



Quality of Aid Management for Microfinance Index

Submission Guide

Background. Since 2002 CGAP has worked with its members to promote more effective aid to microfinance. Seventeen Microfinance Donor Peer Reviews revealed five core elements needed for agencies to improve the way they work, namely: strategic clarity, staff capacity, accountability for results, knowledge management, and appropriate instruments.¹ Further evidence of the importance of the five elements (known as the *Aid Effectiveness Star*) was found in the subsequent Portfolio Reviews, Peer Review Check-ups and Country Level Effectiveness and Accountability Reviews (CLEARs) facilitated by CGAP.² These efforts have been well received and, in many cases, prompted concrete changes. The CLEARs, in particular, have reinforced the importance of coordination and collaboration with microfinance stakeholders in-country.

In October 2006 CGAP's member donors agreed to act on the findings of nearly four years of investigation and learning by signing the Compact for Better Aid for Access to Finance. The Compact puts forth four commitments for donor agencies: to measure the quality of aid management; to implement the "Good Practice Guidelines for Funders of Microfinance"; to improve field-level coordination; and to partner with the private sector.³

As part of the effort to measure the quality of aid management, CGAP has worked with its members and external technical experts to develop the Quality of Aid Management for Microfinance Index. The hypothesis behind the Index is that effective policies and practices are a necessary, although not sufficient, condition for good performance. Therefore, the purpose of the Index is to measure whether development agencies have effective policies and practices in support of microfinance. Specifically, the Index seeks to assess the adequacy of agencies' internal management systems to help them determine where change is needed to increase the effectiveness of systems, policies, and procedures. Much like the Microfinance Donor Peer Reviews, the Index will be carried out in the spirit of mutual learning—the intent is not to judge or criticize but rather to create a momentum for improvement. Given the complexity of this task, the current version of the Index will be tested during a pilot round in 2007. Several feedback moments as well as an assessment of the Index's usefulness and cost-effectiveness are planned as part of the pilot.

The CGAP operational team reviewed the structure, methodology and lessons learned from other indices, such as the Commitment to Development Index (CDI) and the Doing Business

¹ Please refer to http://www.cgap.org/Projects/donor_peer_reviews.html for more information on the Microfinance Donor Peer Reviews.

² Please refer to www.cgap.org/clear for more information on the CLEARs, and to Focus Note 35 for more information on the portfolio reviews

<http://www.cgap.org/portal/site/CGAP/menuitem.2319fcd20442bc5167808010591010a0/>.

³ Please refer to <http://cgap.org/docs/donorguidelines.pdf> for a copy of the Guidelines.



Index. Similar to other indices, the goal is for this Index to include indicators that are simple and clear and which, taken collectively, are comprehensive and clearly relate to effective aid management. The indicators are grouped along the five elements of the *Aid Effectiveness Star* and several indicators also include practices related to in-country collaboration.

The purpose of this document is to explain the rationale and importance of each indicator, describe what it seeks to measure, and how it might be measured. It also includes annexes with definitions of terms (Annex I) and CGAP's charter reporting requirements (Annex II). When first mentioned, terms included in Annex I are presented in bold, italic print.

Guidance for Reporting to the Index. For each indicator there is a list of Illustrative Evidence. Because agencies are organized and operated differently, it is impossible to draft a generic list of evidence that is meaningful for all types of agencies. Agencies should reflect on what evidence they have that best responds to the intent behind what each indicator seeks to measure, and then determine which of their documents or information best relate to the indicator.

If a suggested document does not provide “evidence” of the current policy or practice, it need not be included. If an indicator is sufficiently addressed in one document (a primary source) or in a single list then no additional documents must be provided. It is possible that the information will not be found in a single document and may need to be collected and organized from secondary sources. If neither primary nor secondary sources provide sufficient evidence, agencies may submit a concise (½ page) summary on their current policy and practice, on how thoroughly it is implemented, and any limitations or exceptions.

In a few cases, the agency may only be able to provide samples of its current practice. Sampling, however, presents some challenges because (1) it is difficult for the review board to know the extent to which the sample is representative of the whole, and (2) samples take a longer time to collect and review. The review board will consider how representative the sample is when scoring.

As a rule, the review board will rely on the good faith and signed representations of the agencies' technical officers (e.g. *focal point* or other). Submission of any description of agency practice thus implies that the description is accurate, prevails agency-wide, and is representative of the agency's general practice rather than an example of optimal practice.



1 STRATEGIC CLARITY measures whether the development agency has a *microfinance policy* aligned with good practice that is shared throughout the agency

1.1 *Microfinance* (building inclusive financial systems) substantially addressed in a policy that is in line with major principles of the “Good Practice Guidelines for Funders of Microfinance”

A coherent vision improves quality at every level of an agency. A vision does not dictate one way to support *microfinance*; rather it provides support to diverse approaches and priorities within a framework of basic good practice principles.

Strong policies and a clear vision are mutually reinforcing. Agencies with strong policies that adhere to international standards increasingly embrace a financial systems development approach rather than emphasizing credit as an input or resource transfer. Agencies’ policies should be in line with internationally accepted and endorsed principles of good practices as codified in the “Good Practice Guidelines for Funders for Microfinance.”

Agencies should have a document that lays out their vision and goals in microfinance, including how microfinance is linked to their overall development mission. The microfinance policy should also articulate the principles, guidelines or standards that set a definite and binding common approach for agencies’ actions in microfinance.

Illustrative Evidence. A copy of the microfinance policy. The policy can be distinct or included in a larger private sector or financial sector policy. Where no centralized agency-wide microfinance policy exists, regional or country policies may be submitted.

1.2 *Senior management* commitment to good practice microfinance principles and evidence of agency-wide dissemination

Changes to improve effectiveness in microfinance (and probably other areas) are more likely to be implemented with the strong support of senior management. Such support can come from the head of agency or other senior manager(s). Even in cases where operational staff are the active “champions” of change, the support of senior management that is willing to publicly endorse staff views and emit a forceful edict can be a powerful force for change.

The senior management “champion” does not need to be a specialist on the subject, but should recognize the institutional importance of adhering to microfinance good practice principles. In an agency with decentralized authority, the agency needs regional or country directors that also understand the institutional importance of adhering to good practices. Acknowledging good practice principles is important because some microfinance good practice principles run counter to internal



incentives within agencies (i.e., disbursement pressure, preference for large *programs*, working through governments). Committed senior management can help provide countervailing incentives for good microfinance programming.

The senior management “champion” should enjoy high visibility and significant clout within the agency to attract colleagues’ attention to the subject and be able to make decisions about internal systems changes that affect microfinance (e.g., reporting systems or use of instruments). Senior management should also send strong signals to help ensure that good practices are internalized and translated into results on the ground.

Illustrative Evidence. Documents that demonstrate senior management support for good practice principles in microfinance programming (not simply support for microfinance). Relevant documents are those that highlight senior managements’ attempts to affect the behavior of staff (and contractors) such as endorsement and dissemination of policy statements, procedural guidelines, etc. Other relevant materials might include messages in key meetings as recorded in official minutes; commentary in speeches, interviews, or publications; participation in relevant events, etc.

1.3 Agency’s microfinance policy/strategy recognizes and addresses its capabilities and constraints and where it can most add value

Though a wide range of donor interventions are useful to help build inclusive financial systems, not every agency effectively can or should work at all levels of the financial system. All agencies should consider their capabilities and constraints when formulating their policies and strategies for supporting microfinance.

While policies can be very broad, a good *microfinance strategy* brings focus to the policy, including what an agency can do best given its structure, resources (personnel, financial, instruments, influence, experience) and positioning vis-à-vis other donors and investors.⁴ A strategy should clearly articulate the agency’s perceived advantages and constraints. Such a policy and/or strategy may be agency-wide or at the regional or country level, depending on which is most appropriate for the agency.

To start, agencies should identify their comparative advantage. Comparative advantage may vary from country to country and change over time. Agencies’ analysis should include lessons learned from the agencies’ experiences as captured in information systems or evaluations (e.g., *portfolio reviews* and synthesis studies). Agencies should take into account others’ experiences as well as overall changes in the industry. Comparative advantage can also be influenced by historical track record, geopolitical influence and long experience with specific modes of operation.

⁴ Agencies typically use many different names for what can be considered a policy or strategy. The name of a document is not what is important; but rather the content.



Agencies can use the five elements of aid effectiveness (Aid Effectiveness Star) as one input to determine their comparative advantage.

Illustrative Evidence. The analysis of the agency's comparative advantage may come in a distinct microfinance strategy document or a part of a larger private sector, financial sector, or regional/country strategy document. They can also be articulated as part of agencies' policies. The analysis of agencies' capabilities and constraints may be documented elsewhere, such as in an agency evaluation, presentation, or other strategy documents with a SWOT analysis.⁵ Some evidence that the analysis and the strategy are linked is suggested.

1.4 Compliance with good practice principles checked at all stages of the *project cycle* for microfinance programs and components

A high-quality microfinance policy is only effective when it is consistently implemented. To ensure the quality of aid at entry, agencies must ensure that there are "checks" throughout key decision points in the project cycle to verify whether agreed-upon principles and standards are followed. Though these "checks" do not guarantee that principles are implemented, they do reduce the likelihood of bad programs.

Key decision points include project design (prior to approval), monitoring and evaluation. This kind of oversight is most effective if there is systematic monitoring for compliance with good practice principles as well as consequences for non-compliance. Systems and procedures should identify these key decision points, for example, the requirement to obtain technical clearance prior to a full feasibility study.

Measures that are binding are most effective. However, even non-binding measures can help by promoting a supportive and encouraging environment for compliance with good practice principles. This might include positive incentives for staff awareness of the principles, seeking expert advice, and instituting quality monitoring systems. Agencies can also conduct selective quality checks at all stages of the project design based on the size, strategic nature of the program or other key criteria.

Illustrative Evidence. Project cycle policies and procedures, highlighting key decision points and decision-makers, levels of approval, information required, and whether a process for monitoring compliance is in place. Evidence should indicate at which stages technical expertise or review is included, and if technical clearance or approval is required. Technical clearance or approval is different from a non-binding technical review.

⁵ SWOT is a matrix of Strengths, Weaknesses, Opportunities, and Threats



2 STAFF CAPACITY measures whether the development agency has staff with microfinance expertise to ensure quality of design, implementation, and monitoring of programs

2.1 Designated focal point with microfinance/financial sector experience and responsibility to provide technical advice to program managers

Experience from the *Microfinance Donor Peer Reviews* and Portfolio Reviews strongly suggests that any agency interested in directly supporting microfinance needs an in-house person (or persons) who is a *microfinance specialist* to serve as an internal resource for technical advice and quality assurance.

A focal point should be responsible for spreading good practice principles across the agency. Key roles include 1) facilitating networking and knowledge sharing among staff working on microfinance and the broader industry; 2) providing technical expertise in the early stages of project design and references for outsourcing work; 3) assuring quality during all stages of the project cycle; and 4) facilitating systems for identifying the microfinance portfolio and tracking performance. These roles could be carried out by the focal point directly, or coordinated by the focal point drawing upon his/her network of experts.

Typically, focal points need to balance advisory work with that of managing their own programs. Full-time technical microfinance specialists who have incentives to engage with staff who are not microfinance specialists are the most effective focal points. Without a *mandate* or clear incentives to get involved, focal points may face skepticism and work only with the most receptive colleagues.

The size and location of focal points may differ depending on the structure of each agency, but should be related to the overall microfinance portfolio of the agency, the extent of microfinance expertise beyond the focal point, and the type of interventions supported. Focal points can be gathered in a central unit, or regionally based.

Illustrative Evidence. Any written description of the focal point function, such as terms of reference, job description or summary of key tasks, including comment on whether project management is a key responsibility; list of persons in the focal point and their CVs.

2.2 Agency makes resources available for technical expertise to be involved in the design of all microfinance programs and components

The trend in most agencies is to hire generalists rather than specialists. In some agencies, most microfinance programs and components are managed by staff with little or no microfinance expertise. Yet, the CGAP-facilitated Portfolio Reviews of several agencies confirm the strong link between access to technical expertise and high quality programs.



As stated in 2.1, all agencies active in funding microfinance should have in-house microfinance expertise. To complement the work of the focal point and other in-house microfinance specialists on programming, agencies can find creative ways to increase access to microfinance expertise in headquarters and in the field. Especially for staff without microfinance expertise, incentives should be established for them to systematically seek technical advice early in the project design stage.

Some options for obtaining advice include: placing specialist staff within the agency, recruiting national specialists in-country, and investing in strengthening the focal point. External solutions include regular use of expert consultants for technical troubleshooting, establishing lists of pre-qualified technical service providers and consultants, and signing contracts with local or regional service providers. When outsourcing, agencies should focus on the specific technical expertise required, not only on consultants' or firms' knowledge of the agencies' procedures and policies.

Illustrative Evidence. A list of in-house microfinance specialists, including sample CVs; budgets available for consulting services in the design stage of the project cycle; procedures for accessing specialized expertise; consultant roster, etc. Evidence should demonstrate that access to in-house and external expertise exists and is actively promoted.

2.3 Agency requires and verifies that all staff who manage microfinance programs and components have training/experience

Typical program managers work on diverse sectors. Although microfinance may represent a small part of their portfolio, managers are responsible for many technical decisions that affect the quality of microfinance programs. Such staff require basic knowledge of microfinance good practice principles.

Agencies can significantly improve microfinance knowledge within the agency by developing a minimum level of technical capacity among program or regional officers managing a microfinance portfolio. Not all managers of microfinance programs and components need to be microfinance specialists. At the very least, they should be informed consumers of microfinance technical expertise who are able to ask the right questions, select qualified consultants, and interpret performance reports.

Recognizing that it may not be financially or politically feasible to hire a large number of specialists, agencies should establish minimum standards for all staff managing microfinance and ensure compliance. A minimum standard is three days of *microfinance training* from well-qualified providers or two years of prior *microfinance experience*. (i.e., not including experience on the program or component currently being managed). This standard is a strict minimum and, in most cases, would not be fully sufficient. The right number of training days/years of experience depends on the extent and nature of agencies' involvement in



microfinance. Agencies should put in place the procedures, incentives and resources for adhering to this standard.

Illustrative Evidence. Description of in-house and/or external microfinance training, including frequency and list of attendees; up-to-date documentation that tracks all staff managing microfinance programs and the training they have attended; and arrangement or contract with qualified training providers to regularly train agency staff.

2.4 Agency places microfinance specialist staff in countries/regions where it has its most significant portfolio of microfinance programs and components

An effective strategy for agencies to allocate scarce technical resources is to place microfinance specialists in the countries/regions with their largest microfinance portfolios. Placing microfinance specialists in the field can result in higher program quality in several ways: it provides for more timely and appropriate technical inputs and oversight at all stages, and it facilitates engagement and coordination with local stakeholders on issues related to microfinance.

Microfinance specialists should at minimum have five years of microfinance experience. They could be either in-house donor staff (preferred option), or outsourced staff with a mandate to provide support to programs and represent the agency in donor coordination groups and other fora. Specialists could be full or part-time, based in one country or in the region.

Agencies must determine how to prioritize the placement of scarce resources. The size of the program, however, should be a major criterion. Programs that fund more than \$2 million per year could be candidates for specialist placement. Another approach is to place microfinance specialists in the countries/regions with the three to five largest microfinance programs.

Illustrative Evidence. List of countries with large microfinance programs and components accompanied by list of microfinance program managers working in those countries, whether they are microfinance specialists, and the amounts of the microfinance portfolio.⁶ Another approach might be to indicate where agencies' microfinance specialists are located provided that the size of the programs by country and region is also submitted (see indicator 3.1). It would also be useful to have a definition of the geographic regions used by the agency.

⁶ The definition of "large" should be based on agencies' overall microfinance portfolio.



3 ACCOUNTABILITY FOR RESULTS measures whether the development agency has systems in place that ensure the transparency and performance-based management of microfinance programs and components

3.1 System in place to identify microfinance programs and components from design to disbursement

Some agencies do not know how much money they have invested in microfinance. This “invisible” microfinance happens because programs often originate in numerous departments, the agency lacks a clear vision or definition of microfinance, and internal project coding systems do not identify *microfinance components* of larger projects. Agricultural finance, community development funds or other types of revolving credit funds frequently remain invisible and are far more likely to perform poorly.

Agencies need appropriate systems that make it possible to identify all microfinance, even when it is a minority component in a larger program. Only then will it be possible to ensure the appropriate technical input at the design and other stages of the project cycle. Such systems should be accessible to agency staff and should annually track basic information on all microfinance programs and components, including 1) country/region; 2) funding amounts (disbursed and/or committed); and 3) key staff contacts for the program.

Agencies’ systems should identify microfinance programs and components in the early design stages so that technical input can be brought to bear from the beginning. For the purposes of the Index, microfinance components do not refer to microfinance portions of broader, financial sector programs, or clearly separated microfinance programs within a broad country program; rather they refer to microcredit that is imbedded in other sector programs.

Illustrative Evidence. Working definition of microfinance that the agency uses to determine which operations are subject to the policies (e.g., expert review or reporting requirements) associated with microfinance and a description of the process or system for identifying microfinance programs and components. If possible, agencies should submit printouts from the information systems listing all active microfinance programs and components by country/region with amounts. If this is not possible, an agency may submit other manually-created lists of such programs and components, with an explanation of how they have been compiled and any limitations or shortcomings of the system.

3.2 Microfinance/financial sector specialist required to review microfinance programs and components

Microfinance often requires a considerable amount of technical input in relation to the amount of funding. It requires a business-oriented approach grounded in a clear understanding of banking and finance.



Disbursement pressure is present in every development agency and can override good design. One approach to counter this risk is for agencies to require microfinance/financial sector specialists to review all microfinance programs and components against good practice principles prior to approval. This type of review is especially needed for microfinance components as they are often designed by staff without microfinance experience and have generally performed poorly.

A microfinance/financial sector specialist may either be the main designer and/or the reviewer for programs designed by others. The review should come early enough so that the microfinance specialist has some influence or ability to halt, slow, or limit funding to poorly designed programs. If this review is advisory, that is if the microfinance specialist's clearance is not required for the project to move forward, agencies should demonstrate that the specialist's advice carries weight and is not simply a matter of routine.

Illustrative Evidence Policy or procedure that requires the participation, approval or consent of a microfinance specialist; sample comments on projects by microfinance specialist; minutes of project approval meetings; and list of active microfinance programs and components that were approved by microfinance specialist.

3.3 Agency annually tracks and reports on *performance indicators* for microfinance programs and components

Tracking performance is a critical element of effective aid management. However, most agencies do not adequately track the performance of their microfinance portfolios (including all types of funding, whether financial or technical). What is not measured cannot be managed, and weak performance monitoring systems perpetuate weak providers of financial services.

Programs that are required to report regularly are significantly more likely to perform better. The more transparent the results, the more likely agencies are to learn from programming and take corrective measures when needed. To the extent possible, agencies' decisions on whether to continue, terminate or replicate a program should be guided by performance against measurable objectives. For some types of programs, particularly "meso" and "macro" level programs, performance indicators are harder to define in advance. Nonetheless agencies should have a process for determining when continued support is fruitless, ineffective or simply a waste of resources.

Some regional or centralized monitoring improves effectiveness. When microfinance performance reporting for retail microfinance is limited to the country level, performance measures are less likely to be appropriate and incentives for good performance are more likely to be weak—particularly with programs that channel direct or indirect support (through networks or apexes, for example) to retail microfinance providers.



Agencies should have systems in place to track performance and generate reports with results. Consensus has been reached on a minimum set of internationally accepted core performance indicators for programs that fund retail microfinance providers. Performance tracking is also important for work at the meso and macro levels even though it is more difficult to set standards. When creating reporting requirements, agencies should opt for reporting information that is results-based rather than activity-based, and that is consistent with the nature of the program.

CGAP members agreed on five core areas of performance indicators for retail microfinance in the “Good Practice Guidelines for Funders of Microfinance.” Such indicators should be integrated in program proposals, contractual agreements, terms of references and monitoring and evaluation documents. Indicators should be tracked for all institutions receiving agency funds for core operations or loan portfolios, whether they are directly funded by the agency or through intermediaries (e.g., programs, investment funds, apexes), and should be calculated and reported according to the standard definitions and calculations to allow performance to be compared within the agency as well as with industry benchmarks.

Illustrative Evidence. The agency policy or other authoritative guidance on microfinance performance reporting. If the agency uses a tool (database or log frame), provide a copy, screenshot or sample. Other important evidence includes the most recent list of indicators tracked and a description of how they are calculated, and a printout or other report showing performance indicators for microfinance programs and components. Core performance indicators for retail MFIs may be provided on a consolidated basis as appropriate.⁷

3.4 Agency uses performance-based contracts in its microfinance programs and components

Investing in good technical inputs at the design stage is not sufficient if there is no follow-up monitoring (at least semi-annual) during the project life. Some agencies have agreements/contracts with partners that are often not performance-based. Even if contracts are adequate, they need to be tracked and/or monitored for compliance. Otherwise, poor performance is not caught early on and may lead to major program failures.

Agencies should hold their microfinance partners and contractors accountable for their results. These relationships at all levels and with all partners (apexes, microfinance institutions, technical implementers, etc.) should be spelled out in performance-based contracts. These contracts should include minimum performance targets, a monitoring plan, and consequences for non-compliance, including suspension or termination of funding. Minimum performance targets are especially important—failure to meet them should result in serious sanctions.

⁷ Note that some indicators lose their meaning when consolidated such as portfolio at risk. The agency should indicate whether the consolidated figures are averages or weighted averages.



The nature of the minimum targets, monitoring plan and sanctions for non-compliance will differ based on the type of program. Of course, the effectiveness of performance-based contracts depends on agencies' political will to enforce them, including withholding payments or other penalties or even terminating the contracts of non-performing programs or partners.

Illustrative Evidence. Policy or procedure requiring performance-based agreements; template of an agreement; standard agreement language for monitoring and/or mid-term program review format; list of active microfinance programs and components that have performance targets and a list of those where failure to perform has led to termination or delay of funding.

4 KNOWLEDGE MANAGEMENT measures whether the development agency has systems to create, disseminate, and incorporate learning from its own and others' experience

4.1 Focal point's responsibilities and budget include *knowledge management* for microfinance

Knowledge management is about the identification, creation, dissemination and utilization of knowledge. Knowledge management entails practices used to capture and learn from agencies' own—and others'—experiences. Focal points, as the center of excellence for microfinance within agencies, are best positioned to facilitate knowledge management, both internally and with external partners. Specifically, they should be proactive in capturing lessons learned about successes with a view to replicating them.

Knowledge management should be a core function of the focal point, though not the focal point's exclusive responsibility; it should be included in focal points' terms of reference, and they should be provided the resources to effectively carry out this function within the agency. This responsibility includes delivering relevant information to staff in accessible ways, tracking relevant developments in the industry, as well as organizing internal events for staff. Focal points' annual performance reviews should include an assessment of their knowledge management function.

Illustrative Evidence. Terms of reference, annual work plan or performance evaluation of focal point; budget for knowledge management in microfinance; list of information or website links to information sources made available throughout the agency; and list of listservs or communities of practice for microfinance.



4.2 Agency systematically assesses its microfinance programs and components through reviews or evaluations, and extracts learning

Too often, agencies repeat mistakes and fail to incorporate successes into new program designs because they have not sufficiently learned from previous programs. Most agencies conduct evaluations of individual microfinance programs. Unfortunately, such evaluations rarely influence future agency operations. Thematic, regional or multi-program reviews of agencies' microfinance portfolios, or significant parts thereof, can yield more meaningful learning and inform future program designs and strategic reorientations.

It is essential for agencies to regularly assess their microfinance portfolios. Agencies should have procedures that require them to verify performance, achievement of targets, and compliance with good practice principles. These assessments can be carried out as internal or external evaluations and should require documenting lessons learned.

Illustrative Evidence. External or internal review of overall microfinance activities; list or documentation of changes introduced as a result of such reviews in the past three years; and list of microfinance publications by the agency.

4.3 Mechanism(s) in place for exchanging learning on agency's microfinance programs and latest microfinance developments throughout headquarters and field offices

Knowledge management is perhaps above all an organizational value and requires strong support from senior management. It should be valued and become an ingrained operational habit of all agencies. Effective knowledge management requires appropriate tools and mechanisms. Unless special efforts are made, the best research programs may not translate into institutional learning because of poor links between the research and operational departments.

In general, agencies require a range of mechanisms to reach staff at different levels of technical skills and different geographic locations, etc. Mechanisms to promote learning include technological platforms such as intranets, electronic resource centers, helpdesks and listservs; information resources like short briefs or newsletters; and networking events such as regional staff meetings, microfinance thematic groups, etc. Agencies should make special efforts to integrate field staff into thematic networks because they are often the best source of agency experience and institutional knowledge.

Illustrative Evidence. Link to intranet, internet or listservs; list and explanation of other internal information sharing mechanisms (newsletters, thematic networks, etc.); and a list of other methods for making information available throughout the agency.

4.4 Agency requires staff to actively engage and coordinate with key regional/country-level *microfinance stakeholders*

Increased funding for microfinance has resulted in some countries having significant numbers of agencies supporting microfinance. Without coordination between agencies, the risk of duplication or even conflicting programs is high. Agencies may give partners different signals as to what they expect and the lack of coordination among donors can be confusing and frustrating to government stakeholders.

Donor staff in-country should not only engage with other donors, but also with other microfinance stakeholders, e.g., the national government, microfinance providers, and other types of funders. When planning a microfinance design or evaluation, agencies' internal procedures should require them to notify key microfinance stakeholders in-country (donors and investors, government, practitioners) about the upcoming mission and/or the planned intervention. This upfront consultation allows agencies to avoid duplication, coordinate better with existing programs, design complementary interventions, and receive feedback.

Effective coordination in a country requires allocation of staff time and budget resources, as well as incentives to do so. Agencies should give staff the responsibility and resources to participate in in-country, regional and international forums, workshops and other exchanges. These may include on-site and virtual groups.

Illustrative Evidence. List of agency staff and their membership/participation in relevant donor groups, microfinance and other relevant fora; terms of references of microfinance specialists and managers if they include coordination/collaboration; and policy or memo highlighting the need to engage with key stakeholders.

5 APPROPRIATE INSTRUMENTS measures whether the development agency has appropriate instruments for microfinance that are used in a flexible manner and adapted to market needs

5.1 Able to work directly with *private actors*

Agencies that are able to work with a range of private actors (i.e., outside of government control) are well suited to support microfinance, especially at the micro and meso levels. At the micro level, such actors may include NGOs, regulated microfinance institutions, commercial banks, and cooperatives, etc. Meso level actors include apexes, microfinance investment vehicles, audit firms, information technology companies, and rating agencies, among others.

It is harder to do good microfinance if donors must channel all or almost all support through governments. Experience has shown that governments should usually not be directly involved in the delivery of credit services or the management of credit programs. Government ministries typically lack the technical skills and political

independence needed to manage retail level credit programs. Also, governments are often understandably reluctant to take loans from donors for technical assistance programs (rather than for on-lending), even though such assistance is important to support permanent access to financial services. However, governments are the natural partners when agencies work on the policy environment and the regulatory and supervisory framework.

Illustrative Evidence. Documentation or description of private sector engagement policy; description of guidelines for instruments available to support private actors; list and amount of support to private microfinance actors in previous three years; description of private sector strategy (or interventions); a breakdown of the percentage of microfinance programs or components where funds are directly transferred to private entities and the percentage directly supporting government entities.

5.2 Little microfinance programming is done through credit components of larger, non-financial sector programs

A significant proportion of donor funding in microfinance takes the form of microfinance components. Usually a minority component of larger, non-financial sector programs, these components include credit as a tool for achieving a range of objectives. Microfinance components come in many different shapes or sizes, but they share certain common features: (1) credit is part of a larger non-financial sector program such as agriculture, health, post-conflict rehabilitation, or social services; and (2) credit is often targeted as a one-time or limited-time transfer by the agency to a particular group of people to purchase an input or change their behavior.⁸

Microfinance components have often performed poorly. A perceived trade-off between supporting sustainable financial services and meeting specific objectives for a target group may lead donors to neglect sustainability when working through components. As a result, microfinance components often de-capitalize quickly due to high costs, subsidized interest rates that do not cover costs, and poor collection rates. In the absence of sustainability, credit services may cease when a program is completed.

Whenever feasible, agencies should avoid including microfinance services as minority components of multi-sector programs. Instead, they should institute policies to focus on building the capacity of retail microfinance providers that will be able to provide financial services in the long term. Agencies will be scored based on the percentage of funding spent on components in relation to total committed funds for microfinance, with the target of no more than 10 percent for the highest score.

Illustrative Evidence. List of all active microfinance support divided between stand-alone programs and components, including the amount of funds committed.

⁸ The group may continue to use or “revolve” the funds even if the donor withdraws support.

5.3 Nature and use of instruments are consistent with agency's strategy and with requirements for supporting microfinance well

Microfinance can be supported with a wide range of funding instruments including grants, loans, loan guarantees, equity, etc. Not every agency, however, can or should necessarily attempt to use all these instruments. Agencies do not always match or sequence instruments appropriately to their strategies and market needs. For example, in more mature markets, there is a growing need for more commercially-oriented funding instruments.

Agencies should strive to adapt their instruments to enable them to implement their strategies effectively and to be responsive to market needs. This could entail increasing the flexibility of existing instruments, developing new uses for them or even introducing new instruments. When instruments cannot be adapted to meet the strategy or market needs, the best course of action may be to abstain from launching a microfinance intervention.

Agencies whose predominant funding model is large loans to governments often have a comparative disadvantage with regard to supporting retail microfinance. Introducing flexibility and finding innovative ways to use such instruments effectively is important.

Moreover, relative to many other development sectors, microfinance often requires small programs with intensive technical inputs. The ability of agencies to adapt funding to needs, including allowing for modest program sizes with flexible, patient funding that is of appropriate size for partner institutions is important for meeting the significant capacity constraints at all levels of the financial system.

Illustrative Evidence. List of available support instruments for microfinance, including indication of those most frequently used; description and/or guidelines for use of all instruments for microfinance; and microfinance strategy.

5.4 Policies and procedures governing use of instruments allow for a range of collaborative funding and technical support

Addressing the multiple gaps on the three levels of the financial system requires a complex range of skills and instruments. There are many opportunities for agencies to work together to provide the appropriate mix of financial and technical assistance to a partner. In line with the Paris Declaration on Aid Effectiveness, aid is increasingly being delivered in a multi-donor programmatic approach.

There are numerous options for collaboration. Donors can agree on a common strategy for working in a particular country, allowing each agency to engage with specific financial system stakeholders based on their own strengths. Such collaboration at the strategic level can contribute to the consistent application of good practice principles, avoidance of duplication, and more efficient division of labor. Alternatively, agencies may conduct joint programming with harmonized procedures



and one voice, or combine their funding into a pool that is managed by the agency best equipped to do so. While such partnerships are not necessarily better than strategic cooperation, the ability and flexibility to engage in such partnerships when appropriate is positively correlated with effectiveness.

Procurement procedures and other agency rules can make some forms of collaboration unnecessarily difficult. Though the will to collaborate cannot be prescribed, even the best of intentions has limits unless agencies introduce flexibility in the rules governing the use of instruments—both in writing and practice.

Illustrative Evidence. List (including explanations) of instruments allowing collaboration; generic document on how to proceed in collaborative programs as well as the flexibility or general restrictions to do so; list of collaborative efforts with other donors; copies of strategic agreements, partnerships or engagements in multi-donor funding vehicles; and copies of joint funding arrangements.



Annex I: Definitions for Quality of Aid Management for Microfinance Index

Development agencies often have their own specific understanding of various terms commonly used in development and microfinance. This glossary provides definitions used in the Index to ensure a common understanding of key terms.

CLEARs	The CGAP-initiated Country-Level Effectiveness and Accountability Reviews (CLEARs) emphasize donor systems, communication flows, and practices against the backdrop of building financial systems that work for the poor. They strive to help donors identify gaps in the financial systems in the countries where they work and to design interventions that build on their respective comparative advantages. The CLEARs also aspire to motivate donors to improve internal procedures and systems so that they can work more effectively with others in the field. See: http://www.cgap.org/clear
collaborative funding	Funding in a manner whereby a donor explicitly joins with one or more other donors. A range of collaborative funding options exist that require greater or lesser degrees of common administrative procedures, including pooled funding, parallel funding, co-funding, sector wide approaches, etc.
focal point	A person or persons with specialist microfinance/financial sector experience designated by the agency as a resource or center of excellence for microfinance. While there is no one focal point model, all focal points should be responsible for spreading good practices across the agency. Key roles include 1) facilitating networking and knowledge sharing among staff working on microfinance and the broader industry; 2) providing technical expertise in the early stages of program design and references for outsourcing work; and 3) quality assurance during all stages of the project cycle.
Good Practice Guidelines for Funders of Microfinance	The 2006 “Good Practice Guidelines for Funders of Microfinance” provide lessons learned and practical guidance for donors and investors on how to best interact with and support the various actors in microfinance. See: http://cgap.org/docs/donorguidelines.pdf
knowledge management	The identification, creation, dissemination and utilization of knowledge. Knowledge management thus entails practices used to capture and learn from agencies’ own—and others—experiences. While training may be part of knowledge management, it also includes interpersonal and technological information flows.
mandate	A clear instruction, embodied in written operational policy or organizational procedure, that responsibility and authority are vested in a position or entity.
microfinance	Microfinance is commonly understood as the provision of banking/financial services to lower-income people, especially the poor and very poor. The new vision of microfinance recognizes that microfinance involves building inclusive financial systems. This can be achieved only if financial services for the poor are integrated into all three levels of a financial system: micro (a range of financial and non-financial retail institutions that provide credit, savings, transfers and other financial

	services); meso (financial market infrastructure and services that support the micro level”); macro (policy, legal and regulatory environment for an inclusive financial system). Agencies have different thresholds for what they consider microfinance, for example, as opposed to small and medium enterprise finance.
microfinance component	Microfinance—most often microcredit—included as a part (usually a minority component) of a larger, non-financial sector program, for example agriculture or health.
Microfinance Donor Peer Reviews	The CGAP-initiated Microfinance Donor Peer Reviews focused on what donor agencies can most directly influence: their own procedures, practices, processes and systems. The reviews identified success factors and constraints to applying good practice in microfinance and provided concrete recommendations in Letters to Management for each agency. The learning of the Peer Reviews is summarized in the Aid Effectiveness Star. See: http://www.cgap.org/Projects/donor_peer_reviews.html
microfinance experience	Substantial, prior direct experience in setting up, managing or overseeing microfinance providers and/or programs. This can include work at one or several levels of the financial system. Professional background could include banking, development finance, financial sector, or microfinance.
microfinance policy	A document that lays out an agency’s vision and goals in microfinance and links them to the agency’s mission. The policy also articulates principles, guidelines or standards that set a definite and binding common approach for the agency’s actions in microfinance. This may be a distinct policy or included in a larger private sector or financial sector policy.
microfinance specialist	A person with a minimum of five years of microfinance experience. Unless otherwise mentioned, this person can be an in-house donor staff or a consultant.
microfinance stakeholders	The full range of actors involved in or affected by microfinance, including governments, donors and investors (including development agencies, foundations, social and commercial investors, international NGOs), practitioners, and civil society. These stakeholders can be international or national.
microfinance strategy	A concrete plan for the implementation of an agency’s microfinance policy, including how its resources (personnel, financial, influence) will be best employed to achieve the policy’s goals. This may be a distinct strategy or included in a larger private sector, financial sector, regional/country strategy or policy document.
microfinance training	Externally or internally organized trainings on microfinance-related subjects. Though training can come in many formats, for example, seminars, class room sessions, etc., it must be delivered by someone who is a microfinance specialist.
performance indicators	Indicators that should be treated in the design, monitoring and evaluation of programs that measure performance, rather than just activities or outputs. For support to microfinance providers, CGAP suggests core performance indicators for five areas (see “Good Practice Guidelines for Funders of Microfinance”, page 41).
Portfolio Reviews	CGAP-initiated reviews of project portfolios and country programs. CGAP carried out three such in-depth evaluations of development agencies’ microcredit portfolios. See:



	http://www.cgap.org/portal/site/CGAP/menuitem.2319fcd20442bc5167808010591010a0/ .
private actors	Actors outside government control whether direct or indirect. Includes private individuals, non-government organizations, associations, and for-profit entities.
program/ project	<p>The words program and project are used synonymously in some agencies; in others they have distinct meanings. For the purposes of the Index, only the term program is used. It is meant to encompass individual programs/projects or a group of programs/projects funded collectively and treated as a single undertaking for funding or monitoring purposes.</p> <p>Programs might include a sector-wide approach or country programs that include multiple distinct projects. For many, projects are more narrowly defined as an activity that has its own budget, manager (or management unit), and contract or agreement. This could be either direct support to a single entity or to a group of activities that is run by a single project management unit.</p>
project cycle	All stages through which programming (projects or programs) is initiated, designed, implemented, monitored and evaluated.
senior management	Person(s) at the top echelon of hierarchy with decision-making authority, leverage among staff of all levels and/or influence over policy, strategy, systems and/or implementation of programs. This authority is not necessarily confined to financial sector/microfinance matters.



Annex II: CGAP Charter Reporting Requirements

Agencies may select to fulfill CGAP's Charter Reporting requirements at the same time as submitting information to the Index. The details for Charter Reporting are outlined below—note that they all overlap with information that is also useful for one or more Index indicators. For examples of some agencies' submissions from previous years, please see http://cgap.org/direct/aid/about_donors.php and click on “donor profile.”

Charter Reporting Requirements

- Staff
 - List of microfinance specialists and their CVs
 - List of staff working on microfinance in headquarter and field offices whether full-time or part of their time (including percentage of time working on microfinance)
 - List of members of microfinance practice group

- Microfinance portfolio (three last fiscal years)
 - List of all microfinance programs and components (with components clearly identified)
 - Committed and/or disbursed funding for microfinance by region, by instruments; for components, use funding amounts for components only and provide definition of component
 - Total outstanding microfinance portfolio as of end of last fiscal year