CGAP

The Poverty Audit

Guidelines for Determining the Depth of Outreach and Poverty Impact of Microfinance Institutions

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POVERTY AUDIT[1]

I The Context

The purpose of the Poverty Audit is to determine to what extent an MFI program is predicated on an institutional vision of addressing issues of poverty and catering to the felt needs of the very poor. It seeks to separate out mere public pronouncements from a concrete and sustained commitment to a poverty focus. For this it is necessary to identify how institutional practice and action, through the adopted methodology and through products and services, actualizes the poverty vision.

The Poverty Audit is designed to be used as an integrated element of the CGAP MFI Appraisal Format. As part of the appraisal format it complements the focus on financial sustainability so that donors can identify and make funding decisions based on the twin criteria of poverty focus and institutional viability. The Poverty Audit can also be used as a stand alone tool to determine poverty performance of an MFI and to track performance changes.

The Audit concentrates on five sets of issues:

- the stated vision of the program and how leadership commitment and institutional history provides validation for it
- the targeting strategy and how it reflects the poverty orientation of the program; the depth of outreach of the program
- staff-client interface and assessment of staff responsiveness to client welfare
- the extent to which the thinking behind product design and changes stem from an understanding of poverty and vulnerability
- the extent to which program participation has contributed to changes in client well being

The second section of the Poverty Audit is a set of questions that are meant to be an indicative check-list of issues that need to be addressed, rather than a questionnaire in an interview setting. The third section provides guidelines on how to conduct the poverty audit. Information needs to be gathered through meetings with the MFI leadership, senior staff, field staff, clients and if possible through discussions with some non clients. It is crucial that field visits be undertaken to get a feel for local level operations, for determining staff-client interface and to have a sense of the context of the program and its clientele.

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II Checklist of Issues in the Poverty Audit

2.1 Checklist of Issues: Vision

Institutional Vision

- What problems do the institution seek to address?
- Have they taken cognizance of the situation of poverty?
- How do they seek to address these problems?
- Are the causality sequences well-thought out?
- How well do the institution's strategies for addressing poverty respond to the problems and constraints of the poor?
- What are the perceived trade-offs between achieving financial sustainability and serving the poor? How are/will these trade-offs (be) reconciled/negotiated?
- Is there an articulated strategy for the MFI's stated social mission?

Leadership Vision

- What is the leadership composition? What is the rationale for this composition?
- Is the leadership (both the CEO and the Board) committed to a poverty focus? Have they been able to articulate a concrete strategy for the MFI social mission?
- Is there anything in the leadership's background, in the activities they have engaged in, that indicate a poverty commitment?

Institutional History

- Have there been moments when the institution has taken stock (formally/informally) of its poverty commitment?
- How has such stock-taking influenced programmatic interventions?
- Were there any moments of crisis (natural calamities, political conflicts etc.) where institutional response was motivated by interests of the poor?
- Has MFI mission changed over time? Has new client poverty profile changed over time?

2.2 Checklist of Issues : Targeting Strategy and Poverty Outreach

- What is the targeting criterion? How does it relate to the poverty profile of the country?
- Who are excluded and why?
- Who self-select themselves out?
- Who drops out and why?
- Have any steps been taken to understand and address these problems?

(The CGAP Poverty Assessment Tool needs to be used for empirical information on depth of outreach.)

2.3 Checklist of Issues: Staff-Client Interface

- Do staff incentives promote a poverty focus? Does the recruiting process attract staff committed to reaching the poor?
- Is there a cultural and social compatibility between staff and very poor clients?
- What training/directions do staff receive for providing services in a way that is sensitive to poor people’s lives?
- Do staff have "human" relationship with clients?
- Is staff concerned with client welfare? How is this demonstrated? How is this concern reinforced by management?
- How does staff respond to client problems/ crisis?

2.4 Checklist of Issues: Products and Services

- How well do the products on offer reflect the needs/preferences of poorer clients?
- Has there been any formal/informal assessment of product relevance for various categories of the poor?
- Does the program offer any products especially designed for poorer clients? are there specific loan products designed to assist them during crisis?
- Does design of existing products lead to the exclusion of certain categories of the poor? Is there program pressure to force clients to take on larger loans and constant repeat loans.

2.5 Checklist of Issues: Impacts

- Has the institution conducted any impact study? What are the results? How valid is the methodology? How have the findings influenced program decisions?
- Has there been improvements in the economic conditions of clients? Are clients better able to cope with crisis and lean periods?
- Are clients "planning" for the future instead of being engaged in day to day survival? What are the qualitative changes in this "planning" over time?
- Has program participation contributed to increasing confidence and empowerment?
- Has there been an increase in status within the household? Within the community?

III Conducting the Poverty Audit

Information on the five sets of issues defining the poverty focus needs to be collected at different levels. These include reviewing reports and publications both on the MFI itself as well as the general poverty and microfinance context, discussions with management and staff, clients, and if possible non-clients. The following table summarizes the various activities of the poverty audit:

Activities	Sources of Information	When
Country level poverty documents	Country HDR, Country Poverty reports, Poverty Reduction Strategy papers	Prior to arrival. Consult with CGAP and MFI to be appraised to locate resources
MFI reports	- Annual reports, Impact studies, Market studies etc. - Socio-economic context and profile of regions served by MFI	- Prior to arrival. Consult with MFI - MFI to provide
Head-office briefing	-Vision, mission. -Client profile and targeting methodologies -Products and services—rationale, history -Impacts -Selection of two field sites to be visited	Day 1 activities.
Field activities	- Briefing with staff on center history - PWR of neighborhood/village - Center members placement in PWR - Discussion on non-participation/exclusion - Discussion on impact and its dimensions - Identifying clients for detailed interviews	Day 2 and Day 4 activities
Field activities	Detailed individual interviews of clients and non-clients to determine poverty targeting, vulnerability reduction and economic well-being.	Day 3 and Day 5 activities
Sharing at Head Office	Discussions with HO and field staff on connecting learning from the field with poverty focus of institutional vision, strategy and operations.	Day 6 activities

Information Collected Prior to Arrival

The appraiser should seek to collect some basic information prior to arrival at the MFI. Information on the poverty context of the country is often available from country background documents of UNDP, the World Bank and the regional development banks. For some countries, the UNDP produces country level Human Development Report. Recent World Bank PRSP initiatives can also be valuable resources to understand the general poverty context of some countries. Often, the MFI can point the appraiser in the right direction in identifying and locating such background resources. The appraiser

might also want to contact and discuss the issues of depth of outreach of the MFI industry in the country to get a sense of relative poverty focus of the MFI to be appraised.
The MFI should be asked before hand to produce a summary (2-3 pages) description of the socio-economic context and general poverty profile of the regions they are working in--- this would provide a sense of the geographical targeting (This might not be necessary in case a program is working nation wide). MFI annual reports and general literature would also provide background information on MFI history, vision, client profile, targeting methodology, products and services. Prior to arrival, the appraiser also needs to find out whether any formal impact studies have been conducted. If so, what are the main findings regarding poverty outreach and impact. MFI feedback on the methodology and general credibility of the findings would also be useful. The appraiser might also want to find out if and how the findings have affected operational decisions.

The whole poverty audit is essentially a process whereby such background information is reviewed, clarified and enriched against information from the head office, from staff and client interviews and from what the appraiser observes during the trip.

Head Office Meeting

The appraiser will spend the first day at the head office being briefed about the vision and the history of the MFI and about products, services and systems. At this meeting the appraiser needs to get detailed information on the development of the institution, on the development of products and on commitment and strategic thinking on poverty.

Field Level Discussions and Interviews

The appraiser need to spend the next four days (from day 2 to day 5) meeting with field staff and clients. A major purpose of these field visits is to understand the depth of outreach of the program as well as program impact. Since impacts take time, the appraiser needs to select areas where the program have been in operation for some time. This is also important for assessing if there has been any changes to the depth of outreach over time. Care should be taken to ensure that the sites selected are not unusual or unique. Given the constraints in time it is suggested that appraisers visit two sites and spend two days in each site.

Discussions with Staff

The appraiser needs to have detailed discussions with field staff on the history of the center, the problems encountered in working there, the first people targeted and the rationale for it, the economic and social lives of clients, and the changes that have taken place.

Discussion should also focus on the appropriateness of the financial products (what economic activities do the loans support? how do the clients manage repayment, especially during seasonal lean periods? are there any financial products for emergencies? what is the policy on repeat loan increases? are clients compelled in taking larger loan leading to additional burden?) and staff interaction with clients (staff response to moments of client crisis, cultural and social compatibility between staff and very poor clients, etc.) In these discussions, it is important to involve fieldworkers who have preferably been working with a set of clients for some time.

Discussions with Clients

The client level discussion will determine the following:

1. Relative depth of outreach
2. Impact assessment
3. Products relevance for the poor

Relative depth of outreach

Once the specific areas/ centers/ villages have been selected the appraiser should sit with field staff and the client group to identify the different dimensions of poverty. This would form the backbone for the assessment of depth of poverty outreach and impact. It is thus extremely important that clients are encouraged to describe *their* sense of well being. Other dimensions need to be suggested as appropriate. The appraiser should however have a sense of a set of key poverty related variables in mind based on the background reading of country poverty documents many of which increasingly use a holistic notion of poverty and well being. Specific dimensions of well being based on ethnographic research in different countries have been used to provide an indicative framework below.

Dimensions of Poverty and Well-being

	Hard Core Poor	**Poor**	**Vulnerable Non-Poor**	**Well Off**
Sources of Income				
Levels of Income				
Food Consumption				
Land Ownership				
Housing				
Household Assets				
Empowerment				

Discussion should then focus on a participatory wealth ranking exercise of the village population/community. This is a rapid and effective way of situating clients vis a vis the general population of the community according to levels of well being. While the CGAP Poverty Assessment Tool need be used separately to determine depth of outreach, this exercise too provides a general understanding of who participates and who do not.

The CGAP Poverty Assessment Tool

The CGAP Poverty Assessment Tool (developed in conjunction with the International Food and Policy Research Institute - IFPRI) provides transparency on the depth of poverty outreach of MFIs. It provides rigorous data on the levels of poverty of clients relative to people within the same community through the construction of a multidimensional poverty index that allows for comparisons between MFIs and across countries. It has been primarily designed for donors and investors who would require a more standardized, globally applicable and rigorous set of indicators than what conventional targeting tools provide, to make poverty focused funding decisions. It has been successfully tested in seven countries.

The tool involves surveys of 200 randomly selected client households of specific MFIs and 300 non-client households. The questionnaire includes a variety of indicators to capture the multidimensionality of poverty and to provide for a better approximation of poverty levels. The survey collects information on the demographic structure and economic activities of households, on their footwear and clothing expenditure, on food security and vulnerability, on housing indicators, land ownership and on ownership of assets.

Bivariate analysis of the data provides immediate comparisons of clients and non-clients in terms of different indicators. However the key feature of the Poverty Assessment tool is the Poverty Index. The poverty index is constructed through the application of principal component analysis (PCA). The PCA method is applied to determine how information from various indicators can be most effectively combined to measure a household's relative poverty status. Which combinations of indicators prove the most instrumental in measuring relative poverty in a given survey area will differ, and often in ways that are somewhat predictable. In countries where poverty is extreme, indicators signaling chronic hunger tend to differentiate the relative poverty of households. In densely populated countries, ownership of land and dwellings may better signal differences in relative poverty. The end result of PCA is the creation of a single index of relative poverty that assigns to each sample household a specific value, called a score, representing that household's poverty status in relation to all other households in the sample. The lower the score, the poorer the household relative to all others with higher scores. The scores of MFI client households and non-client households are then compared to indicate the extent to which the MFI reaches the poor. Each assessment study includes a random sample of 300 non-client households and 200 client households. To use the poverty index for making comparisons, the non-client sample is first sorted in an ascending order according to its index score. Once sorted, non-client households are divided in terciles based on their poverty index score: the top third of the non-client households are grouped in the "higher" ranked group, followed by the "middle" ranked group and finally the bottom third in the "lowest" ranked group. Since there are 300 non-clients, each group contains 100 households each. The cutoff scores for each tercile define the limits of each poverty group. Client households are then categorized into the three groups based on their household scores. If the pattern of client households' poverty matches that of the non-client households, client households would divide equally among the three poverty groupings just as the non-client households, with 33 percent falling in each group. Hence any deviation from this equal proportion signals a difference between the client and the non-client population. For instance, if 60 percent of the client households fall into the first tercile or lowest poverty category, the MFI reaches a disproportionate number of very poor clients relative to the general population. It would prove that the MFI is deliberately targeting the very poor. On the other hand if the majority of MFI clients fall into the least poor tercile, one would know that the MFI is not reaching the very poor.

A detailed manual explains how to implement the Poverty Assessment Tool.

The appraiser needs to classify attributes of different groups of the population (hard core poor, poor, etc) by asking participants for distinctions between such groups. For example on food consumption, the appraiser needs to probe to determine what exactly would be the difference, if any, in consumption patterns between the groups. The response might be that the hard core poor face food deficit throughout the year and only eat once during the lean season, the poor generally have enough to eat but consume inferior food especially during the lean season, the vulnerable poor have enough to eat through out the year, the well off eat fish or meat with all their meals. On household assets what may separate the hard core poor from the poor is the ownership of winter clothing or footwear. The vulnerable non-poor may own radios and the well-off may own TVs. It should be realized though that not all categories may be very neat or very descriptive of differences. The point is to try to understand how local people perceive of differences in different groups within the community.

Once such classification is done, participants need to be asked to put specific households within each category. The hard-core poor, the poor, the vulnerable non-poor and the well off in each community would therefore be identified by name. When this is done participants would be asked to identify MFI clients. The appraiser can then determine who MFIs are targeting in terms of client economic and poverty levels. If an MFI is targeting the very poor, most clients would fall within the groups of the poor and the hard-core poor. The appraiser should also try to understand the various forms of exclusion, especially of the very poor.

Impact Assessment

The discussion then moves to the changes that have taken place in their lives since joining the program. However appraisers should also realize that changes are often slow and difficult to attribute to any single event. What is therefore required is not a rigorous proof of the quantitative levels of impact controlling for all other variables nor strict proof of causality but a sense of general trends. The following explains what changes may be expected in different dimensions of well-being identified in the illustrative matrix above.

- Sources of income: For poor people access to microfinance often opens up new income earning opportunities. While levels of income from these new opportunities may not be high, it allows for both a diversification of sources of earnings and better use of household labor. This leads to better crisis coping as well as more sustained income increases. The appraiser should therefore determine whether access to microfinance has diversified income sources. This may not be revealed through direct questioning of sources of earnings because the concepts of work, income and earnings culturally vary.

- Levels of income: it is difficult to get at quantitative estimates of income. What should be attempted is a determination of whether income has increased and find out how and whether this increases are due to program participation. The assessment of income levels need to be tied in with sources of income. New expenditure saving activities (e.g. homestead gardening providing vegetables that they would earlier have to purchase from the market) need also to be accounted for.

- Consumption levels during lean periods and seasonal shortfalls: Economic activities tied to the agricultural cycle result in low employment and earning opportunities during specific seasons. Other activities such as road construction are also seasonal. This translates into lowered levels of consumption for the poor at specific times. The appraiser needs to determine whether program participation has led to a smoothening of consumption levels so that even during lean periods clients can dip into savings or their extra incomes from microfinance funded activities to ensure that they continue to have two (or three) meals a day.

- Coping with emergencies (natural calamities, illness etc.): poverty is about increased vulnerability to life cycle and economic shocks. Even the most rigorous econometric testing point to the positive impact of microfinance in reducing such vulnerabilities. The appraiser therefore needs to determine if and how clients have increased their resilience in dealing with various kinds of emergencies. It is however important to realize that many such changes are very subtle, such as being seen as more creditworthy by informal lenders and well-off relatives and/or being able to take advantage of less exploitative forms of informal financial contracts. Such qualitative changes are quite important in terms of the ability of the poor to deal with risk without taking steps having long term adverse affects (such as withdrawing children from school or selling key assets)

- Household assets: ownership of household assets is an effective indicator of economic status of households. Only a few culturally sensitive asset indicator need to be chosen to determine economic levels. E.g. ownership of sandals (or winter quilt) separate the hard core poor in Bangladesh from the poor and radios separate the poor from the non-poor. Appraisers need to identify specific indicators from the discussions with staff and client groups.

- Housing: housing can also be an effective indicator for differentiating between economic groups. MFIs use the CASHPOR housing indicator or variants of it, very successfully in South Asia. The housing indicator however sometimes does not work well (as in urban areas or as reported in South Africa), and it is important for appraisers to use it only if they

- Land ownership: In land scarce rural regions (such as in south Asia) land ownership effectively separates out the poorest (landless) from the marginal landholders, from the surplus landowners and the large landlords. In certain situations land ownership criteria needs to be further modified according to type of land (irrigated land, non-irrigated land, cultivable land, fallow land).

- Empowerment: being powerless is a critical dimension of poverty. Poor people, especially poor women in patriarchal societies, lack confidence in negotiating public space and in accessing public resources. Microfinance, in providing the poor with economic resources, in building social networks, help increase self esteem and initiate a process whereby the poor gains the courage to plan for the future instead of living from one day to the next. Such attitudinal changes are too easy to neglect but are powerful in terms of their mobility perceptions.

Product relevance for the poor

Client discussions should probe on issues related to financial products, program rules and their appropriateness for the poor, such as, what economic activities do the loans support? how do the clients manage repayment, especially during seasonal lean periods? are there any financial products for emergencies? what is the policy on repeat loan increases? are clients compelled in taking larger loan leading to additional burden? Etc.

If time permits, the discussion on impact and product relevance could also be further probed with individual clients.

Discussions with Non-clients

There should also be some discussion with non-clients on reasons for non-participation, if there are any program/product-driven exclusion, the targeting effectiveness of the program, impact on participants and changes at the level of the community.

Head Office Sharing

After four days of field visit and interviews, appraisers need to hold a discussion at the head office with management and field staff. The purpose of this discussion would be to tie in field observations with the management briefing of program vision and operations. Appraisers need to use this discussion to probe into:

- the targeting strategy and depth of outreach
- the extent to which products are pro-poor and help build client resilience to counter crisis
- the extent to which products assist in increasing economic well being
- field staff – client interface and the extent to which field staff identify with client welfare