CERISE+SPTF

Bringing the Theory of Change of Financial Service Providers into the Business Strategy for Value Creation

Recommendations for investors

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Prepared by

Amelia Greenberg, Cécile Lapenu, Fanny Le Maguet (Cerise+SPTF)

Yamini Annadanam, Rakhat Uraimova (SEPM Professionals Network)

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Glossary

- CP = client protection or consumer protection or customer protection
- CSR = corporate social responsibility
- ESG = environmental, social, and governance
- FSP = financial service provider
- GHG = greenhouse gas
- GLP = gross loan portfolio
- IC = investment committee
- KPI = key performance indicator
- MFR = Microfinanza Rating
- MIS = management information system
- OPIM = Operating Principles for Impact Management
- SDG = sustainable development goal
- SEPM = social and environmental performance management
- SIFEM = Swiss Investment Fund for Emerging Markets
- SPI = social performance indicators
- SPM = social performance management
- TA = technical assistance
- UNSGSA = United Nations Secretary-General's Special Advocate for Inclusive Finance for Development

Definitions

Theory of change: sequence showing how an intervention will achieve an impact. In practice, the theory of change also needs to define who are the target customers and what benefits the investor is trying to create, as well as all of the activities and changes that need to take place in order to effect the desired outcome.

Customer Outcomes: customers' experience and results (positive and negative) that are directly related to their use of financial services.

Outcomes management: Outcomes management is how an organization puts its theory of change into practice: it is a multi-step organizational system for the collection, analysis, and use of customer outcomes data = gathering data on what outcomes the investment is actually achieving or not, and using that to inform updates of the interventions, and potentially of the theory of change

Executive summary

Cerise+SPTF investigated what drives positive change in the inclusive finance sector and how investors in particular can engage to achieve better outcomes for customers. To answer these questions, Cerise+SPTF conducted 18 months of action research with a diverse group of stakeholders and provided intensive and specialized technical assistance to three FSPs. Over the course of the research, though focusing primarily on the role of investors, Cerise+SPTF also identified a number of recommendations for financial service providers (FSPs). The research yielded insights about how to develop a theory of change, and how to use a theory of change in a dynamic and ongoing way to guide investment decisions and oversight.

Theory of change and outcomes management
A theory of change is a simple concept but requires detailed elements, adaptation to context, and ongoing monitoring and adjustment based on data, to be effective. Fundamentally, a theory of change is a sequence showing how an intervention will achieve an impact. In practice, the theory of change also needs to define who are the target customers and what benefits the investor is trying to create, as well as all of the activities and changes that need to take place in order to effect the desired outcome. These activities can be external, such as services offered to investees and their customers, but also internal, such as capacity building of staff. An investor's theory of change also considers whether its investment will address gaps that no other funds are filling. Furthermore, it is important for a theory of change to be realistic. This means in part understanding what outcomes the investor and its investees directly control, versus those that are influenced by a multitude of independent factors. It also means ensuring outcomes management, i.e. gathering data on what outcomes the investment is actually achieving or not, and using that to inform updates of the interventions, and potentially of the theory of change.

Challenges
The research uncovered several common obstacles to effective outcomes management.
For investors, the three most common obstacles were:
- balancing asking for enough data to make good investment decisions without overburdening the investee,
- finding a way to compare outcomes performance across disparate investees,
- limited influence over the outcomes management practices of the investee, and lack of outcomes data.

Additionally, it may be that multiple investors and other stakeholders in the same one organization have different outcome goals.
For FSPs, the most common obstacles are :
- gaps in internal capacity,
- cost,
- poor data quality,
- and lack of buy-in.

Some FSPs also expressed a fear that if they reported negative outcomes, they would lose investment.
Furthermore, for both investors and FSPs, there is a challenge of defining what outcomes their interventions should be seeking to achieve. This is in part because different customers have different outcomes goals themselves. For example, some customers may want to expand their businesses whereas others **prioritize** stability.

This is also in part because the outcomes definitions can be too vague (e.g., “improve well-being”) or unrealistically ambitious (e.g., “end poverty”).

Recommendations
From the insights on common obstacles, Cerise+SPTF developed a series of recommendations for both investors and FSPs.
For improved data accuracy and insights, FSPs can **triangulate** data sources and gather **both qualitative and quantitative data**, while investors can provide technical assistance to investees to **build capacity** for data collection and analysis.
For reporting, investors should **require outcomes** data (what changes did customers experience) rather than just accepting outputs data (what products did the FSP offer).
Investors can also build a **culture of using data for decision-making** by communicating to investees that what constitutes good outcomes management is not sending to funders a report that shows 100% success, but rather it is an ongoing use of outcomes data, negative or positive, to inform strategic and operational decisions that reinforce what is working while adjusting what is not working, This approach also builds **buy-in for outcomes** management within the FSP, from management to field staff, because the FSP sees how having these data helps it to attract and retain customers, as well as mitigate risks.
Another recommendation to investors is to be **cautious about over-burdening investees** with data reporting requirements or asking for data that are not useful to the investee. It is possible to identify a set of **common indicators** can be tracked across various geographies, sectors, and sizes of investees based on expected outcomes from financial inclusion. Each investee can also benefit from gathering data on **outcome indicators that are uniquely relevant to its context**. The investor can develop a methodology to **compare levels of success** of performance across its portfolio that allows for some standardization in data required of investees, but also some customization of the indicators that each investee monitors and reports.
Investors should **note external factors** when they compare the performance of investees. For example, how competitive the market is, the level of economic development, the level of civil unrest or stability, and cultural aspects (e.g., how comfortable customers are expressing levels of satisfaction) can influence outcomes results.
Finally, an investor can promote better outcomes management, and therefore better outcomes, through **active participation in the investee’s board of directors**, for example by asking for outcomes data/ dashboards, advocating to reserve time during board meetings to discuss it, and holding **management accountable to meeting outcomes targets**.

Key lessons
- Transition from a focus on sustainability to impact
- Focus on improvement, rather than demonstration of excellence
- Use the ToC to harmonize expectations and prioritization of activities both internally and with investees
- Understand what outcomes are possible; it is appropriate and fair to hold the FSP accountable to short term goals - the ones it can control
- When FSP are accountable for some short-term goals, this should be discussed between the FSP and the investor
- An FSP cannot mitigate the risk of harming customers without outcomes management.

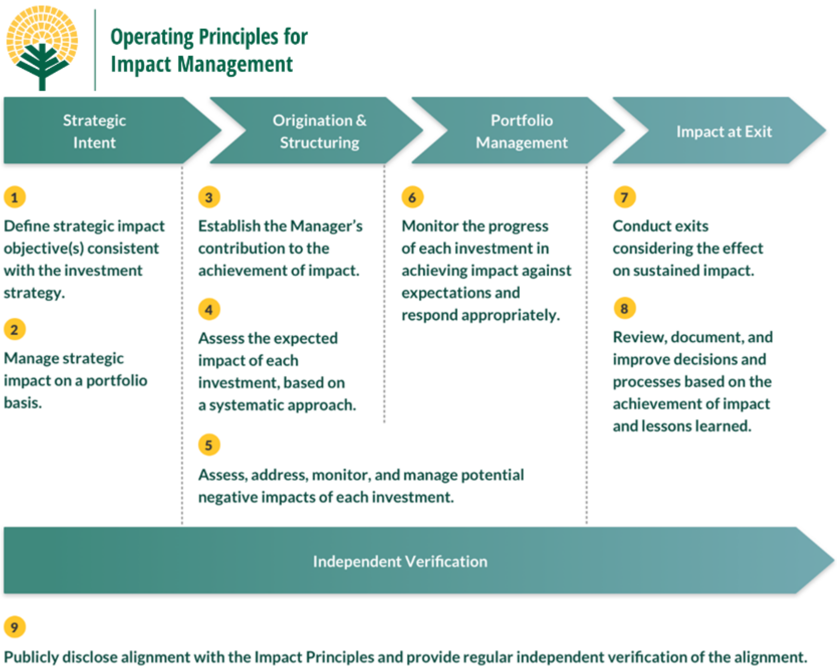
Introduction

Cerise+SPTF investigated what drives positive change in the inclusive finance sector and how investors in particular can engage, at every stage of the investment lifecycle, to achieve their impact goals. The impetus for this project was the honest reflection that each organization, no matter how experienced or committed, has something to learn from its peers, and by pooling the insights of all stakeholders, it is possible to identify a core set of good practices around theory of change and outcomes management that each stakeholder can implement to strengthen its own performance. Cerise+SPTF and its consulting partners from the SEPM Pro Network therefore adopted a global and multi-faceted approach to amassing and recording lessons learned on what works and what does not.

This report is based on 18 months of action research with a diverse group of stakeholders, as well as insights from intensive and specialized technical assistance provided to three FSPs, accomplished over three phases of work:

- Phase 1: stakeholder perspectives on the current theory of change in the inclusive finance sector
- Phase 2: experiences of financial service providers (FSPs) with theory of change and outcomes management
- Phase 3: direct support in developing or updating a theory of change provided to selected FSPs: 2 non-bank financial institutions in India (we call them Partner 1 and Partner 2 in this report), and an international network of FSPs in Africa and China (called Partner 3 in this report).

Cerise+SPTF also contributed learnings from its overall experience in the inclusive finance space over the last two decades.



The report begins by defining key concepts related to theory of change and then uses the framework of the Operating Principles for Impact Management[1] ("Impact Principles") to present learning from the action research. Following the OPIM graphic above, the report first discusses strategic intent guided by a theory of change, then origination and portfolio management. The project has not considered exit strategy, however the report provides relevant publications. Though focusing on recommendations for investors, this report also contains complementary guidance for financial service providers.

The context: current practices on theory of change and outcomes management

Phases 1 and 2 of this research investigated current practices in theories of change and outcomes management, while also identifying common obstacles and lessons learned.

Each phase solicited input from different sources:

- Phase 1 involved document review and interviews with a wide variety of stakeholders in the inclusive finance sector,
- Phase 2 focused solely on feedback from selected financial service providers (FSPs).

Based on these insights, Cerise+SPTF developed recommendations for investors and FSPs on achieving better outcomes for clients.

State of practices on theory of change

Regarding theory of change, there were several key insights.

Set realistic expectations: Microfinance is not a panacea for poverty. This is in part because not every customer is using financial services with the goal of exiting poverty, and in part because so many external factors influence customer well-being.

Ensure on-going performance management: organizations must manage their performance very deliberately and comprehensively, on an ongoing basis, in order to ensure that what they are offering is responding to the needs of those who use it. Generally speaking, this management must involve both the pro-active work of setting up good policies and practices and the post-implementation work of gathering and analyzing outcomes data from both qualitative and quantitative sources.

[1] https://www.impactprinciples.org/

Structure the theory of change: though goals and styles varied widely, common elements did emerge. A theory of change needs to define who the organization is trying to reach, what benefits it is trying to create, and how the products and services offered by the organization will effect that change. In some cases, the theories of changes also included what internal capacity building needed to happen. For investors in particular, theories of change additionally considered whether their funds were addressing gaps that no other funds were filling. Most investors also had a specific theory of change for each fund. For all stakeholders, the theory of change discussion also highlighted the importance of ongoing monitoring, with an ability to intervene and course-correct, as needed.

State of practices on outcomes management

Regarding outcomes management, again the research revealed several key insights.

Stakeholders do not have uniform outcome goals: even within an organization, it is possible for different funds or different products, as the case may be, to have different areas of focus. Regardless of the specific outcome goals, all organizations need strong outcomes management practices. These start with defining the theory of change but also involve defining roles and responsibilities, gathering data on customers' needs for financial services as well as obstacles to using them, using that information to inform product design, and then actually gathering outcomes data and analyzing them by customer segment and by product, so decision-makers can use outcomes data to inform adjustments to strategy and operations.

Triangulate sources of information: The feedback also suggests that it is universally true that triangulating outcomes information will yield better insights than using one source of data only. This typically involves analyzing a mix of qualitative and quantitative data from various sources, such as complaints, transactions, satisfaction surveys, and outcomes data, while also gathering feedback from both customers and staff.

Shorter-term outcomes data is the most actionable. Several FSPs noted the utility of measuring the outcomes that they can actually control. For a financial service provider, this means monitoring whether its product design and delivery channels meet the customer's purpose(s), assessing staff interactions with customers, identifying any challenges customers face when using financial services.

Measure various types of outcomes: It is good practice to measure more than one kind of change, given that well-being is so multidimensional, and different people may use the same financial product for different reasons.

For investors, three main obstacles in the current state of practice emerged: finding the right balance of asking for enough data to make good investment decisions without overburdening the investee, finding a coherent way to compare performance across a portfolio invested in different geographies and sectors, and a lack of influence on the investee if the investor does not have a seat in the investee's board of directors.

Regarding regulation, in most countries, the current focus is on avoiding harm: An ESG approach focuses on risk management, relating both to the environment and to customers, but it does not mandate achieving positive outcomes. This makes it possible for an FSP to be fully compliant with regulation while generating no positive outcomes for customers. However, some FSPs did report that their regulator requires them to collect outcomes data.

Common weaknesses in current practices

The deep dive into the theories of change and current outcomes management practices of FSPs reinforced the general insights from phase 1 research while also revealing fairly common weaknesses in current practice.

Not every FSP clearly defines who it is trying to serve or what specific benefits its products should be creating for customers: There were exceptions, but in the majority of cases the theory of change within an institution did not express how the institutions specific products and services create the desired benefits for customers. Only one-third of the investees already have robust outcomes management practices, and of those who do not yet, some say they are planning to implement this and some are not. Among the FSPs that do define outcomes goals and gather data, setting targets for level of performance is not common. It is also not common for investees to be monitoring negative outcomes experienced by customers. In general, however, the FSPs do collect considerable data about their customers and use various methods and tools to collect data, so there is potential to integrate outcomes data collection into existing systems.

FSPs can see the relevance of outcomes data but tend to have weak systems: Most survey respondents said they saw the relevance of outcomes data for informing product design. But, the majority cited lack of internal capacity to implement a comprehensive outcomes management system. Weak internal capacity can take many forms, including lack of digitized data, inaccurate data, the ability to collect only outreach data, and insufficient skill in data analysis.

FSPs are not always convinced of the business case: The obstacles to implementing comprehensive outcomes management practices are numerous, but chief among them is a lack of belief in the business case. Notably, this is not the case among FSPs who already have outcomes data, but for those not yet collecting it, there is a reluctance to engage. Some FSPs assume the cost of outcomes management will outweigh the benefit, while some mentioned that outcomes management cannot be a priority while they focus on business sustainability. In fact, 62% of survey respondents said they were "too busy with regular work" to do outcomes management too.

FSPs fear losing funding if outcomes are negative. Another frequent piece of feedback was the fear of reporting negative outcomes, particularly to funders. FSPs think that they are supposed to demonstrate excellent outcomes and worry that if their data show mixed results instead, the FSPs may lose access to funding from donors or investors.

Initial recommendations

Given the above, Cerise+SPTF identified some recommendations for investors:

Use the influence of investors to strengthen outcomes management: Investors can support practices to strengthen outcomes management within each FSP and to build a culture of outcomes data analysis and use. This involves not only building the systems to collect and analyze accurate data, but also pushing the investee to gather data from multiples sources and to invest in a mix of qualitative and quantitative feedback.

Use outcomes data as a vehicle for transparency, accountability, and improvement: Outcomes data can be used to improve social and environmental performance rather than with an expectation that FSPs will already have uniformly excellent results and gather data in order to demonstrate this excellence. This in part means investors can and should use their influence to ensure that senior management reviews outcomes data on an ongoing basis and uses it to inform strategic and operational decisions. It also means that investors must communicate their realistic goals to investees, including that outcomes data will always reveal that some people are better off, some worse off, and some about the same, and that that point is to act to address the obstacles faced by those who had a negative outcome while retaining and building on what is working.

Provide support with technical assistance: Any financial assistance that investors can offer to investees to build their internal capacities, particularly in the early stages of building an outcomes management system, seems critical to facilitating improved practice and building buy-in within the FSP.

Ensure adapted reporting requirements: investors must be vigilant about setting up data reporting requirements that are not too burdensome, implying both a limit to the total amount of data requested and a partnership with the FSP to identify which data are useful to the FSP as well. This likely will involve using harmonized indicators across a portfolio when possible but also allowing for some customization in the types of data that each FSP in the portfolio reports.

The remainder of this report presents phase 4 insights and recommendations, built from data gathered in phases 1-2 and concrete implementation of phase 3 regarding current areas of weakness or misunderstanding as well as examples of best practice.

Theory of change: key concepts

What is a theory of change?

A theory of change is a sequence showing how a program or intervention will achieve its impact (Harvard Kennedy School). Its central question is 'What is the causal effect of [a program or policy] on [an outcome of interest]'?
Below is an example of a central question from the inclusive finance sector:

- What is the causal effect of providing microfinance loans on the quality of life of women from low-income households in India?

For an investor, a detailed theory of change clarifies the chain of changes from an investment that are expected to result in the desired development outcomes and specifies the role of the investor. As shared by one of the FSPs in the project: "*It clarifies the pathway from the vision/mission to actual changes.*"

Why have a theory of change?

A theory of change helps an organization build a roadmap from its inputs and operations to its desired outcomes. It has a variety of specific uses and benefits at investors' level:

- creating shared understanding, both internally and externally, of the expected change pathway(s);
- guiding investment and technical assistance decisions;
- surfacing misconceptions and contentious issues related to the process of achieving impact goals;
- providing a framework for monitoring the performance of investees and its own performance in achieving portfolio goals;
- clarifying what data the investor will ask the investees to provide, and why;
- motivating and guiding investees to set up their own actionable theories of change;
- aligning expectations with co-investors in portfolio companies and funds, as well as with the board and leadership team of investees, and with other partners.

Given that impact investors invest in organizations with the intent to contribute to measurable positive social or environmental impact alongside financial returns, a theory of change is essential to impact investment.

How does a theory of change relate to outcomes management?

Outcomes management is how an organization puts its theory of change into practice.

Outcomes management is "a multi-step organizational system for the collection, analysis, and use of outcomes data."[2] The theory of change defines not only what the ultimate impact goals are for the organization, but also the inputs and outputs, as well as the shorter- and medium-term outcomes that the organization expects its customers to achieve on the pathway to the ultimate impact goals.
Once the organization defines all of this, then it can manage itself toward those outcomes. Specifically, it can define the indicators it will use to monitor whether its own internal policies and practices, as well as its actual outputs, and the resulting outcomes, are aligned with those in the theory of change.
For example: a financial service provider will define indicators (e.g., % of new loans given to customers who did not previously have access to formal finance) and also targets (e.g., at least 25% of new loans will be given to customers who did not previously have access to formal finance). Next, the FSP collects and analyzes data from those indicators, and makes strategic and operational decisions based on data analysis.

In summary, the theory of change defines, "Here is what we should do," while outcomes management asks, "Are we doing that?" The theory of change gives a framework to strategic and business plans. Outcomes management monitors and manages performance. A theory of change, just like a business plan, emphasizes positive or desired outcomes. In performance management, however, it is important to track both positive and negative outcomes to fully understand how the situation of the customers changes and what adjustments are needed.

How to construct a theory of change?

A theory of change should articulate in a meaningful and measurable way the expected pathways for achieving impact. Constructing a good theory of change is a multi-step process.

Components of a theory of change

- <u>Base the expected pathways to change on evidence</u>: A theory of change should reflect the latest knowledge in the inclusive finance sector about the sector's social, economic, and environmental impact capability and limitations. For example, in microfinance specifically, research reveals that increasing customer well-being requires a more comprehensive approach than simply providing financial products. Microfinance requires educating vulnerable customers so that they obtain the requisite level of financial literacy to use financial products safely and effectively. Another example comes from research on job creation. Impact studies done by the investor Finance in Motion show that small enterprises are more likely to create jobs while microenterprises are more likely to support self-employment. Therefore, Finance in Motion will have a different theory of change for investments in SMEs versus in microenterprises.

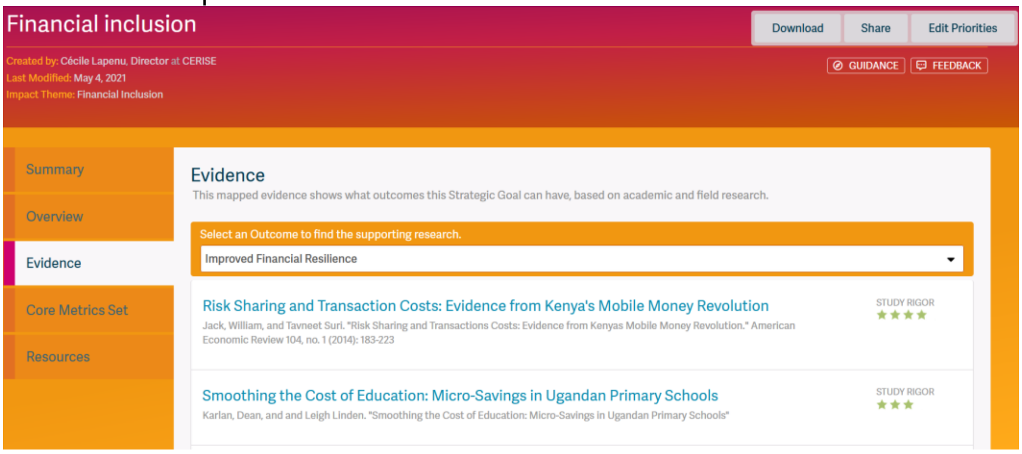
  Regarding the environment, a good starting place is to understand key environmental issues from the client perspective, in a specific country and sector context. Not every investor and financial service provider has the

[2] "Guidelines on Outcomes Management for Financial Service Providers," by Frances Sinha (2016).

expertise to promote green finance at a low cost to reach un(der)banked populations in developing countries. However, Cerise+SPTF argues that understanding the vulnerability of customers to environmental degradation (climate change, pollution, deterioration of natural resources and ecosystems) and helping customers diversify their livelihoods and build resilience in the face of negative environmental impacts, deserves more attention from the entire inclusive finance sector.

- The IRIS Website is an excellent resource for examples of evidence.[3] Create an account, select the impact goals that interest you (e.g. financial inclusion/ improved financial resilience), and then check the evidence gathered from academic and field research, by possible outcomes.

  See the example below:



- <u>Adapt the theory of change to specific characteristics of different customer segments</u>: A theory of change must integrate differences in financial inclusion barriers and how customer segments experience changes.
  For example, there are multiple reasons why microfinance customers may remain un(der)banked: they may live far from the closest financial service provider, they may have language barriers, they may lack the confidence to interact with financial service providers, they may lack access to technology, they may lack identification, or they may be too poor to meet requirements like mandatory savings, among others. There are also multiple reasons why they might struggle to exit poverty: they may be vulnerable to certain types of shocks (e.g., climate change, health risks), they may have income or asset poverty that prevents them from investing in business opportunities. On the other hand, an SME seeking a loan is likely to be very different, with greater financial skills and capacities, but also facing its particular set of obstacles. Therefore, an FSP that serves multiple distinct customer segments would benefit from a different theory of change for each, to clarify the interventions required to overcome the obstacles faced by each segment.

- <u>Clarify key terms:</u> Some key terms in theories of change may not be universally understood by all stakeholders. Some examples are, "just society," "environmentally sustainable society," "better future," and "low-income

[3] https://iris.thegiin.org/plus/home/

customers." A theory of change should explain the definition of each term in such a way that makes it clear how to translate them into measurable outcomes.

- Add contextual elements that can influence a theory of change: In addition to the intervention of a given organization, many other factors influence change. Some are macroeconomic, such as civil unrest, climate change, or a pandemic. Some relate to how culture influences behaviors in innumerable ways, from whether a customer is comfortable using a complaints mechanism to whether she will choose to send her daughter to school or to seek preventive health care. Some relate to the target populations themselves, such as level of literacy or access to savings. The interventions that will work in one context may not work in another, making it useful to consider the context in which the organization will intervene and to adapt the theory of change accordingly.

- Be realistic: Ensure theory of change assumptions are realistic and good enough to drive changes despite imperfect investment conditions. Plan for managing negative pre-conditions. Investors can promote and instill best practices, in governance, labor conditions, client protection, and risk management, where the local business environment is lagging or lacking.

- Define inputs, outputs, and short-, medium-, and long-term outcomes: Uniform vocabulary does not exist for each step in a theory of change, but there is general agreement on the substance of the various elements. Below is a list of the key elements that an organization will include in its theory of change:
    - Inputs. This is finance, human capital, and technology: the resources that will be used to drive the changes.
        For example: who is the organization's leadership and staff? What are its policies? What technologies does it use?
    - Outputs. These are the products and services that the organization offers.
        For example: loans, savings accounts, insurance, payment products, trainings, non-financial services, delivery channels.
    - Short-term outcomes. These are the direct/immediate changes experienced by customers linked to the use of outputs.
        For example: a customer takes out a loan to invest in her business or attends financial literacy training to build her capacities.
    - Medium-term outcomes. These are changes that do not happen immediately after the organization provides its products and services but are built from short-term outcomes, though also influenced by other factors unconnected to the outputs of the FSP.
        For example: a customer receives care at a local clinic paid for by health care insurance she purchased from an FSP; a customer improves (or reduces) her income after the investment of the loan in her business.
    - Long-term outcomes or Impact. These are the most ambitious impact goals. The organization's outputs and management of outcomes can plausibly contribute to these changes, but a variety of external factors and actors also influence them, making it generally not possible for one single organization to guarantee achievement of the goal.

For example: poverty alleviation, women's empowerment, reduced environmental degradation.

- Create a graphic to illustrate the theory of change: Once an organization determines its theory of change, it is helpful to condense the theory of change document into a graphic illustration. A succinct, visual presentation of the theory of change helps communicate it to both internal and external stakeholders in a way that is easy to digest.

Tips on the process of building a theory of change

There is no single correct way to construct a theory of change, but field experience suggests some ways to design the process that are likely to lead to a better result:

- Use a team, not a single person, and include the top management: Include the top management of the organization, from the beginning, in the process of building a theory of change, as buy-in from leaders is essential. But also, include a team of others across departments, and consider having more than one person from each department. This helps with project continuity even when there is staff turnover. Include mid-level managers as well as department heads, since they are the ones who will carry out the initiatives.
- Be clear that theory of change is part of the business plan: There can be a misconception that the theory of change, because it focuses on desired social impacts, is part of corporate social responsibility (CSR). But it is not. Implementing the theory of change is the primary work of the organization. The theory of change says, "given the activities of this organization, here are the predicted outcomes," and it is the business plan, with its corresponding budget, strategy, and oversight, that governs the activities that the organization implements.
- Clarify who should benefit from the organization's activities: In all cases, this involves defining the different types of customers that the organization serves. But some organizations also include desired employee outcomes into the theory of change. Some may focus on the community as well.
- Start by reviewing what staff already know, and what the organization has already documented: Use existing documentation on how the organization manages risks and creates customer benefits as a foundation for the theory of change. If the organization has an ESG policy, has defined its mission/vision, social goals or expected outcomes, and bases product development on the segmentation of customers and understanding their needs, review those as a starting point.
- Use the theory of change discussion to address contentious topics: Building the theory of change may lead to healthy discussions about controversial issues. For example:
    - whether microfinance is more likely to contribute to gender equality than traditional banking,
    - whether increased financial inclusion will automatically lead to job creation and growth of businesses and improved livelihoods,
    - what is the role of fintech companies in inclusive finance,
    - whether banks vs. microfinance institutions have greater capacity to create macroeconomic development impacts such as decent work and economic growth,
    - how strong is the risk that financial institutions can harm customers, especially those with low income and low financial literacy.

Embrace the debate, use evidence to inform the discussion, and seek to address the issues in the design of interventions and the management of outcomes.

- Continuously reinforce the theory of change: For the theory of change to guide practice, it must be widely understood and accepted. Bring it up on an ongoing basis in team discussions to ensure clarity and shared understanding. Monitor how implementation is going and use doubts and feedback to refine it.
- Update the theory of change periodically: The construction of a theory of change is a dynamic and iterative process like business planning. As the organization learns what works and what does not, or as external factors change, an organization should update its theory of change accordingly.

Examples of theories of change

Below are four different examples of theories of change:

- one from a think tank (CGAP) focused on the sector and
- the 3 theories of change designed and discussed during the path of the project:
    - one from a network of FSPs (Partner 3),
    - one from an FSP, focused on social aspects (Partner 2 in India)
    - one from an FSP, focus on environmental aspects (Partner 1 in India)

Since Partner 1, Partner 2 and Partner 3 participated in this project, the information below also summarizes the process to create their theories of change.

The Theory of Change for the inclusive finance sector (CGAP) as a source of inspiration

CGAP is a think tank with extensive experience in the inclusive finance sector. Its contemporary theory of change[4] focuses on two aspects of poverty: the vulnerability of the poor and their microenterprises, and income and asset poverty.

- Desired impact: Improved well-being of poor people.
- Components of the theory of change: CGAP's theory of change posits that by strengthening customer's resilience and enabling them to capture opportunities, financial service providers can contribute to poverty reduction. Its graphical representation does not mention inputs or outputs, but these will be provided from the combined efforts of different inclusive finance actors. The CGAP theory of change instead presents the variety of intermediate outcomes required to achieve the longer-term outcome goals of financial resilience and economic inclusion of poor people. The CGAP theory of change incorporates the idea that country context and prevailing norms influence outcomes and identifies the most relevant ones.

[4] https://www.cgap.org/research/publication/toward-new-impact-narrative-for-financial-inclusion

Updated theory of change for financial services

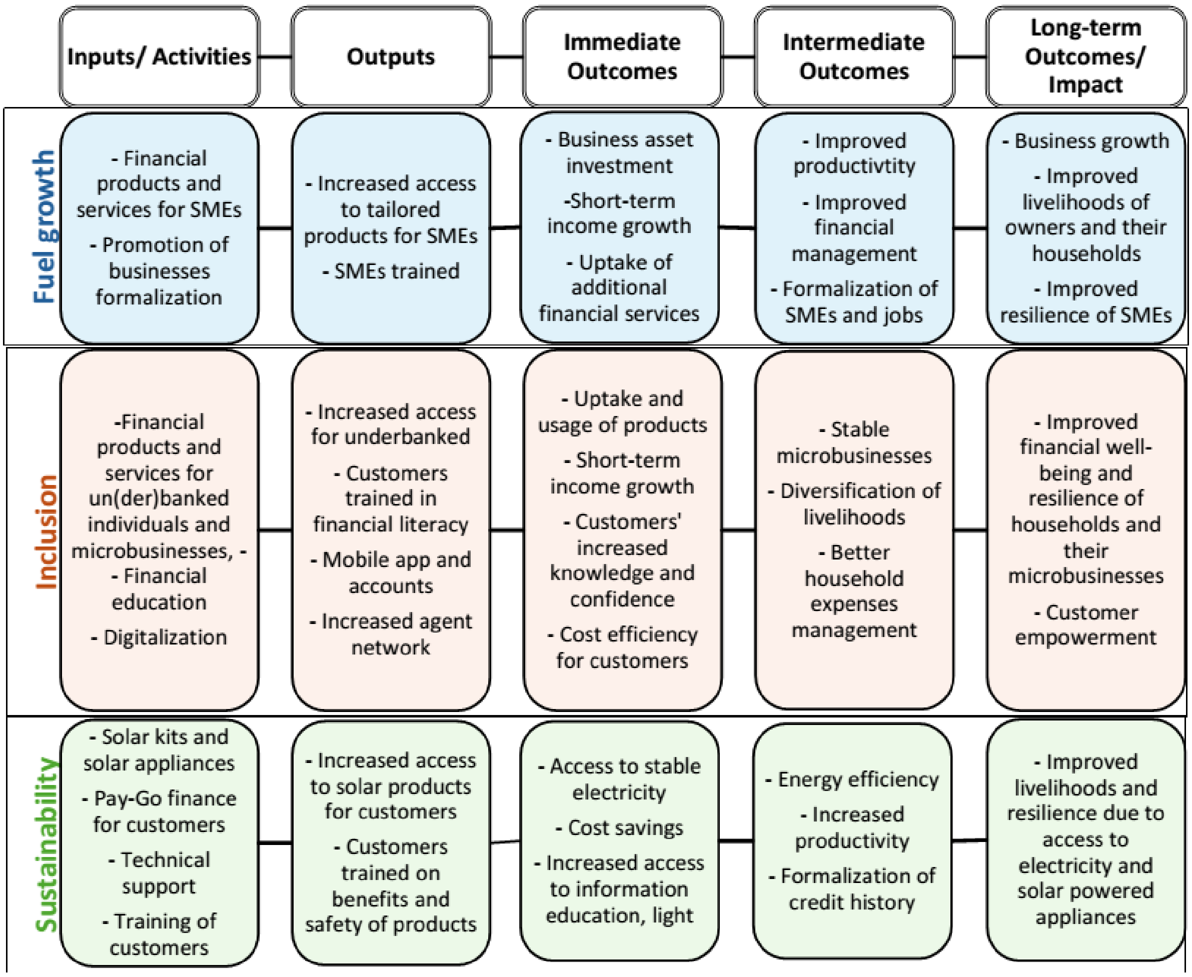
Theory of change at a network or investor level (example of Partner 3)

- Desired impact: Partner 3 is currently refining its vision and mission statements to emphasize business growth as its core pillar within a broader financial inclusion strategy.
  By 'empowering small businesses' Partner 3 aims to 'fuel thriving communities.' At the same time, not all customers have growth capacity or prioritize growth.
  The desired outcomes for customers seeking to grow their businesses will differ from those whose primary business goal is earning enough to cover household expenses.
  Besides business loans, the subsidiaries of Partner 3 offer deposit accounts, payment services, and insurance products, that cater to broader customer groups.
  Correspondingly, the theory of change prototype distinguishes between the business growth pathway and the broader financial inclusion pathway for all customers. The sustainability (climate action) and digitalization pathways reflect the other strategic pillars of Partner 3. In the prototype theory of change, digitalization aims to enhance customer experiences and deepen outreach. As customer outcomes from digitalization closely align with those of financial inclusion, this pillar is integrated into the inclusion pathway. Sustainability is currently defined by Partner 3 as efforts to reduce

environmental footprint (reduced use of water, energy, and fuel in the operations) and improve customers' access to electricity (solar kits, and solar-powered appliances). However, monitoring of organizational footprint is not included in the theory of change, as it is less relevant to customer outcomes.

- Components of the theory of change: The theory of change incorporates aspirational statements of Partner 3's policies and website content for better livelihoods, thriving businesses, and communities, to a chain of specific, observable changes in short-term (immediate outcomes, up to 1 year), and medium-term (intermediate outcomes, up to 3-5 years) that lead up to long-term outcomes directly related to the impact.

- Process to create the theory of change: While the vision and mission statements are still being discussed at a high level within Partner 3, the operational team has already updated the business plan and developed a set of social performance indicators for the subsidiaries. Therefore, the Cerise+SPTF project team constructed a prototype theory of change to visualize connections between vision, mission, strategic goals, business planning, and performance management and to articulate some of the outcomes and related indicators. The prototype is proposed for internal strategic discussions of Partner 3 (Supervisory Board, ESG Committee, and management) to get their buy-in and illustrate the benefits of developing a theory of change for business strategy and including outcomes management in regular business operations.



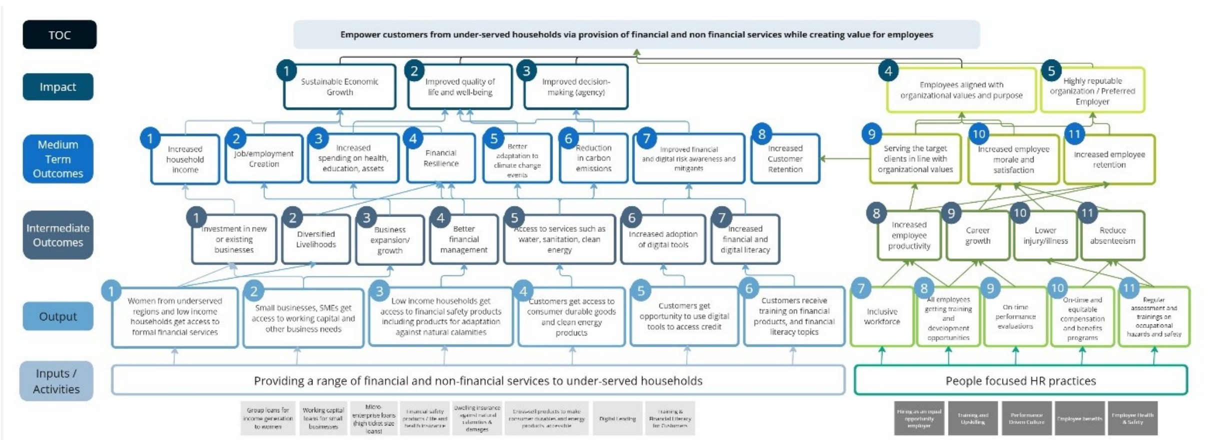
Theory of change at the FSP level, global focus (example of Partner 2, India)

- Desired impact: Partner 2 mission is to empower under-served households by offering a range of financial services, in a manner sustainable for all stakeholders.
  Partner 2 was established in response to a range of challenges faced by underserved communities in India, particularly those relating to access to formal financial services and tailored financial products that meet life cycle needs, particularly affecting underserved populations. Women, especially, encounter gender inequality in accessing financial services, which exacerbates their vulnerability in society. Small businesses also struggle with securing capital, limiting their potential for expansion and success. There is also a limited understanding and availability of affordable insurance products, which leaves clients vulnerable to the impacts of natural and man-made disasters, increasing the hardships for low-income households. Moreover, Partner 2 recognizes the issues arising from the digital divide and gender inequality in digital access, affecting the accessibility of financial services.

Without awareness about financial products and services, these problems are intensified due to a saturated market and over-indebtedness/multiple borrowings. In response, Partner 2 focuses on developing a sustainable model that offers tailored financial solutions, promoting resilience and empowering households to improve their socio-economic conditions.

- Components of the theory of change: theory of change of Partner 2 aligns with the organization's mission of empowering underserved households. The theory of change outlines the strategy of Partner 2 to achieve a sustainable impact for everyone involved, including their employees. The theory of change of Partner 2 has two foundations – client focused activities and the causal chain of outcomes and people focused HR activities and the causal chain of outcomes – both of which culminate into the impact that Partner 2 hopes to achieve. ESG focus is also in-built into the theory of change.

- Process to create the theory of change: Building a theory of change for Partner 2 involved several steps. First, Cerise+SPTF team conducted an introductory meeting with key officials (including their Managing Director) to brief about the project objectives, deliverables, timelines and roles of each party. Then the team requested for and reviewed documents of Partner 2 including SPI Online audits, impact assessment reports, policy manuals to understand the extent of data collected and its usage. In both on-site and offsite visits, one to one online discussions were held with some of the departments, directly working with strategy and social and environmental aspects. Based on these activities, Cerise+SPTF team drafted a work in progress theory of change, social and environmental goals, indicators to present to the team of Partner 2 during onsite visit. A four-day visit concluded with Partner 2 team sharing their feedback and discussing next steps. The team conducted a final virtual workshop with the final draft of theory of change which the management agreed upon. Finally, the team handed over all the materials to the consulting firm hired by Partner 2 to implement ESG to help Partner 2 integrate the theory of change and the indicators into the overall ESG work.



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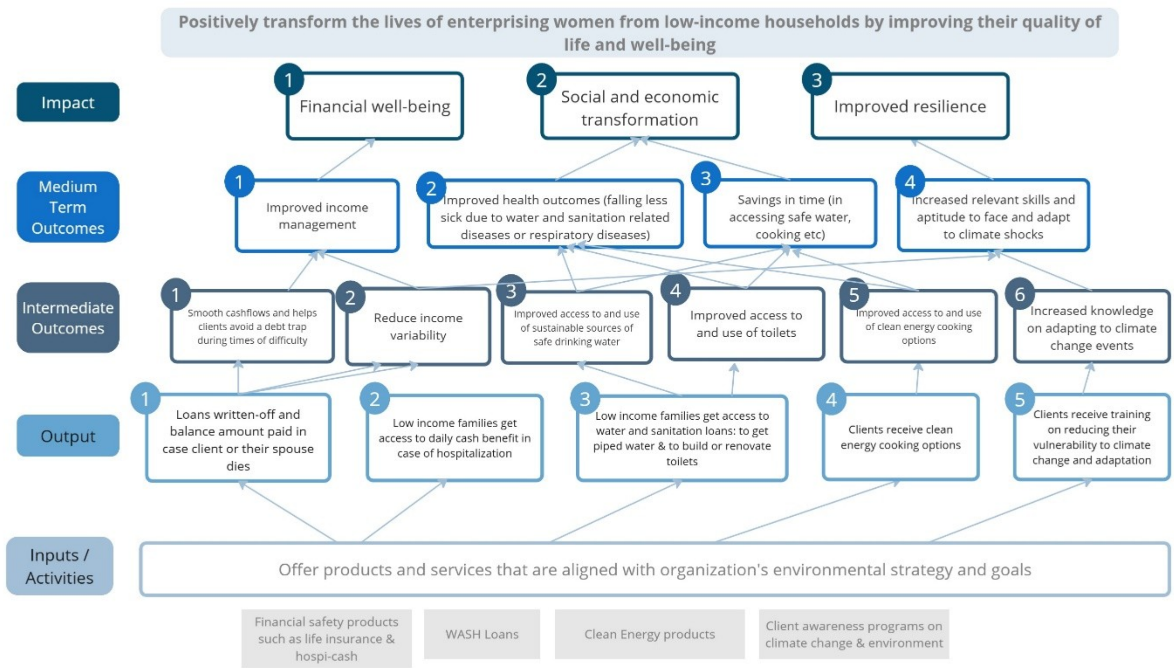
Norfund

Theory of change at the FSP level, focus on environment (example of Partner 1 in India)

- <u>Desired impact</u>: Partner 1 has a vision and mission to transform the lives of enterprising women. It seeks to help women and their entire households; hence, its priority impact areas are financial well-being, social and economic transformation of the household, and improved resilience of the families.

- <u>Components of the theory of change</u>: In the case of Partner 1, the theory of change was bifurcated into social theory of change and environmental theory of change. This was done to keep the visual simple and pathways clear. In both the cases, graphic of Partner 1 maps its inputs / activities (which are its offerings products or services) to outcomes and final impact. Because Partner 1 recognizes that reducing client vulnerability to climate change and environmental degradation is part of what drives client financial and social well-being, its products include those with a green focus. For this report, Partner 1 environmental theory of change is presented. All the pathways in social and environmental theory of change lead to the same long-term outcomes/impact – financial well-being, social and economic transformations of the households and improved resilience of the families to shocks.

- <u>Process to create the theory of change</u>: To build the environmental theory of change, Cerise+SPTF team reviewed the existing strategy documents, had discussions with Partner 1 management and team and conducted desk review on environmental risks and opportunities at customer level. These were analyzed and prioritized for implementation based on Partner 1 mission and vision, cost, and feasibility of implementation. Theory of change graphic then was developed and shared with Partner 1 team for feedback.



With a well-defined theory of change, an investor is ready to engage in each of the pillars of the Operating Principles for Impact Management. The following sections give recommendations for each step of the process.

Strategic intent

In the Operating Principles for Impact Management, the first step is defining strategic intent. This is both fundamental and individual. Each organization sets its own goals and is not obligated to choose one strategic intent over another. There are many ways to do good.

Nonetheless, there are some universal principles.

The first is to link business plan and theory of change.
Secondly, every organization has a moral mandate to do no harm. In inclusive finance, this means customer protection, which encompasses more than the environmental, social, and governance (ESG) framework currently applied in the corporate sector and regulations.
Thirdly, protecting customers from harm is not the same as doing good. To be an impact investor, an organization must go beyond customer protection and create benefits for end-customers.
Finally, each organization should understand what is realistic when defining its respective strategic intent. The text below explains these points in detail and is the basis for defining the strategic intents and expected long-term outcomes.

Integrating theory of change and business strategy

The exercise of defining a theory of change should be embedded, as much as possible, with building the overall business strategy to ensure coherence and joint strengthening. The theory of change should not be left with the "impact team" or the "ESG unit," as it should not live in isolation from the overall business strategy. The objective is to avoid, for example, that the business strategy is promoting products/services that do not fit the theory of change and do not meet the needs of the customers that the organization is aiming to reach. Instead, the business strategy and the theory of change should reinforce each other at least, or even be built together as a unified strategy, including defining the target customer group, setting financial and social targets / KPIs, determining which activities to pursue, and setting up an outcomes management process. Furthermore, when employees have performance goals, these goals should relate both to the business strategy and to the theory of change in a coherent, integrated way. If the business strategy does not facilitate implementation of the theory of change and achievement of its expected results, or if the theory of change is not built on a solid financial foundation, then financial services are unlikely to achieve the desired outcomes for end customers.

ESG does not necessarily guarantee customer protection

Environmental, social, and governance (ESG) risk management is an important first step, more and more required by regulations, but the current general framework does not encompass all elements of customer protection required in the inclusive finance. Therefore, adhering to ESG requirements alone does not protect customers from harm.
ESG practices mostly relate to compliance with regulation. To meet the “S” and “G” dimensions in ESG, organizations must meet minimum standards for labor (e.g., no discrimination, no forced labor, compliance with local labor code) and ethical business conduct (e.g., no corruption, no bribery, resolution of conflict of interests), respectively.
E&S can work together in particular when E focuses on climate and environmental adaptation to protect vulnerable populations. In some cases, climate action will consist of both adaptation and mitigation mechanisms, like investing in low cost efficient green energy solutions to microfinance customers that would potentially contribute positively to social outcomes.
For inclusive finance sector, the Client Protection Standards[5] are an additional set of management practices, ranging from prevention of over-indebtedness, transparency, fair and respectful treatment, data privacy and security, complaints resolution, and responsible pricing and growth. They offer the guidance and oversight that the board of directors, management, and internal audit teams must provide. Furthermore, in order to monitor whether every member of the organization is respecting CP practices, it is important to collect data on customers’ outcomes, in particular the negative outcomes.

Environmental aspect of ESG requirements overlooks vulnerability of low-income customers to environmental degradation. Organizations may limit ‘E’ to monitor their own footprint (and calculation of microbusinesses footprint, though it may be a futile exercise). Moreover, global exclusion lists are aimed at limiting negative impact on the environment (e.g. charcoal production and deforestation) but are generally not relevant to protect customers against climate change. Exclusion lists may work for climate mitigation but not for climate adaptation, so they should not be the only tool to engage on environmental aspects.

This is a concern even for investors that do not describe themselves as “impact investors.” Any investor in inclusive finance should augment an ESG risk management approach by the Client Protection Standards. Impact investors should include management of customers vulnerability to environmental threats.

Doing no harm is not the same as doing good: impact investors should go a step further

The focus of ESG and client protection is to avoid harm. It is not to do good**. An impact investor, by definition, defines a strategic intent to create positive impact from its investments.**
Research indicates that client protection alone is less correlated with increasing clients’ outcomes than good outcomes management practices. But not harming customers is not the end-goal of an impact investor.

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[5] https://cerise-sptf.org/client-protection-pathway/

Furthermore, research shows that targeting development impact broadly (investing in an organization that should benefit the local economy by paying taxes, creating direct employment, providing corporate finance, offering financial services to retail customers, and sometimes including low-income customers) is *insufficient* to create good for customers. This is because sometimes an organization's outputs lead to harm.

An impact investor asks not only whether the customers used a financial service but also whether they benefited from it. For this, **stakeholders committed to impact must prioritize positive outcomes for customers and manage their own activities toward those goals**, aligned with the theory of change.

Realistic impact goals recognize that perfection is unattainable

It is important to define strategic intent with realistic expectations. The Sustainable Development Goals (SDGs) are an important and valuable framework to help all stakeholders unite around a common vision of the ultimate impact goals we can and should achieve for all people, everywhere. The SDG targets offer clear strategic objectives. However, each actor can only contribute within its capacity. Many factors influence long-term outcomes, and most are beyond the control of any one organization.

In the inclusive finance sector, research concludes that the most common benefits for end-customers are improved ability to manage their day-to-day financial lives and to cope with shocks, while some customers use loans to invest in income-generating activities. Of these, some but not all can exit poverty, and some who do exit poverty can fall back into it. On the other hand, microfinance implemented responsibly can create these types of benefits for poor and vulnerable customers: reduced barriers to access, reduced vulnerability to shocks, consumption smoothing, increased ability to invest in economic opportunities, and increased assets. Since some microfinance customers aim for income growth, it is also interesting to measure progress out of poverty, with the understanding that not everyone is using microfinance to invest in an economic opportunity. And of those who do, not everyone seeks dramatic and consistent income growth. Some have more modest goals, such as steady and reliable income.

Furthermore, for all types of customers, outside factors heavily influence a customer's well-being. For this reason, no matter how responsible the practices of the FSP, in any given year, some customers will be better off, some will be worse off, and some will be about the same.

Origination and structuring

How the theory of change informs origination and due diligence

A theory of change guides origination. Thanks to the theory of change, the investor has already defined the answers to three key questions:

- Who do we plan to reach?
- How do we plan to intervene?
- What impact goals are expected from our investments?

Investment officers, along with relevant staff or consultants responsible for origination and due diligence, must follow clear guidelines when selecting investees. Investment officers will ensure alignment between the investor's strategic intent and theory of change with the potential investees, as reflected in the answers to the three key questions.

- Who do we reach: Are potential investees aligned with the investor's geographic and sectoral focus? Do they aim to serve the same target populations?
- How do we intervene:
    - Clarify what products and services the investees want to offer.
    - Assess whether the investees prioritize customer protection and are committed to outcomes management.
    - Assess alignment of expectations regarding investor engagement: role in governance, investment duration, technical assistance, and exit strategy.

  Note that an impact investor should aim for active rather than passive investment. Investing in equity involves ongoing engagement and management throughout the investment lifecycle.
- What are the expected impact goals: Do the investees share the investor's social and environmental objectives? Are they committed to setting and achieving specific targets for the expected change?

Having a well-defined theory of change is crucial for investors during the origination process, as most investees may lack a fully developed and tested theory of change. Despite having vision and mission statements, and in some cases even social goals, very few FSPs have a clear strategy for achieving specific customer outcomes. Most of the FSPs' social strategies are still institution-centric ('be the leader', 'preferred partner') with ambiguous long-term goals ('better future'). A sub-set of FSPs show 'product-centric' strategies ('innovative', 'responsible', 'fair', 'tailored products and services'). A customer outcomes-centric approach is rare.
With a clear theory of change, investors can effectively communicate their expectations, assess alignment with potential investees, direct investments, and guide partners toward achieving the desired customer outcomes.

The theory of change is also useful if an investor is selecting co-investors or partners. By communicating its theory of change, the investor can clarify whether other funds have an aligned vision and commitment to customer outcomes management, regardless of whether they are local or international, private, or blended finance partners.

Due diligence: data and process

During the due diligence process, investment officers or responsible staff/consultants should assess not only alignment with the theory of change but also the willingness and capacity of potential investees to implement the required interventions and monitor performance.

- **Willingness** of the top management to prioritize positive customer outcomes over institutional outcomes (usually, financial results). They cannot view the theory of change as just a "ticking the box" exercise ("*yes, we have a nice vision and mission, yes, we want to reach out to vulnerable clients, yes, we want to provide productive loans*," etc.). Do members of the board and management wish to hold themselves and their organization accountable to creating positive customer outcomes and do they truly understand the resources and effort required to implement a strategy focused on achieving them?

- **Alignment** of goals. Are the stated goals aligned with the investor's strategic intent, but also is the actual strategy put in place?
- **Outcomes management already in place**: Verify to what extent the investee is aware of and has implemented the Universal Standards for Social and Environmental Performance Management ("Universal Standards")[6] which include client protection standards. In particular, determine what outcomes data the investee is already measuring and how it is using those data to inform decisions. Investigate the following:
    - Evaluate the level of implementation of Dimension 1 (Social Strategy) and Dimension 2 (Committed Leadership) of the Universal Standards to see what management *practices* the investee already has in place to select indicators, collect data, analyze data, and report data to management;
    - Evaluate how well the management information system (MIS) and level of digitalization facilitate data analysis;
    - Analyze the data already available on outcomes achieved. Is the investee reaching its goals?
    - Assess to what extent top management and board members have used outcomes data to inform decision making. For example, see dashboards shared with the board and reports sent to management.

  The outcomes management system already in place does not need to be perfect, as the investor can provide support to address gaps throughout the investment lifecycle. Nonetheless, the investee should be aware of its strengths and weaknesses and agree that tracking outcomes data is essential.

Due diligence: capacities to build and rely on

To ensure reliable assessment in due diligence, and subsequently in monitoring, investors should arrange for appropriate training and capacity building for their staff. When relying on **internal staff**, the investor ensures that all its staff involved in the investment process are trained and regularly updated on its own theory of change, as well as basic standards of client protection and SEPM.[7] The investor should also develop and train staff on the concrete steps, processes, tools and quality control to implement in due diligence. This is an on-going process.
When relying on **consultants**, the investor should define clear terms of reference and responsibilities of the consultants and ensure quality control of the assessment done. In this case, investors can find possible support within the SEPM Pro Network.

When relying on **a client protection assessment, a social audit, a client protection certification, or a social rating,** the investor should hire a rating agency or qualified

[6] https://cerise-sptf.org/universal-standards/

[7] A key training resource are the online courses on customer protection and social and environmental performance management offered by Cerise+SPTF.

consultant and ensure that they follow the Cerise+SPTF guidelines[8] on which practices to assess and what methodology to use. At the stage of due diligence, Cerise+SPTF recommends a CP assessment or social audit, or due diligence conducted by internal staff, rather than a CP certification or a social rating, as the latter two can be quite demanding on time and are more expensive than the other options. CP certification or a social rating with a minimum score can potentially be required at some point during the investment lifecycle. If there is already a CP certification or social rating report, due diligence is to check essential practices too, as the situation may have changed, and it is important to follow up on areas of weakness and risk.

Structuring

To guide the decision-making process, an investor can set up minimum eligibility criteria for investments. For example, an investor could choose that at minimum an investee must score a 55% on the SPI social audit tool, while also defining thresholds for dimension 4 of the Universal Standards, which focuses entirely on client protection, and specifically a minimum score for standard 4A on prevention of over-indebtedness. Rules can be flexible, however. The investor may want to consider adjusting its eligibility requirement for newer organizations such as fintech companies, that have innovative ideas and are willing to improve but have significant gaps, often with regards to an incomplete set of policies or practices already in place.

Contracts between investors and investees should include specific clauses and covenants that outline shared customer outcome objectives and detail the data that both parties will monitor, aligned with the theory of change. At a minimum, the contract should require adequate customer protection practices. The graphic below gives an example of covenants related to Client Protection[9].

Example of covenant in loan/grant contract

Commitment to implement Client Protection. Within 90 days of the disbursement date [or contract signature], the borrower agrees to formally commit to implement Client Protection Standards by joining the CP Pathway. The borrower commits to keep an active status on the CP Pathway throughout the whole contract term, and, as such, to comply with all requirements as requested by Cerise+SPTF.
[Event of default] Non-compliance with the above will be considered an event of default.
[Not EoD] Non-compliance with the above will not be considered an event of default but shall be discussed between the Borrower and the Lender in order to find a prompt remediation.

Reporting on Client Protection. The Borrower commits to share with the Lender updated reporting through [CP Full/ ALINUS] within 12 months of signature, and on a yearly basis.

Additionally, some covenants integrate a list of core outcome indicators to report. As part of the process of including these indicators in the contract, the investor will

[8] See the Cerise+SPTF webpage on Third-Party Validation – Cerise+SPTF (cerise-sptf.org)

[9] Link: https://cerise-sptf.org/guidelines-for-implementing-the-joint-statement/

discuss with the investee what output and outcome targets are realistic yet ambitious. This process creates a shared understanding as well as buy-in and sets the expectation that the investee will track progress and adjusting as needed.

See the subsection “Indicators” in the section “Portfolio Management,” below, for specific suggestions of indicators to monitor.

Portfolio Management

Support an integrated vision for theory of change and outcomes management

Build buy-in for outcomes management at the investee level

Reporting to investors is often seen as a burden by investees. To mitigate this, request data that is relatively affordable and easy for the investee to collect, wherever possible. However, some essential data may be challenging to gather. In such cases, it's useful to make a **business case for outcomes management**, demonstrating how it aids in **risk mitigation**. Specifically, show how outcomes management helps investees solve real problems they are facing, such as stagnant growth, client exit, dormant accounts, low use of a delivery channel, negative reputation, and poor portfolio quality. Emphasize how client feedback informs business strategies and adapts product design. Understanding which customers are experiencing benefits and which are worse off also helps the FSP to know what to keep doing and what to change, leading to more satisfied customers, higher growth and reduced customer risks.

See Appendix A: Key messages for the business case of the theory of change.

Define and Monitor Indicators

Investors need to define the indicators to use to track outcomes that are relevant to the investees’ theory of change. It is important to set a shared understanding with investees early on about which indicators will be tracked, why, and how data will be collected, used, and reported. Do this before monitoring begins to ensure a smooth process. Keep in mind data collection challenges, such as indicators that investees may not find useful or feasible to track. For example, if the investor plans to track the percentage of clients categorized as low-income, inconsistencies in definitions or the lack of context-adapted tools may make it difficult to collect accurate data and consolidate findings across the portfolio. A clear definition or a simpler indicator than income, such as rural clients, may be easier to track initially.

When choosing indicators, note that output indicators alone are insufficient to determine whether social objectives have been achieved. Counting the number of customers using a product does not reveal whether the product has been beneficial or harmful. You may not even know who ultimately used the product. For example, a female borrower might have to let a husband/brother/father decide how to use the loan, while she retains only the legal liability. Similarly, repeat usage is not necessarily a sign of positive outcomes. With credit, customers may be trapped in a debt cycle. For other types of financial products, customers might have limited options.

Defining a set of standardized indicators across a portfolio can be challenging due to the diverse sectors in which the investor operates and the varying contexts of investees, even within the same sector. Nonetheless, partial standardization of indicators is possible and beneficial. Measuring and managing impact at the portfolio level helps assess the achievement of broad inclusive finance goals, compare levels of achievement through benchmarks, communicate more effectively with a common language, and avoid social washing.

One way to standardize indicators is to align with the SDGs across the portfolio to assess contribution to sustainability goals. The table below presents possible outcome indicators to monitor, in line with targets for SDGs 1, 5, 8, 10, and 13 for financial inclusion.

Table 1 – Core standard outcomes indicators linked to the SDG

OUTCOMES	SDG	SOURCE
Number of clients gaining access to financial services for the first time	1	Survey/Loan applic./MIS
Borrower retention		MIS
Change in savings	1	MIS
Client Satisfaction		
Number of complaints received in the last 3 months		Complaints mechanism
Of these complaints in the last 3 months, number of complaints coming from women	5	Complaints mechanism
Of these complaints in the last 3 months, number of complaints resolved		Complaints mechanism
Percentage of clients who declared to be satisfied or very satisfied of the FSP		Satisfaction survey
Percentage of women clients who declared to be satisfied or very satisfied		Satisfaction survey
Net Promoter Score (segmented by profile of clients, by products)		Satisfaction survey
Profile of vulnerable clients		
Number of clients being from low-income households (as per national definition or provider's own client segmentation)	1	Loan application/MIS (in % from surveys)
Number of young clients (or borrowers)		Loan application/MIS (in % from surveys)
Financial Health and Client Protection (segmented by profile of clients, by products)		
Percentage of clients who declare that the provider is trustworthy / or that they are treated fairly/ know how to complain		Client protection survey
Percentage of clients who declare that they understand the terms and conditions of the financial services		Client protection survey
Percentage of borrowers considering the repayment as a burden		CP/Satisfaction survey
Percentage of clients who declare that their capacity to manage their budget have increased (control)/ or "participate in key household spending decision"	1	Outcomes survey
Percentage of clients considering that they can cover emergency expenses (e.g. they can raise an amount of 1/20 of GNI per capita) within a short timeframe (e.g. one week)	1	Outcomes survey
Changes for the customers		

Number of borrowers with increased business income (or business assets) on next loan cycle	8	Outcomes survey / Loan application by cycle / MIS
Number of SMEs with increased business income (or business assets) on next loan cycle	8	Outcomes survey / Loan application by cycle / MIS
Number of SMEs with improved business practices (e.g. new products, new markets/clients, new delivery channels, improved HR policies)	8	Satisfaction or Outcomes survey
Number of jobs supported	8	Loan application/MIS
Number of new jobs created	8	Proxy from outcomes survey
Percentage of women borrowers declaring that they have used the loan alone, for own economic activity	5	Outcomes survey
Percentage of customers who declare that their monthly household spendings have increased or increased spending on home improvements, education, healthcare	1	Outcomes survey
Percentage of customers who declare that their number and/or quality of meals have improved	1	Outcomes survey
Percentage of customers who declare that their household assets have increased	1	Outcomes survey
Percentage of customers who declare that their quality of life has improved	1	Outcomes survey
ENVIRONMENT *(indicators should be developed specific to the green products and services offered)*		
Percentage of customers who declare improved health outcomes due to use of clean energy for cooking or increased time for education due to the use of solar panels	13	Outcomes survey
Percentage of customers who reported increased knowledge about sustainable agricultural practices or crop insurance or livestock insurance (depending on the program/service offered)	13	Outcomes survey

Encourage the investee to integrate the theory of change and outcomes measurement into the overall business strategy

The social strategy or theory of change is often developed separately from business planning, involving different teams, agendas, formats (a narrative social mission/vision versus a quantitative business plan focused on financial projections), and key performance indicators (KPIs). This can lead to different or conflicting global objectives and a lack of coherent performance tracking, undermining buy-in. Instead, integrate impact metrics and indicators into the organization's overall business strategy, rather than treating them as separate entities. Using the same formats to capture goals (social, financial, operational, and environmental), objectives, indicators, and targets will make it easier to integrate theory of change goals and objectives into the strategic business plan.

Smooth integration of the theory of change into the business plan may require an iterative process to align social assessments and actions to address gaps with the timing of the business plan. Leadership should be aware of and support the merging of the two exercises. Align the timing of defining or revising the theory of change and the business plan so that the strategic team discusses business objectives through a customer outcomes lens and the operating teams allocate staff time and financial resources for outcomes management in their workplans.

Identify steps to integrate theory of change with strategic business planning:

When executed properly, the theory of change exercise should provide sufficient context and outputs that can be seamlessly integrated into the strategic business plan. In the following paragraphs, the process recommended for Partners 1 and 2 is shared:

- Identify the problem statement(s) that the FSP aims to address through its programs or interventions. This information can be incorporated into the context section of the strategic business plan.
- Develop realistic theory of change in a visual graphic with clear inputs, outputs, pathways to outcomes and final impact. Label the components to facilitate connections with indicators and targets. This visual can be integrated into the section of the strategic business plan that covers the organization's vision, mission, and strategic intent.
- The theory of change graphic should ideally include a 1–2 page(s) narrative explaining the graph. This narrative can be included in the strategic business plan's narrative document. Encourage investees to develop a narrative for their strategic business plan if they do not already practice this.
- Develop social and environmental goals, objectives, indicators and targets as part of the outcomes data management protocol. A summarized version featuring the top 2-3 goals, indicators, and targets could be included in the quantitative targets or KPIs of the strategic plan.

Involve the strategy team in the theory of change exercise:
As previously mentioned in this report, the theory of change exercise should be a cross-functional or cross-departmental activity. Even in small organizations, the individual or department responsible for strategic planning should be involved in developing the theory of change to understand its purpose and utility and to integrate it into the business plan.

Consider the optimal time to introduce improvements:
Updating the business plan is an ideal opportunity to formally integrate the theory of change into the business strategy for value creation. At this stage, the vision, mission, strategy, KPI targets, data protocols, client outcomes analysis for decision-making, and departmental roles and expectations should be fully integrated into the global strategy, ensuring a coherent and unified approach to social and financial objectives.
Updating or changing the core banking system is another opportune time to revisit data needs, the current data collection system, and the integration of core, quality client outcomes indicators for decision-making. Training on the new banking system should include instruction on the new indicators, including how to collect, ensure quality, and report them.

Any change in the MIS system is also an opportunity to embed outcomes management in the financial tracking system:
- identify core client data to be tracked (e.g., unique identifier by customer, core profile indicators, asset, income, changes over time);
- drop any information that is unclear, not used, or too complex to collect by field officers.

Take the opportunity of a new banking system to train staff on the value of customer data, on the requirements for quality, and on the use of the customer data for strategic decisions.

For example, understanding when customers benefit or do not benefit from existing financial products and channels can guide decisions about when and how to digitize, whom to partner with, what types of non-financial services to offer, how to market products, how to disclose terms and conditions transparently, how to structure the complaints mechanism, and how to train staff, among other considerations.

Do a baseline assessment

Every investee should conduct a baseline evaluation of their customer protection or social and environmental performance management (SEPM) practices, as well as their outcomes management. This evaluation should be repeated at least every three years.

For SEPM, a range of assessment tools are available to tailor the evaluation of an investee's performance in specific focus areas of the investment:

- Internal assessment using in-house tools,
- ALINUS (Aligning Investors due diligence with the Universal Standards) and CP Commit tools as the short versions on SPI Online (for debt investment),
- Full audits for a comprehensive assessment on SPI Online (SPI5 Entry or SPI5 Full).

Equity investors should use more in-depth tools to thoroughly assess the alignment of potential investees with the theory of change and the level of implementation of the Universal Standards. See the Cerise+SPTF tools webpage for more information on the free tools offered as a public good for the responsible inclusive finance sector.

For outcomes management, the following example illustrates the strengths and weaknesses that a rapid outcomes management audit can reveal.

A- SPM Department's services, tools and processes

QUESTIONNAIRES	DATA COLLECTION	PROCEDURES	CPS & HOTLINE	SPM WORK PLAN
• Inconsistency of some results • Neutrality of loan officers • Waste of time and information • Questionnaires not always updated (new PPI created in 2016)	• MIS only allows the extraction of PPI and Outcomes data • There is no tool to monitor the SPM Department	• The procedures are well done • Some LO haven't in mind all the information set out in the training guides • Need for small updates	• [redacted] has good client protection standards • The client hotline has proven its effectiveness • Reporting is made	• Willingness to improve training and to collect more data • Short-term vision • No confirmation from management

Monitor, assess, and adjust on an ongoing basis and at all stages

Ensure ongoing monitoring of investments, even if they initially appear promising.

Proactively and continuously assess investment progress.

Monitor at various stages along the flow of funds.

Investors must ensure that capital is used as intended at each stage, from the initial investment to its utilization by investees and ultimately to the provision of financial services to customers.

Analyze data with an awareness of the complexities of interpreting results.

Data analysis is complex for several reasons.
One reason is that operational conditions vary significantly between countries, including differences in regulations, infrastructure, and challenges. Thus, it is overly simplistic to conclude that if people are not better off this year compared to last, the investment failed, or that if customers are better off, the investee's intervention was solely responsible.
Additionally, in countries with favorable conditions—such as good infrastructure and stable government—it is easier to achieve positive outcomes compared to more challenging contexts.
An additional complexity is that averages and aggregate numbers hide different outcomes for specific customer segments. For example, while global data may indicate an overall improvement in customers' quality of life, segmented analysis might reveal significant differences in experiences and outcomes between rural and urban, or female and male, customers. An additional example from an FSP in Senegal illustrates this point: although women make up nearly 50% of its customer base, they typically borrow smaller loan amounts compared to growth-oriented SMEs, which are predominantly owned by men.

Therefore, integrate context and customer segment considerations into the analysis of outcomes data to:

- Understand external influences (e.g., political events or changes in investor operations) when evaluating outcomes.
- Adapt outcome expectations according to contextual differences.
- Suggest using general indicators but set specific targets tailored to each country and context.
- Segment analysis by all customer segments served by the FSP and by product or channel.

Benchmarks are also useful in analysis but must be applied cautiously.

Benchmarks can motivate FSPs to address gap areas when they see their peers performing better. They can also help an FSP identify realistic targets.

However, benchmarks have limitations and context is crucial. While benchmarks on outcomes are beginning to emerge (e.g., from the 60 Decibels Microfinance Index), financial service providers with similar products and policies may operate in very different environments. When comparing investee performance, it is important to consider external factors such as market competitiveness, economic development, and cultural aspects (e.g., differences in expressing satisfaction) and how these elements may influence outcome results.

Guidelines on strengthening outcomes management through technical assistance

Investors should encourage, and if possible, provide technical assistance (TA) to investees to strengthen their outcomes management. Most investees have gaps in this area. Defining and implementing a theory of change and establishing a robust outcomes management process is a step-by-step journey. As a first step, investors should assess the current level of performance in each aspect of outcomes management. Once the assessment is complete, the most feasible initial improvement is typically to focus on enhancing existing data collection and analysis before moving on to new areas.

See Appendix B: Guidelines for Assessing What Technical Assistance to Suggest to an Investee for Strengthening Its Outcomes Management System.

Technical assistance for investees can be used to initiate improvements identified during due diligence or to introduce new approaches, such as developing a theory of change or defining a limited set of meaningful indicators. This TA is not directly tied to monitoring but aims to support investees in strengthening their systems and practices to address weaknesses. A specific focus on outcomes management and theory of change implementation will guide investees on their journey toward achieving better impact.

Note: For a discussion of outcomes management from the perspective of what an FSP should do, see Appendix C "What can be expected from FSP, with potential support from investors?"

Below are some **tips for investors** on how to approach TA, based on field experience:

- **Build general capacities**: Provide technical assistance in the fundamental tasks of outcomes management (e.g., data collection, data analysis and reporting). For now, most FSPs lack the time, human resources, and budget, and may prioritize financial sustainability over outcomes management. Be aware when a particular set of data, or data-collection methodology, is not (yet) aligned to the way the FSP works and guide the FSP toward better alignment.
- **Define the theory of change approach**: This approach is not always well understood and is sometimes reduced to merely defining a "vision/mission," which can end up as lofty wording without clear strategies and activities.
- **Build buy-in**: Initially, buy-in may be low because the investee has not yet established a robust outcomes management process and has not experienced its benefits. The investor should play a role in funding outcomes management and insisting on its integration into overall operations. Once the system is in place and the investee recognizes its value, they are more likely to manage some of the work independently (thus requiring less TA from the investor) and allocate a portion of their budget to it. Starting small and building on early successes can help demonstrate the value of the work to the FSP. Beginning with customer protection practices, which are widely recognized as fundamental to risk management, may also be beneficial.

- **Guide the process**: Set clear expectations for having the right processes in place, including accountability, data collection, analysis, and using data for decision-making. Help the investees collect actionable data.
- **Support improvement**: Act as a partner in the improvement process rather than focusing solely on achieving specific targets. As one expert interviewed for this project noted, "*It is important to collect data not only for accountability, but also to correct and to improve. This is equally true for delivering impact as it is for the financial part.*"
- **Focus on process before adding indicators**: At an early stage, establishing an outcomes management system is more important than requesting additional client indicators. Start by improving the accuracy, analysis, and reporting of data that the FSP already collects.
- **Minimize transferring the investor's own ESG compliance requirements to the investee.** Requirements for ESG compliance or reporting may not always be directly useful for investees. In these cases, use of proxies where possible (example: GHG emissions).

A measured approach to outcomes management

Below are suggestions for reducing the burden and increasing the accuracy and benefit of outcomes management.

- **Reduce the reporting burden:**
    - **Be aware of challenges for data collection and analysis**: discuss the constraints raised by the investee (lack of funding, lack of human resources) and the resources needed for data collection and analysis. Request only the data that the investee truly needs to learn and make decisions. Be strategic about the frequency of data collection and the number of indicators tracked. Prioritize (example above: Do we need to calculate, at the FSP level, the GHG emissions or should we use a proxy?).
    - **Work collectively with like-minded investors** to align expectations and requirements, support reporting and risk management on ESG regulations, use consistent terminology for coherent support.
- **Triangulate sources:** Integrate various approaches and sources of information, from due diligence to regular monitoring, to effectively mitigate risks and evaluate investment outcomes.
  Different sources of information can be used:
    - **National data** at the country level, such as:
        - Findex data on financial inclusion
        - 2X data on gender equality
    - **MIS data** such as:
        - PAR by segment to identify risks of over indebtedness
        - Profile of customers/assets/income captured during loan applications which can serve as a proxy for customers' standard of living and test Target 1.4 of SDG1 (Does the FSP reach the vulnerable?)

        - First-time access to financial services to track financial inclusion, compared to Findex Data
    - **Complaints mechanisms:** A grievance mechanism is a non-negotiable requirement, and customers must be informed about how to use it (e.g., through SPI audits). The results of complaints must be analyzed and segmented by product and client profile. This information should be used to understand customer needs and outcomes, improve products and services, and report on potential negative outcomes.
    - **Satisfaction and Outcomes surveys**: Satisfaction and outcomes surveys: Using a call center or direct visits to a representative sample of customers, the FSP should collect at least the minimum level of customer satisfaction. Additionally, satisfaction surveys can include outcome-related questions (see examples of standard outcomes questionnaires on the SPI Online resource center[10])
- **Emphasize improvement over perfection:**
    - Use outcomes measurement to track changes over time.
    - Make sure data is collected not only for accountability, but also to correct and improve.
    - Investors can foster a culture of continuous learning and adaptation by setting the expectation that outcomes data will reveal both strengths and areas for improvement. This approach ensures that FSPs do not fear being penalized for honest reporting of challenges.
    - Good practice involves achieving improvement over time and, when a negative trend is observed, acting promptly to address it.
    - Recognize that external factors also influence outcomes. The investee uses outcomes measurement to manage what it can control; sometimes a “good outcome” may simply mean that customers are not worse off after experiencing a challenging period (e.g., drought, pandemic).
- **Allow for a customized approach, with a standard set of indicators**.
    - **Be flexible with the theory of change** definition, data monitoring, and reporting. **Discuss the customization** of the theory of change at the FSP level while maintaining alignment with overall goals.
    - Require each investee to report its outcomes. Agree on a minimum set of standards and allow for additional customized indicators.
        - **A minimum set of standard indicators** can be established within a given sector. Standardized measurement improves investment decisions and increases transparency.
        - However, beyond the minimum standard indicators, other **complementary indicators** may be also useful to different investees. Investors should be mindful of the diverse customers and priorities of their investees.
- **Build analytical skills.** Go beyond outcomes measurement to assist investees in developing their analytical skills. Can they segment analysis by key customer characteristics (e.g., gender, location)? Can they link to MIS data and visualize information to highlight key lessons? For example, Partner 3 assesses customer outcomes across its subsidiaries using 60 Decibels microfinance index surveys and MFR impact and outcomes studies. Feedback

[10] https://en.spi-online.org/resources/view/resources-collection-outcomes-and-sdgs#questionnaires

from Partner 3 indicates that insights from these assessments can sometimes be overwhelming.

- **Track and analyze negative outcomes**:
  - Identify risks: Investors should be aware that negative outcomes may sometimes result from factors beyond the FSP's control, and that internal risks, such as employee fraud, are also possible.
  - Outcomes measurement is not just aimed at showing how great the investee is. Outcomes management should identify positive trends and attitudes while focusing on improvements. Reporting should shift from proving good outcomes to using data to continue what works for some people and to determine what changes are needed to improve results for those who are worse off.
    - Focus on negative outcomes: Not every customer will be better off year-over-year, so investors should not expect only positive results. Concentrate on the results for those who did not benefit (e.g., % of clients reporting decreased income or significant repayment burdens) and segment these results to identify the profiles of clients in stress. Negative outcomes often provide the most actionable data. Investors should prioritize honest analysis of both positive and negative results and take action to address negative outcomes.
    - Define an iterative approach to work with the results, focusing on negative outcomes.
- **Help prioritize and take action:** Investees may treat a report as merely "informational" or use the results for communication purposes. They may also develop too ambitious action plans or struggle with identifying which gaps to address first.
  Investors should set expectations that the investee will address 1-3 gaps per year, for example, and jointly determine which gaps to address first. Define concrete and simple action plans.
  The outcomes results should also inform future business plans, including the profile of customers reached, future targets, and actions needed to achieve social objectives.

Leadership on outcomes management at the board level

Through active participation on the board of directors, investors can serve as a hands-on partners, helping to improve both financial and social performance. They should request outcomes data and allocate time during board meetings to discuss it.

- Board members can advocate for the integration of customer outcomes management into the organization's strategy and operations. They should ensure coherence between the theory of change and the business plan.
- Board members can also share expertise in social performance management, including outcomes measurement, to better understand customers' socioeconomic profiles and changes in their quality of life.
- Board members can set the expectation that the FSP will monitor when and how customers experience negative outcomes and take action promptly to improve outcomes for those customers.
  - Examples from the December 6 workshop illustrate that "loan understanding" should be presented as "% of customers who do NOT

understand loan terms and conditions" or "% of customers saying repayment IS a burden". These results should be segmented by customer profile (e.g., gender, age, product) to identify who is most affected.

Indicator	Description	FSP ABC	60dB MFI Benchmark
Client Protection			
Repayment Burden	% saying repayments 'not a problem'	59%	65%
Consumption Sacrifice	% who 'never' cut food consumption to make repayments	76%	79%
Loan Understanding	% 'strongly agree' penalties, fees, and interest rates are clear	12%	71%

Consolidating at the portfolio level

Integration of standardized indicators across the portfolio allows for consistent measurement and management of impact at the portfolio level.
ESG regulations now require reporting on certain core indicators at the aggregated portfolio level (e.g., gender pay gap, GHG emissions).
This remains complex at the portfolio level.

Standard indicators: The indicators that an investor or an investee monitors are typically a mix of outreach, output, and outcome indicators. For example, the FSP may track the socioeconomic and demographic characteristics such as customers' gender or income level. Output indicators can include process and policy indicators, such as if the FSP has a gender policy, or how developed its outcomes management system is ('not developed', 'in development' or 'well-developed'). These indicators can help identify priorities for support on portfolio level for investors. Outcome indicators are those that track changes in customers' lives (see table in the section "Define and Monitor Indicators"). Investors should encourage investees to collect these as well, with a focus on data that are useful for decision-making.

Data checks: It is important to run checks on key values before working with a specific data set (outliers, inconsistent changes from one year to the other, etc.)
For example, when calculating the average loan size in USD, errors can arise from key values such as currency, exchange rate, gross loan portfolio, and number of borrowers. Once computed, values under $100 by investees should be scrutinized (though they may exist) and either excluded or confirmed if possible. Values exceeding $200,000 should also be examined - certain SME-focused FSPs may have average loans in this range or higher. These values should be confirmed or excluded before calculating the average loan size at the portfolio level.
It is important to note that diverse FSPs within a given portfolio may not reveal certain outliers. In such cases, comparing with historical data (if available) or reviewing financial reports on the corporate website could be useful.
For portfolio with a small number of investees, with investors providing direct support (TA or board participation), data collection can be easier, and data quality more carefully checked.

Abler Nordic INVESTMENT FUND FOR DEVELOPING COUNTRIES Norfund

Calculations: The method of calculations should be clarified, whether it is averaging averages or summing totals.
Average of averages
It gives equal weight and importance to all FSPs but can have drawbacks in a diverse database.
For example, to calculate the average share of women borrowers, investors will calculate the share of women borrowers in each FSP then average the averages (or the mean of means).
Sum over total
This calculation has been used in certain cases as it gives for example a better idea of the outreach.
In this case the share of women borrowers is calculated as the sum of all women borrowers in the portfolio divided by the sum of active borrowers in the portfolio.
Weighted averages
Weighted averages can be used in certain cases. If used it must be done accompanied by a clearly explained note on methodology.
One interesting case would be in the case of an investor with different investments in several FSPs. We could then for example calculate the share of women reached either by weighing with investment/FSP's GLP (to integrate the "level of effort" of the investor in the FSP itself) or investment in each FSP/sum of investments (to integrate the level of support for each FSP in the portfolio).

Sample: At this stage, it is generally more reasonable to collect data from a sample of investees that can conduct outcomes surveys.

Analysis of results: It is complex to understand what constitutes a good result. Setting performance targets, and comparing actual performance to targets, provides useful information. In addition, benchmarking can also provide a useful perspective, especially when specific information is available to identify peers, for example by size and maturity and region. However, it is important to remember that comparing one FSP to a peer must be nuanced by understanding internal factors too (e.g., change of leadership, transformation from a microfinance institution to a bank, introduction of a new pilot product that still requires refinement). Likewise, external factors such as political unrest, droughts, or inflation, can make it impossible for an FSP to achieve a performance target that it set before the disaster occurred. For all of these reasons, understanding results involves both analyzing the specific numbers and interpreting them given contextual factors. Furthermore, it is extremely important that FSPs do not feel hesitant to report low performance data to investors. While disappointing, low performance also provides valuable clues about what does not work and what aspects of the theory of change might need to be changed. If FSPs are using data to learn what works and what does not, and taking action to improve in weak areas, on an ongoing basis, this is the main benefit of results analysis and sign of a good investee, even if the results themselves in certain years are mixed.

Reporting/ Annual reports: Annual reports are aimed at sharing the results achieved by the investor. Based on the points above on the analysis, sharing should include important analytical work on the part of the investors.

Exit strategy

Exit strategy was not the focus of this project. However, a responsible investor plans for an exit before investing, at the origination and structuring stages. This includes deciding whom to partner with and what items must be included in a shareholders' agreement, which can sometimes alter the exit terms for existing shareholders.

At this stage, we recommend reading the recent paper on Responsible Exit Rethinking Responsible Equity Exits - SPI Online (spi-online.org).

This note provides a template to help investors navigate the complex terrain of “responsible exits” and focuses on one particularly challenging aspect of the exit process: selecting a buyer who is suitable for the investee, its staff, and ultimately its clients.

A previous paper from 2014 by CGAP and Accion explores social responsibility during equity sales and stimulates a debate on how to exit in a manner that balances the interests of investors, FSPs, and their customers.

Conclusion

This report is aimed, first, at guiding the process to define a clear and actionable theory of change at the investors' level, and second, at giving the investors the keys to guide their investees in the journey of outcomes management driven by their own theory of change.

The investors can use the lessons learned and recommendations to make theory of change and outcomes management a simple and relevant approach for themselves and for the investees to guide achievement of social and environmental goals.

The work conducted has given a good understanding of the state of the practices among FSP and stakeholders, and the cases analyzed show the actual benefits for FSP to get their social and environmental objectives strategized and integrated in the business purpose.

There is a momentum for outcomes management, there are experiences and lessons to be shared on integrating ToC and business plans, there is room to push for further, for smoother implementation of outcomes driven management.

What is the way forward on this journey?

We summarize key actions in the following table, to guide investors in the next steps.

		Convince	Organize	Support	Report	Share
Short run	**Internal**	* Influence, internally, by sharing and discussing the results of this project * Build together your business strategy and your theory of change, with joint teams * Set reasonable expectations, show how it works, the value of ToC and OM, share key messages on ESG as a risk management tool (and not just reporting), or on Client Protection requiring outcomes data to ensure that potential negative outcomes are taken into account	* Define an action plan on how to implement the recommendations of this report * Design an ESG, or preferred, SEPM committee to manage the project internally, ensure coherence within the organization * Finalize and share ToC, transitioning from a focus on sustainability to impact	* Raise awareness internally * Share ToC, indicators to be tracked and how they will be used for decision-making	* Define KPI by pillar: Simple, useful for decision making for investor	* share and discuss the results of this project internally
	With investees	* Create awareness on the driving forces and value for a clear theory of change, reasonable expectations, and solid outcomes management for decision-making. * Share the investors' expectations (what a theory of change looks like, ESG risk management, KPI/OM processes)	* Push for the same pathway (action plan, ESG / SEPM committee, clear TOC with related core outcomes indicators) * build stakeholder engagement plan	* Raise awareness with the investees (board level, workshops, TA) * Share ToC, indicators to be tracked and how they will be used for decision-making by investees	* Discuss KPI by pillar: Simple, useful for decision making at investee's level, a combination of standard and customized indicators * Start reporting with investees who already get some information (60Db projects for example)	* share and discuss the results of this project during monitoring, workshops, newsletter shared with investees, etc.
Long run	**Internal**	* Systematically link reflections on Business plan and TOC with a joint agenda, ensure the key messages on the value of ToC/OM and reasonable expectations are shared, understood, convincing for all staff (all level, new staff, etc.) with training materials, core message sent regularly on annual reports, strategic meetings, etc.	* define tools for due diligence and monitoring, build internal capacities, integrate ToC/OM in Investment committees	* Build internal capacities for staff to "live" with your ToC	* Collect and analyze core data, to guide decision-making at operational and strategic level	* share your experience internally to convince, adapt, improve, use the results * Share your experience with peers to build a sector strategy around ToC and OM
	With investees	* Help create a culture of outcomes management * Influence at investees' board level, push for ToC/OM at Board's agenda	* push for SEPM committees to manage internally ToC, regular SEPM audit, action planning, OM and reporting to Board * Link systematically ToC/BP and OM/Operations: ensure that any time an investee update its BP, MIS, operations, it is linked to the ToC and requested	* 'SEPM' lens should be used in due diligence (Does FSP have a clear E&S strategy? Does it translate into operational plan/ targets? Does FSP utilize outcomes data in business decisions?) * TA support to investees can then address the weaknesses identified during due diligence.	* Ensure, step by step, all the investees are able to define their ToC and report accordingly, with a set of standard indicators reported to the investor	* Share your experience with investees to build a sector strategy around ToC and OM

			outcomes indicators to be reported	* Ensure that any technical assistance project includes a social and environmental lens, * help build internal capacities, at least at the early stages for ToC, OM		

Based on the proposed actions on short and mid run, some tools/support can be identified:

		Convince	**Organize**	**Support**	**Report**	**Share**
Tools needed	**Internal**	PPT with key fact summary and ToC See Appendix B: Examples of ToC (investors)			List of standard indicators to draw from (on this report)	
	With investees	See Appendix A: Key messages for the business case of the theory of change See in the report: Examples of ToC (investees) Toolkit for Board members representatives including ToC, core indicators expected and how to discuss it at Board level	See ToR for SEPM Committee on SPI Online Resource center Fonkoze Haiti SPM Board committee See example of stakeholder engagement plan (Partner 1)	See Appendix C: Guidelines for Assessing What Technical Assistance to Suggest to an Investee for Strengthening Its Outcomes Management System	List of standard indicators to discuss with the investees (on this report)	

The investors can use the lessons learned and recommendations to make theory of change and outcomes management a simple and relevant approach for themselves and for the investees to guide achievement of social and environmental goals.

In particular, these lessons learned are key:

- Transition from a focus on sustainability to impact
- Focus on improvement, rather than demonstration of excellence
- Use the ToC to harmonize expectations and prioritization of activities both internally and with investees
- Understand what outcomes are possible given both the reality that many things influence customers' lives and customers have differing goals for themselves; it IS appropriate and fair however to hold the FSP accountable to short term goals - the ones it can control
- When FSP are accountable for some short-term goals, this should be discussed between the FSP and the investor, raised in the contracting agreement (indicators to report, what to do in case things are not going as expected, potential support in technical assistance or during monitoring, elements that should be discussed at the Board level, etc.)
- An FSP cannot mitigate the risk of harming customers without outcomes management.

Appendices

Appendix A: Key messages for the business case of the theory of change

- From "sustainable investment" (with ESG reporting) to "impact investment" (with outcomes reporting), a clear social and environmental strategy, with expected positive outcomes should be defined to differentiate from mainstream investors
- Triangulating different sources of information makes the Outcomes management system cost effective
    - Draw from accurate MIS data collected when meeting with clients (loans application, transactional data)
    - Use complaints mechanisms, segmenting complaints to identify negative outcomes for clients
    - Collect regularly through call center simple, rapid feedback on a sample of clients
    - Draw information gathered by field officers (qualitative)
    - Collect every 2-3 years more in-depths outcomes data with direct visits to clients
- Early warning sign for risk management in case of negative outcomes:
    - For FSP: client voice can give insights on the risks, and how to adapt products and services
    - For investors/boards: client protection is only fully implemented with a regular feedback on the clients (transparency, fair treatment, risks of over-indebtedness)
- Analytical tool to evidence contribution to impact
    - Investors: Identify assumptions to be tested during due diligence
    - FSP: define and monitor the social & environmental strategy,
    - Map linkages between intended changes and results for coherent strategy
    - Foundation to support evaluation and processes to evidence impact.
- Provide a framework to how we understand impact
    - Build common understanding and a clear roadmap across team(s).
    - Communicate intended contribution to other stakeholders
        - for investors: investment committee, Board, investors;
        - for FSP: staff, board, management, even clients.
    - A framework for outcomes management and focused reporting

Appendix B – Examples from investors

1 - Example of a Theory of change at the investor's level (SIFEM - Swiss Investment Fund for Emerging Markets)

The Swiss Investment Fund for Emerging Markets (SIFEM) focuses on strengthening local intermediaries in their capacity to deliver long-term capital to SMEs and fast-growing companies. SIFEM's role is thus both financial (provision of long-term finance) and non-financial (advice to financial intermediaries). SIFEM states that its theory of change "underpins all of SIFEM's investments."

- Desired impact: SIFEM has four strategic priorities, which it calls SIFEM Outcomes. Both of its theories of change explain how its activities contribute toward those outcomes.
    - SIFEM Outcome 1: Economic viability & resilience
    - SIFEM Outcome 2: Economic opportunities & decent jobs
    - SIFEM Outcome 3: Social inclusion
    - SIFEM Outcome 4: Climate change mitigation & adaptation
- Components of the theory of change: SIFEM defines inputs, outputs, outcomes, and impact. It further explains, "SIFEM invests primarily in funds, which in turn become shareholders in local SMEs and other fast-growing companies in different sectors. SIFEM also acts as a direct lender in investing in local financial institutions, which in turn extend loans to individual clients and local businesses. These two different business lines need to be recognized in differentiated theories of change, i.e. one for fund investments (SIFEM as an equity provider), and another for financial institutions (SIFEM as a debt provider)."[11]

Below are SIFEM's two theory-of-change graphics for its two business lines.

[11] SIFEM's Theory of Change Framework for 2021-24 retrieved from https://sifem.ch/wp-content/uploads/2024/02/SIFEM_Theory_of_Change_2021-24.pdf

Chart 2. SIFEM Theory of Change for investments in funds

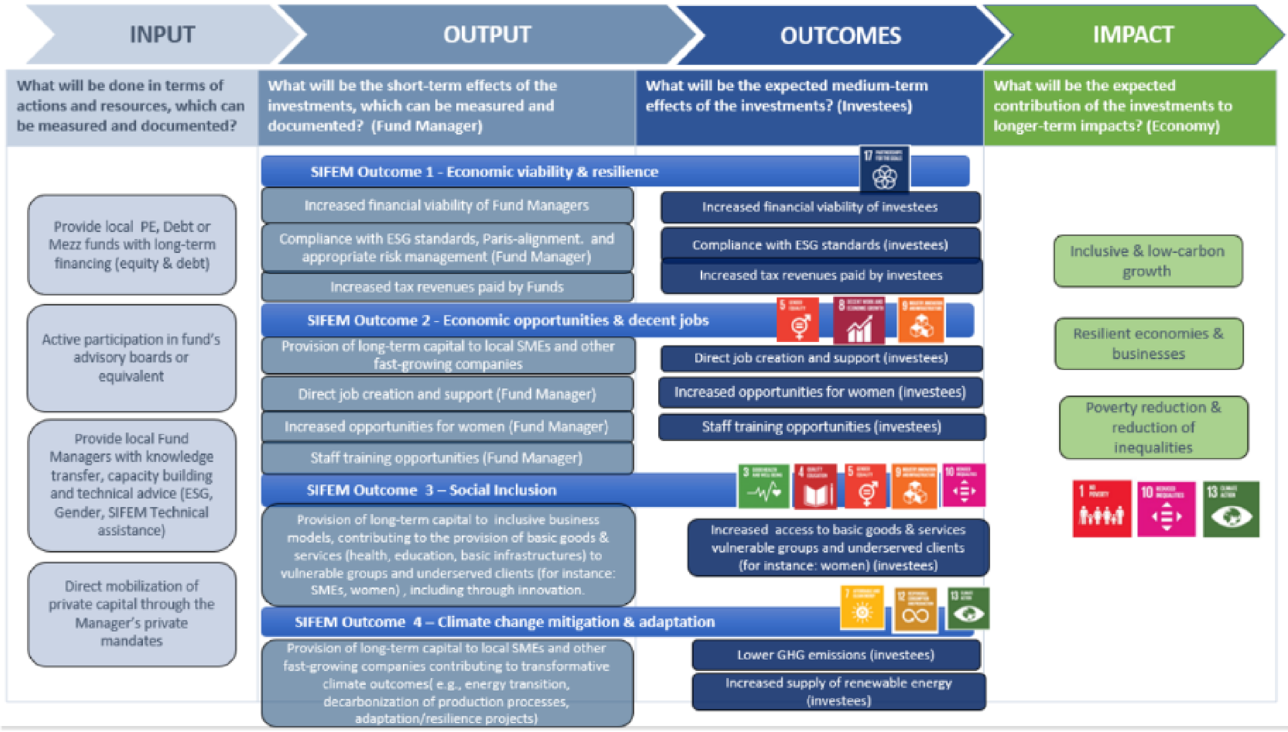


Chart 3. SIFEM Theory of Change for investments in financial institutions

2 – Example of Impact report aligned with SDG framework – Triple Jump

Example from Triple Jump, Annual Impact Report 2022 (https://triplejump.eu/wp-content/uploads/2023/07/TJ-Annual-Impact-Report-2022.pdf)

SDG	Sub-Goal	Triple Jump indicator	2022*	2021*
1 NO POVERTY	1.4 Ensure that all men and women, in particular the poor and the vulnerable, have equal rights to financial services, including microfinance.	Direct beneficiaries reached through Financial Institutions	545,250	540,000
		Average loan size to end-client (EUR)	1,093	1,058
5 GENDER EQUALITY	5.a End all forms of discrimination against all women and girls everywhere.	Women borrowers	82%	81%
	5.5 Ensure women's full and effective participation and equal opportunities for leadership at all levels of decision-making in political, economic and public life.	Women-owned SMEs	35%	36%
8 DECENT WORK AND ECONOMIC GROWTH	8.3 Promote policies that support decent job creation, entrepreneurship and the growth of MSMEs, including through access to financial services.	Jobs supported	151,628	113,985
		SMEs financed	11,955	11,267
	8.10 Strengthen the capacity of domestic financial institutions to encourage and expand access to banking, insurance and financial services for all.	Domestic investees supported with TA	237	219

Appendix C: Guidelines for Assessing What Technical Assistance to Suggest to an Investee for Strengthening Its Outcomes Management System

The critical pieces to a good outcomes management system are that the financial service provider (FSP) is collecting the data it needs, analyzing them, and using the insights from the analysis to inform business decisions. So, when an investor seeks to provide technical assistance to an investee to strengthen its outcomes management system, it should assess the current state of practice in all three of those areas and then direct the TA as needed to improve areas of weakness.

1. **Start by Assessing the Data They Already Have – conduct a data audit** (in due diligence, or to prepare technical assistance support)
    a. **Strategy for data collection and use**. Did the FSP define indicators to monitor aligned with the theory of change and impact goals? What is the data collection process (who does it, how, and when, data storage, verifying data accuracy, data analysis, reporting). Does the FSP collect data using its own staff or via an external entity? Check SPI audit results for standard 1A and 1B (outcomes strategy and data collection), dimensions 2 (oversight and decision-making by board and management), and dimension 3 (using outcomes data to inform product design).
    b. **Nature of the data**. What data, other than financial transactions data, does the FSP collect? At minimum, it is useful to collect the following information per individual customer: gender, age, location, income level. This allows for 1) understanding profile of clients, 2) segmenting analysis of all types of data (e.g., complaints, transactional behavior, outcomes).
    c. **Data sources**. Check whether the sources of information are conducive to outcomes analysis. For example, for any surveys, are the questions coherent with the theory of change? Do they have an appropriate level of details? Do they use the most updated data (e.g., PPI data)? If the FSP stores data in more than one location (e.g., there's a separate database for complaints data vs. for outcomes data vs. for financial transactions), is there a unique customer identifier that allows the FSP to merge the datasets so that it can simultaneously analyze, per customer, his/her financial behavior and other customer data? [NB: There is the caveat that if customers wish to keep data anonymous, such as certain complaints, the FSP would be correct not to track which specific customer is attached to that piece of data.]
    d. **Data quality**. Are the data accurate and complete? Do those who collect data fill in every field? Look at a sample of data to check for obvious errors such as missing data, not useful data (which can be dropped to reduce reporting burden), or nonsensical information (e.g., age is 0, income is negative 5).
    e. **Focus on outcomes**. Does the FSP gather outcomes data, or only output data? If it collects outcomes data, which data? Are the data actionable? Note that shorter-term outcomes data generally are more actionable for an FSP than longer-term data. For example, if the FSP is providing a loan to customers to buy seeds and fertilizer, short-term outcomes could be these:
        i. Did the customer purchase seeds and fertilizer?

ii. Was the customer able to purchase the quantity that s/he wanted?
iii. Did the customer encounter any difficulties with the processes either of applying for that loan or in the receipt of loan funding?
iv. Does the customer feel that access to this loan improved his/her revenue? Explain why or why not.

Longer-term outcomes, such as, "Did this client improved living standard/exit poverty?", are influenced by the customer's access to financial services but also by many other factors, and therefore those data are generally not directly actionable for an FSP.

2. **Support your investees in improving – monitoring or technical assistance**
   a. Address any problems with the quality of existing data: If data are missing or inaccurate for the data fields that the FSP already has, address those issues first. Define data protocols and train staff. Work on data collection tools and data storage processes. If it is challenging to extract data from the MIS and use it for analysis, address this problem too. For example, if key datasets cannot be analyzed jointly because the same customer has two different IDs, one per dataset, improve this system so that each customer has a unique customer ID.
   b. Define the process to report data analysis results to management so leadership can take action. Who sees the results of data analysis? In what format does the data analytics team report the data, and to whom? How should the management team of the FSP be using insights from outcomes data to inform future strategic and business decisions: design a report format, schedule, and procedure for getting the analysis to decision-makers in a timely fashion. Consider what the board should be reviewing and what management should review, as typically the board sees a smaller set of analyses that provides a summary of positive or negative outcomes, whereas management would see a more detailed and comprehensive set of analyses.
   c. Define whether the FSP should collect additional data. Consider the data the FSP already has, compared with the data it would like to have in order to know whether it is protecting customers from harm, offering products and services that correspond to customers' needs and preferences, and achieving its social or environmental performance goals. Once it has clarified what its data gaps are, then it can decide what additional data, if any, it needs to collect, and how. At minimum, however, every FSP should have some outcomes data that allow it to know which customers are better off, worse off, or the same, and some socioeconomic data that allow it to segment its data analysis, because very often different customer segments have different obstacles and preferences and therefore will have different outcomes from using the same product.
      i. **Outcomes data**. If the FSP is not collecting any data, or sufficient data, on customer outcomes, it should begin doing this. There are many possibilities. One that is both efficient and inexpensive is to add outcomes-related questions to an annual satisfaction survey. Another option is to add questions to the loan application process, to be asked of repeat customers. Or, the FSP can hire an external evaluator, such as local researchers/consultants from the SEPM Pro network or

international companies such as 60 Decibels or MFR, to administer an outcomes survey.

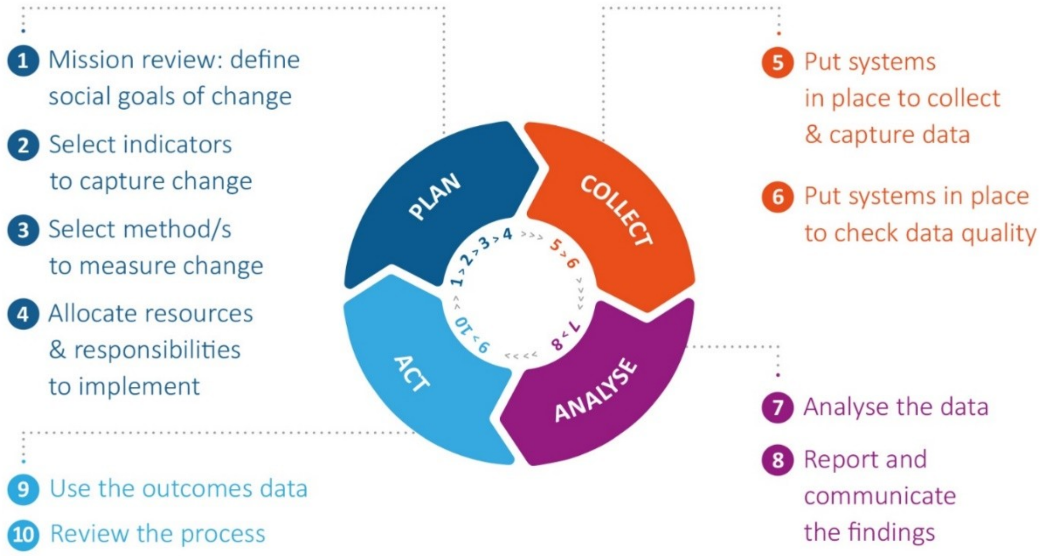
ii. **Socioeconomic data**. If certain customer segments are important to the FSP but the FSP does not yet collect those data, begin collecting it.

d. <u>Strengthen internal buy-in and capacity</u>. Training can be essential to build buy-in, which typically is easiest to do when the FSP understands how outcomes data provides insights that help the FSP mitigate customer protection risks and therefore strengthen the sustainability of the business. Training is also essential if staff will take on new functions related to data collection, verification of data accuracy, analysis, or reporting.

3. **<u>Analyze data with your investees and look for trends by segment – monitoring and use of outcomes data</u>**
   a. Once the FSP is confident that the data it stores are accurate, define the types of analysis that would be useful to the FSP and then conduct those analyses. Every FSP has a different context, so this list will not be uniform among all investees, but some common types of useful analyses are these:
   b. Analyze financial and other data by customer segment. For example, the segments for individual customer loans could be gender, age (young, middle-aged, older), location (rural, peri-urban, urban), and income level (poor / vulnerable / not vulnerable). SME lenders would require different segments, likely by sector and size. The financial activities monitored would depend on what products the FSP offers, but here are some possibilities:
      i. Average loan size
      ii. PAR
      iii. Number of outstanding loans
      iv. Number of outstanding loans per loan product
      v. Number of loans taken in the past year
      vi. Average monthly savings amount
      vii. Average number of deposits made per month
      viii. Customer dormancy (e.g., inactive for at least 1 year)
      ix. Number of policy holders of voluntary insurance
      x. Number of insurance claims filed
      xi. Number of complaints filed
      xii. Satisfaction rate
      xiii. Outcomes

      Look for trends. For example, if certain segments seem to have very different data (e.g., higher PAR, worse outcomes) than others, or if certain regions have a much higher rate of customer dormancy than others, this directs the FSP to investigate further. If the FSP does not have strong internal capacity for data analysis, it is preferable to work with an external consultant both to do the initial analysis and to train FSP staff on how to do those analyses themselves going forward. Also determine how frequently the FSP should conduct this analysis and adjust job responsibilities as needed to make sure the analysis happens at the required frequency going forward. Note that the board should be requesting outcomes data and analyzing it too, to make informed decisions, incentivize quality data, and ensure regular analysis.

Outcomes management is an ongoing process. At any given time, FSPs may be more focused on one phase or the other. The graphic below presents one way of thinking about the cycle, which has the four stages of plan, collect, analyze, and act.



Source: Guidelines on Outcomes Management for Financial Service Providers," by Frances Sinha (2016).

Appendix D: What can be expected from FSP, with potential support from investors?

- **Clarify the Theory of change/ Social and environmental strategy at the FSP level.**
  - Investees should be encouraged to have a clear and coherent theory of change or social strategy that would outline how the organization's vision and mission translates to the expected customer outcomes. The challenge in developing a clearly articulated theory of change or social + environmental strategy that can be integrated into the business strategy is often lack of internal expertise. Some support to the investees may be necessary.
  - Today, most of the intention statements do not capture environmental and climate change issues. Inclusive finance started with social focus however is still new to integrating environmental and climate change concerns into its strategy. Encouraging investees to integrate environmental dimensions more comprehensively within their strategies or Theory of change can foster a more holistic approach.
  - Build the business case internally, on the value of understanding positive and negative outcomes for the customers, to ensure reactivity and adapted products and services for the sustainability of the FSP and better impact on the customers.
- **Strengthen institutionalization and leadership for the Theory of change.**
  - The CEO should champion the process. For example, the director of one institution stated, "*We've spent thousands on financial audits. We can spend a little on impact surveys. It was very clear from our leadership that they wanted these data, and it's a way to hold our individual network members accountable. It's a tool not just for measuring but for managing our bottom line.*"
  - Leadership should develop an organizational culture that prioritizes learning at all levels and promotes a mindset aligned with the Theory of change: who do we want to reach, for what impact? As MFR noted, "What really matters is the institutional willingness to improve based on the results." And one investee said: "*[We] started very early – what is the wish from investors in terms of social goals. How is the board structured and how do we implement that into management decisions. The more we can embed those visions and those expected outcomes – the principles and norms – into our day-to-day operations, the better, because then everything else is natural.*"
  - Involve staff across all departments and seek buy-in across the organization. Integrate the Theory of change and related outcomes management into staff's daily responsibilities. Then people perceive it as important and valuable.
  - Establish structures within the organization to institutionalize outcomes management, such as board committees dedicated to monitoring social and environmental outcomes and tracking achievement of the Theory of change.
- **Push for actionability / decision-making with outcomes data.**
  - **Usefulness**. Align data collection with the criteria that UNSGSA suggests making sure the data collected are useful:
    - Nationally relevant and tested. Reflects local realities.

    - Easy to use. Simple and inexpensive measurement approaches can be applied frequently, in multiple contexts and by non-specialists.
    - Actionable. Measurement should inform decisions.
    - Comparable over time and across countries, to help in benchmarking.
- **Use data to make decisions.** FSPs should use outcomes data to verify achievement of their own targets, and to develop and improve products and services that are adapted to clients' needs. Outcomes surveys, from different sources (MIS, satisfaction, complaints, outcomes surveys, etc.) are likely to reveal that some customers had positive outcomes, some had negative outcomes, and some are about the same. All this information is valuable to the FSP.
    - **Short term/direct outcomes:** FSPs should focus on outcomes indicators that are directly influenced by an FSP's products, delivery, conduct, and practices. Monitoring these specific data is what makes outcomes information actionable.
    - **Negative effects:** It is important for the FSPs to track not just the positive outcomes, but also negative or unintended consequences. The outcomes data that are particularly actionable are the insights that reveal what is not going well. As one interviewee said, "*If a client doesn't like something or isn't happy about something, we can immediately say ok, what can we do to fix that.*" It is important to improve practice for those who have experienced negative outcomes. Even if a large majority of customers show positive outcomes, do not forget about the ones who did not. Follow up with the customers who experienced negative outcomes to see if the FSP can do something to help. *For example, the 60 Decibels Microfinance Index 2022 found that 3 in 4 clients said repayments were not a problem, while 19% said they were somewhat of a burden and 6% said they were a heavy burden. The FSP should not forget about the 6%, but instead investigate why repayments were a heavy burden and consider how to improve this.*
    - **KPI/ Standard set of indicators**: Just as in any other business strategy, key performance indicators should be identified and tracked against pre-set targets. A minimum set of standard indicators, aligned with the financial inclusion global Theory of change should be identified for each FSP. Standard set of indicators can help in benchmarking (see for example the Net Promoter Score in satisfaction surveys). The SDG also offer a common language where Financial Inclusion can play a specific role (e.g. reaching the vulnerable as stated in Target 1.4 of SDG 1). Standards questionnaires and reporting propose today a framework aligned with core SDG targets for Financial Inclusion.
- **Analyze results by customer segment.** Different segments of customers, such as women or low-income rural customers, are likely to have different risks, and may experience different outcomes. FSPs tend to find the data most actionable when they see outcomes results specific to one segment of clients, not overall institutional outcomes performance. More segmentation will help with more actionable results. Understanding and managing customer outcomes can help

organizations both strengthen their business and track achieving social goals.

- Trends in usage (e.g., percentage of active savers, uptake by products, repayment issues) are particularly interesting to study by segment, as they tend to vary across location, gender, age, and other customer characteristics.
- Segmenting by type of products and type of clients indicates where the FSP should continue to do what it is doing and where it can make adjustments in order to serve customers better. For example, some FSPs have found that segmenting data by income level reveals specific obstacles faced by the most vulnerable customers, and this helps the FSP to define a pro-poor outreach strategy.
- Though FSPs may choose to serve a broad range of customers, there are commercial benefits in segmentation and understanding what specific outcomes these customers want to achieve by using financial products and services.

- **Build a solid data collection process.**
  - **Get data from multiple sources**. Analyze complaints, satisfaction surveys, the frequency with which customers transact, which products they are using, PAR levels for loan products, and customers' tenure with the institution. *(still to be developed)*
  - **Gather qualitative data.** Quantitative information is useful but it's not enough. Looking at quantitative data from the system raises a lot of questions that it's only possible to answer with qualitative assessments. As one interviewee explained, "When we look at quantitative data from the system, it raises a lot of questions that it's only possible to answer with qualitative questions."
  - **Collect outcomes results, directly from clients. There are pros and cons to gathering data externally versus internally.**
    - <u>Collaborating with external parties</u>, such as neutral third-party assessors or surveyors that speak the local language, facilitates gathering unbiased and honest client feedback. Clients can be more comfortable sharing honest opinions with them rather than with internal staff.
    - <u>Using the internal team for data collection</u> (for example, in-person or via call centers) can be more affordable and easier to manage. Additionally, listening to its client and seeing whether they are doing well helps the institution reinforce its relationship with clients and remain in touch with the complexity of the issues it is aiming to solve.
  - **Set up regular collection.** Do outcomes surveys on an ongoing basis (some interviewees do them more frequently than others, but doing them at least every three years seems to be a good minimum)
    - Some interviewees advise ongoing monitoring of outcomes to stay informed of evolving needs and challenges.
    - However, other organizations recommend conducting outcomes surveys every other year to keep costs down and allow time for meaningful changes to occur. MIS data can complement on a regular basis what outcomes data have shown.
  - **Use the Cerise+SPTF standard questionnaire as applicable.** FSPs that do not yet collect outcomes data, and cannot afford to hire external parties to collect outcomes data, can use the standardized minimum

set of outcomes indicators that Cerise+SPTF and the e-MFP investor action group[12], are jointly developing, based on field experience and input from partners such as 60 Decibels and MFR.

- **Understand contextual differences.**
  - **Reflect on how context affects outcomes.** Recognize that outcomes may vary across different countries, customer segments, and socioeconomic backgrounds. Interpret outcomes results with context in mind. Adapt strategies and practices to suit the local context and tailor interventions accordingly.
  - **When sharing outcomes data, also provide guidance on how to interpret it.**_Do not send outcomes data to internal or external parties without also meeting with them to help interpret the data. Discuss context and provide opportunities for questions or discussion about negative results in particular.
- **Build capacities internally for Outcomes management.**
  - Invest in a team within the organization and assign responsibility for this (part of a SEPM committee for example). Product teams should be balanced, with representatives from different departments. Their different sets of skills lead to richer insights from data analysis.
  - A senior level manager should be responsible for collecting and reporting data, preferably reporting directly to the CEO.
  - Audit the MIS systems and data collection processes to guide FSP in better implementing concrete data management (identifying key data to be captured in the MIS, incentives and training of staff, data protocols)
  - Incentives for field staff to collect good quality data *(to be developed)*
  - **Digitize outcomes data collection**. Data collection, quality controls, analysis, and reporting are all easier if the FSPs collects outcome data digitally.
  - **Share with teams**. Share results regularly with teams to motivate on the positive results, aligned with the Theory of change, raise awareness on the risks/unintended negative consequences and corrective measures to be implemented, and to motivate the teams in the Theory of change and the value of Outcomes management.
- **Promote transparency and accountability for the Theory of change.**
  - Emphasize transparency and accountability by being open about both good and bad results in line with the social goals.
  - Use outcomes data to hold CEOs and management accountable for achieving positive outcomes results aligned with the Theory of change.
  - Use outcomes data to evaluate the performance of management and provide the Board of Directors with a dashboard for monitoring outcomes. In some organizations, CEOs performance is evaluated using social parameters, such as the SPI score.
  - Share outcomes data with everyone and ask them to help you interpret it.
  - Communicate with regular reporting at the FSP and investor levels on outcomes, achievements on social and environmental strategy.
- **Enhance stakeholder engagement and communication.**

[12] https://en.spi-online.org/resources/view/resources-collection-outcomes-and-sdgs

- **Invest in tools, staff capacity, and visually appealing dashboards**. This helps the consumers of outcomes data to analyze and share findings.
- **Internal communication.** Foster buy-in and understanding across the organization by involving all stakeholders and regularly communicating outcomes data. Building buy-in across the organization early would help the FSP gather outcomes data even before it becomes a regulatory requirement.

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