

SMARTAID FOR MICROFINANCE INDEX 2007

UNITED NATIONS CAPITAL DEVELOPMENT FUND (UNCDF)

Overall Score

83/100

The SmartAid for Microfinance Index (SmartAid) measures whether funding agencies are set up to support microfinance effectively. It scores agencies on a framework of five elements of effectiveness—strategic clarity, staff capacity, accountability for results, knowledge management, and appropriate instruments—that capture the requirements for quality aid management throughout the project or investment cycle. At the Better Aid for Access to Finance meeting in 2006, 29 development leaders representing the largest microfinance funders adopted a commitment to measure the quality of their aid management in microfinance by developing and piloting this Index.¹

At a Glance

Type:	UN agency
Outstanding Portfolio (12/2007):	\$125 million
% of Agency Portfolio:	20%
Primary Instrument(s):	grants
Primary Partner(s):	private sector, non-profit
Primary Source of Funding:	government budget

SmartAid builds on the premise that sound management systems, policies, procedures and incentives are necessary (though not sufficient) conditions for successful programs. In this vein, the Index is inspired by the ISO standards that specify requirements for state-of-the-art products and services and for good conformity assessment, as well as managerial and organizational practice. As such, the Index does not evaluate the on-the-ground performance of agencies' microfinance portfolios. The results of SmartAid, therefore, cannot be taken as a direct proxy for portfolio performance.

The Index is designed to help identify areas in which all types of funders can improve their systems and policies for microfinance programming. Through this process, the aim is to encourage funders to make changes so that microfinance lives up to its potential contribution to improve poor people's lives and deepen financial systems.

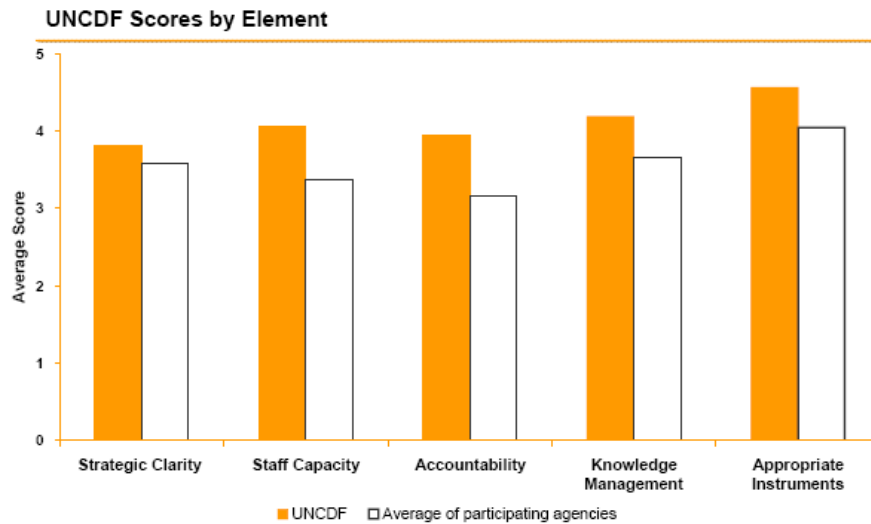
CGAP developed SmartAid in partnership with its members and with advice from experts from the Center for Global Development, OECD, and the United Nations World Institute for Development Economics Research (WIDER) University. 2007 marks the first and pilot edition of SmartAid. Seven funders—AsDB, CIDA, FMO, GTZ, KfW, Sida and UNCDF—volunteered to participate in the pilot.² They represent a variety of funding agencies, including agencies where financial sector/microfinance is one of two or three priority areas and ones where microfinance represents less than five percent of overall funding. The agencies offer the full range of available instruments, and span the spectrum from focusing purely on developmental objectives working primarily with government actors, to taking a more commercial approach with mostly private sector actors.

Participating agencies reviewed and approved SmartAid's framework and methodology for the pilot round. Lessons learned on the relevance of the indicators and the submission and scoring processes will be discussed in a separate report focusing on the methodology. SmartAid will be refined and streamlined based on the learning of the pilot round. The essence of the Index and what it measures, however, will remain the same.

¹ Please see www.cgap.org/betteraid_meeting/compact for more information.

² CGAP and IFC agreed that the IFC would withdraw from the pilot round before its completion.

Key Findings



UNCDF received 83 out of 100 points, ranking consistently high in all elements. It is a small, highly focused, flexible grants-based agency with leaders committed to good practices that have built in-house staff skills. Its greatest challenges are linked to aligning its systems to implement its strategy of addressing all levels of financial systems development and managing the performance of its portfolio.

Strengths	Weaknesses
Strategic Clarity	
<ul style="list-style-type: none"> Strong historical focus on retail start-up institutions in least developed and high risk countries in line with UN priorities, especially UNDP. Strong senior management support for good practices (e.g., eliminating credit components) helps counterbalance the inherent political nature of UNCDF's operations that requires local government participation in project development and approval. 	<ul style="list-style-type: none"> Lack of clarity of what constitutes UNCDF's comparative advantage in meso and macro level work. Existing analysis underestimates constraints and the expertise and resources needed to implement the ambitious new strategy (2008-2011) of the Financial Inclusion Practice Area (FIPA).
Staff Capacity	
<ul style="list-style-type: none"> Strong technical FIPA unit is critical to ensuring quality and consequently maintaining UNCDF's reputation as a competent funder. Regional technical managers and chief technical advisors mostly have strong retail expertise. UNCDF has the budget, procurement flexibility and network to access well-qualified consultants. 	<ul style="list-style-type: none"> Unsure if staff experience is well-suited to new programming at meso and macro levels. Staff may be overstretched to sufficiently manage rapid geographic expansion (about 30 countries) and an increasingly complex technical agenda.
Accountability for Results	
<ul style="list-style-type: none"> All financial inclusion projects are easily identifiable; with FIPA staff having exclusive control over the portfolio and the ability to track all projects. FIPA staff and/or technical service providers (TSPs) are involved in all project designs, this being key to quality when staff have sufficient time and expertise. There are multiple project approval levels, including one involving the government. The risks of political imperatives overshadowing good 	<ul style="list-style-type: none"> Annual centralized monitoring of core performance indicators with reports sent to senior management is adequate though not uniformly implemented; monitoring done by regional advisors and local chief technical advisors is more frequent but of mixed quality. Aggregated project tracking is done via Excel. PBAs do not seem to be systematically enforced given the reported high PAR of many programs. Performance tracking of meso and macro work shows effort to identify appropriate indicators, but

<p>practices exist but seem appropriately managed by the FIPA Investment Committee.</p> <ul style="list-style-type: none"> • Strong emphasis on partners' transparency by requiring retail partners to report to the Mix Market. • Good examples of performance-based agreements (PBAs) for retail partners with performance targets. 	<p>is still nascent, in part due to the greater difficulty of identifying meaningful quantitative performance indicators in such projects.</p>
<h3>Knowledge Management</h3>	
<ul style="list-style-type: none"> • Active externally focused knowledge management (KM) by FIPA, with priority on UNDP, UN Executive Committee, UN Advisors Group, and the Blue Book project. • All eight focal point staff have KM in their job descriptions. Four staff take the lead on KM, with high participation in seminars, events, and workshops. • FIPA staff proactively engage with microfinance stakeholders, including local government. Building strategic partnerships is part of staff's performance evaluation. • Creative Research and Development program provides flexibility for fast recruitment and financial sector assessments, and sets aside needed resources for internal KM and research in key areas like product diversification and remittances. 	<ul style="list-style-type: none"> • Less energy on internally focused KM, which may be appropriate given the small size of agency, but does not address on-going challenge of engaging resident in-country staff in a decentralized structure with many new recruits.
<h3>Appropriate Instruments</h3>	
<ul style="list-style-type: none"> • Flexibility to work directly with private sector actors of all types, primarily through grants. • Demonstrated interest in, and practice of, collaboration with other funders and technical service providers. 	<ul style="list-style-type: none"> • Government approval required, which may slow process and limit freedom to choose and interact with partners.

Recommendations and Outlook

Analysis

UNCDF has a history of supporting the next generation of sustainable financial service providers that focus on poor and low-income people. There is still a need for this type of support given the limited number of retail providers and the limited (and shrinking) number of funders interested in these markets. UNCDF has considerable knowledge to share in supporting retail institutions in difficult environments and nascent financial sectors, and can build on its collaborative relationships to bring other technical and funding agencies to this market.

UNCDF's proposed expansion to the meso and macro levels is understandable given the constraints faced by many of their retail partners. UNCDF's argument that, as a UN agency, it has an advantage in working with governments to address policy and financial infrastructure constraints is credible—particularly in the context of the least developed countries. At the same time, its strategy is ambitious because the agency has not traditionally specialized in financial sector development or reforms. Managing micro, meso and macro levels may exceed the capacity of FIPA's staff, both in terms of the complexity of managing all levels simultaneously and the sheer volume. UNCDF's systems and human resources have not fully followed the 2002 shift in strategy, especially given the many positions yet to

be filled. For example, job descriptions heavily focus on retail portfolio management which is only one aspect of what is needed to support broader programs.

To fulfill its 2008-2011 strategy, UNCDF should ensure that its ambitions match its resources and capabilities. For work on meso and macro levels, UNCDF should adopt a more modest approach until it can build a staff mix with more relevant experience and expertise, as well as partner with other funders with greater expertise working at these levels.

Good Practice Highlight

All FIPA programs are under the same budget code. This allows for one country program to overspend in any given year, and another to under-spend without going through a process of budget revisions. As UNCDF FIPA approaches its overall spending limits, budgets are reallocated to countries that require more funding in a given year. This avoids the disbursement pressure to spend funds in countries where the absorptive capacity is low.

Suggestions to Increase Agency's Effectiveness and Scores

- Conduct a strategic review based on experience to date working at the macro and meso levels, in addition to the micro level. A detailed SWOT analysis could be part of the review.
- Prepare a human resource development plan to support UNCDF's strategy, taking into account all levels of staff, including chief technical advisors. When appropriate, send staff to specific policy-related trainings.
- Manage geographic expansion; grow at a pace that ensures continued quality with regard to staff recruitment and training, and technical inputs at all stages of the project cycle.
- Undertake regular independent portfolio reviews (every two to three years) to obtain detailed information on the quality of the portfolio.
- Prioritize improving the portfolio of retail providers supported, including rigorous enforcement of performance-based agreements.

Methodology

SmartAid builds on a framework of five elements of effective aid management developed over a two-year period following the completion of 17 Microfinance Donor Peer Reviews facilitated by CGAP.³ SmartAid 2007 consists of 20 equally weighted indicators, four for each element that are described below. For each indicator, a funder may score between 0 and 5 points, for a total maximum of 100 points. Funders receive an overall score out of 100 in addition to scores on each element, representing the simple average of the element's four indicators.

The assessment is based on self-reported documentation from the participating funders, following instructions in the SmartAid Submission Guide. Scores are determined by a review board of four persons with extensive microfinance expertise and broad experience working with a range of funding agencies. Each review board member independently scores agencies against all indicators prior to a meeting where final scores are agreed.

³ Please see www.cgap.org/Projects/donor_peer_reviews.html for more information.

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”	Strategic Clarity
1.2	Senior management commitment to good practice microfinance principles and evidence of agency-wide dissemination	
1.3	Agency’s microfinance policy/strategy recognizes and addresses its capabilities and constraints and where it can most add value	
1.4	Compliance with good practice principles checked at all stages of the project cycle for microfinance programs and components	
2.1	Designated focal point with microfinance/financial sector experience and responsibility to provide technical advice to program managers	Staff Capacity
2.2	Agency makes resources available for technical expertise to be involved in the design of all microfinance programs and components	
2.3	Agency requires and verifies that all staff who manage microfinance programs and components have training/experience	
2.4	Agency places microfinance specialist staff in countries/regions where it has its most significant portfolio of microfinance programs and components	
3.1	System in place to identify microfinance programs and components from design to disbursement	Accountability for Results
3.2	Microfinance/financial sector specialist required to review microfinance programs and components	
3.3	Agency annually tracks and reports on performance indicators for microfinance programs and components	
3.4	Agency uses performance-based contracts in its microfinance programs and components	
4.1	Focal point’s responsibilities and budget include knowledge management for microfinance	Knowledge Management
4.2	Agency systematically assesses its microfinance programs and components through reviews or evaluations and extracts learning	
4.3	Mechanism(s) in place for exchanging learning on agency’s microfinance programs and latest microfinance developments throughout headquarters and field offices	
4.4	Agency requires staff to actively engage and coordinate with key regional/country-level microfinance stakeholders	
5.1	Able to work directly with private actors	Appropriate Instruments
5.2	Little microfinance programming is done through credit components of larger, non-financial sector programs	
5.3	Nature and use of instruments are consistent with agency’s strategy and with requirements for supporting microfinance well	
5.4	Policies and procedures governing use of instruments allow for a range of collaborative funding and technical support	

UNCDF Scores by Indicator

