

Best Practices and Standards

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Research findings in Pakistan show programs that have pursued financial sustainability have achieved far greater outreach than programs that have provided subsidized credit and relied on continuing donor support to make up the remaining losses.

There are currently three primary methodologies followed in Pakistan; first the community-based methodology (used by Rural Support Programs), the Grameen/solidarity group model and a hybrid individual lending and community-based methodology. A number of international best practices are applied in Pakistan including:

- Credit discipline needs to be transferred to the community group, which acts as a guarantor, especially in rural areas where there is greater social pressure.
- Loans to first time borrowers should progress from small to larger amounts, experiences in Pakistan have shown that larger loans given to first time borrowers have resulted in repayment problems.
- Support and analysis of the client's business plan is crucial, as it must reflect the current market and be developed through training support if necessary.
- Default must be dealt with promptly and without indulgence.
- Role of savings is as important, if not even more important, than credit.

Unfortunately, most of the capacity and products of microfinance organizations are geared towards the provision of microcredit rather than microfinance, which is defined as the full range of financial services such as savings, insurance and others.

Best Practices Among Microfinance Practitioners

Among microfinance providers, **Kashf Foundation** was the first to implement international best practices by choosing to focus only on microfinance, serving in priority women and by seeking financial sustainability. Its success has been confirmed by impact studies revealing that 85% of Kashf clients have recorded an increase of income, while 67% have recorded an improvement in the household diet.

Kashf Foundation has also ensured that its institutional development is geared towards sustainability by imposing high performance standards in terms of productivity (600 clients per loan officer, branch offices serving 1,800 to 2,400 clients) and costs control (sustainability of each branch within two years, control of operating expenses, streamlined cash management systems).

The **First MicroFinanceBank Limited** was the first institution in the private sector to be licensed as a formal MFI under the regulatory framework of the Microfinance Institutions Ordinance, 2001. Commencing with an equity base and no donor funds, the First MicroFinanceBank Ltd has been the exemplary institution to operate and financially sustain under the regulatory framework, which can be vouched by operational self-sufficiency of 105.34% and financial self-sufficiency of 77.05%. FMFB has been instrumental in developing research-based products and introducing a range of financial services including savings instruments, fund transfer services and very low cost micro-insurance services, in addition to micro-credit in Pakistan.

During its learning experience in microfinance, the **Bank of Khyber** has identified a series of successful practices:

- Individual lending is a costly practice, but it is an essential service to offer to clients.

- Staff motivation and capacity building is crucial for the institutional development of a microfinance program.
- Loan portfolio quality is improved with smaller loan sizes and shorter terms.
- Dependency on external funding, rather than on savings mobilization, creates impediments for further growth.
- Commercial banks cannot reach clients at the grassroots level, but rely on intermediaries and on other mechanisms.

The **Urban Poverty Alleviation Program (UPAP)**, part of the NRSP, has placed significant focus on the timely and efficient recovery of loans. With a recovery rate of approximately 99%, UPAP is sustainable, keeping its cost down through low profile settlement offices and its closeness to clients.

Best Practices Among Supporting Organisations

The **Pakistan Microfinance Network** publishes a Performance Indicators Report (PIR) bi-annually, with the aim of improving transparency and efficiency within the microfinance sector in Pakistan. Started in 1999, the PIR includes indicators on sustainability, efficiency, portfolio quality and savings mobilisation. It also provides a sector overview and an analysis of the performance of individual members.

The PIR sets industry benchmarks in Pakistan, while promoting self-regulation and credibility within the microfinance industry. As reported by PMN, PIR has been instrumental to changes in the Pakistani microfinance industry, for example in separating microfinance from other development activities, promoting delinquency management and allowing individual members to compare their performance over time and against peers. PMN has established close links with the Microbanking Bulletin (MBB) in setting indicators and defining and calculating ratios.

Standards

The Pakistan Microfinance Network has pioneered the push for a standardized representation of financial and operational data among MFIs in Pakistan. Its Performance Indicators Report remains the most accurate and comprehensive source of information on practices and standards in Pakistan.

Client Outreach

The largest outreach is obtained by organisations using community-based methodologies – namely Rural Support Programs and the National Rural Support Program (largest microfinance provider). However, the Grameen model has progressed rapidly in recent years and increased significantly its outreach, with the successful example of Kashf Foundation.

Recovery rates

The Grameen/solidarity group model maintains the highest recovery rate of any of the methodologies used in Pakistan, with a recovery rate of 99.5% as of May 2002. Two thirds of PMN members post recovery rates higher than 95%. Peer pressure and group supervision to ensure timely loan repayment appear to be the most effective practice, although, this high recovery rate could possibly be attributed to the smaller loans offered.

Financial and Operational Self-sufficiency

Organisations using a mixed methodology, combining individual lending and CBOs, seem to have a higher operational self-sufficiency. As of December 2002, only the NRSRP, Orangi Pilot Project and the First Microfinance Bank were financially self-sufficient (ratio above 100%). Kashf Foundation was operationally self-sufficient.

Portfolio at Risk

Reported in mid-2002, the Grameen/solidarity group model was the only methodology for which organisations post a PAR under the 5% internationally accepted threshold. As of the end of 2002, Kashf Foundation and the First Microfinance Bank were the best performers, with respectively PAR at 0.2% and 0%, followed by Taraqee with 2%.

Best Practices Among Funding Organisations

The literature suggests that donor organizations should ensure their financial support has the maximum impact possible. An emphasis is placed upon the need for extensive research on funds recipients and to ensure that the aims the MFI holds are commensurate with those of the donor. Furthermore it is suggested that donations be made to those organizations that are operating in line with best practice, norms of the day including;

1. Reliance on market-orientated interest rates,
2. Emphasis on providing incentives and facilities for saving mobilisation;
3. Commitment to achieving financial self-sustainability; and
4. Procedures aimed at reducing transaction costs.

Sources

- *'Country paper on Pakistan microfinance in the private sector'*. Roshaneh Zafar, Managing Director, Kashf Foundation. November 2002;
- *Performance Indicators Report, January-December 2002. Report No.6* Pakistan Microfinance Network;
- *Pakistan National Development Report 2003*, UNDP