ADVANCING GOOD GOVERNANCE in International Development

Making Market-based Approaches to Development Work for the Poor

4 – 5 June 2015

Rhodes House, Oxford

Opening Keynote: A Story of Love and Loss: Lessons for Using Market-based Approaches to Social Development

Vikram Akula, founder of SKS Microfinance, one of the word's largest financial inclusion companies, delivered the seminar's opening remarks. He shared a number of lessons learned from his experience founding and managing the company, including navigating the lead up to its wildly successful IPO in 2010, the fierce political backlash that followed and his eventual exit from SKS. While microfinance undoubtedly benefits from the influx of capital afforded by the market model, Vikram sounded a note of caution with respect to managing the transition to scale. Without an effective framework to manage this transition, microfinance institutions risk overly focusing on profits to the exclusion of the poor, the people their sector is intended to serve.

Key Points from the Session

1. **In scaling up, microfinance enterprises should not lose focus on the importance of training the borrower group.** Best practice in microfinance involves training peer-lending groups before a loan is given, whereby borrowers receive instruction on the loan repayment process, their obligations vis-à-vis repayment, and their obligations vis-à-vis each other. Empirical evidence shows that this training is indispensable to the success of microfinance, since it fosters right-sizing of loans; group cohesion and confidence; and timely repayment. However, as the microfinance crisis in 2010 showed, in trying to reach increasingly more borrowers, microfinance institutions sacrificed this crucial element of group training, resulting in some incidents of over-indebtedness.. In managing the transition to scale, therefore, microfinance enterprises must be careful not to lose sight of borrower interests for commercial motives, even if commercialization is couched in the language of promoting the outreach of the social enterprise.

2. **To scale up effectively while staying true to the goals of social enterprise, social entrepreneurs should pay heed to the "Three C's."** First, social entrepreneurs should deliberately cultivate the right **culture** in their organizations. While culture "just happens" in smaller enterprises, it must be purposely created and reinforced in large-scale operations, with a clear and definite tone from the top that is firmly committed to the enterprise's guiding purpose. Second, large-scale social enterprises must formulate the appropriate operational rules, via **codes of conduct.** Rather than providing staff with incentives to sign up more and more borrower groups, rules should incentivize staff behaviours which reinforce core principles and social purpose (for example, the essential group training at the outset of the loan transaction). Third, social entrepreneurs should be mindful to issues of **control** – in particular, how the institution's priorities can be shifted away from the social purpose and towards profit-maximizing as a direct result of the influx of capital and private-sector expertise.

3. **Further legal reforms are needed to buttress the work of social entrepreneurs, including in microfinance.** Although the development of the B-corp (benefit corporation) legislation is a much-welcomed development in microfinance and social enterprise, this type of legislation needs to proliferate beyond the handful of jurisdictions, which have adopted it to date. Additionally, more case law interpreting such statutes would help illustrate how these statutes can be used to hold social enterprises accountable for their social impacts. Furthermore, for social enterprises, rules

on executive compensation should be developed which tie a higher fraction of compensation to the social performance of the enterprise.

4. **Social enterprise must be aware of the vested interests they are challenging.** Vikram noted the “ferocious” challenge that vested interests can present when engaging in innovative, socially disruptive work in the difficult environments that microfinance must penetrate. In the case of microfinance, these vested interests included traditional village moneylenders, corrupt politicians, vernacular media, and some bureaucrats who held rigid public sector ideologies.

Emerging Questions

1. How can microfinance institutions and other social enterprises effectively and pro-actively tackle any vested interests and regulatory concerns, which may impact on their business models?

2. How can the values and communication gap between social entrepreneurs and traditional private capital players be bridged to ensure that social enterprises do not lose sight of their social purpose when taken to scale?

3. Does the rise of terminology such as “financial inclusion” detract focus from the primary goal of poverty alleviation?