs with growth potential**, whereas 58% of MIVs focus on MFIs with GLPs > \$ 100 mill.
- ✓ **NMI is an active investor and sits on the board of most equity investments**, whereas only 49% of MIV equity investments are linked to a board seat.
- ✓ **NMI offers technical assistance for capacity building**, whereas only 15% of MIVs provide (direct) technical assistance.

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### 1.4 NMI's policies

NMI's policies on business integrity, AML & anti-terror and excluded businesses are based on international standards. NMI's policies are briefly described below and can be obtained upon request.

- **Anti-Money Laundering/anti-Terrorist Financing Policy:** This policy adheres to the international standards and includes an evaluation of risks, i.e., country risk, regulatory requirements, association with persons covered by restriction lists issued by UN or FATF, and other issues relevant for the evaluation of risk.
- **NMI business integrity policy:** NMI has a zero-tolerance approach to corruption, money laundering and economic crime. Guided by the frameworks set forth in the OECD Convention Against Bribery and the UN Convention Against Corruption, NMI is dedicated to promoting

<sup>1</sup> 2017 SYMBIOTICS MIV SURVEY: <https://symbioticsgroup.com/wp-content/uploads/2017/09/Symbiotics-2017-MIV-Survey.pdf>

integrity, transparency, and accountability through its business dealings. NMI requires high standards of business integrity from employees and business partners and communicates its no-tolerance approach to all stakeholders.

- **NMI Microfinance Exclusion List:** This policy is based on best practice in the microfinance industry, which is an adaptation of IFC’s general exclusion list.
  - Production or activities involving forced labour<sup>i</sup> or harmful child labour<sup>ii</sup>.
  - Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements.
  - Production or trade<sup>iii</sup> in: (i) weapons and munitions; (ii) tobacco; or (iii) hard liquor.
  - Gambling, casinos or equivalent enterprises<sup>iv</sup>.
  - Any business relating to pornography or prostitution.
  - Trade in wildlife or wildlife products regulated under CITES<sup>v</sup>.
  - Production or use of or trade in or storage of hazardous materials such as radioactive materials<sup>vi</sup>, unbounded asbestos fibers and products containing PCBs<sup>vii</sup>.
  - Cross-border trade in waste and waste products unless compliant to the Basel Convention and the underlying regulations.
  - Drift net fishing in the marine environment using nets in excess of 2.5 km in length.
  - Production, use of or trade in pharmaceuticals, pesticides/herbicides, chemicals, ozone depleting substances<sup>viii</sup> and other hazardous substances subject to international phase-outs or bans.
  - Significant<sup>ix</sup> conversion or degradation of Critical Habitat<sup>x</sup>.
  - Significant alteration, damage, or removal of any critical cultural heritage<sup>xi</sup>.
  - Production or activities that impinge on the lands owned, or claimed under adjudication, by Indigenous Peoples, without fully documented consent of such peoples.

### 1.5 NMI’s applied industry standards

NMI supports and builds our policies on industry standards in the microfinance sector. We have selected the initiatives we support carefully, based on what is most specific to the field we operate in. The initiatives we support are briefly described below.

NMI approach to social performance is particularly based on the Client Protection Principles (CPPs) and the Universal Principles for Social Performance. These two initiatives build on each other. The CPPs define how any microfinance client should be protected to ensure “no harm is done”. The Universal Principles for Social Performance supports the MFIs in delivering output that has positive impact on their clients lives.

We are members of the Smart Campaign

The Smart Campaign is a global effort to unite microfinance leaders around a common goal: to keep clients as the driving force of the industry. The Smart Campaign has developed the Client Protection Principles.



We endorse the Client Protection Principles and require our investees to do the same

- Client Protection Principles:
1. Appropriate product design and delivery
  2. Prevention of over-indebtedness
  3. Transparency
  4. Responsible pricing
  5. Fair and respectful treatment of clients

6. Privacy of client data
7. Mechanisms for complaint resolution

We are members of the Social Performance Task Force (SPTF)

The Social Performance Task Force (SPTF) is a non-profit membership organization with more than 3,000 members from every stakeholder group in inclusive finance. SPTF engages with these stakeholders to develop and promote standards and good practices for social performance management (SPM). The SPTF has developed the Universal Principles for Social Performance.



We incorporate the SPTF's Universal Principles for Social Performance

1. Define and monitor social goals
2. Ensure board, management and employee commitment to social goals
3. Design products and delivery channels that meet clients' needs and preferences
4. Treat clients responsibly
5. Treat employees responsibly
6. Balance financial and social performance



We are members of Mix Market

MIX Market is an online platform that allows users to assess market conditions, individual MFI performance, and the financial inclusion landscape. Mix Market has been key in building benchmark performance data on microfinance, which is a principle element for professionalisation of the industry.



We are members of FIEC

FIEC is a membership council representing the leading private entities making active, long-term, and sustainable equity investments in institutions focusing on under- or unserved clients, with the goal of achieving greater financial inclusion.



## 2 The Social Performance Management system (SPM)

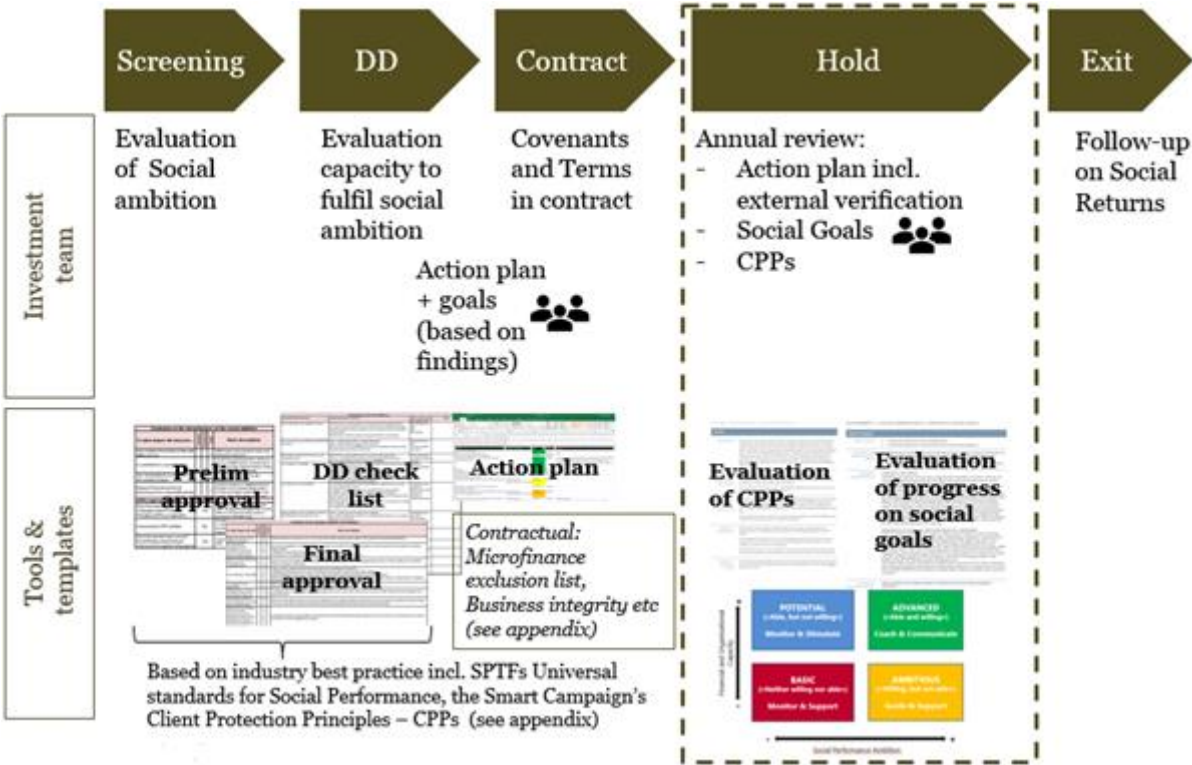
NMI's social mission and guiding principles are translated into the processes, procedures and tools we use in our daily work. This Social Performance Management system (SPM) consists of 3 elements:

- 1) Social performance practices in the investment process
- 2) Quarterly monitoring of MFIs' social performance
- 3) NMI's social ownership agenda and annual review of each MFI

### 2.1 Social performance practices in the investment process

The outcome of the first step in the investment process - screening - is a preliminary investment proposal, which is presented to our Investment Committee (IC). In this step, the social ambition of the MFI is evaluated. The purpose is to ensure that the MFI's mission is aligned with NMI's social

mission and guiding principles and that the MFI has a track record that verifies commitment to the social mission.



If the preliminary proposal is approved by the IC, the case moves into due diligence (“DD”). The outcome of this step is a final investment proposal, which is presented to the IC. During due diligence the MFI’s capacity to fulfil its social mission is evaluated using NMI’s guidelines and a standard template. The guidelines and templates are based on SPTF’s Universal Principles for Social Performance and assess if management systems which enable the MFI to deliver on its social mission are in place. Elements evaluated include the board and management’s commitment to the social mission, how financial and social goals are balanced, if clients and employees are treated fairly and respectfully, if products are designed to match client’s needs, if prevention of over-indebtedness is incorporated into policies and procedures of the MFI, etc.

The assessment of capacity forms the basis for NMI’s ownership agenda (action plan). In the social ownership agenda, we specify how NMI will support the MFI in strengthening social performance and if there are specific goals we will focus on, e.g., avoiding mission drift, developing new products, reducing interest rates, obtaining a social rating or CPP certification, etc. The most crucial elements of the ownership agenda are incorporated into the contract.

During the investment period (“Hold”) we monitor social performance on a quarterly basis and review the social goals, CPPs and action plan on an annual basis. This is described further below. Upon exiting the investment (“Exit”) we assess the social output generated during the entire investment period.

**2.2 Monitoring MFIs’ social performance**

An important part of NMI’s SPM system is the ongoing monitoring of the MFIs’ social performance. This is done in three steps, which are included in the contractual agreement made at the time of investment.

1. Quarterly, the MFIs report on key social performance indicators including data on outreach, portfolio quality, pricing, client retention, employment, tax paid, serious incidents, etc. The data from each MFI is analysed and shared internally to inform NMI’s investment directors about positive developments and elements to be improved.
2. Annually, NMI follows up on the social goals established at the time of investment and assess whether the MFI is progressing in the right direction. Furthermore, the MFI’s adherence to the Client Protection Principles is assessed.
3. As a principle, the MFI should go through external verification every 2-3 year for example a social rating or audit conducted by a professional rating agency or an accompanied self-assessment using the SPI4 tool<sup>2</sup>. This provides an external assessment of the institution’s social performance and valuable insight into areas of improvement. An alternative is to opt for a CPP certification, which provides an independent, objective seal of confidence that a financial institution has adhered to all the standards of the Client Protection Principles.

### 2.3 NMI’s social ownership agenda and annual review

The annual review of social goals and CPPs, mentioned above, is conducted by the NMI investment team. Thereafter, the social ownership agenda is review and revised in a collaboration between the investment team and MFI with support from NMI’s social performance coordinator and NMI’s TA facility coordinator. This process is in place to ensure that we uphold a focus on the social mission and guiding principles during the investment period.

## 3 NMI’s reporting on social performance

Quarterly, we aggregate the social performance data received from the MFIs into a report we share with NMI’s owners and investors. This report provides a snapshot of how NMI contributes to key social performance indicators through the MFIs we are invested in.

Annually, we report on NMI’s impact and the progress we have contributed to achieving for each of the portfolio MFIs both in terms of the key social performance indicators on outreach, portfolio quality, pricing, client retention, employment, etc., as well as in terms of product development, price reductions, social ratings, product development, CSR initiatives, etc.



In the annual report we also give an update NMI’s Social Performance Framework (this document) and other additions or changes during the past year.

<sup>2</sup> The SPI4 is a social performance assessment tool that helps MFIs evaluate their level of implementation of the Universal Standards for Social Performance Management, including the Smart Campaign Client Protection Principles. An accompanied self-assessment is conducted by the MFI with support of a validated SPI4 auditor.



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<sup>i</sup> Forced labor means all work or service, not voluntarily performed, that is extracted from an individual under threat of force or penalty.

<sup>ii</sup> Harmful child labor means the employment of children that is economically exploitive, or is likely to be hazardous to, or to interfere with, the child's education, or to be harmful to the child's health, or physical, mental, spiritual, moral, or social development.

<sup>iii</sup> This applies when these activities are a substantial part of a project sponsor's primary operations.

<sup>iv</sup> This applies when these activities are a substantial part of a project sponsor's primary operations.

<sup>v</sup> CITES: Convention on International Trade in Endangered Species or Wild Fauna and Flora. A list of CITES listed species is available from their website: [www.cites.org](http://www.cites.org).

<sup>vi</sup> This does not apply to the purchase of medical equipment, quality control (measurement) equipment and any equipment where NMI considers the radioactive source to be trivial and/or adequately shielded.

<sup>vii</sup> PCBs: Polychlorinated biphenyls - a group of highly toxic chemicals. PCBs are likely to be found in oil-filled electrical transformers, capacitors and switchgears dated from 1950-1985.

<sup>viii</sup> Ozone Depleting Substances (ODSs): Chemical compounds which react with and deplete stratospheric ozone, resulting in the widely publicized 'ozone holes'. The Montreal Protocol lists ODSs and their target reduction and phase-out dates.

<sup>ix</sup> Significant conversion or degradation means the (i) elimination or severe diminution of the integrity of a habitat caused by a major, long-term change in land or water use; or (ii) modification of a habitat that substantially reduces the habitat's ability to maintain viable population of its native species.

<sup>x</sup> Critical habitat is a subset of both natural and modified habitat that deserves particular attention. Critical habitat includes areas with high biodiversity value that meet the criteria of the World Conservation Union (IUCN) classification, including habitat required for the survival of critically endangered or endangered species as defined by the IUCN Red List of Threatened Species or as defined by national legislation; areas having special significance for endemic or restricted-range species; sites that are critical for the survival of migratory species; areas supporting globally significant concentrations or numbers of individuals of congregatory species; areas with unique assemblages of species or which are associated with key evolutionary processes or provide key ecosystem services; and areas having biodiversity of significant social, economic or cultural importance to local communities. Primary Forest or forests of High Conservation Value shall be considered Critical Habitats.

<sup>xi</sup> Critical cultural heritage consists of (i) the internationally recognized heritage of communities who use or have used within living memory the cultural heritage for long-standing cultural purposes; and (ii) legally protected cultural heritage areas, including those proposed by host governments for such designation.