Microfinance is a potentially powerful tool to fight poverty and help poor people raise their income, accumulate assets, and cushion themselves against external shocks. At the same time leaders of the movement recognize the need for a hard-nosed commercial outlook if it is to be sustainable. To this end many specialized microfinance providers have formalized and scaled up their activities while, in the other direction, many regulated financial institutions have expanded downstream.

Good reasons exist to welcome a boundary blur between microfinance and mainstream banking. Only with commercial capital can demand for financial services among poorer people be more fully met. Closer integration also promotes innovation and greater responsiveness to the diverse client needs. However, the danger that commercialization of microfinance will lead to an over-preoccupation with profitability at the expense of poverty reduction and other development goals is great—mission drift is an ever-present possibility for MFIs and often irreversible.

Because microfinance is motivated by development as well as economic goals, the question arises how best to evaluate performance against multiple and potentially conflicting goals. The main issue is not so much the desirability of broader performance measurement but its feasibility. Technical performance management “by numbers” is difficult under the best of circumstances; measuring the impact of microfinance institutions using even crude estimates of household income is technically difficult, expensive, and perhaps better left to independent researchers who can do it more rigorously. However, the potential of microfinance as a development tool will only be realized if financial institutions systematically and routinely measure performance, and if they do it in response to internal demand, not in response to pressure from other organizations.

**KEY CONCEPTS**

Three key dimensions of social performance are *breadth of outreach* (the number of people using services during any period of time), *depth of outreach* (the social status of clients at the beginning of any period), and *impact* (the net benefits to clients and those indirectly affected by their use of financial services). Financial performance is primarily the percentage of the service’s full cost that is directly paid for by the users.

Innovations that reduce the costs of providing services bring improvement in both financial and social performance. But other decisions entail a trade-off over time between them. For example, raising interest rates on loans is likely to improve financial performance (assuming inelastic demand) but at the expense of current social performance (due to reduced net benefit per client and possible short-term reduction in breadth and depth of outreach). Most benefits of trade-offs only come over time because future social performance depends on both current social performance and on how financial performance affects the capacity to supply services in the future.

Another example is the growth rate of the MFI. Many MFIs have emphasized the prime importance of serving more clients through growth. The cost of investing in new capacity has a negative financial effect in the short term, but this may eventually be offset by economies of scale. Improved financial performance is also necessary for growth in order to mobilize resources; therein lies the case for lowering current social performance to enhance future
social performance. In contrast, other MFIs have opted for a slower growth strategy: putting greater emphasis on current depth of outreach and impact. Such decisions reflect variation in time horizons and, more importantly, path-dependent judgments about how current performance is likely to affect future social performance opportunities.

Figure 1 provides a graphical framework to aid thinking about such strategic “win-win” options and trade-offs between financial and social performance. The preferences of the MFI, or its mission, are represented by a set of indifference curves (C₁, C₂, and C₃). The top preference is at the top right corner of the box, since this is the point at which both social and financial performance are at their highest. Conversely, the lowest preference is at the bottom left corner. The indifference curves each represent a set of points whose current social and financial performances are equally attractive. Movement upward and to the right, or to a higher indifference curve, thus represents a move to a preferred level of overall performance.

From any given initial level of actual performance (pₜ), an MFI is limited in how it can change its position within the next time period. Line PPᵣ₊₁ reflects this room to maneuver and is determined by the scope for policy change, operational reforms, investments, innovations and growth. Change possibilities over one period are illustrated by the five arrows:

1. The horizontal arrow represents a growth-first strategy, subject to the rule that current social performance should not get any worse.

2. The vertical arrow represents a current clients-first strategy, subject to the rule that financial performance should not get any worse.

3. The arrow pointing upward and to the right represents an intermediate strategy. Assuming the MFI is successful in reaching the PPᵣ₊₁ line, then this strategy is optimal; in the case shown, it is pᵣ₊₁⁺.

4. The arrow moving up and to the left represents a trade-off strategy of improved current social performance at the expense of financial performance.

5. The downward sloping arrow also represents a trade-off strategy—this time to enhance financial performance by reducing current social performance.

In addition to illustrating strategic options, the diagram clarifies the reality of mission drift: an unplanned or hidden change in preferences and resulting behaviors. Mission drift is, at the heart, a response to past performance—less rational than a conscious change in preferences but more than ignorant of actual performance outcomes.

As an example, assume that an MFI takes actions intended to take it from point pᵣ to pᵣ₊₁⁺, but actually ends up at pᵣ₊₁#. This in itself is better described as mission failure.
than mission drift. From this new starting point it is unlikely the MFI would continue to aim for $p_{t+1}^*$ in the second period—$p_{t+1}^*$ might even fall completely outside any realistic assessment of what is possible. In such a situation, choosing a new target outcome for the next period without a change in underlying preferences is better described as pragmatism than mission drift.

At the opposite extreme, an MFI could redefine its preferences in order to provide a retrospective rationalization of the actual performance outcome. In this example, the MFI could express a stronger preference for financial performance over social performance (i.e., making the indifference curves steeper until $p_{t+1}#$ becomes the optimal target rather than $p_{t+1}^*$). This is closer to the idea of mission drift, but it would also be a case of self-serving opportunism and is better regarded as a special case.

A general definition of mission drift is that the steps taken to achieve a given performance outcome directly induce changes in preferences. Managers use current performance to reset their desires and preferences for what is possible in the future; they change the shape and slope of the indifference curves to reflect what they see as the new reality.

In a mythical world of perfect information, the directors of an MFI would set performance goals, the managers would make decisions to achieve them, employees would systematically monitor outcomes, and everyone would learn. Unfortunately, leaders of MFIs are handicapped by the lack of timely and reliable evidence about performance. Mission drift occurs when their goals and preferences for the future subconsciously change in response to actual performance outcomes rather than being a fixed point against which performance can be guided and assessed.

**APPLICATION**

Since an important key to avoid mission drift is an accurate assessment of performance, this section blends the framework presented above with our research experience with nonprofit MFIs through the Imp-Act program. We follow this discussion with other lessons we have learned regarding organizational leadership among successful MFIs.

**Revising Social Performance Assessment**

Three broad points of consensus emerged from our research as to what any system of social performance assessment should include. First, MFIs with an explicit poverty mission should routinely monitor breadth and depth of outreach. Although it was not possible to agree on a standard set of indicators for this, there was methodological convergence between many MFIs and their sponsors to adopt a combination of proxy poverty indicators. Leaders in the field use a simple but transparent scorecard calibrated against national household survey data and poverty estimates.

Second, MFIs should routinely monitor client exit and turnover. If clients choose not to leave and are not hoodwinked or coerced into using services, then this is a useful indication that the impact of the services is less likely to be negative. It follows that outreach data should, at the very least, be supplemented by statistics on exit, including routine reports on why clients leave—particularly those who only recently joined and whose understanding of the terms of service could have been inadequate.

Third, MFIs should invest in capacity to assess progress toward social goals by giving voice to loyal clients too, through appropriate market and impact research. Questionnaire-based surveys, semi-structured interviews of key informants, and focus groups—all with the priority to test, update, and augment existing organizational knowledge of clients’ experiences rather than to provide rigorous proof.
Imp-Act stands for “Improving the Impact of Microfinance on Poverty: An Action-Research Program” and was sponsored by the Ford Foundation. It was launched in 2000 to explore ways of improving the measurement and management of poverty reduction by MFIs. Twenty-two organizations successfully bid for support to carry out their own action-research over a three-year period, ending in April 2004. These comprised sixteen direct providers of microfinance services, three NGO promoters of user-controlled savings and credit groups, and three MFI networks.

One premise of the program was that debate over the social performance of MFIs was dominated by external interests (e.g., governments, donors, and researchers) at the expense of MFIs themselves. Participants were therefore given freedom to explore ways of improving their social performance assessment systems to meet their own needs rather than externally-dictated ends. For more information, see Copestake, Greeley, Johnson, Kabeer, and Simanowitz’s book, Money with a Mission, Volume 1: Microfinance and Poverty Reduction, published in 2005 by ITDG Publications. Or visit www.imp-act.org.

of impact—can accomplish such purposes.

Returning to the theoretical framework summarized by Figure 1, these practical lessons amount to defining the Y-axis (social performance) as the number of active users adjusted for loyalty and client satisfaction (as a proxy of service quality) and poverty status (with greater weight given to poorer or otherwise disadvantaged clients). Social performance is improved by serving more clients, by serving poorer clients, by broadening the range of services they receive, by serving them for longer periods, and by ensuring that services do no harm. While this definition falls well short of capturing all aspects of an MFI’s social mission (e.g., community-wide impact), it does provide a baseline for assessment.

**Performance Possibilities**

Without denying the scope for managerial wizardry, the major determinants of financial performance are well understood: realistic pricing of products (particularly interest rates), strong cost control and productivity enhancement, risk and liquidity management, portfolio quality control, and continual innovation in response to customer requirements and market conditions. The key question concerns how much scope MFIs have to systematically improve social performance while handling these financial pressures. Our analysis of MFIs participating in the Imp-Act program highlighted four areas.

First, targeting has a critical bearing on depth of outreach. Serving geographically defined poorer areas does not necessarily mean lower profits because such areas may have limited competition, but it often results in significantly increased depth of outreach. Some MFIs directly target poorer clients by using a poverty means test instead of focusing solely on geography. This is more controversial; deliberately excluding better-off clients can reduce opportunities for cross-subsidization and growth and can weaken an MFI’s competitiveness. But as with geographical targeting, such targeting can also help an MFI to develop its comparative advantage in a specific market segment. Small Enterprise Foundation in South Africa is a particularly interesting example because it operates poverty-targeted and non-poverty-targeted services alongside each other. This enables it to vary the balance between social and financial performance goals through strategic reallocation of resources between them.

Second, an even more powerful, yet indirect, targeting mechanism is product design. Most MFIs began by replicating products pioneered by others—solidarity loans of Grameen Bank or village banking services on the FINCA model, for example. However, most have become more flexible, have diversified their services, and often have simplified product terms and conditions. These changes exert a powerful influence not only on profitability but also on the kinds of clients attracted and the extent to which clients benefit.

Third, internal organizational changes (e.g., front-line staff recruitment, training, and performance incentive systems) are critical. Performance contracts that seek to align financial rewards of staff to those of the MFI have become standard practice, but better social performance assessment (particularly of staff- and branch-wise exit rates) creates opportunities for aligning staff incentives to social goals as well. Social performance management can significantly improve staff motivation, retention, and productivity.

Fourth, an MFI’s room to maneuver depends upon their operating environment—particularly the extent of unrealized demand, opportunities for innovation, the extent of regulation, and access to different forms of finance. While individual MFIs have little influence over these changes, the range and quality of the external relationships they forge with other commercial and non-commercial organizations is a critical determinant of their social performance. In many
countries a scissors-like combination of increased competition and more stringent terms of aid have reduced short-term room for maneuvering, forcing more radical cost-saving innovations. While MFIs compete with each other, they also collaborate extensively through both informal and formal networks. They seek flexible financial and technical support from donors and governments but are also wary of being overly controlled by them. Strong financial performance and a good understanding of the wider financial system have opened up opportunities for some to mobilize equity and finance debt to permit faster growth.

Although the very existence of MFIs may be a symptom of the mainstream financial system’s limited outreach, the quality of an MFI’s relationship with it nevertheless remains critical to its performance. Meanwhile, donors and specialist intermediaries provide MFIs with financial and technical support that can help soften the trade-off between growth and depth and quality of outreach. The main challenge facing MFIs is to make good use of such support without becoming overly dependent on it or allowing it to undermine their financial discipline and autonomy. Performance possibilities or strategic options faced by MFIs may have narrowed somewhat due to increased competition and tougher terms of donor funding, but they remain substantial.

Leadership Implications
Our Imp-Act program research revealed that mission and vision statements covered all aspects of outreach, but that their significance depends on how much weight MFI leaders and boards actually attach to them in decision making. Tension often exists between board members and senior managers—those with stronger commercial business or banking backgrounds and those with stronger social or volunteering backgrounds, respectively.

The phenomenon of mission drift is also manifest in these terms. The appointment of those with more commercial experience in a quest for improved financial performance may be seen by other board members as a means to improve long-term social performance, but leaves open the question whether they will be able to retain control. In the case of MFIs aiming for transformation into commercial banks, new board members also bring financial responsibilities to commercial investors and private for-profit shareholders. These changes can become self-reinforcing if newcomers also perpetuate further the simplistic understanding of the nature of poverty (i.e., simply a lack of access to credit). In terms of Figure 1, such drift takes the form of a cumulative flattening of the indifference curves.

Larger MFIs have been able to avoid such danger by combining the acquisition of financial expertise with sustained investment in improving and updating internal understanding of the nature of poverty at all levels of the organization. This can be harder for smaller MFIs for whom the bigger danger may be more mission lock-in than drift—being unable to control or limit the process of commercialization once it has started. Leaders also have a vested interest in lack of transparency about social performance to the extent that uncertainty and ambiguity give them more room to maneuver in the struggle to reconcile multiple internal and external expectations and demands.

**CONCLUSION**
Mission drift can most precisely be defined as retrospective changes in stated preferences to fit unplanned performance outcomes. This is more likely when an MFI’s goal setting, performance assessment, and management systems are weak. Evidence from Imp-Act suggests that many MFIs do have strong social and financial performance preferences, significant room for maneuvering to manage them, and scope to better do so. Improved goal setting and strategic planning, routine monitoring of the poverty status of clients and ex-clients, a capacity for follow-up research into the reasons behind observed changes, and periodic internal and external reviews of these activities and systems can all be carried out more cost-effectively and systematically. This can help accelerate the pace of innovation and growth in a more poverty- and gender-aware manner and help reduce mission drift. It can also help to moderate some of the more extravagant claims concerning the potential of microfinance as a development tool.

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