Evaluations as Mirrors and Co-constructors

An Empirical Investigation of a Microfinance Rating Agency and its Rating Practices from 1999–2014

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Sofia Nilsson Altafi

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To
Mamma

Foreword

This volume is the result of a research project carried out at the Department of Marketing and Strategy at the Stockholm School of Economics (SSE).

This volume is submitted as a doctor's thesis at SSE. In keeping with the policies of SSE, the author has been entirely free to conduct and present her research in the manner of her choosing as an expression of her own ideas.

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List of abbreviations and acronyms

APR	Annual percentage rate
CAR	Capital adequacy ratio
CB	Credit bureau
CEO	Chief executive officer
CGAP	Consultative Group to Assist the Poor
COO	Chief operating officer
Crore	A crore is a unit in the Indian numbering system equal to ten million, 10,000,000
EIR	Effective interest rate
FDO	Field development officer
HR	Human resource
INR	Indian rupee
JLG	Joint liability group
Lakh	A lakh is a unit in the Indian numbering system equal to one hundred thousand, 100,000
MBT	Mutual benefit trust
M-CRIL	Micro-Credit Ratings International Limited
MFI	Microfinance institution
MFO	Microfinance organization
MIR	Microfinance institutional rating
MIS	Management and information systems
NABARD	National Bank for Agriculture and Rural Development
NBFC	Non-banking financial company
NGO	Non-governmental organization
OER	Operating expense ratio
PAR	Portfolio at risk
RBI	Reserve Bank of India

RM	Regional manager
RoA	Return on assets
Rs	Indian rupee
SDI	Subsidy dependence index
SHG	Self-help group
SIDBI	Small Industries Development Bank of India
SPM	Social performance management
USD	United States dollar

Chapter 1

Introduction

Microfinance started receiving increased attention in the mid-1990s, after the World Summit for Social Development underscored the importance of improving access to credit. In 1997, a global goal of ensuring delivery of credit to 100 million of the world's poorest families by 2005 was announced at the World Micro Credit Summit, a target that was achieved well ahead of time. The year 2005 was proclaimed as the international year of microcredit by the United Nations, and, in the next year, the Nobel Committee decided to award the Peace Prize to microfinance. In 2008, microfinance was identified as one of four tools that the United Nations acknowledged as having an impact on the first Millennium Development Goal, i.e., the eradication of extreme poverty and hunger (United Nations, 2008). Over 200 million people in the world today have an outstanding microfinance loan with one of the 3,700 microfinance organizations (MFOs).[1] A majority of these people – 116 million – live on less than USD 1.25 per day and can be defined as persons living in poverty according to the World Bank's definition. Of these impoverished borrowers, 83%, or 96 million, are women (Reed, 2014).

[1] I have chosen to use the term "microfinance organization," abbreviated as "MFO," to refer to providers of microfinance and related services. Although a more common term is "microfinance institution," abbreviated to "MFI," the term "MFO" evokes an organization that can be either for-profit or nonprofit and that can offer other services in addition to the purely financial. The term "MFI" brings to mind a more narrow definition of a microfinance provider as a for-profit organization offering financial services only.

As microfinance has come to be recognized as an effective and efficient poverty alleviation tool, the availability of funds has increased, and this in turn has further bolstered the perception of microfinance's efficacy (Romani and Lerpold, 2010). As a result, during the last two decades, microfinance sectors have developed in many countries around the world and attracted ever-increasing sums of public and private investment money. In 2010, it was estimated that MFOs had assets amounting to USD 68 billion. Of this, USD 13 billion was foreign capital from development finance institutions, institutional investors, and individual investors (Reille, Forster, and Rosas, 2011).

The hopes for the future of microfinance are also high; during the Microfinance Investor Roundtable in Washington, D.C. in 2006, McKinsey & Company estimated that there were an additional 1.5 billion potential microfinance clients in the world (Swanson, 2007; Swibel, 2007). Seen from the point of view of the volume of capital needed, the International Association of Microfinance Investors estimates that an additional USD 270 billion is needed to tap into this unmet demand (Trant, 2010), and in 2007 the research department of Deutsche Bank estimated the funding gap to be USD 250 billion (Dieckmann, 2007).

As microfinance has developed into a new type of parallel financial market offering financial retail services primarily to poor women in developing countries, there has also been an emerging need to assess and evaluate MFOs. In mainstream financial markets, credit ratings conducted by credit rating agencies represent one of the longest-standing and most recognized external evaluation practices. The credit rating industry dates back 100 years to the first publication of Moody's pioneering bond books (Sylla, 2002). Rating agencies aim to provide public information about the default risk of a debtor, or of a debt instrument, in the form of a rating grade. In recent years, credit ratings have received harsh criticism for their role in financial crises such as the 1997 Asian financial crisis (Duff and Einig, 2007), the failure of Enron in 2001, and the 2007-2009 subprime mortgage crisis (Neate, 2011; Bolton, Freixas, and Shapiro, 2012). At the same time, with the adoption of the Basel framework, which ties bank capital requirements to credit ratings, the importance of credit rating agencies and their

evaluations has increased, and they continue to be central actors in most financial markets (Darbellay and Partnoy, 2012).

Ratings of MFOs have also become increasingly sought-after and taken for granted aspects of microfinance markets; by 2012, over 2,350 microfinance ratings had been completed around the world (Abrams, 2012).[2] However, evaluations of MFOs differ in several important regards from evaluations in mainstream financial markets. To illustrate some of the unique particularities of evaluating MFOs, I will provide an example from another type of evaluation, namely the "Microfinance India Awards," which, in 2012, was given to Cashpor along with the following statement from the jury:

> "This Award is in recognition of Cashpor Micro Credit's sustained efforts in reaching the poorest in a difficult underserved region and achieving double bottom line performance with undiluted commitment to alleviating poverty in India. Cashpor is a leader in incorporating principles of responsible finance and social performance management in its business practice and has demonstrated successfully that working with below poverty line households in rural areas too can be a financially viable and operationally scalable model" (Microfinance India, 2012).

The above quote illustrates how the boundaries of microfinance are drawn between various conflicting and inherently paradoxical demands and expectations, among which the most notable is that of having a social calling on the one hand and being financially sound on the other (Battilana and Lee, 2014). Microfinance is a relatively novel phenomenon, charged with the challenging task of helping the world's poorest and most disadvantaged people move out of poverty through self-help and entrepreneurship. At the same time, these organizations are expected to demonstrate organizational efficiency, economies of scale, and attractive financial outcomes. The microfinance project thus rests on two inherently contradictory goals: to do good and to do well. There are many areas that may involve difficult balancing acts for the evaluator when assessing MFOs, such as how to assess

[2] This figure only refers to so-called "microfinance ratings" conducted by the four specialized microfinance rating agencies MicroRate, M-CRIL, Planet Rating and MicroFinanza Rating (see Chapter 2 and Chapter 6), and excludes all ratings conducted by any of the mainstream corporate rating agencies.

increased efficiencies in light of targeting the poorest clients, how to assess expansion plans while maintaining close relations with communities, and how to assess raised loan fees in light of high payment burdens on poor women. In this light, rating MFOs should in many ways involve more complexities than those related to determining the grade of financial instruments in more homogenous and established settings.

Microfinance ratings are important as they provide information for those who seek to invest in MFOs. They, however, also provide MFOs with important information about how they should structure themselves and behave in order to be "proper," "right," and "good" organizations. For MFOs, this is not always straightforward, given the duality of expectations described above. Consider, for instance, the attempt of the Indian MFO SKS Microfinance to list on the Bombay Stock Exchange. For a financial institution, this would be a perfectly natural step in order to secure access to funds in an expansion phase. Yet the listing of SKS Microfinance in 2010 spurred an upsurge in criticism from various parties towards commercialized microfinance as a whole, eventually leading to SKS Microfinance lowering its interest rates (Mader, 2013).

All organizations have a basic need of being valued by their environment. Organizations that are valued in their social context are also perceived to be legitimate actors. Put differently, a legitimate organization is one whose existence, structures, and deeds are deemed to be proper and desirable by society at large. Such organizations are also in a better position to attract needed resources and enhance their survival prospects (Suchman, 1995). However, how organizations are to be valued is almost never clearly delineated. Instead, it is left to the individual organization to infer this based on feedback from its environment (Meyer and Scott, 1983; Meyer and Rowan, 1977). MFOs interpret what is expected of them, how to organize their activities, what characteristics to incorporate, and what outcomes to deliver by reading different signals such as media reporting and direct contact with clients and investors. Of particular importance are signals from those in their environment that are widely recognized as reviewers of MFOs (Zuckerman, 1999).

Although external evaluation systems such as microfinance ratings and awards are not engaged in and do not take action responsibility for the mi-

crofinance project, they contribute to rendering visible ideas of what constitutes "good microfinance." By giving their views on, expectations of, and hopes for microfinance, evaluators such as these project idealized images of microfinance and of MFOs. Evaluation systems include some organizations and exclude others, they draw attention to specific organizational features that they consider valid and appropriate while ignoring or criticizing others, and they endorse certain organizational outcomes while rejecting others. In this way, accounts and assessments by significant evaluators indirectly work as normative guidance for organizations, signaling a set of criteria and ideals for how they expect organizations to act, which goals to pursue, and how to structure themselves. When such idealized images are disseminated in the sector via rating reports and awards, these images become visible for and usable by organizations. Organizations that are successful in reflecting idealized images as projected by significant evaluators are also assumed to be more legitimate than others.

While the extant literature on external evaluations of organizations accounts for effects such as reactivity (Sauder and Espeland, 2009; Espeland and Sauder, 2007), this literature is limited by its assumptions of stability over time in evaluative practices and in the idealized images projected through these. An interesting question to ask is how the idealized images as projected in microfinance ratings unfold over time as the field undergoes change and transformation. It is also likely to be assumed that the specific vantage point and market position of the evaluator play a role in changes to evaluative practices and in the idealized image.

Some evaluators and the images that they project are more salient and visible and have a greater effect on the legitimacy of organizations than do others. Just as MFOs are assumed to attempt to reflect expectations from their environment in order to be perceived as legitimate actors, earlier studies have suggested that evaluators also grapple with the challenge of reflecting external demands and expectations. This means that raters constantly seek to understand and interpret what is expected of them and their evaluative practices, what type of organization is worthy of a certain rating grade, and what the recommendations should be. Should the evaluator's verdict deviate too much from societal views, the evaluation may be seen as imbalanced and unreasonable, and the evaluator risks losing legitimacy. Earlier

assumptions have thus mainly been that evaluators function as passive messengers of societal expectations and demands, assembling these into legitimate idealized images (Ruef and Scott, 1998; Bitektine, 2011).

It is, however, likely that some idealized images codified by evaluators are more than mere reflections of broader societal expectations. It is, for example, plausible to ask whether evaluators function as a type of selective sieve by cognitively taking in, digesting, sorting out, and prioritizing among expectations and demands in complex organizational environments. Taking this reasoning one step further, certain external evaluators may even see it as their role to put forward idealized images that radically differ from broadly held ideas, beliefs and prescriptions about organizations, thus playing an active role in the construction of an idealized image as opposed to solely reflecting societal expectations and demands. Such reasoning implies that certain evaluators not only render visible a legitimate image, but that they also deliberately aim to create new or alter existing expectations and demands on organizations, thereby guiding the development of the field.

In this light, I here aim at investigating how rating practices are constructed and work. By studying, over time, the evaluative practices of a significant rating agency, and specifically the idealized organizational images – or templates – that it projects in the complex and rapidly changing context of microfinance, I seek to contribute to the understanding of how such practices are constructed and change. I further want to shed light on how codified templates correspond to trends and events in the microfinance sector, as well as how changes in the same can be related to the situated vantage point and market position, as well as the perceived role of the rater. My research aim will be reached through the exploration of the following two broad questions, the first of which will be divided into three separate and more manageable sub-questions as the study evolves:

Question 1: How do rating practices and the templates projected through these change over time?

Question 2: How do changes in rating practices and in the templates projected through these relate to trends and events in the sector, as well as to the rater's market position?

My focus is neither on the level of the acting organization, nor on the level of the organizational environment and society at large, but rather on an intermediary level where evaluative activities take place. By studying, over time, the templates produced by one significant evaluator in a sector characterized by ambiguity, complexity and transformation, I will be well positioned to understand how rating practices are constructed and work. I will also be able to provide an account of how changes in rating practices relate to their context.

In doing so, the study will add to the growing stream of literature on evaluators and evaluative practices. I also contribute to the relatively few earlier qualitative studies on microfinance ratings. Addressing gaps in the literature that explores evaluative practices and change, I investigate empirically how a significant evaluator reflects, as well as constructs, templates for organizations in the field of Indian microfinance. I also relate changes in rating practices and in the encoded template to the macro and meso contexts in which they are embedded. The empirical focus is not, however, on the effects and impacts of such evaluative processes and the projection of idealized images, but rather on the content of and changes in such idealized images.

Research strategy and empirical setting

To investigate the role of an evaluator and its evaluative practices in the creation of a template to guide organizations in the field, a single case study has been conducted of the specialized microfinance rating agency Micro-Credit Ratings International Limited (M-CRIL). M-CRIL is a global pioneer in the field of microfinance ratings: it was the first agency to conduct social ratings, the first agency to conduct microfinance ratings in India, and the only rating agency in India that specializes in rating MFOs. The agency started off as the sole rater in the Indian microfinance space, although over time, corporate rating agencies moved in and threatened the market position of M-CRIL.

Microfinance rating reports constitute fruitful empirical material for capturing idealized images of MFOs. To capture the codified template, I have used 57 microfinance rating reports produced by M-CRIL that span

15 years, from 1999 to 2014. Microfinance ratings are assessments of organizations as a whole, and not of a single financial instrument. This means that raters evaluate the MFO's legal form, governance model, internal systems and processes, performance, and future direction. Rating reports also reflect how organizational features are understood in terms of how different organizational aspects are categorized in the reports. Not only do rating reports provide rich organizational representations, but in doing so, they reveal which organizational aspects the raters consider to be relevant to include in a rating report, emphasizing some parts while leaving out those organizational features that are thought of as irrelevant, unnecessary, taken for granted, or impossible to evaluate. Capturing the codified template has thus also involved assessing the gaps, i.e., what aspects that have been left out of the rating exercise.

Apart from descriptive passages, rating reports also include implicit and explicit normative and prescriptive components, that is, the rater's judgments as well as articulated recommendations. Rating reports point out what the rater perceives as organizational flaws and strengths, along with comparisons of the rated organization to its perceived peers, as well as with other standards employed. Ratings also involve the distillation, or commensuration, of various organizational aspects into a single letter on a quality scale. Factors such as these make rating reports ideal for investigating the template and how this has changed as the Indian microfinance sector has evolved.

With the help of NVivo, the 57 sample reports were organized and analyzed. First, I identified changes in the actual structuring of the text, including categories, headings, indicators, and illustrations. The texts were thereafter categorized longitudinally along the broad and theoretically grounded organizational elements of structures, procedures, social outcomes, and financial outcomes. Finally, I coded a select sample of reports by descriptive and normative text to capture changes in the strength of ratings.

Although these texts represent the locus of my inquiry, they cannot be understood in isolation from their context. Taking the analysis up one more level, there is a need to explore how changes in evaluative practices relate to M-CRIL's position within the field, as well as how they correspond to sec-

toral transformation processes and shifts. To paint a broader picture of M-CRIL's role and position in the Indian microfinance field, as well as in relation to the other rating agencies, I conducted a small but comprehensive market mapping of ratings in the Indian microfinance sector from 1999-2014 and reviewed documents and reports produced by M-CRIL. I also conducted a limited number of semi-structured interviews with M-CRIL and other key players in the Indian microfinance field between the years 2011-2013. Based on a review of secondary data such as government documents and sectoral reports, I made a retrospective study of the developments in the Indian microfinance sector, including the main trends and jolts. During the research process, I alternated between the different levels and studied developments and occurrences at the micro, meso, and macro levels in parallel in order to relate and make sense of the rating reports.

Organization of the dissertation

This dissertation is organized as follows. In the next chapter, I introduce more in-depth the empirical phenomenon of microfinance ratings and the specialized microfinance rating agency M-CRIL. I also describe the first specific sub-question. In Chapter 3, I first present extant research on evaluations and thereafter build a theoretical model for investigating the organizational template. I also introduce two theoretically derived sub-questions. In Chapter 4, I discuss the research methodology and design employed to operationalize the research questions. Chapter 5 has been divided into two main parts. In the first part, I present the empirical data, including changes in M-CRIL's rating instrument, how different organizational elements have been evaluated over time, and changes in descriptive and normative text. In the second part of the chapter, I provide an analysis of the empirical investigations and present the main findings thereof. In Chapter 6, I attempt to contextualize changes in evaluative practices and in the template, as well as discuss how such changes relate to macro and meso level factors. In Chapter 7, I conclude the dissertation by summarizing the findings and discussing their implications.

Chapter 2

Microfinance ratings and M-CRIL

Microfinance markets

Microfinance services – as opposed to financial services in general – are commonly defined as a broad range of retail financial services, such as loans, deposits, payment services, money transfers, and insurance, to poor and low-income people and their microenterprises by both formal and semiformal institutions. Further, microfinance is intended for those groups of society that for various reasons remain outside the mainstream banking system. Many providers of microfinance also offer non-financial services such as training and welfare services. Unlike conventional bank loans, microcredit is often extended to groups of largely female borrowers who, instead of supplying conventional collateral, guarantee the loan jointly, rendering social capital critical to the success of many microfinance programs (Lerpold, 2012).[3]

As empirically demonstrated (Khavul, Chavez, and Bruton, 2013) and conceptually argued (Kent and Dacin, 2013), microfinance sectors are complex settings that encompass numerous competing expectations and demands. Most early providers of microfinance around the globe were nongovernmental organizations, operating on a nonprofit basis and often offering subsidized interest rates covered by soft loans and donations. Although

[3] Although group-based loans are common in the microfinance sector, an increasing number of microfinance loans also go to individuals.

microfinance to a large extent grew from social roots, since the 1990s there has been a growing number of commercially oriented and operated microfinance organizations (MFOs), indicating a movement away from a dependency on donations, grants, and subsidies towards an arena where or-organizations increasingly focus on selling services/products, generating positive financial results for investors, and operating on market terms (Drake and Rhyne, 2002). Many of the newly established MFOs have started their operations using a for-profit model, and many nonprofit MFOs are transferring or transforming their microfinance activities into for-profit businesses and in many cases, regulated financial institutions. Private capital first began entering the microfinance space about a decade ago, but it was not until Mexican MFO Compartamos generated USD 458 million through an initial public offering in 2007 that investors saw the real potential in microfinance (MacFarquhar, 2010). Commercially oriented, as opposed to socially driven, investors bought most of the shares. The Compartamos case raised issues regarding whether the sizable profits and high interest rates upon which such organizations were built were defensible in light of such organizations' stated social missions (Rosenberg, 2007). Throughout the transformation process, critical voices have argued against this approach, fearing that it leads to mission drift and exploitation of the poor (Augsburg and Fouillet, 2013).

The sector's proven potential for economies of scale has resulted in a small group of very large and structurally relatively homogeneous organizations. Today, banks and financial companies make up 39% of the organizations in the space and serve 60% of all clients, non-governmental organizations make up 36% of the organizations and serve 35% of clients, and credit unions and rural banks make up 25% of the organizations and serve the remaining 5% of the clients (Rhyne, 2010). Microfinance has grown exceptionally during the last decade; at the end of 2012, over 3,700 MFOs reported data to the annual State of the Microcredit Summit Campaign. In 2010, it was estimated that MFOs had assets amounting to USD 68 billion (Reille et al., 2011). In many parts of the world, microfinance sec-

tors have developed into parallel semi-formalized financial markets that supply financial and related services to poor and unbanked people.[4]

Microfinance sectors as mediated markets

As in mainstream financial markets – where a few state-authorized credit rating agencies have a considerable impact on money flows – rating agencies and ratings have gradually become commonplace aspects of most emerging microfinance markets. Markets wherein third parties such as rating agencies act as significant critics, and whose evaluations confer legitimacy on actors and objects have been referred to as "mediated markets." In mediated markets, intermediaries play a central role in indirectly organizing transactions and directing the flow of resources (Zuckerman, 1999). Zuckerman (1999) strategically chose a mainstream financial market to typify a mediated market since securities analysts, as opposed to solely end customers, exercise a great deal of control and power by reviewing and certifying products in such markets. As discussed below, similarly to a mainstream financial market, microfinance sectors are also partly mediated, not as much by securities analysts but by rating agencies that contribute to the shaping of patterns in the sector, both symbolically and in material ways. Despite the fact that rating agencies themselves do not take part in the flow of exchange, they make credit recommendations and disseminate rating grades that influence how funds should be directed.

MFOs are mainly funded via bank debt, member savings, grants, equity and retained earnings. Ratings are typically relevant during the capital allocation process to MFOs via, e.g., bulk lending from banks. To impart a clearer understanding of this process, I use an illustrative example from Ananth (2005, p. 4). If an MFO estimates a loan requirement of, for example, USD 250,000 for its target constituency, it approaches a bank for that amount. The bank views it as a loan being extended "to the MFO," i.e., as organization-based lending, not finance for the underlying pool of borrowers, i.e., asset-based lending. Accordingly, pricing is a function of the rating of the MFO, and the bank typically allocates capital in keeping with the rat-

[4] An unbanked person is someone who does not have his/her own bank account.

ing obtained by the MFO, e.g., in the form of a microfinance rating. Notably, when the MFO on-lends the USD 250,000 to its clients, it further allocates capital against this portfolio to take care of unexpected losses on this portfolio and to satisfy capital adequacy norms under which it may be operating. This results in a double counting of capital requirements for that particular portfolio of microloans, once by the bank and again by the MFO, which is also reflected in the final pricing.

Significant international microfinance supporters have played key roles in the promotion of tailor-made ratings for the microfinance sector, i.e., microfinance ratings and social ratings. Mainly catalyzed by global donors such as the Ford Foundation and the Inter-American Development Bank, four specialized microfinance rating agencies came into being during the early years of 1997-2001: MicroRate, Micro-Credit Ratings International Limited (M-CRIL), Planet Rating and MicroFinanza Rating. These four specialized microfinance rating agencies are present in most microfinance markets around the globe, and together they have undertaken a large share of the world's MFO-specific ratings.

Broadly, there are three rather different types of rating products available for MFOs: microfinance ratings; social ratings; and mainstream credit ratings. Microfinance ratings, which constitute the core rating product of the specialized rating agencies and which is also the focus of my dissertation, are comprehensive assessments of the organization in its entirety. The Rating Initiative gives the following description of this type of assessment:

> "[Microfinance] ratings not only measure the MFI's creditworthiness, but also its trustworthiness and excellence in microfinance. They incorporate features of a credit rating but also include a deeper level of analysis in order to evaluate the institution´s effectiveness in reaching micro entrepreneurs with high quality loans. A [microfinance] rating is typically an integral assessment of the MFI's global performance (strengths and weaknesses), which can be assigned a rating or grade according to the evaluator's own scale" (The Rating Initiative, n.d.).

By 2012, over 2,350 microfinance ratings had been completed by the four specialized rating agencies (Abrams, 2012). Many mainstream credit rating agencies have also introduced a similar product, which they refer to as "microfinance gradings." For simplicity, I employ the term "microfinance rat-

ing" in this dissertation to refer to this type of comprehensive organizational assessment, although other names exist, e.g., "performance ratings," "global risk assessments," "institutional ratings," and "microfinance gradings."

Another type of rating is social ratings, which aim at evaluating both the MFO's social risk and its social performance, where the former refers to the risk of not achieving the stated social mission, while the latter refers to the likelihood of contributing social value. The Rating Initiative elaborates further:

> "…what a social rating can achieve is an analysis of the steps towards achieving impact: the processes undertaken by an MFI toward its desired goals, and the results, to the extent of analysing outreach and quality of services provided" (The Rating Initiative, n.d.).

The demand for social ratings have been small in comparison with microfinance ratings; between 2008 and 2013, a total of 416 social ratings had been undertaken by the four specialized rating agencies (The Rating Initiative, 2013).[5] Apart from social ratings, a number of initiatives have been launched to assess and audit the social impact of MFOs, e.g., the CERISE Social Performance Indicators and Moody's Social Performance Assessment.

In more recent years, advanced financial market instruments such as securitizations of portfolios, structured-debt instruments, portfolio buyouts and even bond issues are some of the liability products that have been under development for MFOs. These conventional financial market instruments do not commonly undergo ratings by the specialized microfinance raters, which lack state accreditation,[6] but rather by mainstream credit rating agencies. These ratings, referred to as "credit ratings," differ in many important ways from microfinance ratings.

[5] This figure refers to the number of social ratings conducted until September 2013. The social ratings conducted by M-CRIL that are included in this figure are from 2011 to September 2013.

[6] In 2007, Micro Finanza Rating was licensed by the Ecuadorian banking and insurance regulator, thereby becoming the only specialized rating agency that is authorized by a regulatory body (Kirchstein, 2011). In 2014, the agency was also authorized by the regulator in Bolivia (Micro Finanza Rating, n.d.).

A credit rating is a focused assessment of the creditworthiness of a borrower with respect to a particular instrument. In mainstream financial markets, credit ratings are, through regulation, necessary for accessing capital, and they influence the price of funding for many companies (Farrington, 2005, p. 1).[7] While microfinance ratings are not automatically used publicly, credit ratings are made publicly available, and the credit rating agency monitors the instrument and makes adjustments when necessary. During this process, the rating agency has privileged access to private information sources of the issuer (Duff and Einig, 2009). Another differentiating factor between microfinance ratings and credit ratings are in the benchmarks used; microfinance ratings claim to compare MFOs with each other, whereas credit ratings claim to compare MFOs with other mainstream financial institutions (Farrington, 2005; interview with Ravi Kumar Dasari, 12 November 2011).

Global players have also promoted the funding of rating exercises of MFOs through the establishment of rating funds. In 2001, the Inter-American Development Bank and the Consultative Group to Assist the Poor (CGAP) established a subsidy fund for external ratings of MFOs, the Microfinance Rating and Assessment Fund, also known as Rating Fund I. The European Union later joined as a core supporter of the fund. From its inception till 2008, Rating Fund I co-financed a total of 423 ratings until it was finally closed as planned. Following the closing of the initial fund, Rating Fund II was set up in 2009 by the Inter-American Development Bank and the Andean Development Corporation and financed by the Multilateral Investment Fund. The second fund had as its main focus the goal of strengthening the rating market in Latin America and the Caribbean. Rating Fund II closed in 2012 after having co-financed 82 ratings (Rating Fund II,

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[7] The credit rating industry dates back 100 years to the initial publication of Moody's pioneering bond books. States regulate credit rating agencies via national financial market regulatory frameworks. Despite harsh criticisms of the role that credit rating agencies have played in global financial markets, the reliance on such agencies has grown, and credit rating agencies have become increasingly important. This reliance was reinforced with the adoption of the "standardized approach" developed by Basel II, in which credit rating agencies are used to determine risk weights for capital requirement. Globally, the credit rating sector is characterized by an oligopolistic structure dominated by a few large players, with Moody's, Standard & Poor's and Fitch making up the core (Duff and Einig, 2009). The business model for credit rating agencies changed in the 1970s, when they moved from being paid by the investor to being paid by the debt issuer (Jeon and Lovo, 2013; Smith and Walter, 2001).

n.d.). The Rating Initiative was launched in 2008 by Luxembourg-based Appui au Développement Autonome and others and focused on African MFOs. The fund terminated its co-funding mechanism by the end of 2011. During this period, based on the reports made available on the fund's website, a total of 273 ratings were co-funded and publicly disclosed (The Rating Initiative, n.d.).

Another agency that indirectly has promoted ratings and, more generally, has worked to foster transparency and standardization is MIX Market, the largest publicly available microfinance database. MIX Market does not finance rating exercises, but it encourages MFOs to disclose a wide spectrum of data of which ratings make up an important component. The level of transparency for each organization is indicated through MIX Market's "diamond system," and the maximum score of five diamonds is reserved for rated MFOs that have uploaded their rating reports to the Internet. Although microfinance ratings are not automatically made available to the public, the above initiatives have aimed to promote transparency and raise awareness of microfinance ratings by making them available to the public via their open-access online databases.

Indian microfinance: A mediated market under transformation

A country with an exceptionally big, fast growing, and long standing microfinance sector is India. Indian microfinance has evolved into a popularly used instrument expected to help break the vicious "cycle of poverty" for the country's 827 million poor (Chen and Ravallion, 2008). Indian microfinance has, over a period of time, undergone a substantial transformation process characterized by unpredictability and contestation. It is also a sector wherein ratings and rating agencies have come to play an important role. Factors such as these render the Indian microfinance sector particularly suitable for empirically investigating evaluative practices in a rapidly changing and uncertain environment.

As I elaborate on with much detail in Chapter 6, the Indian microfinance project emerged from a historical context of state intervention and

subsidies in banking, an expansive cooperative movement, and well-recognized problems connected to rural indebtedness and impoverishment. In this light, the expectations for microfinance in India stretched far beyond those of a simple financial inclusion agenda to encompass broader issues of women's empowerment, rural development, and a rectification of past and present social and economic injustices. Although the legacy of the Indian microfinance sector has social roots, recent years have given rise to an aggressive yet highly contested commercialization process.

Adding to the confusion, formal, specific rules governing microfinance have until recently been lacking, and it has largely been up to the individual MFO to dictate the conditions, leaving the sector to evolve in a regulatory void. Instead of formal regulation, a few national and regional meta-associations have produced codes of conduct for MFOs to adhere to, and norms produced by global microfinance initiatives, aiming at standardizing, increasing transparency, and protecting clients, have been introduced. The precarious loan situation has remained off the regulatory radar; the group constellations are not registered entities; the rate of interest is set by the MFO; and centralized credit bureaus are just now evolving, making it difficult to control for over-lending or client indebtedness. These factors imply that the relationship between the individual client and the MFO oftentimes has been a balancing act between financial goals, social impact, and reaching scale in operations.

Although microfinance in India has been described as the silver bullet for poverty alleviation and women's empowerment, the sector has experienced several crises. On numerous occasions, media has reported on characteristics and events including antagonistic encounters between microfinance clients and MFOs, harsh competition, an over-supply of credit, callous collection practices, and avaricious executives and owners.

Further, in the Indian context, it is possible to conduct microfinance activities under several legal models. This has led to fragmentation in the sector, although a few huge, commercially driven and regulated MFOs manage a large portion of the portfolio, while there are numerous unregulated nonprofit MFOs with limited client bases. The flow of funds to the sector has also shifted over the years, moving from donations and grants toward more commercially oriented money and even an initial public offer-

ing. To conclude, the Indian microfinance sector exhibits heterogeneity and fragmentation; it evinces diverse performance standards and lacks formal rules; and uncertainty persists about where the lines of responsibility should be drawn. While the sector has undergone tremendous growth, a series of crises has shook the sector and resulted in declining repayment rates and harsh criticism.

M-CRIL: India's only specialized rating agency

In 1998, Micro-Credit Ratings International Limited, referred to as M-CRIL, carried out the first rating in the Indian microfinance sector. Since then, M-CRIL has been the only rating agency in India that specializes in microfinance. The agency was started as a spin-off from its parent organization EDA Rural Systems Private Limited, which, in the 1990s, developed a consultancy focused on livelihood and enterprise support, as well as on the emerging field of microfinance. M-CRIL and EDA are co-founded and owned by the British-Indian couple Sanjay Sinha and Frances Sinha. Sanjay Sinha is the managing director of M-CRIL and the executive director of EDA, and Frances Sinha is the managing director of EDA and a member of the board of M-CRIL. Since its inception, the company has been able to attract some of the most eminent Indian and international microfinance experts to its board. In 2007, M-CRIL had a team of 14 rating analysts, a majority of whom had a background in economics (Chetan, Sinha, and Khan, 2003; M-CRIL, 2008; interview with Sanjay Sinha, 12 October 2011).

Apart from ratings, M-CRIL offers research services, including policy reports for donor organizations and financial regulators, as well as sector studies and reviews. One such publication is the *M-CRIL Microfinance Review*, which is an analysis of the Indian microfinance sector and industry averages of key performance indicators. The agency also manages one of the most comprehensive data sets of Indian MFOs, and many publications on Indian microfinance are based on data collected by M-CRIL, e.g., the annual *State of the Sector Reports*. The only agency that comes close to having initiatives of similar scope is Credit Rating Information Services of India Limited (CRISIL), which has produced two well-circulated reports about

Indian MFOs over the years: *India Top 50 Microfinance Institutions*, from 2009, and *India's 25 Leading MFIs*, from 2014.

Both M-CRIL and EDA engage in microfinance advocacy on a national and global level through, for example, the United Nations Advisors Group on Inclusive Financial Sectors and the International Social Performance Task Force. M-CRIL's executive director, Sanjay Sinha, is also an author of numerous articles on microfinance and ratings and has been published in leading national papers such as the Indian daily *The Economic Times* (Sinha, 2007a; Sinha, 2007b; Sinha, 2008b).

Although M-CRIL has a clear Indian focus, in 2008, it had conducted ratings in 32 countries in Asia, Europe and Africa, and in 2007, it was estimated that M-CRIL controlled 38% of the entire Asian microfinance rating market (Appui au Développement Autonome, 2008). By September 2011, M-CRIL had undertaken over 1,100 microfinance ratings (M-CRIL, 2012).

M-CRIL's microfinance rating instrument

M-CRIL's microfinance rating, which is the agency's core rating product, takes a broad look at the MFO and aims at capturing not only the creditworthiness of the organization but also the strengths and weaknesses in the provision of financial services to low-income clients. Various dimensions or aspects of the rated organization are assessed and compared against preset standards and ideals. Qualitative dimensions or aspects are translated into a grade. The results of these processes are given different weightages, which thereafter are consolidated into a final rating grade. This grade reflects all the dimensions or aspects that the rating instrument deems important and that M-CRIL sees it as possible to capture.

The rating process of M-CRIL is described as thorough, with intensive field-level exchanges and communication. The rating exercises are typically based on a visit by a team of at least two analysts to the MFO. All rating reports pass through a rating committee before being formally approved (interview with Alok Misra, 30 April 2012). The assigned rating is thereafter valid for one year.

As has been touched upon above, the Indian microfinance sector has undergone a rather dramatic transformation process over the last two dec-

ades, with massive growth, commercialization, and numerous crises. Looking at M-CRIL's description of its microfinance rating instrument, the agency also seems to have revised its approach over the years. In 2003, M-CRIL described its microfinance rating as follows:

> "The M-CRIL rating evaluates the strengths and weaknesses of the operations of the financial service provider to low-income clients – bank or MFI – as well as its creditworthiness. It assesses the risks associated with lending to the organization and assigns a grade based on the extent of risk. Some categories of risk that form the basis of the assessment are external risk, credit risk, market risk and the risk of fraud. With reference to these, the critical aspects covered are – the quality of governance, the depth and efficacy of management systems and the financial health of the institution" (M-CRIL, 2004, p. iv).

One decade later, in 2013, M-CRIL elaborates on its core rating product:

> "In addition to the risk aspects covered in a traditional Financial Rating, [the Microfinance Institutional Rating] also includes the principles of client protection, the alignment of practices with stated social goals, and responsible financial performance, thus providing a holistic opinion on the long term sustainability and creditworthiness of Microfinance Institutions. Integration of key social issues into the rating framework also addresses public policy concerns on institutional practices in lending to the poor" (M-CRIL, 2013).

The above quotes indicate that M-CRIL over the years has made some changes to its main rating product. In an initial attempt at approaching my first broad research question – *How do rating practices and the templates projected through these change over time? (Question 1)* – I have articulated the following empirically-oriented sub-question:

> **Question 1a:** How does the microfinance rating instrument change over time in terms of factors such as rating categories and sub-categories, indicators, and weightages?[8]

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[8] Although this study is situated in the management field, it is worth noting that a growing, albeit still small, stream of studies based in quantitative traditions within the fields of economics and finance have been motivated by the empirical phenomenon of microfinance ratings. Previous studies have attempted to

capture the impact of microfinance ratings on the sector and found that some, but not all, rating agencies and their ratings have an impact. Hartarska and Nadolnyak (2008) looked at ratings conducted of MFOs by specialized microfinance rating agencies and found that funders such as banks and investors consider rating reports in their funding decisions, thus suggesting that ratings impose market discipline and help MFOs attract money. Another study by Garmaise and Natividad (2010) suggests that ratings do not have any impact on the amount of funds available, but that they reduce the cost of funds. Another group of studies have taken an interest in the relationships between assigned ratings and MFO size, profitability, risk, efficiency, solvency, and social performance. Results indicate that size, profitability, and productivity are positively related to ratings and that risk is negatively related to the same. Perhaps more surprisingly, there is little if any correlation between the assigned rating and efficiency, solvency, and social performance. On the contrary, MFOs with weak financial performance but strong social indicators, i.e., those that lend very small amounts of money to the poorest, receive poor ratings (Beisland and Mersland, 2012; Gutierrez-Nieto and Serrano-Cinca, 2007; Gutierrez-Nieto and Serrano-Cinca, 2010). Studies such as these have mainly focused on correlating assigned rating grades with various other factors. No study has however so far taken an interest in the more qualitative aspects of microfinance rating instruments. In addition, there is a lack of longitudinal studies that track changes over time in the underlying mechanics of rating MFOs.

Chapter 3

A theoretical model for investigating the organizational template

In the preceding chapter, I gave an overview of the empirical phenomenon of microfinance ratings and set the stage for the first specific sub-question. In this chapter, using a step-by-step approach, I develop a model that can be used as an analytical tool to further the broad research enquiry from a theoretical angle.

Evaluations and reactivity

Microfinance ratings constitute one of many examples of the recent surge in external evaluation systems that categorize, order, and compare organizations and organizational outcomes; other common examples include rankings of universities, ratings of the most socially and environmentally friendly companies, *Fortune* magazine's list of the World's Most Admired Companies, and wine ratings by connoisseurs. Evaluation systems such as these play an important role in structuring the social world, and especially in the case of organizations.

Earlier research has empirically demonstrated that evaluation systems such as ratings and rankings are reactive, meaning that organizations and individuals change their behavior in reaction to being evaluated, observed, or measured. Power et al. (2009), for instance, show that international business school ranking systems lead to changes in practices and cognitive

frameworks among those institutions being evaluated. Espeland and Sauder (2007), who also focus on university rankings, suggest that rankings alter the evaluated members' expectations and permeate institutions through the mechanisms of self-fulfilling prophecy and commensuration.[9] First, rankings influence external audiences such as prospective students, since a school's position on the list will likely affect the number of applicants that the school will attract. Second, past judgments about a school may influence current evaluations, thus reproducing these judgments. Third, if resources are linked to rankings, universities may use rankings as a means to justify resource allocation decisions. Finally, the study finds that rankings encourage schools to shape themselves to be more closely aligned with the ranking template, thus reinforcing the validity of the measure.

Another form of reactivity as identified by Espeland and Stevens (2008) is Foucault's concept of discipline, which is elaborated on below.

> "Disciplinary practices define what is appropriate, normal, and to what we should aspire; they also define which kinds of persons should be subjected to which forms of knowledge, applied by which groups of experts" (Espeland and Stevens, 2008, p. 414).

Building on the concept of discipline, Sauder and Espeland (2009) argue that evaluations such as rankings are especially difficult for organizations to decouple as they are commensurate, relative, and broadly circulating measures that are internalized by the organizational members, either because of the anxiety that they produce or because of the allure that they possess, thus rendering rankings self-disciplining. In a 1996 article, Elsbach and Kramer (1996) study the "top 20" business school rankings and show

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[9] Commensuration is a complex social process that involves transforming qualities into quantities by measuring different entities with a common metric, e.g., market prices, scores that evaluate the quality of water, and IQ tests, thus giving different entities a metrical relation to one another. Espeland and Stevens (2008) describe the specifics of commensuration: "Commensuration creates a specific type of relationship among objects. It transforms all difference into quantity. In doing so it unites objects by encompassing them under a shared cognitive system. At the same time, it also distinguishes objects by assigning to each one a precise amount of something that is measurably different from, or equal to, all others" (Espeland and Stevens, 2008, p. 408). As complex social phenomena such as poverty, crime, and intelligence are translated into simple numbers, individual experiences and events are cognitively transformed into general categories, thus changing the way we relate to the social world (Espeland and Stevens, 2008).

how deans, professors, and students at institutions ranked at the bottom of the "top 20" used several defense mechanisms to justify their poor placement. For example, they argued that important dimensions of their school had been ignored by the ranking system, and instead of comparing themselves with the top-ranked schools, they started comparing themselves with those groups that would raise their level in the ranking.

Other studies have empirically demonstrated that external evaluations impact organizational behavior in order to better comply with the evaluative criteria; companies that initially receive poor environmental ratings subsequently improve their environmental performance more than other companies (Chatterji and Toffel, 2010), and, while financial statement transparency and regulatory involvement do not impact financial sustainability and outreach indicators of microfinance organizations (MFOs), some microfinance ratings exert a disciplining impact on the same (Valentina Hartarska, 2009).

As seen above, there is strong evidence showing that significant evaluation systems are reactive and lead to behaviors that are self-fulfilling. The evaluated organization reacts to the evaluator's measures, tries to make sense of the judgment, and strives to change accordingly. By focusing on the responding organization, studies such as these thus suggest that evaluations pervade institutions via the acting organization. A subsequent question, however, is why organizations care about evaluations such as ratings and rankings in the first place. External evaluators do not take an active part in the flow of exchange in the market, and they do not take any active responsibility for organizational behaviors or outcomes. As such, why are organizations so eager to conform to the voices and verdicts of such external observers?

Evaluations and legitimacy

By conforming to the ideals, practices, and standards projected by significant evaluators, organizations gain and maintain crucial legitimacy (Ruef and Scott, 1998; Zuckerman, 1999). Within the neo-institutional framework, the concept of legitimacy helps explain why some organizations can

be stable, attract needed resources, and enhance their survival prospects while others cannot. 'Legitimacy' refers to a generalized perception

> "that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions" (Suchman, 1995, p. 574).

Legitimacy thus gives indications of which organizations and organizational features are likely to be seen in the future and which are likely to die out. Notably, legitimacy goes beyond how widespread and diffused an organizational practice or structure has become, to also take into consideration whether it is culturally and cognitively endorsed (Colyvas and Jonsson, 2011). Perhaps not surprisingly, gaining legitimacy is especially important for new organizations (Singh, House, and Tucker, 1986), emerging industries (Deeds, Mang, and Frandsen, 2004), and for organizations undergoing transformations due to complex changes in the environment (Dacin, Goodstein, and Scott, 2002).

In legitimacy assessments, a natural first question is often which social actors are doing the legitimating work; legitimacy for whom? As argued by Meyer and Scott (1983, p. 201), sources of legitimacy are those "who have the capacity to mobilize and confront the organization." According to Ruef and Scott (1998, p. 880), an organization's legitimacy is determined

> "…by those observers of the organization who assess its conformity to a specific standard or model. All stakeholders participate in this process, evaluating one or another aspect of the organization with varying degrees of knowledge and with varying degrees of influence on the overall level of legitimacy."

Significant external evaluators such as rating agencies have the power to indirectly sanction and reward organizations, they have authority, and they have inherently elevated social positions. It is thus plausible to argue that organizations gain legitimacy if they succeed in reflecting the standards and models that are projected by these evaluators, and risk losing the same if they fail to do so (Zuckerman, 1999). Several earlier studies have also applied intermediaries such as ratings and rankings as proxies for legitimacy and the related concept of reputation: Hamermesh and Pfann (2012) use

the *US News and World Report* ratings of graduate programs as a proxy for reputation; Ruef and Scott (1998) use evaluations and accreditations by professional and industry trade associations of hospitals as proxies for moral legitimacy; numerous studies have used *Fortune's* ranking of The World's Most Admired Companies as a proxy for reputation and found a positive effect on stock market and accounting performance (Black et al., 2000); and Zuckerman (1999) uses product categorizations made by securities analysts as a proxy for illegitimacy. Actors and products that deviate from and fail to conform to accepted and legitimate ideals and models are punished by these analysts by not being certified. As a result, the demand for these products falls and the firm suffers.

Evaluators and their evaluative practices are influential not only because they direct the flow of funds in sectors through their recommendations and endorsements, but also, perhaps more importantly, because they implicitly signal what is expected of the individual organization in order for it to be perceived as a legitimate and righteous actor. By measuring, judging, ordering, and comparing organizations, external evaluation systems codify normative images of organizations.

The template

A helpful concept in understanding how evaluating intermediaries such as ratings and rankings inform organizations about expectations and demands is that of template.[10] DiMaggio and Powell defined a template as "the tak-

[10] Readers who are familiar with the organizational ecology framework may ask how the definition of the template differs from that of the organizational form. Although related, there are important differences between the two concepts. Most importantly, organizational ecologists, or density-dependence theorists, focus on the comprehensibility and taken-for-grantedness of an organizational form (Hannan and Carroll, 1992). Within this framework, the focus is thus on the classification of organizations as members of a known category or organizational form. Those interested in the template, however, take the analysis one step further to more profoundly understand the structures, forms, techniques, strategies, and goals that are perceived as true, right and appropriate for a given actor at a given time. Yet, the question of which category to belong to or organizational form to adhere to is not always straightforward, as some organizations may be grouped into several categories (Ruef and Patterson, 2009) or only partly in a category (Hannan, Pólos, and Carroll, 2007). Organizations that may belong in multiple categories or adhere to several or undefined, ambiguous or unknown organizational forms are potentially less successful than those whose categories are more straightforward (Hsu, Koçak, and Hannan, 2009; Hannan et al., 2007).

en-for-granted beliefs and widely promulgated rules" (Powell and DiMaggio, 1991, pp. 27-28) in the organizational environment. Building on this, D'Aunno, Succi, and Alexander (2000) set forth the following definition of the template:

> "Organizations often arrange their core activities according to accepted models, or templates, in their field. These templates are patterns for arranging organizational behavior that specify organizational structure and goals and reflect a distinct set of beliefs and values. (…) Some templates are so repetitive and enduring across an entire organizational field that actors take it for granted that this pattern is the right way to organize…" (D'Aunno et al., 2000, p. 679).

The concept of the template has been used to analyze radical organizational change, which, in theory, occurs when there is a shift from one template to another (Greenwood and Hinings, 1996; Johnson, Smith, and Codling, 2000; Voges, Tworoger, and Bendixen, 2009). D'Aunno et al. (2000) use rural hospitals as empirical grounds to show that organizations are more likely to abandon a template in highly competitive markets with strong but heterogeneous institutional forces. This definition of the template highlights the structural and systemic aspects of organizations (Greenwood and Hinings, 1996).

Inspired by the literature on strategic reference groups, which stresses that organizations are categorized and compared based on cognitive understandings of groups, Wedlin (2007) broadens the definition of template to include cognitive aspects. Within such a framework, categorization of and comparisons among organizations go beyond similarities in formal structure to also include identity-related features such as image, reputation, character, and strategic qualities.

> "Template denotes a generalized notion of an organizational group that serves as a comparison for assessing whether an organization belongs in a particular category or class… The template provides a basis of comparison and creates perceptions of similarity and comparability among organizations" (Wedlin, 2007, p. 25).

Templates thus bring together organizations that belong to the same category and are perceived to be similar. At the same time, templates also indi-

cate where the borders should be drawn between different categories (Wedlin, 2007).

However, templates do more than define and clarify category borders; in addition, they signal what is expected of the organization by specifying measures for competition and comparison and by promoting role models, best practices and ideals. Templates are implicit cognitive maps that help inform same-category organizations how to act in specific situations, what structures to reflect, what rules to abide by, what to strive for, and what to achieve.

> "While they are not directly imitated, templates channel and support the imitation and diffusion of models and practices as they direct attention to specific ideals and characteristics considered valid or desirable, as well as promote specific role models for the field" (Wedlin, 2007, p. 37).

Evaluation systems such as rankings, ratings, and awards play important roles in uncovering and codifying templates. They do this by delineating what is perceived as success and failure and what is demanded of organizations. A codified template as projected via ranking lists, rating reports, and award ceremonies works as a yardstick against which organizations can compare themselves. Czarniawska (2007) as well as Anand and Watson (2004) show how awards, by demonstrating what is being valued by society, contribute to shaping normative aspects of the environment. Awards are best understood not in terms of what they confer upon the winners, but in terms of what they mean to and actually do for the other actors in the sector, as well as for shaping the image of the sector in society at large.

When codified templates are disseminated in the field, these become visible and usable for organizations. Encoded templates may however vary in terms of how visible, widely diffused, accessible, and strong they are. While a project evaluation document may be an internal and classified document, many external evaluation systems, e.g., ranking lists, rating reports, and award ceremonies, are widely diffused and publicly announced, which makes them especially accessible for organizations. Depending on the type of evaluation mechanism, the encoded template may also be more or less comprehensive and sophisticated. Templates as encoded in external evaluations that contain more elaborate accounts and holistic assessments can be

assumed to be more readily available for the evaluated organization and others, e.g., a lengthy award statement, a thorough project evaluation document, or a rating report, as opposed to a simple position on a ranking list or a rating grade.

Microfinance rating reports provide a fruitful ground for exploring the organizational template of MFOs. There are many ways of analyzing the core significance of a rating report. One way is to treat rating reports as a kind of practical assessment that captures important aspects of the organization in order to coordinate among and provide standardized information to different market actors. An alternative or complementary way of understanding rating reports, which I employ and expound upon in this dissertation, is viewing them as encapsulating and reflecting particular norms, rules, role models, and best practices (i.e., an organizational template) that implicitly and explicitly signal how same-category organizations are supposed to be structured, organize their activities, formulate their goals, and contribute to the betterment of society.

Rating reports constitute rich empirical material as they aim at providing elaborate accounts of the rated organization, including aspects such as organizational history and track record, methods and techniques employed by the organization, legal status, strategies, and services/products offered. They reflect how various organizational features are understood in terms of how they are organized under different rating categories and subcategories. Microfinance ratings measure how well different MFOs match up to a given ideal using a common scale, thereby serving indirectly to order and rank rated MFOs and enabling comparison among them. This process is further reinforced with the distillation, or commensuration, of various organizational aspects into a single letter grade on a quality scale. Rating reports reveal which organizational aspects that the rater considers to be most relevant, as some organizational features are emphasized, while those organizational aspects that are taken for granted, considered irrelevant or unnecessary, or regarded as impossible to evaluate are excluded from the assessment. Further, microfinance rating reports contain and transmit representations of how MFOs should be structured and organized and how microfinance activities are to be carried out, signaling what is deemed as good, just, and appropriate microfinance practice.

I have argued here that the supply of codified templates may vary between fields and that different templates may diverge in terms of the ease with which organizations can access them. In addition, codified templates may fluctuate in strength and intensity; although a template by its very definition is normative, a strongly codified template is explicitly evaluative and prescriptive as opposed to descriptive and factual. The strength of the codified template can be assumed to increase with the proportion of explicit value judgments, instructions and recommendations about what is good and bad, appropriate and inappropriate, and what is expected of the organization in order to improve that it contains. In addition to descriptive passages, microfinance rating reports also include explicit normative elements, e.g., the rater's judgments of the MFO's past activities and the outcomes of these, postulations of future outcomes and risks, and strategic recommendations. Rating reports point out what the rater perceives as organizational flaws and strengths, along with comparisons of the rated organization to its perceived peers, as well as with other standards.

A subsequent question is for whom the template is relevant. As argued by D'Aunno et al. (2000) and Wedlin (2007), templates help recognize and shape organizational fields by signaling which organizations belong to the field and how they are internally hierarchized. An organizational field, as introduced by DiMaggio and Powell (1983), refers to

> "…those organizations which, in the aggregate, constitute a recognized area of institutional life: key suppliers, resources and product consumers, regulatory agencies, and other organizations that produce similar services or products" (DiMaggio and Powell, 1983, p. 148).

The template as projected in microfinance rating reports is an idealized, normative image of organizations that operate within the field of Indian microfinance. Although not all MFOs participate in rating exercises, the templates as projected in such reports are widely diffused throughout the field and beyond. This implies that the templates impact not only the rated MFOs, but also all of the MFOs that identify themselves with the organizational field of Indian microfinance.

A key concept underlying the organizational field idea is that organizations within the same field exist in common conditions (Scott, 1994) and

face the same isomorphic expectations from the environment. Earlier theories suggest that organizations in the same field will ultimately develop similar practices and structures. More recent studies, however, show that these isomorphic pressures result not only in increased homogeneity but also in differential responses and resistance (see, e.g., Czarniawska and Sevón, 1996). Templates cannot be directly imitated or adopted by organizations, e.g., as with a corporate responsibility code of conduct, a specific ISO standard, or the Global Reporting Initiative Guidelines, as templates are abstract, cognitive and not formalized, written down or conceptualized. Instead, templates signal which practices and organizational objectives are appropriate in a particular sector and what same-category organizations informed by the template are expected to contribute to society. In her study of business school rankings, Wedlin (2007) shows that the template allows for variation among schools, since it is sufficiently abstract and ambiguous to leave room for local translations.

External evaluators and the templates they project play particularly important roles in some field contexts. Although much of the evaluation research undertaken to date has been situated in the university sector, focusing on the impact of university rankings, I posit here that templates as projected by evaluating intermediaries play an especially significant role in fields where evaluators shape market patterns, not only discursively, but also substantially and materially by, e.g., directing transactions, recommending how resources should flow, or certifying products (Zuckerman, 1999). Zuckerman's (1999) study is, for instance, set in the mediated financial market, wherein securities analysts and their product certifications have a lot of power.

It is also plausible to assume that significant evaluators and their templates are particularly important in complex, emerging and transforming environments that lack clear, fixed and taken for granted role models, best practices and standards. In such contexts, evaluators and the templates they project clarify what is expected of organizations, as well as which organizations are perceived as legitimate.

Evaluation practices as social processes

So far, my analysis of evaluation practices and templates has focused primarily on the evaluated organizations. The next step is to shift the focus to the evaluators, examining the processual aspects of how templates are encoded and how evaluation practices unfold. Evaluations such as ratings are commonly seen as rigorous assessments of organizations based on predetermined instructions and guidelines as to what type of information and data is relevant and how best to make sense of it and convey it to readers. The codified template is, however, a theoretical concept and not something that is available as a practical tool for the evaluator. The template thus differs from, e.g., the rating agency's actual rating instrument, which typically is a proprietary model for rating that has been developed in-house and is treated confidentially as part of the agency's core competence, competitive advantage, and unique selling point. While a microfinance rating instrument is an explicitly codified tool that is readily available for use by the raters, the template is a cognitively deduced abstraction about how organizations should ideally be structured and operate.

While acknowledging that evaluations are systematic assessments based on formalized instruments, Bitektine (2011) broadens the idea of evaluations as social negotiation processes wherein several actors take active roles. As opposed to seeing evaluation practices as involving one or several professional raters with specific academic backgrounds and prior professional experience, Bitektine (2011) argues that evaluations are highly social processes that involve other evaluators and their judgments, all of which are embedded in a social context of expectations and demands.

> "As actors discuss and negotiate the most appropriate judgment with respect to an organization and communicate it to others in their social network, they produce common understandings (Meyer and Rowan, 1977) about what the appropriate judgment is" (Bitektine, 2011, p. 166).

Understanding evaluations as a social process of judgment formation suggests that evaluators follow internalized schemas of what is socially defined as "normal," "true," "right," and "good," without, or in spite of, calculating

the consequences and/or expected utility of such an approach (March and Olsen, 2004). According to this perspective, raters are constantly trying to understand and interpret what is expected of them as evaluators, which type of organization merits a high or low rating grade, and what their recommendations should entail. In addition, evaluators are constrained by the incomplete availability of information about the organization, limited time periods for study, and a finite attention span. Factors such as these serve to significantly increase the costs of information search and processing, thus contributing to the practice of evaluators "borrowing" judgments from others.

Ruef and Scott (1998) argue that the greater the extent to which assessments rely on and reflect the norms, values, and cognitive scripts that are currently dominant in the organizational environment, the more salience they have for the organization. In order for the evaluation to be credible, evaluators should attempt to give prescriptions that converge with broader societal expectations. In a study of Atlanta Symphony Orchestra performances, Glynn and Lounsbury (2005) show that critics' reviews of the orchestra tend to change when there is a shift in the broader institutional environment. For example, when an exogenous shock hit the orchestra in the form of a labor strike, the institutional environment shifted from an aesthetic sensibility to a commercially oriented logic. At the same time, the discourse of critics also shifted to become more attuned to market realities, rather than focusing solely on the aesthetic aspects of the symphony. The study suggests that the judgments of critics in the cultural domain converge with broadly held expectations and demands on organizations.

Should the evaluator's verdict deviate too much from the views of other audiences, or from norms and values that are perceived as "good," "proper," and "right" for a given actor, the evaluation may be seen as "imbalanced," "unreasonable," and "inappropriate." Furthermore, the completion of too many such evaluations may negatively impact the evaluator's credibility, authority, and legitimacy (Ruef and Scott, 1998). In addition, the greater the visibility of an evaluator's assessments, the more scrutiny they will receive, and, hence, the greater the risk of sanctions if the judgments tend to deviate from the prescribed norm. The same institutional forces that lead to isomorphism in organizational structures thus also promote

homogeneity in social judgments (Bitektine, 2011; DiMaggio and Powell, 1983).

It is also possible to assume that other actors take part in the social negotiation process that constitutes an evaluation. By contesting the results of the assessment, giving suggestions, or providing selective information, the evaluated organization may, for instance, attempt to influence the evaluator's work and judgment. Even the end users (e.g., the clients or customers) of the evaluated organization may take part in this process by voicing concerns and/or attempting to push the evaluation in certain directions. This means that the construction of the template is a complex social process in which many players are actively and directly involved.

The seemingly endless supply of evaluation organizations – many of which are nascent – that endeavor to measure and order other organizations also implies a certain degree of competition, suggesting that there may be several encoded templates competing for space and attention from actors in the same organizational field. As noted by Bitektine (2011), not all evaluators are equally likely to be able to acquire resources and survive in the long term; instead, some legitimacy assessments are more important than others, and not all constituencies have equal weight. The salience of legitimacy assessments may also vary over time and space (Vergne, 2010). One way of assessing the salience of an intermediary is to apply Mitchell, Agle, and Wood's (1997) stakeholder framework and analyze the intermediary and its assessments vis-à-vis its possession or attributed possession of power, legitimacy and urgency.[11]

The rapidly changing, globalizing, and increasingly complex world of organizations creates keen competition, and the role and function of evaluators have also been questioned: credit rating agencies have been severely criticized in the aftermath of recent financial crises (Mathis, McAndrews, and Rochet, 2009); university rankings are disliked and even despised by those in academia (Wedlin, 2007), and environmental ratings of companies are condemned as being insufficiently rigorous by environmentalists (Chatterji, Levine, and Toffel, 2009). This implies that evaluators need to build,

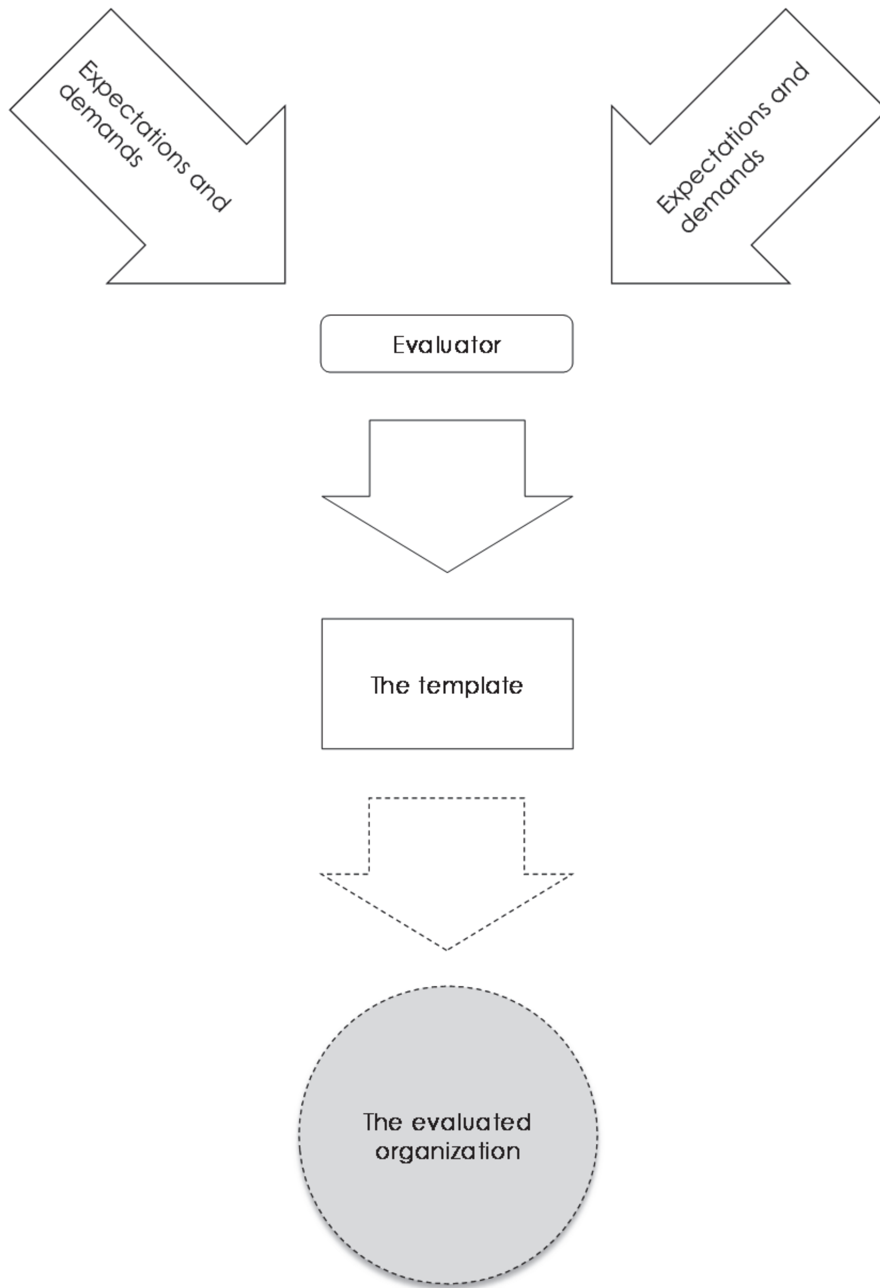
[11] In Chapter 4, I analyze Micro-Credit Ratings International Limited (M-CRIL) with this framework.

maintain and retain population-level legitimacy. In addition, each evaluating organization needs to carefully safeguard its own reputation and legitimacy.

The content of an evaluation is thus more than a reflection of the rules, norms and values that inform the given field; it is a reflection of how the evaluator understands and interprets its role in the field as well as the implications of these rules, norms and values for the evaluation exercise. Such reasoning suggests not only that microfinance rating reports mirror the rules, norms and values that inform the microfinance field, but that such reports also reflect what the rating agency believes is an appropriate evaluation of a given MFO at a given point in time.

Taking the above one step further, it is plausible to suggest that certain legitimate and significant evaluators also play a role in co-constructing the template that they project, thus not solely reflecting broadly held expectations and demands. Such reasoning implies that certain especially prominent evaluators go beyond reflecting or translating complex external expectations and demands on organizations, actually fulfilling the role of either creating new expectations or filtering away existing ones, and thus contributing to the shaping of the field via a codified template.

Figure 1. The organizational template as projected by an evaluator



Encoding organizational elements

As I have argued above, organizations may garner legitimacy as the result of being evaluated. More specifically, the type of legitimacy bestowed on the basis of evaluations such as ratings and rankings is normative in nature and works on an organizational level, as opposed to a population level. Moral legitimacy, which is also referred to as normative legitimacy (Scott, 1995), reflects a positive, prescriptive, normative evaluation of the organization and its activities in relation to the audience's socially constructed value system. Normative systems include both values and norms. While values indicate what is considered good/bad and right/wrong, norms specify how things should be done. Normative systems thus confer rights, responsibilities, and privileges and define goals and acceptable ways of achieving them, thus following the "logic of appropriateness" (Suchman, 1995; March and Olsen, 2004).

In a study of university rankings, Wedlin (2007) approaches the idea of an encoded template in terms of what values pertaining to universities are projected in ranking systems. A first such value that these rankings promote is a "customer approach" to education by assessing the usefulness of education for different stakeholder groups (i.e., students, alumni, companies and client firms). Second, rankings encourage business schools that are "international," often manifested by the number of languages required or offered, international programs, and exchange programs. Third, rankings focus on measures of "employability," i.e., the value of education in terms of the career opportunities available to graduates.

Moral legitimacy is commonly thought of as "sociotropic," meaning that it rests on judgments about whether a given activity is "the right thing to do" as opposed to whether or not it benefits the person or agency making the assessment (Suchman, 1995, p. 579). Taking the example of microfinance ratings, these evaluations are treated as neutral and qualified assessments of MFOs, and the evaluator is assumed to be an unbiased expert. Evaluators such as microfinance rating agencies are not directly involved in the flow of exchange in the market, and they do not take responsibility for organizational activities and outcomes. Instead, they con-

tribute to shaping market patterns through, e.g., product recommendations and endorsements (Zuckerman, 1999; Meyer, 1996).

Moral legitimacy can be broken down into three distinct forms: evaluations of structures; evaluations of procedures and techniques; and evaluations of outcomes and consequences (Suchman, 1995).[12] Structural elements reflect Weberian traditional authority and are based on the idea that some actors are perceived to be more worthy of exercising power than others. The evaluation of structural elements refers to how systems of activity that recur constantly over time are assessed, thus answering questions such as "Does the organization have a quality control department?" (Suchman, 1995, p. 581). Organizations that successfully reflect the structural arrangements required by important institutional referents are treated as right, good and worthy of legitimacy.

Closely related to structural elements are procedures and techniques. Legitimacy based on procedures reflects a type of legal-rational authority that is value-rational and based on adherence to rules of proper behavior. While legitimacy derived from structural aspects focuses on more general and systematic organizational attributes, procedural legitimacy focuses on the evaluation of discrete routines and activities viewed in isolation, such as, "Does the organization inspect its products for defects?" (Suchman, 1995, p. 581). Because organizational structure largely consists of static, consistently replicated procedures, procedural and structural elements are closely related.

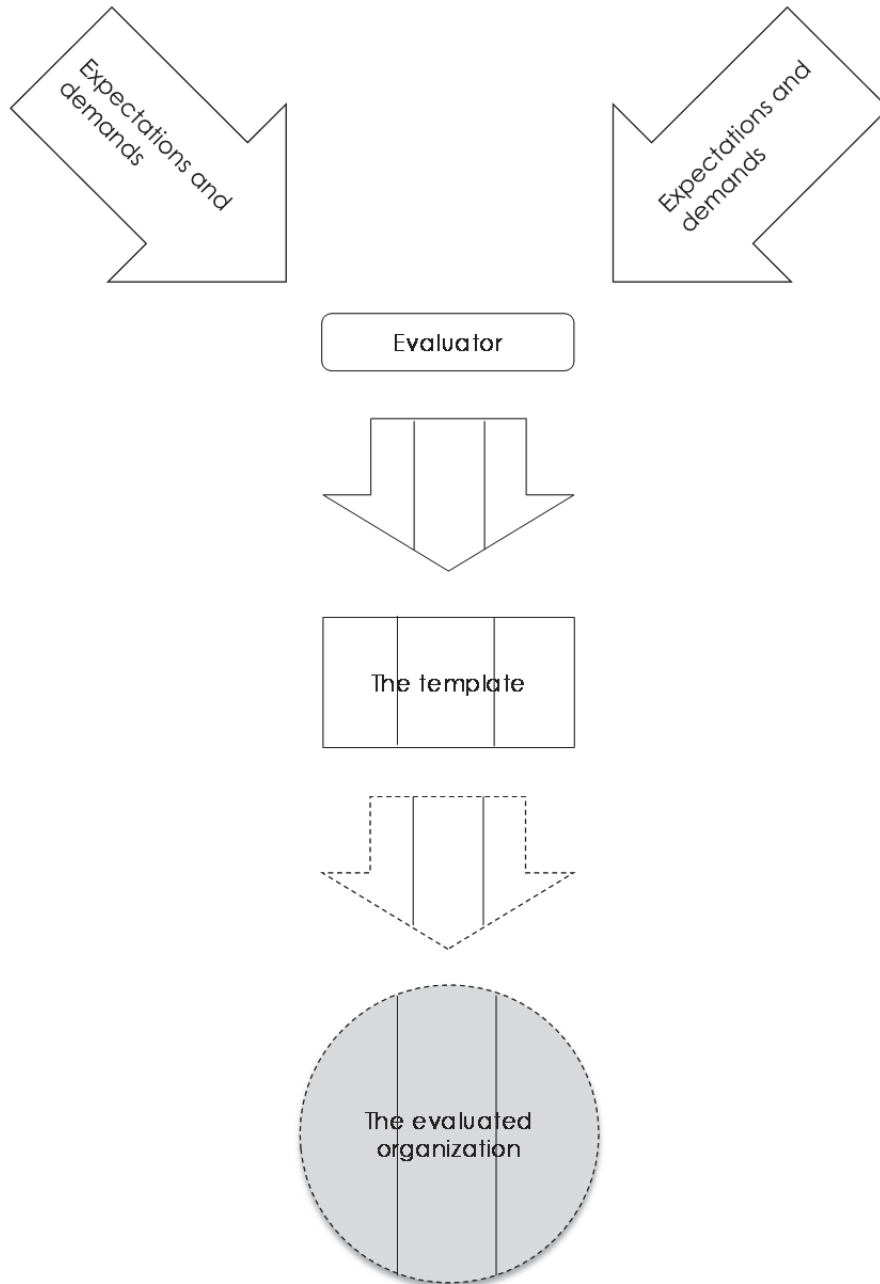
Finally, legitimacy based on outcomes is related to the pursuit of particular goals. This type of evaluation also reflects Weber's legal-rational authority, but it is instrumentally rational. The organizational element of outcomes is bolstered by widely held notions about organizational effectiveness, which support the idea that organizations should be judged by what they accomplish. This includes consumers' socially defined perceptions of product utility, quality, and added value. However, Suchman (1995) points out that some organizations may generate outputs that are inherently

[12] Suchman (1995) also includes a fourth form of moral legitimacy: personal legitimacy. This is a rarer but conceptually important source of legitimacy that rests on the charisma of individual organizational leaders. The personal legitimacy of leaders and representatives corresponds to the Weberian ideal-type of charismatic authority.

ambiguous and difficult to measure. In the absence of clearly measurable outputs, adherence to socially accepted structures and "sound practices" may serve to demonstrate that the organization is making an effort to achieve its ends, although these are difficult to capture.

One way of approaching the idea of an encoded template is thus via Suchman's (1995) typology of evaluations of organizational elements. When applying the foundational organizational elements of structures, procedures and outcomes, as has been done in Figure 2, the model becomes more complex. The evaluating intermediary is assumed to filter, order and make sense of relevant pressures and expectations, and to codify these into a configuration of organizational elements, which, taken together, represents the template.

Figure 2. The organizational template disentangled into organizational elements



The time dimension

In this discussion, I am interested in changes in evaluative practices and the template. The tracking of changes over time in the template – and in the constellations of elements that it reflects – allows for a more profound understanding of how evaluative practices work and how they potentially guide field development. Thus, instead of looking at the dynamism within the acting organization, my focus here is on how prescriptions and demands as codified in the template change over time.

To my knowledge, the only study that has longitudinally tracked changes in the mechanics used to construct evaluation procedures is a study by Schultz, Mouritsen, and Gabrielsen (2001) of a Danish ranking system used to assess companies, similar to that employed by *Fortune* magazine. The authors of the study use the ranking as a proxy for reputation and suggest that reputation is "sticky," meaning that it is durable and tends to persist over time. The study finds that the system favors firms already included in the rankings. The "stickiness," the authors argue, is paradoxical, since ranking criteria are far from stable: they shift over time and become increasingly complex; the measurements are built on fragile statistical methods; and the respondents themselves change over time. Although the ranking system develops by extending criteria, respondents tend to attach similar judgments to the new criteria, thus reinforcing already established judgments, similar to the "halo effects" that other studies have found (Brown and Perry, 1994). This means that large and visible companies that already are ranked high are favored and thus tend to stick to the top of the list. In this way, although the system may change, the mechanics of the construction of reputation tend to underpin and strengthen the judgments that have already been made, hence the concept of "stickiness" with regards to reputation.

Making changes in the rating criteria (and thus impacting the template) may also pose challenges to the legitimacy of the evaluator, since much of the credibility assigned to ratings and ranking models builds on the fact that they are perceived to be largely consistent and stable over time, as opposed to dynamic and opportunistic. To my knowledge, the only study that discusses the evaluation process in light of broader shifts in the evaluator's social context and addresses potential legitimacy threats to the evaluator is

an unpublished 2011 study by Patterson. In exploring credit rating decisions by a prominent 19th-century credit rating agency (now known as Dun & Bradstreet) before and after a series of events that threatened its legitimacy, the author demonstrates that intermediaries such as rating agencies are sensitive to external changes and threats to their legitimacy. In the case of Dun & Bradstreet, the agency made a key shift in its rating methodology in order to defend its legitimacy. More specifically, the credit rating agency abandoned a long-term perspective that considered more individualized, contextual details in determining ratings and instead adopted a perspective that focused on a more narrow set of easily justifiable status characteristics. This suggests that the evaluative practices of evaluators may fluctuate over time as the result of external shocks (Patterson, 2011).

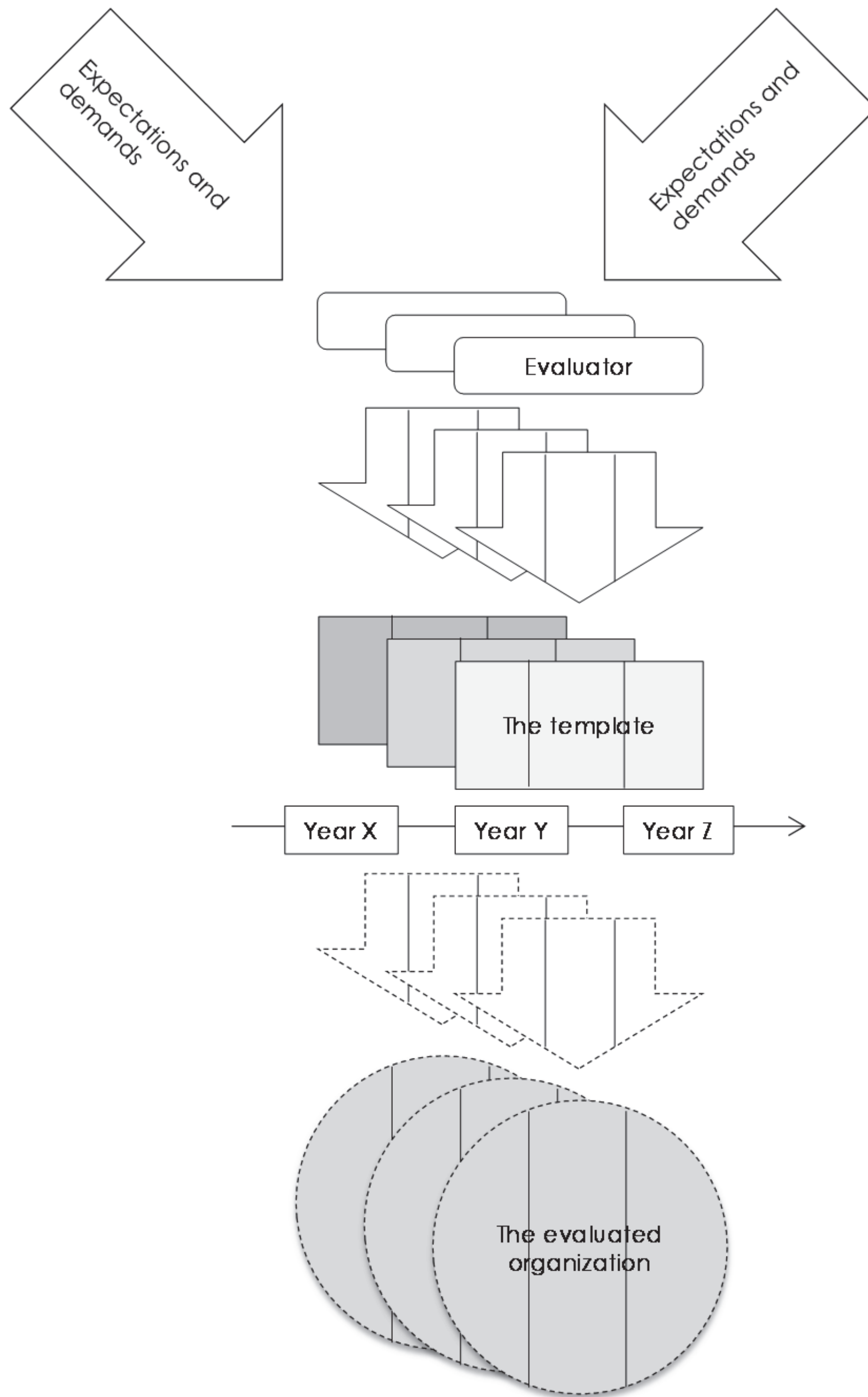
Collet and Vives (2013) take the analysis up one level and contextualize changes in rankings with macro level shifts. By analyzing the *Financial Times* Global MBA Rankings, Collet and Vives (2013) show that American schools have declined over time, to the advantage of European and Asian schools. Rankings such as the *Financial Times* Global MBA Rankings assign a great deal of weight to salary variables, and the authors find that the shift in rankings corresponds to an erosion of the differences in salaries between these regions. European MBAs have, however, experienced an unusual increase in salaries despite low aggregate economic demand and a rising supply of graduates.[13]

In the current research, I am interested in understanding how the content of the template corresponds to sectoral trends and events, thus implying the existence of a change process and a time dimension. What has often been lacking in earlier studies is the longitudinal perspective. Apart from the abovementioned studies, the majority of earlier studies have focused on how evaluated organizations react to being evaluated. These studies have also been able to demonstrate strong responses, dynamism, and adaptation strategies stemming from within the evaluated organization. At the same time, the extant research has assumed that evaluative practices and the encoded template remain stable, fixed, and unaffected over time. As shown

[13] The study does not provide a clear explanation for this phenomenon although two potential reasons that are discussed are the slow pace in which management education in Europe became legitimate as well as the geographic proximity of European schools to local labor markets.

graphically in Figure 3, by tracking changes over time in the encoded template and related elements, it becomes possible to attain a more profound understanding of the role played by evaluative practices in the construction of templates to guide organizations in the field.

Figure 3. Changes over time in the organizational template



In this chapter, I have developed a model for how the abstract concept of the template, as projected through evaluative practices, can be investigated in depth. First, in a discussion grounded in the findings of a growing number of studies on this and related topics, I have argued that external evaluations such as ratings and rankings are important for organizations, as they prompt organizational reactions and attempts at adapting. By conforming to the idealized image as projected in external evaluations, organizations may garner moral legitimacy, which is critical if the organization is to survive and sustain itself. To understand the mechanisms through which evaluations work to impact organizations, I introduced the abstract notion of the template, which contains "patterns for arranging organizational behavior that specify organizational structure and goals and reflect a distinct set of beliefs and values" (D'Aunno et al., 2000, p. 679). By pointing at best practices, ideals, and acceptable models, evaluation systems such as ratings and rankings play important roles in uncovering and codifying templates for organizations in the same field.

In the next step in my analysis, I shifted the focus to the evaluators and their evaluative practices in an attempt to unfold the processual aspects of how templates are encoded and what they contain. I argued that an evaluation such as a ranking or a rating must be understood as the result of a social negotiation process, as opposed to a rational, systematic assessment conducted by a single evaluator. Evaluators and their practices are embedded in social contexts which are infused with norms and values prescribing what is considered a "good" and "proper" evaluation. An evaluation is thus a reflection of how the evaluator perceives its own role in the field, as well as of how the evaluator interprets the implications of the norms and values in the process of conducting the evaluation exercise. I further argued that it is plausible to suggest that prominent evaluators may play an active role in the co-construction of the template they project. This means that evaluators potentially go beyond simply reflecting the complex external expectations facing organizations and also engage in the process of creating and modifying the template, thus contributing to guiding organizations in the field. In devising the approach I used to address the idea of an encoded template, I was inspired by Suchman (1995) description of organizational elements of structures, procedures and outcomes. I posit that it is possible

to deduce an idealized image of the organization, by analyzing how these elements are assessed by the evaluator. Finally, since I am interested in changes in evaluative practices and the template, a time dimension was introduced.

With the above model in mind, I will now return to my first research question: *How do rating practices and the templates projected through these change over time? (Question 1)*. To address this broad question, three sub-questions have been generated. In the preceding Chapter 2, I developed the first such sub-question, which is empirically grounded: *How does the microfinance rating instrument change over time in terms of factors such as rating categories and sub-categories, indicators, and weightages? (Question 1a)*. The exploration of this question will cast light on how the microfinance rating product, from the point of view of the raters, has changed in terms of which empirical organizational features are evaluated in the ratings, how the raters categorize these different features, and how the rating categories relate to each other and to the final rating grade. The question will also provide answers as to how MFO performance is assessed by raters, which indicators are in use, and which performance aspects the raters seek to capture.

The question does not, however, allow for a greater understanding of how the rationale for evaluating different organizational elements of the MFO has changed, how the raters implicitly and explicitly justify and rationalize their evaluations of different cognitive organizational elements as the field develops, how potential tensions are dealt with in the reports, and how articulate and explicit the reports are in their judgments and final verdicts. Using a more theoretical lens, the first research question does not provide answers as to what normative image(s) (i.e., templates) of the Indian MFO can be derived from and are signaled in the reports and how these have changed over time. To complement the above, the following more theoretically grounded sub-questions have thus been developed:

Question 1b: How does the template change in content over time?

Question 1c: How does the template change in strength over time?

Finally, to contextualize the findings of the above questions, and relate rating practices to the macro and meso levels in which they are embedded, the following research question will be investigated: *How do changes in rating practices and in the templates projected through these relate to trends and events in the sector, as well as to the rater's market position? (Question 2)*

Chapter 4

Methodology and research design

In this dissertation, I aim at investigating how rating practices are constructed and work. I am especially interested in ratings and the organizational templates that are codified and projected through these in the complex and rapidly changing context of Indian microfinance. In Chapter 2, I introduced the empirical phenomenon of microfinance ratings and the specialized microfinance rating agency Micro-Credit Ratings International Limited (M-CRIL). In Chapter 3, I developed a theoretical model for how the abstract concept of template can be investigated in depth. In Chapter 3, I also articulated the broad research questions presented in the introductory chapter in more specific terms. In this chapter, I describe how the empirically oriented question has been approached methodologically, as well as how the theoretical model has been operationalized and executed through my research design. I also discuss the contextualization of evaluative practices. Finally, I elaborate on the various considerations and choices made as regards methods, as well as on the delimitations that these imply.

A single case study of the unique microfinance rater M-CRIL

Merriam (1988) defines a case as a unit, an entity or a phenomenon whose boundaries have been clearly defined by the researcher. With preset demarcations, it becomes easier to determine what will not be studied and what is

not included in the case. In this light, my research approach can be defined as a longitudinal case study of an evaluator and its evaluative practices. More specifically, this dissertation is a case study of the specialized rating agency M-CRIL and its evaluative practices in the Indian microfinance sector from 1999 to 2014, rendering the case mainly empirical (Ragin and Becker, 1992, p. 223).

The main criticism of the case study method is that one or a few cases are insufficient in order to generalize the findings to other situations. Eisenhardt (1989), among others, has tried to reconcile the case study method by blending it with principles from quantitative traditions and increasing the number of cases. However, Flyvbjerg (2006) argues that case study research can contribute to scientific development since much earlier knowledge and discoveries have emerged from case studies, since cases play an important role in human learning, and since falsification is possible via case studies. Thus, instead of counting the number of cases, the depth and rigor of the analysis as well as the specifics of the case should be at the center of the discussion when assessing the case method (Dyer and Wilkins, 1991).

Ideally, the best way to go about to answering the research questions that I have set forth in this dissertation would be to analyze the evaluative practices of and the relationship between several different rating agencies with varying levels of significance and impact and which occupy different positions within the space. However, in order to attain a profound understanding of how rating practices are constructed and work, I have focused on a single intermediary, M-CRIL, and its ratings of microfinance organizations (MFOs) over the period 1999-2014.

As I elaborate on in Chapter 2 and Chapter 6, the specialized microfinance rating agency M-CRIL is for several reasons a particularly interesting evaluator. The agency pioneered microfinance ratings in India in 1998 and was one of the first to conduct this type of assessment globally. It is the only rating agency in India that focuses solely on the microfinance sector, and it is deeply embedded in the sector. The other six agencies that conduct ratings of MFOs are large corporate credit rating agencies whose microfinance activities constitute only a small portion of their respective portfolios. Applying the organizational field definition (DiMaggio and

Powell, 1983), M-CRIL is the only agency that defines itself as participating in the microfinance field, that shares the same meaning system as other field members, and that primarily interacts with MFOs and other organizations within the field. The other rating agencies are part of the mainstream capital market, and all stand at the fringes of the microfinance field; their core competence can be found in corporate ratings, and their businesses would only be marginally affected if microfinance was to be excluded.

M-CRIL is also interesting because its role and position in the Indian microfinance space has changed dramatically over the years. Recently, the role of M-CRIL and its ratings has weakened; state-accredited credit rating agencies, along with mainstream rating products, have entered the rating game and have started to take market share.

Moreover, M-CRIL is the first of its kind globally and one of the world's biggest agencies in terms of the number of microfinance ratings undertaken. It is one of four specialized microfinance rating agencies in the world, and, as such, it takes an active part in collaborative efforts together with the other three specialized agencies. M-CRIL is a recognized microfinance authority whose board members constitute some of the world's leading microfinance experts. The agency is often invited to participate in various expert constellations in India and in global forums. M-CRIL was also one of the first agencies to launch a social rating product in 2004-2005, and it is currently the only agency that offers social ratings in India. M-CRIL compiles and disseminates reports and publications, organizes microfinance seminars for policymakers and microfinance practitioners, and manages one of the most comprehensive data sets on Indian MFOs. The only other agency that comes close to matching M-CRIL's level of contribution is Credit Rating Information Services of India Limited (CRISIL), which has produced two comprehensive reports on Indian MFOs, one in 2009 and one in 2014.

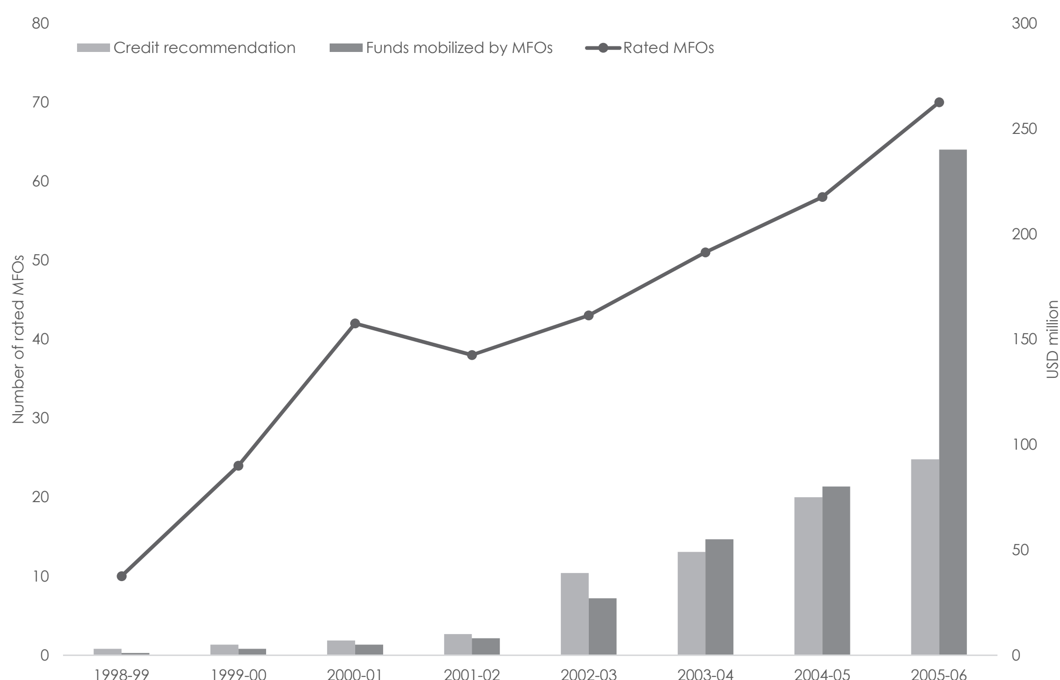
Assessing the salience of M-CRIL and its microfinance ratings

As I argue in Chapter 3, significant evaluation systems play important roles in rendering templates visible and powerful, since their practices lead to idealized organizational images – templates – being both codified and disseminated. When templates are encapsulated in objects, or artifacts, in the forms of, for example, rating reports, ranking grades, or awards, they become more accessible for the assessed organization. However, given the vast number of intermediaries that are producing external evaluations, not all intermediaries have an equal impact on organizations.

To analyze the specific salience of M-CRIL and its ratings, I will apply the framework for assessing stakeholders as developed by Mitchell et al. (1997) and analyze M-CRIL's possession or attributed possession of power, legitimacy, and urgency. M-CRIL's power is here defined as the extent to which it has coercive, utilitarian, or normative means to impose its will on the rated MFOs (Mitchell et al., 1997, p. 865). One way of assessing the agency's power is to tabulate the number of ratings conducted by M-CRIL per year out of all ratings conducted of Indian MFOs. As I show in Chapter 6 (see Table 18), M-CRIL has dominated the microfinance rating market over the years, holding a majority share of the market until 2007-2008. Since that time, M-CRIL's market share has gradually decreased.

Another proxy for M-CRIL's power is to assess the credit recommendations made in the agency's ratings versus the actual flow of funds to the rated MFOs. Figure 4 shows the growth in M-CRIL-conducted microfinance ratings from 1998-2005, as well as the lending recommendations made by the agency during those years versus the actual funds mobilized by the rated MFOs.

Figure 4. M-CRIL ratings, credit recommendations, and funds mobilized by M-CRIL-rated MFOs



The figure has been derived from M-CRIL (2006b, 2008).

According to the figures in Figure 4, which were released by M-CRIL, around 2003-2004, the amount of funds mobilized by the rated MFOs starts surpassing the rating recommendations provided by M-CRIL. According to 2008 estimates, 98% of M-CRIL's rating assignments were realized in the entire Asia region (Appui au Développement Autonome, 2008). The above graph thus suggests that the flow of funds to the rated MFOs has exceeded the credit recommendations made by M-CRIL. However, the issue of whether or not these funds were mobilized as the direct result of M-CRIL's ratings remains unanswered here.

A third way of assessing the relevance of M-CRIL ratings is to determine whether the price of funds decreases for MFOs that have been rated above investment grade as compared to unrated MFOs. A study by Gar-

maise and Natividad (2010) on microfinance ratings by specialized rating agencies generally supports this claim. Also, according to an anecdotal account from Brij Mohan, a board member of M-CRIL who also is the former executive director of the Small Industries Development Bank of India (SIDBI)[14] and the founder of the SIDBI Foundation for Micro Credit, banks often inquired as to whether an MFO had been funded by SIDBI and thus had been rated above investment grade by M-CRIL and deemed creditworthy. When this was indeed the case, the banks would offer a better interest rate, thus validating the value of M-CRIL's ratings (interview with Brij Mohan, 25 May 2012). This suggests that M-CRIL ratings have had the power to indirectly sanction and reward MFOs for much of the last 15 years, and that banks, along with other funders, have considered rating grades when making funding decisions.

As to assessing the legitimacy of M-CRIL, the legitimacy concept is very broad and difficult to operationalize; below is one attempt to do so:

> "…a condition reflecting cultural alignment, normative support, or consonance with relevant rules or laws, depending on whether the emphasis is on cognitive, normative, or regulatory aspects of institutions" (Scott, 1995, p. 45).

On a general level, it could be argued that rating agencies have an innate basis for legitimacy based on three chief characteristics: they are commonplace and recognizable actors in most financial markets; they seek to enact aspects of modern organizational models (e.g., accountability, professionalism, and efficiency); and they enjoy the privileges of state accreditation, which is advantageous yet arduous to attain. When it comes to the specific legitimacy of M-CRIL, the agency is a deeply embedded actor in the microfinance sector and is regularly invited to participate in committees, conference panels, global initiatives, and other forums where microfinance expertise is sought. However, what M-CRIL lacks is regulatory support; it is the only rating agency active in the microfinance sector that lacks government accreditation. This became an issue in the period of 2008-2009 when the new Basel II standards were adopted by the Reserve Bank of India. Within this framework, banks are asked to apply external ratings conducted

[14] SIDBI has been the leading wholesaler in Indian microfinance for an extended period of time.

by credit rating agencies approved by the Reserve Bank of India in order to reduce risk weightage.

M-CRIL has relied on two different revenue models over the years. Until 2008, the agency followed the "investor pays" model, and, as such, much of the ratings were paid for by SIDBI, while the MFOs made only minor contributions. Since 2008, the "issuer pays" model has been adopted, which means that the MFOs pay for the ratings. The "issuer pays" model, which is also the leading model among the large corporate raters, is often criticized as potentially causing conflicts of interest, since the agency is paid by the banks and companies that they are supposed to objectively evaluate. Critics contend that such a relationship may lead to rating agencies assigning higher-than-warranted ratings to issues they rate (Alessi, Wolverson, and Sergie, 2013). At least until 2008, M-CRIL largely managed to avoid potential threats to its legitimacy due to perceived conflicts of interest.

Another factor that could hurt the perceived legitimacy of specialized rating agencies is their double role as consultants and evaluators (Kirchstein, 2011). In addition to providing rating services, M-CRIL also performs various sector-level services, but the agency does not engage in consultancy work for individual MFOs.

M-CRIL has chosen to address any potential conflicts of interests with the implementation of a rating committee function. All rating reports pass through a "rating subcommittee" consisting of two "independent directors" before being formally approved. The independent directors also make up part of the M-CRIL board, together with Frances Sinha, Sanjay Sinha, and Alok Misra, who are part of M-CRIL's operations team and therefore are not considered to be independent. M-CRIL refers to the other individuals on its board as "independent," both because they are not staff members and because the sitting fees and honoraria they earn from M-CRIL constitute relatively small parts of their respective annual incomes. These directors are some of the most prominent individuals in the Indian microfinance sector and beyond.

A related notion is the concept of urgency, defined as the degree to which stakeholder claims call for immediate attention. To contextualize this vis-a-vis microfinance ratings, I would argue that M-CRIL ratings are underpinned by a certain degree of urgency. All M-CRIL ratings are valid for

one year, after which a rating update is recommended. Many MFOs are rated more than once; from January 2006 until June 2007, of the 94 MFOs that had been rated by M-CRIL in India, 40 MFOs had been rated once, while 54 MFOs had been rated two to six times (M-CRIL, 2007). This suggests that rating frequency was considered important. A sudden or unexpected rating downgrade potentially makes it more difficult to attract resources from banks, investors, and donors. Until 31 March 2008, M-CRIL's ratings contained a rating grade along with a credit recommendation, which is a recommendation of an exact amount (in INR or USD) that the rated organization would be able to absorb during the coming year according to the rater.[15] The urgency associated with M-CRIL ratings decreased after 2008-2009, when the rating agencies approved by the Reserve Bank of India entered the market.

To complement this analysis, the visibility, economic stakes, and perceived risk of social sanctions connected with M-CRIL ratings should also be considered (Bitektine, 2011). First, the visibility of M-CRIL reports is relatively high, as these commonly are disclosed via publicly available microfinance databases such as MIX Market, the Microfinance Rating and Assessment Fund, Rating Fund II, the Rating Initiative, and Microfinance Gateway, as well as on individual MFO websites, which suggests that the evaluator would likely invest more time and resources in the process of completing a thorough due-diligence analysis. M-CRIL faces the risk of both economic losses and social sanctions if its assessments are perceived to be incorrect time after time. As with mainstream rating agencies, M-CRIL's reputation is crucial for its continued successful operation. Consequently, if its assessments are known to be wrong, the agency's reputation would be threatened among MFOs, funders, and regulators.

A qualitative approach

To approach my research enquiry, I have primarily leaned on a qualitative method. To analyze the concept of strength, I have however adopted a quantitative word count approach. I acknowledge that one method is not

[15] The last report in my sample to have a credit recommendation is the 2008 Grameen Koota report.

better than the other; instead, methods complement each other. My research enquiry however, which aims at understanding and interpreting rather than at explaining and confirming causalities, is more suitable for a qualitative approach. Further, my aim is to investigate how evaluative practices are constructed and work, rendering the research primarily descriptive in nature.

Rating reports are first and foremost collections of texts, and a large part of my investigation rests on a qualitative textual analysis. As elaborated on by Munir and Phillips (2005), textual accounts, as opposed to, e.g., actions, are imperative for understanding normative aspects of the organizational environment.

> "…in modern societies the production of institutions is a largely textual affair. As our experiences of one another are increasingly mediated by systems of communication that do not allow for the direct observation of one another's actions, it is also increasingly the case that we understand each other through complex collections of texts" (Munir and Phillips, 2005, p. 1669).

A textual analysis places language at the center. Yet, language is ambiguous, unstable and context dependent. This implies that language never is neutral, but rather the result of sense-making, interpretations and contextualization. A text analysis of a rating report must thus build on an in-depth analysis of the meaning of language for a given actor and at a given place and time. The same terminology may carry vastly different meanings and be associated with different connotations depending on the context. The coding and analysis of M-CRIL rating reports are thus representations of occurrences in situ, and my focus has been to try to understand and interpret these based on the meaning that they carry. Although report formats and designs may fluctuate over time, rating reports are rather predictable in terms of formal structuring, and this also facilitates the analysis of larger samples. In addition, the relatively standardized format of rating report documents renders them conducive study objects for tracking changes over time.

An alternative approach would be to apply a quantitative, statistical method, e.g., in the form of a word count. Such approach would not be as flexible as a qualitative one and it would not allow for rich and nuanced "thick descriptions" (Merriam, 1988, p. 29) of the evaluative practices. It

would for example not have enabled an analysis of the meaning associated with the changes in the content of the template. At the same time, a quantitative method would perhaps have increased the validity of the study since the replicability would have been more straightforward. It would also have been possible to analyze a larger number of rating reports, for instance produced by different evaluators, and make a comparison of templates. Making causality claims between the micro, meso, and macro levels and revealing explanations for changes in evaluative practices may have been possible with a larger sample and a quantitative method.

Sampling of rating reports

As a first step in the process of capturing changes in evaluative practices, I have mainly relied on rating reports produced by M-CRIL. My rating report sample consists of 57 microfinance rating reports of 12 MFOs covering the time period 1999-2014. The type of sampling employed can be described as "purposeful," in the sense that the reports, or cases, were chosen to represent ratings of MFOs with certain attributes. These attributes or criteria were to a large extent decided prior to the execution of the study, rather than as the study progressed. As elaborated on below, the approach to sampling can also be described as "maximum variation sampling." Maximum variation sampling involves selecting a small sample with significant diversity in order to enable high-quality and detailed descriptions of each case, thereby demonstrating each case's unique properties, as well as highlighting shared patterns that cut across cases (Patton, 1990).

To gain insights into how evaluative practices change over time, I wanted to study ratings of a diverse sample of MFOs. However, in order to limit the heterogeneity within the sample, I sought to include the rating reports of a manageable number of MFOs. I also wanted to identify rating reports of MFOs with many rating updates over as long a timespan as possible. I sought out rating reports that covered as long a time period as possible in order to keep the rated organization constant over time, as well as to be better able to identify changes in the rating over time. Since M-CRIL was one of the first rating agencies to conduct MFO ratings globally and the first one to do so in India (beginning operations in 1998-1999), my

sample represents ratings from 1999-2014. Of the 12 MFOs whose cases were studied, three are represented with only one rating report (Annapurna, ASPL, and RGVN), since these were the only M-CRIL rating reports available for the years 2012-2014. On average, my sample includes 4.75 reports per MFO. A detailed list of the sample is included in Appendix 1.

Given that the Indian microfinance sector is characterized by heterogeneity in formal structure and explicit practices, and because it is unclear how different types of MFOs are evaluated, I also wanted my sample to represent this diversity. As such, the sample includes ratings of MFOs with varying predetermined attributes. To enable systematic comparisons and arrive at more robust results that can be generalized analytically, my main criteria for my sample selection, apart from number of updates and time span covered, were: (1) profit orientation and legal form and (2) microfinance delivery model. I wanted my sample to include both regulated, for-profit forms and unregulated, nonprofit forms, as well as MFOs that had undergone transformation from one legal form to another. As to delivery models, I sought to include MFOs that provided microfinance services via joint liability groups and self-help groups. Table 1 and Table 2 summarize these attributes within the sample.

Table 1. Legal form in sample reports

For-profit and regulated	*(15)*
Non-banking financial company	14
Private limited company	1
Not-for-profit and unregulated	*(37)*
Public charitable trust	16
Society	12
Section 25 company[16]	8
Cooperative society	1
Ratings of two MFOs in the same report	*(5)*
Public charitable trust and non-banking financial company	2
Society and non-banking financial company	3
Total	**57**

Table 2. Delivery model in sample reports[17]

Joint liability groups/Grameen groups	30
Self-help groups	14
Self-help groups and joint liability groups/Grameen groups	13
Total	**57**

To summarize, the variation in the sample is thus in the form of time, rating updates, profit orientation and legal form, and microfinance delivery model.

The sampling was constrained by the fact that I lacked direct access to M-CRIL's complete rating report database. Instead, the sampling process involved a dialogue with M-CRIL about my main preferences and considerations, and it was M-CRIL that made the final decision as to which reports I could include. However, in this respect, M-CRIL made a concerted effort to accommodate my requests and granted me access to all the reports

[16] An Indian "section 25 company" is a not-for-profit company formed under the Companies Act, 1956.

[17] Several of the more recent rating reports also describe MFOs extending loans to individuals.

that I asked for. As the work progressed, the sample grew in size, and more reports were included to confirm patterns and improve saturation.

In 2009, CRISIL compiled a report of the 50 biggest MFOs in terms of portfolio size, entitled "India Top 50 Microfinance Institutions" (CRISIL, 2009). In 2009, these 50 MFOs had outstanding loans amounting to INR 76,500 million[18] and nearly 12 million active borrowers. The reports that are included in my sample represent some of the biggest MFOs in India; out of the 12 MFOs in my sample, nine were on the top 50 list and seven were among the top 16 MFOs in 2009. Only three sample MFOs were not part of the top 50 MFOs (due to the fact that they were established late, in 2007, 2008 and 2012, respectively). The seven MFOs in my sample that were among the 16 biggest MFOs in 2009 had loans outstanding exceeding INR 37,000 million and nearly 6 million active borrowers, indicating that they together represented half of the Indian microfinance sector in terms of loans outstanding and reach.

As to comparing credit recommendations to actual funding, it was possible to make an assessment of 23 reports out of the total 57 reports in the sample. In these 23 reports, M-CRIL had made aggregate credit recommendations amounting to INR 5.80 billion. According to the subsequent rating updates, the aggregate actual flow of funds into the MFOs amounted to INR 6.66 billion. This means that M-CRIL's credit recommendations had been exceeded by approximately 15%. Again, although it is difficult to ascertain whether these funds were mobilized as the direct result of M-CRIL's recommendations, it is plausible that there may be a correlation between credit recommendations and actual funding.

When analyzing the sample MFOs according to changes over time in terms of "Members," "Active borrowers," "Portfolio size," "Average loan size," "Staff," "Staff productivity," "Return on assets," and "Portfolio at risk," the sample exhibits the same trends as the sector as a whole. This means that indicators such as "Members," "Active borrowers," "Portfolio size," "Average loan size," "Staff," "Staff productivity," and "Return on assets" have all increased while "Portfolio at risk" has decreased. Financial performance during the first five years of ratings was, for example, relative-

[18] From 1999-2014, the INR/USD exchange rate has fluctuated from 39-608 (Free Currency Rates, n.d.).

ly bleak compared to the years to come; from 1999-2004, more than half of the reports indicated a negative return on assets,[19] while in the 2005-2014 period, only five out of 33 reports documented a negative return on assets.[20]

Table 3. Annual spread of sample reports

	1999	*2000*	*2001*	*2002*	*2003*	*2004*	*2005*	*2006*	*2007*	*2008*	*2009*	*2010*	*2011*	*2012*	*2013*	*2014*
Reports	*2*	*0*	*4*	*4*	*7*	*7*	*6*	*5*	*3*	*5*	*5*	*1*	*2*	*3*	*2*	*1*
Cashpor	1						1	1			1	1				
GVMF	1		1		1	1	1	1	1	1	1					
SKS			1		2	1	1	1								
Spandana			1	1	1	1										
BWDA			1	1		2			1	1						
Mahasemam				1	1	1	1	1		1	1					
SNFL				1	1		1			1	1		1	1		
Grameen					1	1	1	1	1	1						
Guardian											1		1	1	1	
RFVN														1		
ASPL															1	
Annapurna																1

All sample reports provide one of the following rating grades: α+, α, α-, β+, or β.[21] There is only one instance in my sample in which the grade β- has been assigned (in the "Management" rating category of BWDA, 2001). This means that the sample MFOs have been assessed as having "very high safety and good systems" to "moderate safety and moderate systems" or as being "above investment grade" or "creditworthy" by the rater. Such rating grades represent reports of MFOs that generally are perceived as rather sound according to the raters; they are far from being "underdogs," and there are even a few "superstars" within the sample. The reports bestowing a grade of α+ served as especially interesting cases to confirm trends and patterns.

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[19] Out of the 24 reports from 1999-2004, 14 had a negative return on assets, eight had a positive return on assets, and in two reports, this indicator was not available.

[20] Out of the 33 reports from 2005-2014, five had a negative return on assets and 28 had a positive return on assets.

[21] No report in the sample has been rated gamma (γ), which denotes the highest risk.

Sampling within the sample

When analyzing the strength of the template, I analyzed a smaller sample within the sample. A discussion about how the concept of "strength" has been operationalized is presented in the following section. As to the sampling, I wanted to include reports from the early years as well as from the most recent years in order to enable comparison over time. When choosing which reports to include from both the early years and the most recent years, I also considered the rating grades assigned. To reduce "variance," I wanted to include reports from the two groups with equivalent rating grades.[22]

Given the main sample, and based on these two main criteria – year of rating and rating grade assigned – I was able to identify seven suitable reports from the early years of rating (1999-2003), here referred to as Group 1, and seven reports from more recent years of rating (2011-2014), here referred to as Group 2. The reports in Group 1 have been assigned slightly higher rating grades. Five of the Group 1 reports also represent the first assessments conducted by M-CRIL of these MFOs, while the reports in Group 2 largely consist of MFOs that have been rated before. The sample that was selected to analyze the strength of the template is summarized in Table 4.

[22] M-CRIL changed its rating scale from ten to nine grades in 2005 and again from nine to eight grades in 2010. However, the threshold for "investment grade" has always been at β; this is why I have decided, as a means of enabling comparison, to consider the grades α+++, α++, and α+ as belonging in a single grade group.

Table 4. Sample reports coded for descriptive and normative text

Year rated	*MFO*	*Grade*	*Governance*	*Management*	*Financial performance*	*Update*
Group 1 (1999-2003)						
1999	GVMF	α-	NA	NA	NA	0
1999	Cashpor	β+	NA	NA	NA	0
2001	GVMF	β+	α-	α-	β+	1
2001	SKS	β+	β	α-	α-	0
2001	BWDA	β	α-	β-	β+	0
2002	BWDA	β+	α-	α-	β+	1
2003	Grameen Koota	β	α	α-	β	0
Group 2 (2011-2014)						
2011	Guardian	β	β	β+	β	1
2011	SNFL	β+	β+	β	β+	5
2012	RFVN	β+	α-	β+	β+	0
2012	Guardian	β	β+	β+	β	2
2012	SNFL	β	β	β	β+	6
2013	Guardian	β	β+	β+	β	3
2014	Annapurna	β+	β+	β	β+	0

Structuring and coding the text

Structuring of categories, headings, and indicators

I first sought to understand how the rating format and the categorization of different headings and indicators in the reports had changed over the years. I developed a map showing how the reports are structured in terms of categories, headings, subheadings, indicators, tables, and graphs. Using this as a basis of comparison, I analyzed changes in the organization of the reports; how the raters structure the reports in terms of headings, subheadings, indicators, tables, and graphs, and how these practices have changed or remained constant over time. I was also able to track when the raters introduced a new heading or indicator into the reports and when they abandoned existing features. To understand the relative proportion of cate-

gories and headings, I examined how much space in the reports was occupied by each of the respective categories. This analysis was contrasted with changes in the rating weights as given by M-CRIL, along with benchmarks used and indications of changes in standards. I also analyzed changes in the design and layout of the reports. This step helped me develop an understanding of how the raters categorize different organizational features and how the relative weight of different rating categories as employed by the raters have shifted in content and importance over time.

Coding organizational elements

As I discuss in the theoretical model presented in Chapter 3, in developing a model via which to analyze changes in the organizational template, I have followed Suchman's (1995) paper, in which he distinguishes between different organizational elements used by intermediaries to bestow moral legitimacy on organizations, namely, structures, procedures, and outcomes. Although I was inspired by Suchman's (1995) typology of organizational elements, these had to be adjusted to fit the empirical context of microfinance rating reports. During the process of coding the rating reports, more detailed and operationalized versions of the three general organizational elements of structures, procedures, and outcomes emerged.

When analyzing how structural aspects of MFOs are assessed, my empirical investigation has focused on how the reports discuss the formal structuring of the MFO, its legal form, and the organization of power, delegation, and monitoring. Much of the text that relates to structural aspects can be found under the rating category "Governance." However, there are also passages elsewhere in the reports that elaborate on this theme, including the sections "Microfinance operations," "Organizational background," and "Internal control systems." The empirical material has thus been derived from all instances in the reports that include discussions pertaining to structures.

The rating reports evaluate the MFOs' procedures, techniques, processes, and systems in areas such as accounting, management and information, and human resources. One area that transcends many of these themes is how the reports discuss the relationship between the MFO and its target

constituency, i.e., the predominantly Indian women who access microfinance products.[23] The reports contain numerous accounts of this relationship through, e.g., group formation, group meetings, loan applications, loan appraisals, and financial transactions. Over time, the complexities involved in analyzing this relationship from a rating perspective have emerged, including factors such as how to represent and rate the MFO's procedures for assessing loan eligibility, its prepayment policy, and its procedures for dealing with defaulting clients.

One important conclusion drawn from the initial coding work, which is in line with earlier research, was that when analyzing the organizational element of outcomes in the context of microfinance ratings, a distinction should be made between social outcomes and financial outcomes. "Social outcomes" refer to intentional outcomes resulting from microfinance loans that cannot be explained using a commercial rationale. The main areas here include how the raters relate to the mission and vision of the organization; the MFO's definition of the target group; and which products and services that should be offered. Instances when the reports discuss these themes without considering their impact on the financial performance of the organization, they are coded as "social outcomes."

"Financial outcomes" refers to those outcomes that have a direct impact on the financial results of the organization. This includes an analysis of how the raters relate various financial indicators that impact the organization's financial performance, e.g., sustainability and profitability, growth, productivity and efficiency, and risk indicators. The following table summarizes the themes that were used to guide the coding of different organizational elements.

[23] I have chosen the terminology "target constituency" to refer to the individuals and groups of individuals that are associated with an MFO as the primary "target" for its interventions. The reports employ a broad repertoire of phrases, some of which only are present in the earlier reports and some of which emerge during more recent years, e.g., "clients," "customers," "members," "borrowers," "joint liability groups," "self-help group," "sangams," "centers," "federations," "group representatives" (e.g., "animators" and "leaders"), "women," "entrepreneurs," "beneficiaries," and the "field-level."

Table 5. Coding themes

Organizational element	*Structures*	*Procedures*	*Social outcomes*	*Financial outcomes*
Main coding theme	Legal form Ownership arrangements Role and responsibilities of board Place of board in organizational structure Formalities and organization of board work Eligibility for board participation Level of centralization/decentralization Internal hierarchy	Identification of operating areas and target constituency Assessments of target constituency Financial transactions Repayment procedures Relationship between target constituency and staff Relationship between staff and MFO Internal systems	Mission and vision statements Target group Products and services	Profitability Scale and growth Efficiency Cost Risk Interest rate

In total, 57 reports consisting of a total of 1,443 pages were analyzed. An average report contains around 25 pages and 45,000 characters (without spaces). The organizing and coding of such large amounts of text was facilitated by the data analysis software package NVivo (Vallance, 2005). NVivo was used to code the text into the abovementioned organizational elements. First, the rating reports were uploaded into NVivo. Thereafter, all text pertaining to the different elements and sub-elements was coded. I did not code all text in the reports; for example, I did not code text that was deemed to fall outside the various organizational elements identified in this chapter (e.g., financial statements).

When the coding was completed, the text was extracted based on the organizational elements of structures, procedures, financial outcomes, and social outcomes, as well as the abovementioned sub-elements. These groups of text were then organized chronologically. When the elements had been structured chronologically, they were deep-read and analyzed in an attempt to identify patterns and changes in how the elements were assessed over time.

The elements were also analyzed using a comparative approach whereby I looked for patterns and changes in how elements were assessed depending on the profit-orientation and regulated form of the rated MFO, as well as the operational model employed by the MFO (i.e., joint liability groups, self-help groups, and individual). I also noted when changes had not occurred.

To further strengthen the investigation, I conducted a simple word count analysis to show how certain terminology was associated with specific time periods in the ratings.

Coding descriptive and normative text

To analyze the concept of strength, I coded a sub-sample consisting of 14 reports, all of which were part of my larger sample.[24] Drawing inspiration from the field of ethics, the sampled reports were coded based on the following categories: descriptive text, normative value text, and normative prescriptive text (Burnor and Raley, 2010).

Descriptive text

Purely descriptive text includes general, factual descriptions of social objects and are either true or false. This type of text can contain causalities, and they can be historic, pertaining to the present time, or predictive (i.e., they can refer to the past, present, or make predictions about the future). Descriptive text can also include data such as performance indicators presented in tables and graphs. Descriptive text thus refers to the rater's observations of and comments about various organizational features,

[24] An extensive discussion of the sampling process is offered in the subsection titled "Sampling within the sample."

activities, and outcomes that do not include an explicit judgment about whether they are good or bad or what should be done about them. Instead, descriptive text describes the item being discussed, for example as high/low, decreased/increased, and focused/diversified.

Normative text

Normative text states whether something is good or bad, or whether an action is right or wrong. Normative text appeals to some norm, rule or standard and describes what the situation should be. There are two main subcategories of normative text: normative value text and normative prescriptive text. Normative value text includes an articulated value judgment of some kind, e.g., a social phenomenon may be judged as inadequate/adequate, reasonable/unreasonable, good/bad, and encouraging/discouraging. This type of text also includes claims of etiquette, prudential claims, and legal claims.

Normative prescriptive text includes suggestions and recommendations for actions, e.g., what the MFO should or should not do, according to the rater. Such statements include terms such as “should,” “ought to,” and “need to,” or they include specific recommendations and suggestions. Normative prescriptive text thus instructs how to get closer to the norm or standard. This type of text contains an explicit or implicit value judgment.

The coding was carried out on a sentence-level basis. Table 6 provides examples of how the coding rules have been applied; I have underlined the terms that motivated my coding decision.

Table 6. Sample extracts of descriptive and normative text

Descriptive text	*Normative text*	
	Normative value text	*Normative prescriptive text*
"Net operating margin for SNFL has increased sharply for 2010-11 on account of significant drop in Financial Cost Ratio (FCR)" (SNFL, 2011). "RoA at SMBT level dropped sharply during 2009-10 as the Loan Loss Provisioning was introduced at SMBTs and provisions on full portfolio was created during the year" (GVMF, 2011).	"ASA is taking steps to minimise overdues through incentive systems for the staff and steps like these have contributed to a much better recovery performance by the newer branches" (GVMF, 1999). "Decision making in CFTS is reasonably efficient, with responsibilities being delegated clearly all management and operational levels" (Cashpor, 1999).	"It should work on developing and implementing management systems that will enable periodic assessment of the programme on various performance parameters related to portfolio quality, efficiency and profitability" (BWDA, 2001). "Few issues in MIS, HR and Internal Audit too need to be addressed on immediate basis" (GVMF, 2011). "There is scope for further diversifying the portfolio by gradually reducing the exposure to animal husbandry loans which presently stands at 40% of the current loan portfolio" (GVMF, 1999).

I acknowledge that semantics is a complex field of study and that the intricacies of language go far beyond what can be detected by the simplified model presented above. Specifically, the fact-value distinction is an area of much debate and controversy (e.g., Putnam, 1998; Smart, 1999). However, in order to get a feel for the "strength" of the template, I had to make several compromises in the operationalization of the research question.

Several of the sentences excerpted above that have been coded as descriptive contain, for the seasoned microfinance expert, an implicit value judgment. For example, it is reasonable to assume that a low portfolio risk and a high return on assets are considered to be good. There are also many grey zones in which the terms used to describe a social phenomenon may be seen as both descriptive and normative, e.g., frequently employed words such as "moderate," "strong," "gain," "experienced," "qualified," "committed," and "motivated." While the first three of these terms have been coded

as value-loaded and thus normative, the latter four have been coded as descriptive.

Another challenging area is how to treat formal rules and text that addresses compliance with regulation. Although one may argue that the nature of such text is normative, it has not been coded as normative if it does not contain any explicit value statement (e.g., good or bad); see the example from RGVN (2012) in Table 7.

While recognizing that there may be a fine line between the domains of descriptive and normative language, I have decided to adhere to a policy of stringency in my coding work and have thus coded indeterminate or ambiguous samples as descriptive rather than as normative. Below are several examples of how sentences that may be interpreted as ambiguous have been coded.

Table 7. Sample excerpts illustrating the application of coding principles

Descriptive text	*Normative text*
"RGVN (NE) cites good staff behaviour and less time consuming meetings as its competitive advantage" (RGVN, 2012). "The organisation's financial sustainability in terms of its dependence on subsidies and its return on funds is low…" (Cashpor, 1999). "The high level of savings mobilisation has also translated into a high internal circulation of group funds as loans to members" (BWDA, 2002). "RGVN (NE) complied with the RBI guidelines by charging an interest rate of 26% per annum… Its practice of collecting stationery charge of Rs 5 from clients is not in compliance with the RBI guidelines" (RGVN, 2012). "The CEO has more than 21 years of experience in developmental activity" (Guardian, 2013).	"Sound development strategy and highly experienced Board and top management" (Cashpor, 1999). "Swayam Krishi Sangam (SKS) has a reasonably good performance on financial and managerial aspects but moderate performance on governance and strategy aspects" (SKS, 2001).

Contextualizing the text at the macro and meso levels

The phenomena in focus – i.e., evaluation practices, and particularly rating reports – may not be explained in isolation, but must be treated as an immersed part its environment. In order to develop a more nuanced understanding of changes in evaluative practices and in the template, I have drawn on Fairclough's (1995) multi-level framework when designing my research approach, including the three analytical levels of micro, meso and macro. While the micro level consists of the texts (i.e., the rating reports), the meso level focuses on the characteristics and situated vantage point of the producers of the rating reports, namely, the rating agency M-CRIL, and the macro level relates more broadly to events and trends in the sector.

To paint a picture of M-CRIL's role and position in the Indian microfinance sector, as well as in relation to the other rating agencies, to better understand how and why formal changes in the reports have occurred, and to get M-CRIL's viewpoints on changes in its rating system and in Indian microfinance as a whole, I conducted a series of interviews and relied on secondary material produced by M-CRIL and others.

Nine interviews were conducted with eight key individuals associated with M-CRIL, such as board members, founders, and staff, all of whom were selected with assistance from my chief contact, the founder of M-CRIL Sanjay Sinha. These meetings were spread out over a three-year period, between the years 2011 and 2013. Starrin and Renck (1996) describe the qualitative interview as a non-standardized but guided conversation. The interview method applied was a semi-structured one; I let the conversation flow freely, but used a prewritten questionnaire adhering to different themes to guide the conversation. All interviews were recorded and have been transcribed apart from two, during which extensive notes were taken. The interviews lasted from 45 minutes to three hours. Appendix 2 provides the list of questions used to guide the interviews. To complement the interviews, I reviewed most of the publications, reviews, articles, and policy papers produced by M-CRIL over the years.

To capture changes in the Indian microfinance sector, secondary material was used in the form of reviews, sector reports, and newspaper articles. To attain a better understanding of the other players in the sector, I conducted interviews with corporate rating agencies, regulators, and meta-organizations. A detailed list of respondents is provided in Appendix 3. In addition, a few CRISIL rating reports were analyzed to track changes in rating methodology over time.

I conducted a small but comprehensive market mapping of ratings in the Indian microfinance sector. I was able to amass and confirm historic rating data from all rating agencies active in the Indian microfinance space apart from one[25] from 1999-2014.

During the research process, I alternated between the different levels and studied developments and occurrences at the micro, meso, and macro levels in parallel in order to better understand and make sense of the rating reports.

Validity, reliability, and ethics

As a means to increase confidence in (Denzin, 1978), as well as complete (Shih, 1998) my findings, I have attempted at triangulating my empirical material. Triangulation refers to the observation of the research issue from more than one angle, and to use several methodological approaches. Denzin (1978) identifies four different triangulation forms, of which I primarily avail methodological triangulation and data source triangulation. First, I have combined different types of primary and secondary data from different points in time to validate my findings. My primary data first and foremost consists of the 57 rating reports in my sample. I have also compiled historical data on M-CRIL's and the other rating agencies' respective market positions during the time period 1999-2014. My secondary data consist of various material produced by M-CRIL over the years, as well as sector reports and analysis, government documents, and extant research studies. In addition, I use multiple sources of data to validate my findings (data sources triangulation). I have conducted interviews with M-CRIL and other

[25] SMERA never responded.

important players in the field. The interviews with M-CRIL were conducted at several occasions during the time period from October 2011 to May 2013. In Chapter 7, I discuss how the different data sources and methodologies were used to answer the research questions and support the findings.

As suggested by Morse, Barrett, Mayan, Olson, and Spiers (2002), I have, during the process of conducting my inquiry, also worked to improve the validity and reliability by implementing integral and self-correcting verification strategies. This has involved, for instance, making an effort to be actively responsive and open to new findings and theoretical insights. More importantly, this has meant that poorly supported ideas and paths that have proven irrelevant have been relinquished despite their personal importance to me. In addition, I have regularly presented extracts and individual chapters from my dissertation to academic audiences during research seminars and conferences and I have solicited comments and reviews from peers. I have also invited M-CRIL to review the manuscript and provide comments on the parts of this dissertation that specifically deal with that organization. The text was revised based on M-CRIL's comments in instances in which there were factual errors or misunderstandings.

As noted above, the sample size was expanded and more reports were included in order to confirm or deny the presence of overarching patterns. Although my sample includes a spread of reports from the genesis of the ratings in 1999 through 2014, I have relatively few reports from the period following the Andhra Pradesh crisis of 2010-2011 and the introduction of M-CRIL's third rating report format. This is due to the fact that demand for M-CRIL's ratings has gone down considerably and there are no reports available, according to M-CRIL. The analysis would have benefited from the inclusion of more post-crisis ratings in the sample.

Reliability is defined as repeatability over time, e.g., whether a different researcher would arrive at the same conclusions given the same research question. To increase what Merriam (1988) denotes as the "degree of dependence," I have striven to illuminate the assumptions upon which the study rests. More importantly, I have delineated in detail the research process and the technical steps in my analytical framework that eventually led to my conclusions. Further, I have worked according to clearly delineated rules within well-defined categories when coding the texts. This means that

my analysis has been far from the type of ill-defined process often described as a "black box" or "mysterious metamorphosis" (Merriam, 1988); rather, it has followed a rigorously delineated process.

More specifically, when approaching the rating reports, I have employed what can be termed a "directed content analysis" (Hsieh and Shannon, 2005), involving a mix of both deduction and abduction. Although I have not engaged in hypothesis-testing or verifying or falsifying already-existing theories, my research questions build on the neo-institutional framework and the inherent assumptions that underlie it. The rating reports were coded based on previously identified categories relating to the organizational elements of structures, procedures and outcomes, as well as descriptive and prescriptive text. Throughout the process of coding and analysis, I have carefully developed, revisited, and, when necessary, revised the themes in each coding category.

An alternative would be to have a more open-ended approach in which rating categories were developed based on the empirical material. Analysis of evaluators and evaluative templates constitutes a relatively nascent research area that has given rise to some intriguing research questions. Such a context called for a semi-deductive analytical strategy wherein the chief conceptual categories were already defined but were adjusted to the empirical material as the process progressed.

Finally, Kvale (1997) highlights three aspects of research ethics: informed agreement, confidentiality, and consequences, which are addressed in the following brief discussion of this study's ethical considerations. First, rating reports are generally publicly disseminated, and many of the rating reports that are included in my sample are widely available via various websites. Prior to the interviews, I introduced myself, and explained, in broad outline, the intentions of my study. Informed consent was reached in accordance with Kvale's definition. Throughout the research process, I have engaged in an ongoing dialogue with M-CRIL via Sanjay Sinha and Alok Misra. They have agreed to participate in the study.

Delimitations

Capturing the template: An iterative social negotiation process

In this research, I have chosen to focus on one single evaluator, M-CRIL. This allows for rich and thick descriptions and a profound understanding of M-CRIL's rating reports and the templates that these codify. At the same time, I acknowledge that I have adopted a relatively simplistic definition of the encoded template as a one-way projection by one rating agency. As I discuss in Chapter 3, it is likely to assume that the construction of the template is an iterative social negotiation process in which many players are actively involved. Although rating agencies may "uncover," or co-produce, the template, Greenwood and Hinings (1993) argue that two levels of analysis are pertinent; the institutional sector where organizational forms are legitimated and the organizations that enact these forms. I have here focused on the institutional arrangements as required by an institutional referent, i.e., M-CRIL. To include the materialized organizational level arrangements would, e.g., involve taking into the analysis how M-CRIL's encoded templates are understood, made sense of, and adopted by different organizations. Another missing part is to explore how rated organizations indirectly and directly try to influence and modify the template. Such a game most probably involve both power and interests and some actors may have more influence over deciding the faith of the template. Due to the inherent limitations of a doctoral dissertation, I have excluded an analysis of the MFOs. The analysis would probably have benefitted from capturing MFOs' reactions to ratings and delineating the role of MFOs in the social process of rating. At the same time, several prior studies have focused on organizational responses to evaluations, but few have concerned themselves with the role of the evaluator and evaluative practices per se.

Sampling bias

Hazelkorn (2012) notes that while there are more than 16,000 higher education institutions worldwide, rankings only capture the top 100. As with university rankings, any ratings system necessarily excludes a vast number of

entities. In the context of the current analysis, the sample is restricted to ratings conducted by M-CRIL. When doing the sampling, I recognize that there are biases. Only a certain type of MFOs decide to submit to the rating process, and of these, only a few are chosen to be rated by the specialized rater M-CRIL. It is for instance plausible to presume that only MFOs of a certain size, age, and degree of influence choose to subject themselves to rating, since the rating exercise is costly. In addition, a large proportion of MFOs are unlikely to be given the minimum rating grade required for them to be considered creditworthy, and as such, these organizations are less likely to ask for a rating (M-CRIL, 2006b). The above suggests that the MFOs in the sample have a certain level of legitimacy and recognition.

Further, MFOs that are not dependent on debt funding are less likely to pursue rating. For example, the Self-Employed Women's Association (SEWA) was only rated by M-CRIL during the agency's initial years of operation. SEWA is a labor union of impoverished, self-employed female workers participating in the informal economy; it has a membership of approximately 1.2 million women. Actors such as SEWA represent one type of organization that is excluded from this study. At the other extreme are organizations such as SKS Microfinance, which ceased its pursuit of M-CRIL ratings in 2006 and switched over to seeking ratings from the Standard & Poor's-controlled CRISIL. This decision probably reflects the fact that a corporate rater such as CRISIL lends more credibility in the eyes of the type of investors that SKS tries to attract.

As discussed, several MFOs in the sample have undergone transformations and transferred their microfinance activities to non-banking financial company structures. When this happens, the raters have continued to rate both entities for some time, and then have ultimately focused on the organization that engages in microfinance activities, i.e., the non-banking financial company. However, it is not always clear whether the surviving nonprofit structure is still operating. This means that organizations engaged in non-financial services that are related to microfinance are left out of the analysis.

At the same time, when recalling the discussion in Chapter 3, extant studies suggest that the encoded templates as projected by a significant

evaluator such as M-CRIL are disseminated in the microfinance field and addresses all members, rated and non-rated, of the field.

A beginning and an end

As to the time period analyzed in the study, there are no ratings available prior to 1999. This does not mean, however, that MFOs did not exist in India before that time. On the contrary, it is reasonable to assume that ratings were introduced when the sector had already been in operation for some time and was ready to pursue ratings. The advent of the ratings thus cannot be said to coincide with the genesis of Indian microfinance. Conversely, the most recent report in the sample does not represent the "end" of Indian microfinance.

Employing the above-delineated research design and methodological considerations, I now present an investigation and analysis of the micro level, namely, the report texts, which are here represented in 57 microfinance rating reports.

Chapter 5

Textual investigation and analysis of rating reports from 1999–2014

I have devoted this chapter to the first research question and its three sub-questions. I first present a textual investigation of the Micro-Credit Ratings International Limited (M-CRIL) sample reports from 1999-2014. Thereafter, I make an analysis of the empirical investigation and present the main findings. I have divided the textual investigation into three sections, in each of which I explore the three sub-questions (1a, 1b, and 1c) as developed in earlier chapters.

A textual investigation of rating reports from 1999–2014

M-CRIL's rating instrument

As a first step, I will investigate how the raters formally relate to their rating instrument in terms of how the reports are structured and how different organizational features are categorized. I will also discuss changes in how M-CRIL perceives the importance of different rating categories over time. As in most rating industries, M-CRIL's rating instruments and weightages are proprietary secrets. By tracking and analyzing how the reports have changed in terms of formal structure over time, I intend effectively to map M-CRIL's rating instrument and methodology, thereby exploring the fol-

lowing empirically driven research question: *How does the microfinance rating instrument change over time in terms of factors such as rating categories and sub-categories, indicators, and weightages? (Question 1a).*

Report format, structure, and design

Since the first microfinance rating report was completed in 1998, M-CRIL has made several formal revisions to its primary microfinance rating product. The agency has launched updated microfinance rating products twice over the years, once in 2007 and once in 2012:

- First format: "Micro-Finance Rating – Risk Assessment," 1999-2006
- Second format: "Credit Rating," 2007-2011[26]
- Third format: "Microfinance Institutional Rating (MIR)," 2012-2014[27]

The changes into new and revised products with new product labels have been accompanied with new designs; from black-and-white Microsoft Word documents in the early years, to color and two columns in the second format and colored PowerPoint presentations in 2011 before the "Microfinance Institutional Rating" was launched in 2012. The first pages of the three formats are provided in Appendix 4. According to Alok Misra, the chief executive officer of M-CRIL, this is also a way to meet the requirements of investors, who want brief and concise information (interview with Alok Misra, 30 April 2012). A summary of the main changes is found in Table 8.

[26] This rating report format was the result of a collaborative partnership between M-CRIL and MicroRate, which I describe in more detail in Chapter 6.

[27] This rating report format was the result of a collaborative undertaking between all four microfinance rating agencies, which I describe in more detail in Chapter 6.

Table 8. Summary of major revisions in M-CRIL's microfinance rating format

Year	*Product name*	*Design*	*Rating scale*	*Credit recommendation*	*Projected cash flow and financial statements for 5 years*	*Rating outlook*
1999-2001	Micro-Finance Rating – Risk Assessment[28]	Word document, 1 column, black and white	10 points[29]	Yes	No[30]	No
2002-2005	As above	As above	As above[31]	As above	Yes	No
2006	As above[32]	As above[33]	9 points[34]	As above	As above	No
2007	Credit Rating	Word document, 2 columns, color	As above	As above	As above	Yes
2008-2009	As above	As above	As above[35]	No[36]	No[37]	As above
2010	As above	As above	8 points[38]	As above	As above	As above
2011	As above	PowerPoint presentation, color	As above	As above	As above	As above
2012-2014	Microfinance Institutional Rating	As above	As above	As above	As above	As above

All rating reports contain a rating grade represented by one of the Greek letters α, β, and γ, sometimes in tandem with plus or minus signs.[39] The rat-

[28] The Cashpor rating from 1999 was, however, entitled "Microfinance Capacity Assessment."

[29] α+++, α++, α+, α, α-, β+, β, β-, γ+, γ

[30] The first report in my sample to have the category "Projected cash flow and financial statements for five years" is a report assessing GVMF from November 2001.

[31] The last report in my sample to use a ten-point scale is the report about Grameen Koota from December 2005.

[32] The last report in my sample to have this product name is about Grameen Koota, from February 2007.

[33] The last report in my sample to have this design is about Grameen Koota, from February 2007.

[34] α++, α+, α, α-, β+, β, β-, γ+, γ

[35] The last report in my sample to use a nine-point scale is the report about Cashpor, from July 2010.

[36] The last report in my sample to have lending recommendations is the report about Grameen Koota, from March 2008.

[37] The last report in my sample to have the category "Projected cash flow and financial statements for five years" is the report about SNFL, from July 2008.

[38] α+, α, α-, β+, β, β-, γ+, γ

[39] Farrington (2005) points out that M-CRIL's use of a Greek letter scale, as opposed to the traditional Latin, gives an indication that its rating product is different from other forms of rating products.

ing scale was revised once in 2005 from ten to nine points, and once again in 2010 from nine to eight points. In 2005, the top grade, α+++, was removed from the scale, and in 2010, the top grade, α++, was removed. However, M-CRIL has kept its minimum level for "investment grade" at β and above. When displaying the rating scale, M-CRIL also graphically indicates that the grades α+, α++, and α+++ all belong to a separate group.

Table 9. M-CRIL's rating scales from 1999-2014

1999-2005 10-point scale	2006-2010 9-point scale	2011-2014 8-point scale	
α+++			
α++	α++		
α+	α+	α+	
α	α	α	
α-	α-	α-	
β+	β+	β+	
β	β	β	Above investment grade
β-	β-	β-	
γ	γ	γ	
γ-	γ-	γ-	

Similar to a mainstream credit rating, M-CRIL's microfinance ratings also included exact recommendations on the absorption capacity of each microfinance organization (MFO) until March 2008. The grade β+ is the cutoff point between investment-grade/creditworthy, and high-risk, organizations. For MFOs rated β+ or above, a lending recommendation was made in INR or USD. Organizations achieving a β grade usually also received a credit recommendation. During the early years of rating, the reports also specified how much of the amount that was to be in the form of grant. Among the four specialized microfinance rating agencies, only M-CRIL's microfinance rating product has ever contained an exact lending recommendation (Sinha, 2008a).

Broadly speaking, although the reports have undergone changes in how they are formally structured, three main rating categories have been given a separate rating grade over the years.[40] These rating grades are weighted into a final rating grade for the MFO as a whole. The names of the categories have changed slightly over the years; for simplicity, the following labels will be used to refer to the three main categories:

- First rating category: "Governance"[41]
- Second rating category: "Management"[42]
- Third rating category: "Financial performance"[43]

As mentioned, exact rating weightages are proprietary secrets. However, in the 1999 reports, the rating weightages are explicitly described. The following table summarizes changes in rating weightages from 1999-2014; it contains information gleaned via interviews and e-mail correspondence with M-CRIL.

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[40] In the 1999 reports, the respective category rating scores are given as a percentage and not as a Greek letter.

[41] The following headings have been used for the first rating category: "Organizational indicators"; "Organizational aspects"; "Governance"; "Governance aspects"; "Governance aspects and strategy"; "Governance aspects and operational strategy"; "Governance and strategy"; "Governance and operational strategy"; "Governance and strategic positioning."

[42] The following headings have been used for the second rating category: "Management"; "Organization and management"; "Management/Resource indicators"; "Managerial factors."

[43] The following headings have been used for the third rating category: "Economic/Financial indicators"; "Financial performance"; "Financial."

Table 10. Changes in M-CRIL's rating weightages

Rating categories	*1999*[44]	*1999-2006* *First format*[45]	*2007-2011* *Second format*[46]	*2012-2014* *Third format*[47]
Governance	16%	20%	30%	40%
Management	38%	30%	30%	30%[48]
(Client protection and transparency)	Not present	Present in a grey box in the 2006-2007 reports but with 0% weight-age	Not present	(7-8%)[49]
Financial perfor-mance	46%	50%	40%	30%

What can be noted is that there has been a clear shift in rating weightages away from "Financial performance" to "Governance." The rating weight-age of "Financial performance" has decreased by 16-20 percentage points between the years 1999-2014, falling from 46%-50% to 30%. The rating weightage of "Governance," on the other hand, has gone up from 16% to 20% in 1999 to 40% in 2012-2014. According to Sanjay Sinha, however, the rating weightages are not followed strictly but rather are used as guide-lines for the raters.

> "However, since we do not use the rating tool strictly but rather rely on comparison with the rating grades achieved by other MFIs that we have rated recently, these weights are for guidance rather than specifically for scoring" (e-mail from Sanjay Sinha dated 21 August 2013).

Sectoral averages and upper-end figures

Since 2001, M-CRIL relates the rated MFOs' portfolio at risk[50] and operat-ing expense ratio with its peers by including comparisons, presented in ta-

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[44] Rating weightages as indicated in rating reports from 1999.
[45] These figures were gleaned from e-mail correspondence with Sanjay Sinha (20 August 2013).
[46] These figures were gleaned from e-mail correspondence with Sanjay Sinha (20 August 2013).
[47] These figures were gleaned from e-mail correspondence with Sanjay Sinha (20 August 2013).
[48] Interview with Gunjan Grover (25 April 2013).
[49] A sub-category entitled "Client protection" is included in the "Management" category.

ble form, with "upper-end" MFOs, as well as with the entire M-CRIL database. The "upper-end" figures reflect MFOs with either the top 10% scores or the top ten MFOs. In the second format launched in 2007, the comparison is extended to also include the two indicators "Return on assets" and "Borrowers per staff".

In 2003, M-CRIL claimed that its rating assessments rely on an instrument designed specifically for the conditions and nature of MFOs operating in Asia, and that its India rating grades are comparable with other M-CRIL ratings in the region (Mahasemam, 2003, p. 17). The figures provided in the reports from 2011-2014 only include comparisons with an Indian sample, while the "upper end" figures are removed. What is noteworthy is how the financial performance of the "upper-end" MFOs has changed in terms of decreased portfolio at risk and operating expense ratio and increased return on assets and staff productivity (borrowers per staff) over the years.

Table 11. Changes in key benchmark indicators in M-CRIL ratings

Sample	*Portfolio at risk (60)*	*Operating expense ratio*	*Return on assets*	*Borrowers per staff*
2001 (upper-end sample)	6%	20%	NA	NA
2005 (upper-end sample)	2.3%	17.8%	NA	NA
2007 (upper-end sample)	2%	14%	NA	NA
2009 (upper-end sample)	2%	13%	6%	300
2011 (overall India sample)	0.7%[51]	8.6%	6.8%	285
2012-2014 (overall India sample, non-Andhra Pradesh)	1.8%	11.7%	3.9%	270

M-CRIL notes that the performances of the "upper-end" MFOs or the overall database, respectively, do not necessarily reflect M-CRIL's rating standards (Mahasemam, 2003, p. 5), implying that there is potentially a dif-

[50] In 2011, the "portfolio at risk" indicator was changed from 60 days to 30 days, and in 2014 it reverted to 60 days.

[51] Portfolio at risk (30).

ference between how M-CRIL relates to sectroal averages on the one hand and to rating standards on the other.

There are a few occasions when the raters acknowledge that they have made adjustments in their rating instrument and in the thresholds used for different rating grades.

> "M-CRIL reviews the instrument based on ongoing experience and revises it periodically (roughly at two year intervals). This involves verifying the rating outlook with the actual credit performance. These revisions of methodology and instrument are based on advice from M-CRIL's Board of Directors comprising technical experts in the field of microfinance. In the past, reviews have led to the strengthening of the minimum conditions for various rating grades, capital adequacy norms, redistribution of weights across indicators, and the relative weights between the governance, management and financial sections of the instrument" (M-CRIL, 2006b, p. ix).

In the 2001 ratings of GVMF and SNEHA,[52] for instance, the raters note that they have adopted "stricter standards."

> "The lower overall rating grade is on account of dilution in concentration of operations, lower per member savings performance caused by a substantial number of new members in the programme, weak capital adequacy levels and the stricter standards (that are based on the changing outlook of the microfinance industry) that M-CRIL now employs" (GVMF, 2001).

> "The downgrade also results from the stricter standards (that are based on the changing outlook of the microfinance industry) that M-CRIL now requires on qualitative and quantitative parameters such as strategy and strength of field operations as well as capital adequacy" (SNEHA, 2001).

During the time period 2003-2005, M-CRIL has had a tendency to lower its assigned rating grades for those MFOs that already had been rated by M-CRIL. This means that there has been a negative shift between previous ratings and their updates.[53] M-CRIL explains these downgrades as being due to a strengthening of the rating methodology and increased minimum

[52] Reports of SNEHA are not included in the sample.
[53] Source: (M-CRIL, 2006b).

performance levels on critical indicators from 2003-2005. Differently put, from 2003 to 2005, the bar was raised, making it more difficult to attain a given rating grade. M-CRIL explains this as follows:

> "This is partly because M-CRIL's concern to keep up with the dynamics of the microfinance sector results in a continuous strengthening of its rating methodology and improvement in the minimum performance level on critical indicators for achieving particular grades. With better experience and stricter conditions applied in the update, ratings have resulted in downgrades for a number of rated MFIs sometimes *despite an improvement in some of their performance indicators*" (M-CRIL, 2006b, pp. 7, *italics* in original).

During the time period 2005-2007, there has, on the contrary, been a "positive" shift in the distribution of grades between previous ratings and their updates, implying that M-CRIL, in its rating updates, has had a tendency to upgrade MFO ratings. M-CRIL explains this by citing the "significant extent to which there have been improvements in the performance" (M-CRIL, 2007, p. 59) of many MFOs. As a result, the agency argues, modifications in the rating methodology have not been necessary.[54]

Alok Misra also explains that the rating standards differ depending on the age of the rated MFO.

> "For example, if there is an institution that is started in the year 2010 and you want to rate it in 2011 or 2012. It is just building its portfolio. I cannot expect the institution's operating expense ratio to be 8% as it still has not achieved the scale. It has to be given some leniency. On the other hand, if there is an institution which has been existent for the past seven years and its operating expense ratio is 16%, it will get penalized. You can't have a universal [standard]. The regional characteristics should also be considered" (interview with Alok Misra, 30 April 2012).

Indicators

An important part of the reports are the various indicators, ratios, and other data presented in table form or in different types of graphs. These include comparisons with other MFOs, as well as changes over time.

[54] Source: (M-CRIL, 2007).

Indicators mainly aim at capturing the financial performance or standing of the organization and can be grouped into several broader categories, although there are areas of overlap between these: portfolio/asset quality; capital adequacy and solvency; sustainability and profitability; growth and size; asset/liability management; and efficiency and productivity.

Two clear changes can be noted during the time period 1999-2014: (1) the number of indicators has changed, and (2) the type of indicators used in the reports has changed. To start with, in the 2001-2003 reports, there were 28 indicators in use. In the 2007-2010 reports, this increased to 46 indicators. In the 2012 reports, the number of indicators was reduced to 35.

As to the type of indicators employed by the raters, several changes can be noted. There has been an overarching emphasis on portraying the MFO's portfolio risk. Risk indicators became increasingly prevalent over time, especially after 2007, with the raters analyzing and displaying in graphs and tables the portfolio at risk from various perspectives, making comparisons of the portfolio at risk at different levels with sectoral averages, and presenting the MFO's loan loss reserves and write-offs. In the early ratings, the "Cumulative repayment rate" was a common indicator. In 2007, the "Cumulative repayment rate" was replaced by precise figures on the portfolio with arrears in short time intervals (e.g., portfolio in arrears 1-30 days, 31-60 days, and 61-90 days). During the initial years, the reports also tracked "Group-level savings," but this metric was abandoned after a few years. Until 2003, the "Subsidy dependence index" is used in the reports when discussing the organization's financial standing. This indicator was then removed; instead, "Return on assets" is calculated and presented. In 2008, the more financially oriented metric of "Return on equity" is introduced, only to be removed in 2009. There has been an increasing focus on tables and graphs that illustrate the MFO's growth and expansion in outreach and portfolio. Over time, the raters increasingly consider the MFO's debt leveraging and how well the funding is managed. Efficiency and productivity indicators are common in different forms; e.g., the metrics of "Cost to company per employee," "Cost per borrower," and "Active borrowers per members" are used in the later reports from 2007 but are abandoned after 2010. A detailed mapping of indicators is provided in Appendix 5.

Rating categories and headings

When analyzing categories and the headings used thereunder, there have been several changes over the years. It is possible to categorize the reports into three groups according to their heading structure: 1999-2006; 2007-2010; and 2011-2014. These groups more or less correspond to the three formal formats as developed by M-CRIL and described above. Below follows a mapping of how the structuring of the reports has changed over the years in terms of categories, headings, and subheadings; Appendix 6 provides a condensed account of these changes.

In broad outline, the rating reports can be divided into six main sections. In the first section, the rating grade is indicated along with the rating rationale, the strengths and weaknesses identified by the raters, and key indicators. The second section contains a background to and an overview of the organization and its microfinance operations. In the three subsequent sections, the three main categories that are being rated are discussed in detail, i.e., "Governance," "Management," and "Financial performance." The reports end with financial statements, future projections and appendices.

First rating category: "Governance"

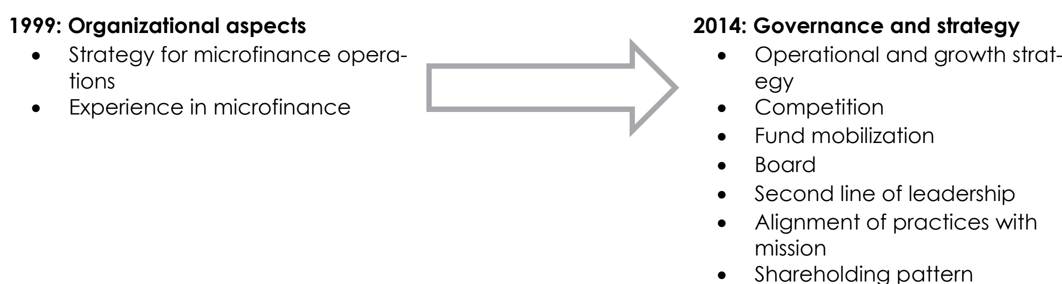
The "Governance" category includes a range of headings, which have changed as well as expanded in scope since the beginning of ratings. In the initial 1999 rating reports, the "Governance" category was called "Organizational aspects" and only included the two headings "Strategy for micro-credit operations" and "Experience in credit." "Organizational aspects" was changed to "Governance aspects" in 2001. The term "strategy" entered the heading in 2003 and changed to "Governance and strategic positioning" in 2007, and then to "Governance and strategy" in 2011.

The "Governance" category has changed incrementally over time, although there was a peak in 2006 when the number of headings and subheadings covered under "Governance" more than tripled from five in 2004 to 18 in 2006.[55] The amount of text space that the category receives in the

[55] In 2006, the topics included, among other things, the MFO's strategies in areas such as microfinance operations, growth and expansion, funds mobilization, leadership development, human resources, product development, and equity mobilization, as well as experience in microfinance; organizational structure; second line of leadership; competition management; board composition; interest rate structure; and

reports has more than doubled between 2001 and 2012, increasing from approximately 5% to 12%.[56] During the years 2006-2007, "Political environment/risk" is included as a subheading under "Governance." There has been an intensifying emphasis on expansion; for example, the heading "Strategy for microfinance operations" turned into "Operational and growth strategy" in 2007. Along with growth came the concept of competition management, which received a heading of its own in 2004. Other additions are "Mobilization of funds, which became a heading under the "Governance" section in 2006, and "Equity mobilization," which was a "Governance" heading from 2006-2008. In 2012, in the new rating product, the heading "Alignment of practices with mission" also was included for the first time as part of "Governance."

Figure 5. Changes in headings under the "Governance" category



Second rating category: "Management"

The headings covered under the "Management" category have also undergone some changes. In the early reports, the category included a heading called "Decision making"; however, it only appeared sporadically in the re-

political risk. In the 2012 reports, the "Governance" category had been boiled down to the following themes: governing board; alignment of practices with mission; operational growth and strategy; competition; second line of management/leadership; fund mobilization; and shareholding pattern.

[56] A simple assessment of the amount of space given to the "Governance" category in the reports was made by calculating the total number of words and the number of words in the "Governance" section. A sample consisting of six reports from 2001, six reports from 2006, and three reports from 2012 was used in this calculation.

ports from 2004 to 2006 and thereafter disappeared completely. Two new headings entered the “Management” category in 2007: “Staff productivity” and “Operating efficiency.” A few reports also included “Loan write-off” and “Analysis of accounting policies” as subheadings under “Accounting and MIS.” Two other notable changes include the additions of “Financial planning and cash management” and “Internal control systems,” which became headings on their own in 2006 after having previously been merged in the heading “Financial planning and control systems.” In 2011, “Internal control systems” was changed to “Internal audit and control.”

In the new rating product of 2012, a full section called “Client protection” that includes seven subheadings was added under the “Management” category. The heading “Quality of clients/member groups” is abandoned in most sample reports. Issues on client awareness that had been discussed under “Quality of clients/member groups” are, after 2012, discussed under the new subheading of “Transparency” as part of “Client protection.” However, issues pertaining to the quality and dynamics of the group have been eliminated completely.

Figure 6. Changes in headings under the “Management” category

1999: Managerial aspects

- HR quality and management
- Accounting and MIS
- Tracking system for overdues
- Financial planning and control systems
- Quality of clients/member groups
- Infrastructure
- Decision making

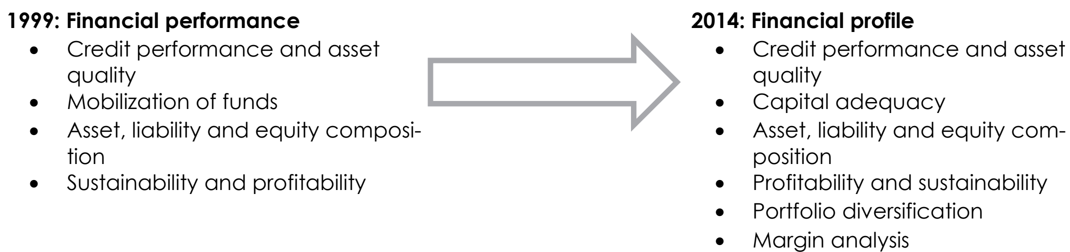
2014: Organization and management

- HR quality and management
- Staff productivity
- Operating efficiency
- Accounting and MIS
- Tracking system for overdues
- Financial planning and cash management
- Internal audit and control
- (Quality of clients/member groups)
- Infrastructure

Third rating category: "Financial performance"

The headings under the "Financial performance" category have remained relatively stable over time. One change is the heading "Asset, liability and equity composition," which first transitioned into "Mobilization of funds, equity and capital adequacy" and thereafter into simply "Capital adequacy" in 2011. There was also an addition of two new headings in 2012: "Margin analysis" and "Portfolio diversification."

Figure 7. Changes in headings under the "Financial performance" category



Non-rated sections

All reports are initiated with a section that includes the rating grade, the rating rationale, a summary of the organization's performance, and identified strengths and weaknesses. In the period 2007-2010, a lengthy subsection entitled "Country overview" was included in this section, and some reports also contain "State overview." Until 2006, this was followed by a section that includes "Organizational background" and "Microfinance operations," which later became "Microfinance operations." An organogram of the internal hierarchy was introduced in this section in 2005 as well.

In the 2006-2007 reports, a grey text box with the heading "Client protection and transparency" was included between the "Governance" and the "Management" categories; it is, however, not given any rating weightage (according to an interview with Sanjay Sinha, 12 October 2011) and it is unclear under which, if any, category it belongs. In this box, the following themes are addressed under subheadings: "Policy and mechanisms,"

"Communication and transparency," "Responsiveness to clients," "Fair pricing," and "Staff behavior." These subheadings are similar to the section "Client protection" that was introduced under the "Management" category in the 2012-2014 reports. In the 2012-2014 reports, "Client protection" is, however, given a 7% to 8% rating weightage (interview with Gunjan Grover, 25 April 2013).

The appendices, which are found last in the rating reports, become lengthier with time and come to include the profiles of board members and, in two cases, "Microfinance policies and products."

Structure of reports

Several interesting changes in how the raters categorize and emphasize different headings and indicators over time can be noted. Accounts associated with the MFO's mobilization of funds can be found under several rating categories over the years. In the early reports, such accounts were presented in table form in the unrated background section, as well as under a separate heading in the "Financial performance" category, indicating that this has an impact on the rating grade. In 2006-2007 and onwards, an assessment of the MFO's fund mobilization as well as its equity mobilization were also introduced under two separate headings in the "Governance" category, suggesting that fund mobilization was considered twice, or at least from two different angles, by the raters (see '(2)' in Appendix 6).

A closely related theme to fund mobilization that can be found under several different categories is that of organizational growth and expansion. The growth of the MFO, commonly measured in terms of outreach and portfolio, is presented in both text and table form in the unrated background section. Over time, however, this topic begins to garner an increasing amount of space under the "Governance" category, and in 2008, it is incorporated as a distinct heading, "Operational and growth strategy," and remains as such for the remainder of the period studied (see '(6)' in Appendix 6).

In 2007, the two headings "Operating efficiency" and "Staff productivity" were introduced under the "Management" category, along with graphs illustrating the MFO's developments in these areas. The operating efficiency (or the operating expense ratio) measures the MFO's operating expenses

(i.e., salaries, travel, administrative costs and depreciation expenses) in relation to the average loan portfolio. A large driver of operating efficiency is staff productivity. There are different variations of "Staff productivity" ratios that measure the number of (active) clients/borrowers per field/total staff. The MFO's "Operating expense ratio" and "Staff productivity" are also central indicators in the "Financial performance" category. This suggests that the two indicators "Operating expense ratio" and "Staff productivity" are considered more than once in the rating.

In 2007, the former "Management" category heading "Financial planning and control systems" is divided into two distinct headings: "Financial planning and cash management" and "Internal control systems." Cash management is also partly discussed under the "Financial performance" category "Asset, liability and equity composition" (see '(7)' in Appendix 6).

The heading "Quality of clients/member groups" was removed from a majority of the reports after 2012. Instead, issues pertaining to client awareness that had been discussed under this heading came to be discussed under the new subheading of "Transparency" as part of "Client protection." In the same time frame, discussion of issues pertaining to the quality of the group was abandoned completely (see '(8)' in Appendix 6). An analysis of the headings suggests that the role of the group began to receive less attention, as was also the case with the topic of decision-making, which was abandoned completely in 2007.

Evaluating organizational elements

The mapping process described above has exposed changes in M-CRIL's rating instrument in terms of which empirically defined organizational features are included in the reports, how these are categorized by the raters, the relative weightage assigned to different categories, and in the indicators used. This exercise entailed a hands-on mapping of concrete changes in how the reports are structured. However, it did not help explain how more theoretically derived organizational elements such as structures, procedures, social outcomes and financial outcomes are evaluated. Nor do I know how potential tensions are dealt with in the reports. To further the analysis of changes in the template, I will now apply the theoretical model as devel-

oped in Chapter 3 on the sample of 57 M-CRIL rating reports in an attempt to explore the texts in a framework guided by the following research question: *How does the template change in content over time? (Question 1b).*

When analyzing changes in the rationales and justifications used to evaluate the core organizational elements of structures, procedures, social outcomes, and financial outcomes in the reports, three different rating regimes, or templates, were identified: Template I from 1999-2004; Template II from 2005-2011; and Template III from 2012-2014. This section presents these three templates. This section is closely rooted in the nuances and details of the accounts in the reports in order to allow the reader to develop a strong sense of the material. As such, this section contains many quotes and excerpts from the report.

Template I: 1999-2004

Template I: Structures

The structural aspects of MFOs were afforded limited attention in the reports from the period 1999-2004. The concept of governance, for instance, is only gradually introduced into the reports during this period. In the early years of rating, the term "governance" was not used; instead the terms "organizational aspects" and "organizational indicators" were used to refer to issues pertaining to the board, organizational experience, and strategy; these are topics that were later referred to as "governance and strategy."

COMMUNITY OWNERSHIP AND TRANSFORMATION HESITATION

Closely linked to the issue of governance is the assessment of the MFO's legal form. Of the 24 reports from 1999-2004, 19 assessed nonprofit societies and trusts, one assessed a private limited company, and the remaining four were ratings of for-profit and regulated non-banking financial companies. Many of the ratings of nonprofit legal forms (i.e., trusts, societies, and section 25 companies) discuss how the organizations are involved in a broad range of development activities apart from microfinance, e.g., health, education, and veterinary services. The raters see it as important that the rated organization distinguishes between specific microfinance activities and any other non-credit activity.

> "Microfinance is ASA's largest programme. Apart from this the other programmes in which the organisation is involved in are: Networking federations to address social issues; Community training on Dalit empowerment issues; Awareness campaigns on different government programmes and on local governance; Training NGOs and government bodies on PRA. (…) The credit and non-credit activities are clearly demarcated and two separate executive directors, are in charge" (GVMF, 2001).

> "Though SKS prepares audited financial statements separately for the microfinance operations, a lot of the microfinance programme expenses are charged to the SKS NGO or grant accounts which is not a true indicator of the programme's performance" (SKS, 2004).

During the initial years of rating, little attention was given to the legal status of the rated MFO. Gradually, however, the topic of transformation began to emerge and increase in significance. Transformation refers to the process by which the nonprofit and unregulated MFO either transforms into, or transfers its microfinance operations to, a for-profit and regulated non-banking financial company.

The reports describe how several of the MFOs have plans to transform their microfinance operations into non-banking financial companies. However, the non-banking financial company structure is initially regarded as challenging and risky, and the raters give two main reasons for this. First, non-banking financial companies are constrained by the regulator to mobilize savings, while trusts and societies are under less rigorous regulatory control. Savings mobilization was, as discussed in the following sections, a typical MFO activity in the early sample. Second, the boards and management teams of the rated MFOs were not deemed qualified enough to take their respective organizations through the transformation process or to handle the regulatory demands imposed on non-banking financial companies. Factors such as these rendered the raters uneasy about the prospect of transformation.

> "Transformation process: BWDA has taken over an NBFC to carry forward its microfinance programme. NBFC requires stricter compliance in view of stringent RBI guidelines, and hence more management control. The relative inexpe-

rience of BWDA has made the transformation process critical and any lapse might lead to operational difficulties" (BWDA, 2004, 2nd update).

"Key risk factors. (…) Legal transformation: SKS proposes to establish an NBFC for microfinance operations that would lend to a large number of Mutual Benefit Trusts (MBTs) promoted by the organisation. The proposed legal transformation would introduce uncertainties with respect to management control, nature of relationships between the numerous entities, which in turn could induce a degree of risk" (SKS, 2001).

The dominant idea at the time was that the non-banking financial company should be, at least in part, community-owned. This was to be made possible by mobilizing savings among the target constituency, which was to be formalized under mutual benefit trusts. The mutual benefit trusts in turn use the savings as equity investment in the non-banking financial company (e.g., Mahasemam, 2005). Another transformation alternative presented in the SKS rating reports is to direct grants from donors to the target constituency, with the condition that the grant money must be invested as share capital of mutual benefit trusts. The mutual benefit trusts subsequently reinvest the funds as equity in the non-banking financial company.

"ASA has been contemplating transformation into an NBFC to carry out its microfinance programme over the past two years. For this purpose, it has registered its branches as Mutual Benefit Trusts (MBTs) over the past year. Mr Devaraj, the Managing Trustee and Gram Vidiyal is the Settler for all the MBTs. These MBTs are to be the equity holders in the NBFC. The Grameen Foundation has provided grant support worth Rs 10 million to these MBTs through ASA to invest in the NBFC" (GVMF, 2004).

"Spandana plans to transfer its microfinance programme to a separate company. The application for obtaining an NBFC (Non-banking Finance Company) license from RBI has already been made… With questions about the acceptability of converting member savings into equity through a mutual benefit trust, the transformation into a formal and regulated entity needs further consideration" (Spandana, 2004).

When the issue of transformation into a non-banking financial company that is partly or fully community-owned emerges, governance is often

brought up as an area that needs to be addressed. The transformation plan of SKS, which involves ownership and board representation of the target constituency, poses governance-related problems for the raters, as the target constituency is perceived to be unqualified as board members of a non-banking financial company and the organization risks losing control.

> "Lastly SKS plans to convert its legal status into an NBFC that will be owned jointly by its clients, employees and a group of foreign investors. (…) The proposed Board of Directors consists of the representatives of management, representatives of the MBTs and other equity investors. This change in the organisational structure would mean a substantial change in the control structure and the resultant decision making process. (…) However given the fact that SKS wants to give members a stake in its proposed NBFC structure, the quality and awareness of its groups is inadequate for the management of the ownership responsibilities arising thereafter" (SKS, 2003, 1st update, underline in original).

The example of SNFL merits mention, as the organization has a rather unique organizational setup in that it is already a non-banking financial company that is fully owned by mutual benefit trusts, which are called SMBTs. SNFL and the SMBTs have separate boards of trustees. The board of the SMBTs consists of nine to ten trustees: three are nominated by Loganathan, who is the settler of all SMBTs and also the promoter, secretary, and executive director of the mother organization; four trustees are elected from the general body of the member self-help groups; and two to three trustees are co-opted from the local areas. The raters argue that this arrangement poses a risk to the organization, as the trustees are potentially unqualified and too much power may be vested in any one individual member.

> "One area of concern that remains unattended is the long-term governance system of SMBTs. As of now, the governance system of SMBTs largely remains vested with the settler, Mr Loganathan. The caliber of trustees of SMBTs in terms of governance remains to be established. This coupled with the lack of a proper succession planning poses a serious risk in terms of long-term governance control of organization" (SNFL, 2003).

GOVERNANCE MODEL: INTEGRATED, LOCAL, AND INCLUSIVE

In discussions of the role of the board during the initial years of rating, a notable characteristic emerges: such instances are relatively sparse, and the discussions are typically brief. Little elaboration is presented, for example, about the relationship between the board and the executive management. The early reports commonly describe how the chief executive officer/director is part of the board along with senior staff members, and both the board and the management engage in policy decision-making. In the first two examples from early ratings of Spandana and Grameen Koota, the MFOs receive scores of α- and α, respectively, in the "Governance" category, indicating that their governance models were seen as strong.

> "Spandana now has a seven-member board that includes the Director (Ms Padmaja Reddy). The present board members are all professionally qualified. The board has a diverse composition with participation from NGO leaders, a Christian priest, housewives and senior organisational staff" (Spandana, 2001).

> "Grameen Koota, which focuses only on microfinance, has a thirteen-member board. The board meets biannually and amongst others consists of client representatives, two staff members and two trustees. Though the board was formed only in 2001 and the organisation has had only two board meetings so far, it has drawn substantially from the experience of its one active board member, who has provided both policy and operational direction" (Grameen Koota, 2003).

Having first-hand knowledge of local conditions is highlighted as a positive quality of board members.

> "Since all staff and board members are from the local area, awareness of local conditions is very good and decisions are taken in a consultative manner" (Spandana, 2001).

> "The board members have long experience of development activities and good knowledge of the local area" (BWDA, 2004, 3rd update).

During the early rating years, the raters describe internal decision-making processes and the role of staff with words such as "participative," "demo-

cratic," and "effective," and staff members at different levels are encouraged to take an active part in decisions that are both operational and policy-oriented in character. First-hand knowledge of local conditions is also highlighted as a positive quality of staff members.

> "Most decisions for day to day planning as well as deciding broader policy issues are taken by a core committee of ASA which consists of the Head Office staff and representatives from the branches. Overall decision making is reasonably participative as consultation with other stakeholders of ASA does take place in decision making. It is further possible to increase the level of inputs of branch level staff in operational decision making" (GVMF, 1999).

> "The decision making process at BWDA is quite participatory. All the district and block Coordinators are members of the Sub-Committee and decisions are taken in a democratic manner. A staff discussion is held prior to board meetings and the issues arising thereof are discussed during each board meeting" (BWDA, 2002).

The target constituency is also seen as an important group in decision-making at different levels, including the group level, operational level, and policy level.

> "The board of the organisation also consists of six elected group members, which reflects the involvement of clients in the policy decisions" (Grameen Koota, 2003).

> "The board of the organisation is reasonably qualified and experienced in microfinance. The inclusion of two group representatives helps to focus on issues directly relevant to clients" (Mahasemam, 2003).

Raters also note the importance of capacitating the target constituency to enhance its participation in board decisions; in the 2001 GVMF rating, e.g., the MFO's efforts to increase the decision-making capacity of the target constituency are commended.

> "ASA is governed by a six member board which is headed by Mr S Devraj as the Chairman and Managing Trustee. Out of the remaining five members, four are academics and one is a federation leader. The board meets three to four

> times during the year and discusses broad policy issues (…) In 1997 [ASA] began organising the SHGs into block level federations called 'Gram Vidiyal' (…) The introduction of the Gram Vidiyal has enabled substantial participation of members in policy formulation. At the same time, the focus on awareness generation and constant training of members has strengthened the quality of membership" (GVMF, 2001).

Finally, the raters encourage the implementation of internal audits. During these initial years of rating reports, the internal audit function is categorized under the head office, and the audit reports are sent to the executive manager, thus limiting the audit exercise to the branches.

> "ASA has established a separate internal audit department at the head office. (…) Separate internal audit reports are prepared and sent to the head office every month. Based on these the head office conducts surprise visits to selected branches. However, though the organisation has good internal audit systems in place, it is facing a resource crunch thereby limiting the efficiency of these systems" (GVMF, 2001).

Template I: Procedures

POVERTY TARGETING

In the early reports, the sample MFOs are described as being regional in their outreach scope. This "geographical concentration" is also acknowledged as a "key strength" in many reports. The raters assess the portfolio diversification in terms of loan purpose, e.g., animal husbandry, trade, agriculture, and consumption, and not in terms of geographical coverage, i.e., several states and/or districts within states.

Targeting and client identification, referring to the processes via which the MFO selects the area to work in and identifies eligible group members in the given villages, are described at length in the reports under the sections "Microfinance operations" (in the background section) and "Strategy for microfinance operations" (under the "Governance" category). The early reports contain descriptions of the village selection process, which commonly includes poverty assessments, as well as the subsequent step of identifying group members according to the MFO's own eligibility criteria. The following excerpt illustrates how this process is described.

> "Generally for this process to be effective a new branch (area) is selected based on predefined criteria, which include village density within a 15 km radius of the proposed branch, presence of commercial banks for smooth fund management, communication facilities, a diversified economic activity base and a peaceful environment. (…) The criteria for village selection are the level of poverty, which is determined through informal conversations with the local people in the target village. In addition, there should at least be 40 poor households; the number required for one Centre. The Staff gather this information through informal conversations or make estimates from census data stored at the SKS or the local mandal office. Apart from this, the decision to start work in the new village is made based on other factors like road accessibility and political stability and safety, so that there is effective management of the programme" (SKS, 2003, 2nd update).

CAREFUL GROUP SELECTION

In the 1999-2004 reports, the process of forming and grooming groups – commonly referred to as "group formation and regularization" – is described in depth. This step is preceded by the village/area selection process and followed by the loan application process. This activity takes up considerable space in the reports under the category "Microfinance operations"; accounts are provided of the MFO's considerations regarding member selection, group composition criteria, different types of organized meetings, trainings offered by the MFO to the group, activities undertaken by the group, as well as the final formalization of the group, e.g., by means of passing a test or by opening a joint bank account. In the SNFL 2002 report, the description of the group forming and grooming process takes up approximately one-tenth of the entire text of the report. Below is an extract from the SKS 2003 (1st update) report.

> "After selection of a particular village, entry point meetings called group projection meetings are conducted to inform and sensitise the village about the organisation, its objectives and the services it proposes to offer. The larger projection meetings are sometimes followed by mini-projection meetings of smaller groups. Group formation begins after this wherein 5 member groups are formed based on pre-specified criteria of eligibility and group composition like economic status, age, marital status and mutual trust. Homogeneity in groups formed is ensured through parameters like age categories. At this stage, a housing survey is also conducted to classify potential members according to

their poverty level, assessed on the basis of asset ownership and income. SKS defines the very poor as its target clientele and 50% of all its clients come from that category. Neighbours are encouraged to be part of a group, whereas not more than one member per household can be part of the same group. Other homogeneity criteria, as set out by the organisation are also applied at the time of group formation. The preliminary groups thus formed are subjected to a 5 day systematic training programme called the Compulsory Group Training (CGT)" (SKS, 2003, 1st update).

What is noteworthy in these extracts, apart from their detailed nature, is the importance placed by the raters on the concept of group homogeneity, implying that the MFO is not only expected to form groups, but also to take into consideration the internal composition of the group.

INDEPENDENT GROUPS

In the early reports, the raters encourage the MFOs that employ the self-help group approach to build groups that are "strong" and engage in issues other than strictly financial concerns.

"Strong groups are the key strength of BWDA's microfinance programme. The groups confidently manage their own affairs, maintain their own accounts and take decisions. The groups meet once a week and the attendance during these meetings is good. Several groups have taken the initiative (with support from BWDA staff members) to access bank loans directly and their repayment performance on these loans is good. The overall savings and credit performance of the groups is quite good. Groups visited have also shown the capacity to undertake other development work in their villages, such as obtaining government drinking water supply connections for the village" (BWDA, 2001).

Although less elaborated upon, the raters also note such behavior in the reports of MFOs employing the joint liability group approach.

"Soon after the initiation of savings activity, loans are extended to group members. All credit transactions take place at the group-level. Apart from the regular microfinance meetings, a separate monthly meeting is organised in all villages/slums where discussions are held on other issues such as the education of girl children and savings" (Spandana, 2004).

> "Moreover, a Centre Fund contribution is also compulsory for all members. Under this, a member has to save Rs 1 per week for the centre. The fund thus created can be used for a common social function" (GVMF, 1999).

The reports comment on how accounting records are maintained at the group level and whether this activity is undertaken by the group, the group's leader/animator/secretary, or by MFO staff. The raters do not seem to differentiate between self-help groups and joint liability groups in this regard; instead, all groups are encouraged to take on the activity of keeping records of financial transactions. The below extracts are from rating reports of MFOs that promote joint liability groups. It is noteworthy that the raters also seem to expect the MFO to empower the groups to manage their own financial records.

> "With ASA field staff undertaking accounts keeping at the centre meetings, members do not play an active role in this. Efforts at strengthening the functioning of the groups need to be continued" (GVMF, 1999).

> "Group meetings concentrate largely on financial transactions and are conducted efficiently. (…) Members are mostly illiterate and are not trained to maintain accounts on their own – these are maintained by the centre manager and the centre leader crosschecks the entries" (Grameen Koota, 2003).

Another group-level activity that is highlighted in the early reports of those MFOs that work with self-help groups is that of mobilizing and circulating savings at the group level. The joint liability group approach may also involve a savings component, but the savings are collected by and kept with the MFO. Group-level savings are either deposited in a bank account (external to the MFO) and/or are used as internally circulated funds in the group at an interest rate decided on by the group itself. The MFO can encourage and facilitate this type of saving and internal lending activity, and it can also use the group's savings behavior as a criterion when assessing the group's eligibility for an external loan. The following excerpts demonstrate the positive response to group-level savings exhibited by the raters.

> "BWDA has also been quite successful in mobilising savings at the group-level – the average savings per member stands at Rs 1,100 (31 December 2000). The

high level of savings mobilisation has also translated into a high circulation of group funds as loans to members" (BWDA, 2001).

"Visited groups also exhibit good management capabilities in handling large volumes of internal funds, as reflected by high group-level savings and an impressive internal circulation of group funds as loans" (SNFL, 2002).

Further, the group-level savings only appear in the group's own records; they are never represented in the financial statements of the MFO, they cannot be used by the MFO for on-lending, and they are, at least not formally, collateral, although the groups can choose to use them for repayment of delinquent loans (e.g., BWDA, 2004, 2nd update). In the rating of BWDA, the raters also encourage the MFO to track defaults in the internal savings pattern.

"During the rating team's visit to some of the SHGs, instances of internal default by members were observed. (…) …tracking of delinquent individual borrowers is not adequate. (…) However, if internal default increases and goes unnoticed by BWS, it may increase the incidence of delinquent individual borrowers… (…) BWS should also track internal circulation within the SHGs and prevent any abnormal rise in internal defaults" (BWDA, 2004, 3rd update).

The amount saved at the level of the group, and thus not collected by the MFO, is indicated in a table entitled "Microfinance programme: (Operational highlights)" in all reports of BWDA, SNFL, and Mahasemam until 2004, 2002, and 2004, respectively; e.g., in the 2002 report of SNFL – a non-banking financial company applying the self-help group model – the quoted figure that had been saved at the level of the groups amounted to almost INR 40 million.[57] As mentioned above, these funds are outside the control of the MFO and are not included in its financial statements.

The early reports also record the capability of the group in making decisions at the level of the group and the center (a center is a cluster of groups).

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[57] From 1999-2014, the INR/USD exchange rate has fluctuated from 39-68 (Free Currency Rates, n.d.).

> "Members can be encouraged further to take a more active role in operational issues and transactions at the Centre level" (Cashpor, 1999).

> "ASA's focus on regular group training at the centre level meetings has generated awareness on a variety of issues and has increased the members' decision making capacity and their ability to enforce norms" (GVMF, 2001).

In the early reports, the raters describe the process and the criteria used by the MFO to determine if and when the group should be granted an external loan, commonly involving a grading exercise to assess loan eligibility. Such assessments are based on group-level aspects pertaining to savings behavior, meeting culture, and time elapsed since group formation. The following excerpts illustrate how the raters describe the process of loan eligibility.

> "SHG performance is then evaluated by the SMBTs or SNF on aspects like savings consistency, internal circulation of funds and attendance. Groups are graded (A, B, C or D grades) on the basis of the evaluation. Only the A and B grades of groups are eligible for external loans" (SNFL, 2002).

> "Soon after the initiation of savings activity, Income Generation Loans are extended to group members. These are provided to members in the group in the ratio of 2:2:1. Within 22 weeks from the date of group formation, all members in a group are eligible to receive loans. This is likely to be changed to 9 weeks in the near future. All credit and savings transactions take place at the group-level and are compiled daily at the branch level" (SKS, 2001).

ZERO-TOLERANCE POLICIES AND STAFF INCENTIVES

In the earlier reports, the repayment culture was emphasized, and there was little, if any, room for accepting defaults. The raters acknowledge and encourage the implantation of so-called "zero tolerance" of arrears policies in order to reach and maintain a portfolio at risk close to zero.

> "The organisation has zero PAR which is a direct result of its 'zero-tolerance' policy for overdues wherein the Sangam Managers have clear instructions not to leave a centre meeting without collecting the day's due. In this the Sangam Managers take the support of the entire branch. In rare cases where the dues cannot be collected, the MIS recognises these as overdues on the same day and the BM initiates action" (SKS, 2003, 2nd update).

> "BWDA creates loan loss provisions based on ageing of its portfolio. Loans overdue for more than a year and a half are written off. The field officers are not told about the write off policy, in order to maintain the pressure of recovery on the groups" (BWDA, 2004, 2nd update).

Connected to the above is the issue of incentive systems for staff remuneration. In the 1999 rating of GVMF, this approach was welcomed as something innovative. The ratings describe incentive-based remuneration systems as mainly being based on repayment rates and number of clients reached.

> "Over the last one year ASA has also been computing the PAR for each member of the field staff – this forms part of the basis of an incentive system for compensation, and is an interesting and useful innovation. (…) ASA's credit performance is reasonable with a repayment rate of 90% and a PAR (>60 days) of 11%. Thus, most of the overdues to the organisation are usually in the range of 15-45 days. ASA is taking steps to minimise overdues through incentive systems for the staff and steps like these have contributed to a much better recovery performance by the newer branches" (GVMF, 1999).

SYSTEMS IN PLACE

The raters also place a significant amount of weight on the MFO's management and information system, accounting system, and tracking system for overdues, and there is considerable deliberation of the efficiency of internal procedures for collecting and monitoring data and the extent to which the systems are complementary to each other. Having adequate such systems in place is an explicit consideration in the "Management" category.

> "The organisation has demonstrated a focused strategy for microfinance and has attained high levels of portfolio quality and credit performance from its groups. However, the organisation needs some support to further upscale its management and accounting systems and skills, and therefore, in addition to the loan funding from SIDBI, capacity building support is also recommended" (Spandana, 2001).

There is also a push in favor of computerizing systems.

"M-CRIL strictly recommends that SIDBI should not disburse funds till the organisation has… computerised its MIS and developed an efficient loan tracking system" (Mahasemam, 2003).

"BWDA has good accounting and MIS. At present, the record keeping is manual but it is being computerised in the four northern branches and at the head office. It is expected to be fully operational by the end of this financial year" (BWDA, 2004, 2nd update).

Template I: Social outcomes

The early reports reflect a social orientation in terms of organizational outcomes. The eligible microfinance target constituency, for instance, consists of poor women, commonly in rural areas, who are organized into groups.

"CFTS has a very clear approach in terms of the degree of focus on micro-credit, involvement of women, identification of the poorest borrowers and development strategy for credit operations" (Cashpor, 1999).

"ASA has a very clear policy in terms of degree of focus on micro-credit, involvement of women and development strategy for credit operations" (GVMF, 1999).

"SKS aims to provide high quality credit and savings services based on the Grameen model to poor women in the Deccan region" (SKS, 2003, 1st update).

"Spandana places its main emphasis on strengthening the socio-economic status of women through use of microfinance services as a tool" (Spandana, 2001).

"BWDA has a clear development strategy of focusing on the economically weaker sections of society" (BWDA, 2001).

Template I: Financial outcomes

When assessing the financial outcomes of the organizations during the early years of the reports, the raters push for improved financial results in order to reach financially sustainable – and later on, profitable – operations. The

following excerpt from the report on SKS is illustrative of the rating rationale.

> "BWDA has weak performance on sustainability with its Subsidy Dependence Index (SDI) at 308.7%, which is, nevertheless a considerable improvement over last year's level of around 1 150%" (BWDA, 2002).

> "The organisation's financial sustainability in terms of its dependence on subsidies and its return on funds is low, mainly because it is a young organisation and needs some time before it can be financially sustainable. The Subsidy Dependence Index (SDI) of CFTS is poor and presently stands at 675%. CFTS's operating efficiency ratio is also poor and has been measures at a very high 376% (due to the present outreach and staff structure relationship), though this ratio should improve in the next one year with a rapidly growing portfolio and slower growth (than before) in the operating costs" (Cashpor, 1999).

When explaining the overall rating grade, the raters largely rely on the financial standing of the organization, at least in the explicatory text. The capital adequacy as well as the financial sustainability seem to be especially significant, with minimum threshold levels for the capital adequacy required in order to attain a certain rating grade. The following extracts illustrate the raters' standpoint.

> "The overall rating of GK remains unchanged despite improvement on all aspects, due to minimum conditions applied to the financial indicators: Capital Adequacy Ratio and Return on Assets. (…) The financial performance grade of GK is moderate at β. This is same as that in the previous rating. Although, [the] organisation has improved it performance on all financial parameters, the grade was restricted, as GK could not qualify the minimum standards set for the critical indicators like Capital Adequacy and Return on Assets." (Grameen Koota, 2004).

> "ASA shows growth in operations as well as improved performance on productivity, capital adequacy and profitability. It has improved its operating expense ratio significantly, but due to a decline in the effective interest rate necessitated by legal and political constraints in the state of Tamil Nadu, a negative return on assets continues. Whereas a consistent growth in operations, effective strategy to handle competition and the political environment, a decline in the operations expense ratio and an improved position on capital ade-

> quacy albeit slightly, are reasons for encouraging sign – these are not adequate to result in an upgrade in the rating as the low capital adequacy continues to be a matter of concern" (GVMF, 2004).

Template II: 2005-2011

Template II: Structures

THE NON-BANKING FINANCIAL COMPANY: REGULATION AND GROWTH POSSIBILITIES

The expression of doubts pertaining to the non-banking financial company structure that was observed in the earlier reports changes rather quickly, and the non-banking financial company becomes the endorsed legal form, while other legal forms are associated with problems and risks. Of the 27 sample reports from the period 2005-2011, 11 are of non-banking financial companies and 16 are of nonprofit trusts, societies and section 25 companies. Apart from BWDA, which had already undergone transformation into a non-banking financial company in 2003-2004, Grameen Koota, GVMF, Mahasemam, and SKS all registered or acquired non-banking financial company structures for their microfinance activities during the years 2005-2011, as described in the reports.

Over time, the raters begin to see it as increasingly necessary to operate one's microfinance operations under a non-banking financial company structure, and in the 2007-2009 reports, the raters have added the following general passage as part of the "Country overview" text.

> "Presently, there is no regulatory mechanism in place for mFIs except for those that are registered as NBFCs. NGO-mFIs, non-profit companies, and mutual benefit mFIs are regulated by the specific Act under which they are registered and not by the Reserve Bank of India. As such, they are not subjected to minimum capital requirements and other prudential norms."

The two main justifications for promoting the non-banking financial company structure in the reports are the regulatory framework, which includes stringent supervision under the Reserve Bank of India, and the growth potential associated with the non-banking financial company.

> "Another major point where BWDA scores over other similar MFIs in the state is the legal entity of an NBFC, which is more recognised and regulated" (BWDA, 2006).

> "Grama Vidiyal Trust's (GVT) microfinance operations were transferred to GVMFL, an NBFC, in January 2007. GVMFL was founded by the promoters of GVT to transform to a better regulated legal form enabling the organisation to mobilize equity from external and domestic financial institutions" (GVMF, 2009).

> "GK records good performance on governance with a grade of α. This is two levels up from the previous grade of β+ and has been brought about by transformation to more appropriate legal structure and simultaneously a remarkably stronger governing board" (Grameen Koota, 2008).

After 2006, the legal status of the MFO is only explicitly addressed under a specific heading for those organizations that do not operate as non-banking financial companies, and where the legal form thus is perceived as an area of concern. For those operating as non-banking financial companies, legal form is not an issue. In the sample, a few MFOs did not transform their microfinance activities into a non-banking financial company but instead opted to retain nonprofit status: Cashpor and Guardian are nonprofit section 25 companies during most of the sample period and Mahasemam is a trust (although it also has a sister-organization, which is a non-banking financial company, called SMILE that solely conducts microfinance operations). For these MFOs, the raters bring up and assess their respective legal forms. The main problem with not being a non-banking financial company relates to the constraints faced by such organizations in mobilizing equity (Tier 1 capital) to leverage funds and thereby achieve maximum outreach.

> "In view of the rapidly expanding portfolio and huge demand for microfinance in the area, the fund requirement for on-lending has increased considerably. MT's legal status as a Trust limits its fund leveraging capacity. Therefore, the group formation, and client related activities are all performed by MT, which earns a 7% fee for this services. However, this is not a formalised relationship and a formal contract might lead to potential service tax liabilities. While this is also an ingenious model to continue collection of savings (still a regulatory grey area for Trusts and Societies), it may not be suitable for MT in the long run.

The problem of capital adequacy also becomes a hurdle for further expansion, as the Trust cannot raise equity" (Mahasemam, 2009).

"Being a not for profit company, CMC has limited access to Tier 1 capital but it has done well to mobilise subordinate debt. The Tier 1 capital adequacy of CMC on 31 March 2010, was low at 4.7% but improved significantly from 0.2% on 31 March 2009. Its Tier 1 and 2 CAR was a reasonable 12.4%. Using the strict criterion for Tier 2 capital applied to the banking sector, CMC's CAR amounts to 9.4%. (…) CMC's financial performance is good with a grade of α-. The organisation achieved a much better profitability by a reduction in the OER, reduction in the financial cost ratio and also due to a change in accounting policy w.r.t. the recognition of income on assigned portfolio. CMC's CAR improved to 12.4% from 10.5% earlier. It was able to mobilise Tier 2 capital and also had internal profit accruals. However, CMC did not register improvement in its financial grade because of its limited Tier I capital (Cashpor, 2010).

LEGAL SEGREGATION OF ACTIVITIES

When the issue of transformation emerges, the raters reemphasize the importance of having focused microfinance operations; it is recommended that the non-banking financial company should concentrate solely on providing microfinance services. When MFOs undergo transformation into non-banking financial company structures, any non-financial, or "credit plus," service should thus be kept outside the organizational realm of the non-banking financial company, typically within the original nonprofit trust or society.

"The organisation received NBFC licence in January 2005 from the Reserve Bank of India (RBI) and the microfinance operations of SKS NGO were completely handed over to the NBFC in September 2005. SKS was promoted by Mr Vikram Akula and a few of his associates in 1997 and registered under the Societies Registration Act, 1860. (…) After gaining experience in development work, he decided to promote SKS to run a professional microfinance programme besides working on other areas like education and technology. With the formation of the NBFC, SKS NGO now works exclusively on education and other development programmes" (SKS, 2006).

In the 2004 report (2nd update), BWDA takes over a non-banking financial company called BFL. Apart from microfinance, BWDA engages in development programs such as veterinary services, reproductive health care, vocational training, and exhibitions for promoting the sale of products manufactured by self-help group members (BWDA, 2002). When the organization transforms, the development activities are kept under the aegis of the nonprofit BWDA, while microfinance activities are to be carried out under BFL. In the 2008 report, the raters appear to be displeased that BFL and BWDA have failed to segregate their respective financial and the non-financial activities.

> "Lack of a focused strategy: At present BWDA and BFL are involved with varied forms of microfinance and share the resources and systems to implement the same. This lack of a focused approach does not augur well for the future especially given the increasingly aggressive nature of the competition. (…) The CEO has multiple responsibilities for both BWDA (including its development activities) and BFL" (BWDA, 2008).

THE MONITORING ROLE OF THE BOARD

The raters' perception of the ideal character, place, and responsibilities of the board also changes over time; in the new preferred model that emerges, there is a clear separation between the board and the executive management, and the board's role as an overseer and controller begins to take shape. One area of responsibility that is increasingly attached to the board and which grows in significance over time is that of internal auditing. Internal auditing is discussed under a separate heading from 2006 onwards and receives its own heading in 2008, "Internal audit and control," under the "Management" category.

From 2005 onwards, it becomes increasingly common to encounter reports audit teams or audit committees that consist of selected board members and which report directly to the board as opposed to the executive management. In such a setup, the internal audit function can thus be found above the executive management level in the organizational organogram.

> "The internal audit function is reasonable. The organization has a 40 member internal audit team, led by the Chief Manager – Internal Audit. The internal

> audit team is divided into five teams of six members each. Each team audits one branch in a week. Thereafter, the respective team leader prepares the center visit report on a prescribed format and submits it to the Head of the internal audit. He then consolidates the report and submits it to the Board of Trustees" (Mahasemam, 2009).

> "The audit involves the thorough checking of all records and sample verification of client passbooks, apart from visiting kendras. (…) However, the present system of passbook verification on sample basis is clearly inadequate and needs to be done more frequently and should include a 100% passbook verification, especially since the field staff is allowed to make on the spot emergency loan disbursements to the clients from collections. The report for the main audit is sent to the Board" (Grameen Koota, 2008).

In the case of GVMF and Cashpor, the internal audits also cover the head office; for Cashpor, this implies that the executive management would be scrutinized and evaluated by the board members.

> "GVMFL has a good Internal Audit system. It conducts four types of branch audit. (…) Currently the audit involves a comprehensive audit of the branch operations. The internal audit team plans to commence the audit of Divisional offices, Regional offices and other HO departments. The IA team prepares audit reports and sends these directly to the CEO" (GVMF, 2009).

> "CMC's governance has strengthened with active participation of the Vice Chairperson in the Board and the audit committee (…) The audit department currently audits branch offices and district offices. The Board and the Audit Committee plans to bring Head Office departments in the ambit of the internal audit too. This will however, require substantial capacity building and an increased independence. The audit team will also need personnel from Accounts, ICT and other management domain apart from the microfinance operations. (…) CMC's Board has an audit committee, which consists of three senior board members. The committee receives a summary report from the internal audit department and provides strategic inputs to the department" (Cashpor, 2010).

INDEPENDENT AND EXPERIENCED PROFESSIONALS

There is a gradual move towards placing more emphasis on board composition and the qualities of individual board members, who commonly are re-

ferred to as "experienced professionals." During the early years of rating, the board is mentioned in more general and impersonal terms, but with time, more details about the individuals and their personal backgrounds, qualities, experiences, institutional affiliations, and roles in the board work enter into the reports. Below is an example of the detailed descriptions of the board members of GVMF in the 2008 report.

> "The newly constituted five member Board of Directors of GVMFL comprises of:
>
> - Mr S Devaraj – Founder of ASA, GVT and GVMFL. He has 30 years' experience in the development sector
> - Dr Rinnie Devaraj – Co- promoter, head and professor in economics, Holy Cross College, Tiruchirapalli, Tamil Nadu
> - Mr Chris Brookfield – Managing Director, Unitus Equity Fund
> - Ms Kim Totah – Co-founder and partner of McCabe and Totah, LLP
> - Mr Pasupathy Gopalan – VP Strategic Marketing and Corporate Business Development, Cypress Semiconductor Corporation
>
> The Directors are highly respected people in their respective fields and bring a lot of value to the Board of GVMFL. The diversified experience generates independent opinion and corporate culture" (GVMF, 2008).

Also, in 2007, the term "independent director" is first introduced, implicitly referring to a board member who neither owns, nor represents anyone who owns, any stake in the MFO; who is not a lender to the MFO; who is not an executive or member of the staff; and who is not part of the organization's target constituency. Since that time, the explicit call for independent directors with knowledge in and professional experience from relevant sectors, e.g., development, microfinance, finance, academia, social work, banking, and the corporate sector, became much more prevalent.

> "BFL has a ten-member Board. All 10 Directors are shareholders. An institutional representative in the form of SIDBI nominee has been taken on Board in August 2008. The members are experienced professionals and together hold significant experience in banking, academics and social work. However, the board does not have any independent director; this has the potential to ad-

versely affect the image of the organisation and/or the quality of governance in the medium to long term" (BWDA, 2008).

"Stronger governing board: The governing Board of the new entity consists of seasoned microfinance and corporate professionals. Three independent directors have been brought in, apart from investor and management representatives. The new Board can be expected to add significant value to the organisation" (Grameen Koota, 2008).

In the 2008 rating of Mahasemam, which is a registered trust, the raters use the logic of growth and organizational size to explain why the board in its current state is weak and should include qualified and experienced professionals.

"MT has an eight-member governing body consisting of the President Dr Sethuraman, his brother Mr Rajagopal, people from social development background and two representatives of SHGs. Out of the eight members, seven are part time trustees. (…) In view of the size of operations and its growth strategy, M-CRIL feels that the Board members experience in microfinance is limited and lacks diverse expertise. The MT Board could be strengthened by inducting some qualified and experienced professionals from the microfinance sector" (Mahasemam, 2008).

A similar scenario is set forth in a discussion of Grameen Koota, whose transformation into a non-banking financial company necessitates independent directors with relevant sectoral expertise, according to the ratings, as opposed to having unqualified staff and members of the target constituency as board members.

"GK continues to have a weak governing body. This weakness was pointed out at the time of last rating (in September 2005) also, but the matter remains unresolved. The governing Board does not have members with expertise in microfinance. Out of the 11 members, 9 are internal to the organisation. They are employees, clients and trustees of GK The other two are independent members, but do not have relevant experience to monitor and guide the organisation effectively. Thus, the decision making authority rests with the top management comprising of the CEO and COO. The Board meets on a half-yearly basis and has a low level of influence and involvement in operations. In the

> context of the emerging NBFC structure, taking independent directors and experts in the field of microfinance on the Board would add to the credibility of the organisation" (Grameen Koota, 2007).

In its 2010 rating, Cashpor, a nonprofit section 25 company, scores an impressive α in the "Governance" category. It seems as if Cashpor gets everything right, according to the raters: it has a qualified, well-connected, and independent board engaged in issues such as innovation, strategy formulation, and regulatory compliance, as well as in monitoring the performance of the management; and the administrative formalities are adhered to. On top of this, the board has demonstrated a commitment to ensuring that Cashpor's practices are aligned with its social mission.

> "CMC has [a] strong Board of nine members, comprising of one executive member, two nominee members representing the lenders and six external independent members. Board members are highly qualified and experienced at apex management level in banking, corporate and development sectors. The two Nominee Directors represent ICICI Bank and Dia Vikas Capital. (…) Governing Board of CMC is observed to be very strong and the organisation fairs very well on this parameter" (Cashpor, 2010).

THE DIMINISHING ROLE OF THE TARGET CONSTITUENCY

Members of the target constituency serving as shareholders and board members is regarded as problematic. This is illustrated in the ratings of SNFL, a non-banking financial company that acts as the lending arm of a unique and complex setup of organizations that includes mutual benefit trusts, which are called SMBTs, SNFL, and ASSEFA. ASSEFA is the original organization that started the development activities. SNFL lends to the SMBTs, and the SMBTs in turn lend to the self-help groups, which are formed by ASSEFA. SNFL exercises control over the SMBTs through the settler of all the SMBTs, who is the executive director and founder of ASSEFA. The self-help groups own the SMBTs and hold a majority share of the SNFL equity. Many of the trustees of the SMBTs are elected from the general body of the member self-help groups. They are perceived as unqualified by the raters, despite attempts at building their capacity, and the raters call for independent directors as board members of the SMBTs.

> "…the governance calibre of elected and co-opted trustees of the SMBTs is nowhere near the mark, in terms of providing strategic guidance and external interface. Though in past, SNFL has conducted capacity building programmes for board members of SMBTs from the grants received from SIDBI, they are yet to reach a desired level that requires intense and sustained inputs" (SNFL, 2005).

> "At the level of SMBTs, the quality of governance is weak and revolves around the office of SMBT Chairperson. Representation of SHG members on the Board does not significantly contribute to the quality of governance due to limited awareness and capabilities. (…) Absence of independent governing board members is a cause for concern at SMBT level" (SNFL, 2009).

During this period, the previously popular idea of community-owned non-banking financial companies is now challenged by the raters, who point to the lack of awareness and understanding that the target constituency has about their roles as investors and shareholders and the inability of the rated MFOs to handle such large numbers of shareholders, as well as the regulatory uncertainties pertaining to these situations.

> "The organisation has the strategy of encouraging its borrowers to invest in its equity. Fulfilling legal formalities related to issues of shares and providing information to shareholders has become cumbersome and expensive. Non-observance of the requirements of law and lack of clarity among the borrowers regarding the equity investment is a risk" (BWDA, 2007).

> "Mahasemam has mobilised a significant amount of client savings through the POWER Trusts, which have been used to capitalise SMILE Ltd, the NBFC. (…) Although the POWER Trusts invest only a part of the savings and maintain sufficient liquidity to manage payouts, the strategy of investing client savings mobilised by Private Trusts into equity of a for-profit company may not be an appropriate one in view of the absence of a clear regulation from the Reserve Bank of India in this regard. Another issue of concern is the lack of awareness among clients of the fact that their savings are being utilised to invest in a company and they, in effect, have ownership and voting rights in the company. Although the Savings Pass book provided to clients mentions that the savings are like 'ownership savings' (panguthokai semippu in Tamil, the local language), this has not been clearly explained to the clients in spirit" (Mahasemam, 2006).

The 2011 report describes how the organization is considering co-opting the SMBTs and turning them into branches.

> "SNFL is open to the option of converting the SMBTs to branches. (…) Due to overlap in functions of Chairperson and RM, SNFL plans to gradually abolish the post of Chairperson and replace them by RMs. However, removal of Chairperson in one visited SMBT has caused problems for SNFL as the Chairperson had gained political mileage in the area" (SNFL, 2011).

In 2006, the heading "Equity mobilization" enters the reports and the role of private equity starts receiving attention. The raters argue that, in order to sustain growth and improve their capital adequacy, MFOs should work to attract investments in the form of private equity instead of relying on savings mobilized by the target constituency.

> "The capital adequacy position of SNFL as on 31 March 2008 was reasonable at 24.0%, but is lower than the figure of 28.1% a year ago. SNFL is not prepared to obtain external private equity funding because it does not want to dilute the ownership stake of the SMBTs. Going forward, this could become a problem for the MFI if the capital adequacy goes below acceptable standards. The present value which is required to be statutorily maintained is 12% and which needs to be raised to 15% from 1 April 2009 as per RBI guidelines" (SNFL, 2008).

> "The organisation has shown good performance on its strategy of mobilising funds. Transformation to an NBFC is a positive strategic initiative aimed at mobilising larger amounts of funds. Equity mobilisation efforts have led to a private equity investor (Aavishkaar Godwell) investing Rs 9.2 [crore] as preference share capital in the NBFC taking the capital adequacy to 18.5% as on 31 March 2008. Equity has also been mobilised from employees and High Net Worth individuals, including the trustees of TMT. Sweat equity to the tune of Rs 1.4 crore has been allotted to the Chairman and Managing Director" (Grameen Koota, 2008).

> "Equity Mobilisation: In light of the current constraints faced in mobilising loan funds, BFL has been focusing on mobilising equity. (…) However, this source is not adequate to meet the expansion plans and thus BFL has changed its focus to mobilising institutional equity (up to 25% of total share capital) from 'social investors'. As at the time of last rating, the organisation continues

> to face tremendous difficulties in managing a large number of shareholders and finds it difficult to comply with many legal provisions such as delivering share certificates, annual reports, maintaining shareholders' records etc. However, still the promoters do not want to opt for any 'commercial' institutional equity investor as this would mean dilution of their management control in the company. The promoters are seeking 'social investors' who would be long term investors without asking ownership in the Board" (BWDA, 2008).

Template II: Procedures

EXPANSION AND COMPETITION MANAGEMENT

The assessment of procedures, techniques, and strategies employed by MFOs has undergone changes in terms of content as well as form as compared with the 1999-2004 reports. In the later reports, more emphasis is placed on encouraging MFOs to grow and expand their operations. There are also expectations that organizations demonstrate viable growth strategies that are geographically diversified. While earlier reports identified local knowledge and geographical concentration as key strengths in order to keep costs down, there are, in the more recent reports, examples of how the raters see this as a significant risk and source of weakness.

> "**Localized resources can hamper expansion plans outside Tamil Nadu:** GVMFL's Tamil Nadu based vision has so far resulted in a TN-specific business model which can create problems in expanding to other states in the future" (GVMF, 2008, **bold** in original).

Closely related to the above is the topic of competition and competition management, which becomes more prevalent in the reports over time and receives its own heading in 2004. Competition is assumed to cause high client dropout rates, potential over-indebtedness, and an increasing staff attrition rate, and the MFOs are expected to have strategies in place to mitigate competition.

> "CMC has the policy of making disbursements and collections in the branch offices which is a competitive disadvantage since other MFIs make all transactions in the field. To counter the competition in the longer run, CMC intends to rely upon its transparent policies, low rate of interest and an improved rela-

tionship with its clients. To build a strong relationship, CMC plans to increase the scale of its non-financial services or credit plus services. It also gives a high emphasis to proper staff behaviour and conduct in its trainings. CMC also prefers to include women field staff in its operations team to make its clients more comfortable" (Cashpor, 2010).

"As there are still many areas untouched by microfinance, ASA-GV does not plan to take the competition head-on and instead focus on the untapped markets, which is a wise strategy. However, as the microfinance sector has become very dynamic, the markets might become competitive sooner than expected and thus ASA-GV would be required to move fast and effectively to fully utilise the first mover's advantage" (GVMF, 2007).

In this light, competition management strategies tend to override the foregoing procedures aiming at identifying focus areas and target groups, and the language in the reports from 2005-2011 changes markedly in terms of the descriptions of competition management strategies and the "growth potential" of the "market" as opposed to "the level of poverty" of the "village"; below are extracts that illustrate this shift.

"Before starting a new branch, an extensive survey of the area is conducted. The survey team is composed of two ASA senior staff with the Divisional Manager (Regnér and Edman) and the Branch Manager (BM). Competition from other MFIs is analysed before spreading operations into new areas. Senior staff from an old branch, along with 3-4 junior/new staff members, opens a new branch" (GVMF, 2007).

"SKS has grown its microfinance operations tremendously since the last rating. As most of AP is saturated with microfinance operations, it did well to start operations in other under-served states. (…) The organisation's strategy to achieve the projected growth targets incorporates a market survey, categorisation of areas by growth potential, placement of managers with professional qualifications and local knowledge, standardised business processes to make the processes and systems scalable and decentralised decision making at the area office level" (SKS, 2006).

THE LOST GROUP

Over time, there is a reduced focus in the reports on the process of group formation, and the lengthy background descriptions seen in the earlier years are gradually removed. The concept of group homogeneity is dropped completely, and group composition is not assessed at all. In 2003, the group formation process of SKS was described at length, but in the 2006 rating of the same organization, it had been reduced to the following.

> "Operations are largely based on the Grameen Bank methodology" (SKS, 2006).

Another rather dramatic change is found in the reports on GVMF. Text describing the group formation process took up two-thirds of a page in the 2001 report, and was thereafter gradually shortened. In the 2008 and 2009 GVMF reports, there is no discussion pertaining to the group formation process; the last description of GVMF's group formation process is found in the 2007 report.

> "Once potential members are identified, Field Officers conduct a Compulsory Group Training (CGT) for four days at the end of which a Group Recognition Test (GRT) is conducted. Subject to passing this test successfully, groups are organised according to the Grameen model. After four weeks of regular meeting, the first external loan is extended to the groups" (GVMF, 2007).

An interesting case is that of BWDA, which took over a non-banking financial company called BFL in 2003-2004. In the subsequent BWDA reports of 2006 and 2007, the rating exercise covers both BWDA and BFL, and in 2008, the rating only covers BFL. In these reports, the process of group formation is not given much attention; instead, the raters state that "group promotion" is carried out by BWDA, for which BFL pays its sister organization.

> "Lending is mainly through groups (15-20 members each). The process of group formation is undertaken by BWDA, and groups are 'handed over' to BFL at the time of loan disbursement. BFL pays group promotion charges to BWDA for the services rendered by them" (BWDA, 2008).

This setup, however, poses some problems for the raters, as the quality of the groups is no longer under the control of BFL, which extends the loans to the groups. To ensure quality, the raters call for better internal auditing of these processes.

> "Presently, the quality of field operations at group-level (formation, meetings, collections etc.) is not adequately focused upon under internal audit, same holds true for the reasons for overdues and the quality of overdues tracking by staff. The moderate level of internal control system weakens the credit culture. (…) The rating team could visit very good groups as well as delinquent ones and the ones on the verge of dissolution due to discord/disharmony. Lack of quality control mechanisms for processes of group formation and group meetings has led to such large variances in the quality of groups" (BWDA, 2008).

There are also a few examples where the raters encourage more individualized (as opposed to group-based) collection and tracking practices as a measure to decrease risks.

> "During the rating team's visit to some of the SHGs, instances of internal default by members were observed. In all such cases, the internal savings of the group had been used for ensuring the timely repayment of loans by the SHG to BWDA. Although tracking of delinquent SHGs is diligent, tracking of delinquent individual borrowers is not adequate. This is not likely to have a negative effect on the repayments to BWDA in the short run. However, if the internal default increases and goes unnoticed by BWDA, it may increase the incidence of delinquent individual borrowers and adversely affect the good credit culture built in the programme. This can cause a reduction in the internal circulation in the SHGs and their federations in the short run" (BWDA, 2004, 2nd update).

> "Collections were made from each individual separately which leads to a better identification of borrowers and limits the role of centre leaders. (…) After counting of the repayments, amount is handed over to one of the members, on rotational basis, to be sent to the branch office" (Cashpor, 2010).

GROUP-LEVEL AUDIT AND CONTROL

The role of the group in recordkeeping becomes less of an issue in the 2005-2011 reports. This may be explained with the fact that group-level

recordkeeping is often associated with the self-help group model, and the number of reports of MFOs that promote self-help groups decreases slightly over time in the studied sample. However, in the 1999-2004 reports, there are examples of the ratings taking note of how accounts are maintained in MFOs that mobilize joint liability groups as well (e.g., GVMF, 1999). Moreover, although all BWDA reports contain text about how the groups are able to independently record their financial transactions, as of 2004, this begins to be seen as problematic for the raters, since the MFO lacks insight into and control over group affairs. The raters therefore call for more monitoring and auditing of the groups' records.

> "Most of the groups maintain their own records, with the assistance of the Cluster Coordinator. The accounts of all groups are supposed to be audited by the statutory auditor of BFL on an annual basis (based on Receipts and Payments statement, Trial Balance and Income and Expenditure Account prepared and sent to the auditors by BFL staff), however there are substantial audit arrears on account of inadequate focus and follow-up. At one of the branches only about a third of the SHGs had got audited on statutory basis for the year 2007-08" (BWDA, 2008).

The phenomenon of group-level savings and internal circulation of savings used to be an activity that was acknowledged and assessed by the raters in the case of MFOs that mobilize self-help groups. However, over time, it loses importance in the reports, and the raters cease to follow and monitor the amount saved and circulated. In the subsequent reports of SNFL from 2003 and 2005, the box indicating the group-level savings says "Nil," and in the 2008 report, the box has been dropped completely. The raters did, however, continue to mention the importance of savings and internal circulation of funds elsewhere in the text, but they do not track and record the amount. Intriguingly, in the SNFL report from 2009, the following passage is found:

> "Progress reports from the FEs are also sent to SNFL. Along with financial statements and portfolio data, SMBTs also send to SNFL, the savings and inter-lending data for each SHG. This data is captured by the Field Staff on monthly basis and is used by SNFL to verify group transaction quality before loan sanction" (SNFL, 2009).

The above indicates that the figure capturing "group-level savings" is available but that the raters no longer see it as a relevant factor to consider in the rating exercise.

There are clear regulatory constraints regarding the collection of savings from the public by non-banking financial companies and section 25 companies. As regards other legal forms, the raters' interpretations of the regulatory framework have fluctuated over the years, but in more recent years, the view is that the collection of savings from the public is banned by regulators for all legal forms.

> "GK being a trust is not legally authorised to mobilise savings. Collecting savings was possible in the past due to a relatively liberal regulatory environment. However, recently it has become a risky proposition in light of the stricter regulatory environment. The impending transformation to an NBFC structure also precipitated termination of the savings product so as to obviate legal complications" (Grameen Koota, 2007).

> "The overall rating of Mahasemam has been subjectively reduced by one notch from α- to β+. Although the quality of Mahasemam's management systems has improved and the organisation has also maintained its performance grade on profitability and sustainability indicators, the strategy of mobilising equity from client savings is a major issue on account of lack of clear regulation in this regard" (Mahasemam, 2006).

It is notable that while the regulatory framework impedes MFOs from collecting savings (see Chapter 6 for more details), it does not restrict MFOs from encouraging and facilitating group-level savings and internal circulation of these funds. In the later reports, general descriptions and assessments of savings behavior are generally rare. One exception is the 2008 rating of SNFL, where the raters commend the organization for its group-level savings mobilization and fund circulation, although the exact figures are not captured in the reports. The organization scores an impressive α and is praised by the raters.

> "SNFL does not collect savings or security deposits from SMBTs or clients. The savings pooled in by the SHG members either rests with the SHG or is internally rotated among its members on need basis. SNFL actively promotes

> savings mobilization and internal circulation of funds, which considerably strengthens the SHG cohesiveness. (…) The quality of the SHGs promoted by ASSEFA/ SMBTs is much better than that of other MFIs as there is an abundance of credit-plus activities and there is a strong push towards thrift and internal circulation of loan funds, with the objective of making SHGs self-reliant. The community ownership model also helps generate goodwill and promotes repayment" (SNFL, 2008).

TOWARDS FORMALIZATION AND STANDARDIZATION IN THE LOAN PROCESS

While the raters over time elaborate less and less on group formation and group functions, the processes of formal loan applications and the internal loan appraisal procedures of the MFO – i.e., the sequences of events leading up to the MFO making a decision as to whether to approve a loan to the target constituency, either directly or via the group – begin taking up an increasing amount of the raters' attention as part of the background section on "Microfinance policies." Over time, the raters' focus shifts from the group grading to the internal procedures of the MFO vis-à-vis the loan application process, including extensive discussions of the MFO's loan-sanctioning authorities at different hierarchical levels. The reports describe how the groups' actively submit their loan applications to the MFO for the MFO to act upon, as opposed to descriptions of the group rather passively being provided an external loan in the 1999-2004 sample reports. The group gradings are still present in the reports, but they take up less space.

> "After six months of savings, SHGs submit loan applications to the SMBT. On receiving the loan application, a Field Staff from some other cluster conducts an SHG rating exercise on various parameters and assigns grades from A to D (with A being the best). Loans are recommended only for SHGs falling in the A and B categories. All the loan applications are required to be submitted by 15th of every month. The loan committee at the SMBT level, consisting of the BDM and the CEO consolidates the various loan requirements and forwards it to the FEs. The FEs checks the consolidated loan applications for policy compliance verify the group rating and forward the documents to SNFL. The applications to SNFL are supposed to be received by 25th of every month. At the SNFL level, the loan committee (consisting of the CMD, GM and a member of the Board) appraises and approves the loan amount. The cheque of

> the approved loan amount is sent to the concerned SMBT for disbursement to the SHGs" (SNFL, 2009).

The raters' emphasis on formal loan application processes as part of the organizational policies does not necessarily mean that these were lacking during the earlier years of rating; indeed, there are a few indications in earlier reports (e.g., under the categories "Accounting and MIS" and "Financial planning and control systems") that groups filled out forms and applied for loans. But in later years, the raters start treating official loan applications originating from the groups, as well as well-defined loan sanction authorities at different hierarchical levels, as central MFO policies.

As to loan appraisals, the years 2006-2007 see the introduction of various types of secured/collateralized/guaranteed larger loans to individuals, businesses, and entrepreneurs; e.g., the 2006 BWDA rating introduces secured loans to individuals; the 2007 GVMF rating describes the introduction of business loans that need two guarantors; and in the 2006 SKS rating, the organization is described as piloting an individual loan product. For secured/collateralized loans to individual entrepreneurs, loan appraisals change shape over time; instead of discussing the group, the ratings begin to discuss how the MFO ensures that business plans are viable in terms of, for example, profitability and cash flows.

> "Loan applications from individual entrepreneurs are also taken up on the recommendation of groups (through a resolution) and most individual applicants are relatives of SHG members. Loan appraisal for loans to individuals is based on asset verification by Branch Managers and certificate of valuation of assets by local government valuer (in the case of secured loans). In the case of unsecured loans to individuals, the aim of asset verification is to assess the capacity of the client to repay the loan" (BWDA, 2008).

The interest rate is a central subject. With the "Client protection and transparency" box present in the 2006-2007 reports, the raters, for the first time, give hints of the preferred form for communicating the interest rate to the target constituency, i.e., as effective interest rate.

> "SKS is also in the process of introducing new passbooks, which would clearly specify the role of the client and field officer, effective interest rates and contact details of the organisation. (…) SKS' charge of 12.5% flat interest in AP and 15% flat in other states with 1% service charge results in an effective interest rate of 28.8%. SKS quotes effective rate of interest to its clients and its pricing is reasonably well transparent" (SKS, 2006).

> "CMC displays a good service orientation towards its clients, with strategies in place to ensure transparency on products, communication of effective interest rates and timely disbursement" (Cashpor, 2006).

When evaluating the actual financial transactions between the MFO and the target constituency, i.e., disbursements and repayments, the reports describe a process that seems increasingly standardized, wherein formalities as regards, for example, loan agreements, appropriate physical venues, and the terms and conditions are specified. There are also examples of the rating reports explicitly acknowledging the use of signatures and receipts throughout the loan process, e.g., when financial transactions are being made and when applications and loan contracts are being agreed upon.

> "It also does not provide any receipt for repayment collections which make the collection process even more vulnerable and weakens Guardian's control mechanism" (FR, Guardian, 2009).

> "Illiterate clients are trained to put their signatures before they are considered for application. Successful loan completion of a Group Recognition Test (GRT) makes them eligible for borrowing first cycle loan. Loans are initially approved by the group and loan applications are signed by the group leader on behalf of the group members. Loan applications are then collected and recommended by the Centre Managers and are then sanctioned by the Branch Managers (BMs)" (Cashpor, 2010).

The reports describe the actual transactional procedures in more detail, and several aspects of this process become increasingly standardized, such as loan disbursement being made at the branch, loan utilization checks, and prepayments being allowed. From 2009 onwards, the disbursement of the loan to the target constituency is given more attention, with the raters de-

scribing the MFO disbursement policy in detail and noting the "witnesses" present during the transaction event.

> "For loan disbursement, cash is physically transferred from HO to branches in a company vehicle under the custody of Loan Disbursement Officer (Kaldor), who is appointed on a rotation basis by HR department. These LDOs are AMs from a different area. Thereafter, the loan is disbursed at the branches under the supervision of the appointed LDO. The repayment is collected in center meetings and the amount so collected is deposited in the bank account the next day" (Mahasemam, 2009).

The reports also assess whether or not the MFO actively ensures that the target constituency uses the loans in the manner agreed upon. When a decision has been made to extend a loan to the target constituency, the rating reports note if the MFO conducts a so-called "loan utilization check." Loan utilization checks are encouraged by the raters and are assumed to lead to higher repayment rates. Although such checks are prevalent throughout the reports, an intensifying emphasis on the concept can be noted over time.

> "As per ASA's experience, defaults occur if the loan is misused for some other purpose. To address this problem, the organisation is planning to put in place a member verification team to strengthen the current loan appraisal and verification system. The role of this team would be to visit clients and verify loan utilisation" (GVMF, 2006).

RULE-BASED STAFF-CLIENT INTERACTIONS

The centrality of the staff becomes more evident over time. The reports describe in depth the MFOs' recruitment processes, internal training and capacity-building programs for staff, performance appraisals for staff, and staff turnover ratios. The following passage from a report on SNFL (2009) captures the expectations of the raters.

> "The grade on organisation and management is low at β. (…) The current state of HR function within SNFL is inadequate. (…) SNFL currently does not have an HR manual which details organisational policies and procedures related to recruitment, training, performance evaluation, promotions, remuneration and staff welfare. (…) With respect to transfers currently there is no formalised

> policy… (…) Staff training is not a formalised and systematic activity and takes place largely on the job…" (SNFL, 2009).

Further, the role of staff in operational decision-making procedures, which was discussed under a separate heading in the 1999-2004 reports, is addressed only sporadically (e.g., in GVMF, 2006) before it completely disappears from the reports.

Around 2007-2008, a change in how staff incentives are discussed can also be noted as the raters start making note of the systems being linked to reaching preset targets, as opposed to limitless growth in number of clients or size of portfolio managed, as well as considering staff compliance with and adherence to processes. The reports also note whether the incentive systems are provided to field staff only.

> "Staff behave respectfully with clients and regular attendance of clients in group meetings is one of the criteria for deciding the incentives of the field staff. (…) Mahasemam has developed a good incentive system for its FDOs whereby incentives are provided for maintaining attendance in group meetings, the amount of savings collected, number of clients and loan portfolio managed as well as repayment rate on loans" (Mahasemam, 2006).

> "The incentives have been linked to achievement of basic minimum targets with respect to outstanding portfolio. Staff with less than 98% repayment rate is not eligible for incentives. Currently there are no incentives and/or disincentives to check for adherence to processes and compliance to policies" (BWDA, 2008).

> "The Area Managers, however, get incentivised based upon the number of supervisory visits they make to the branch offices. This is to keep their focus exclusively on the compliance of policies and not on growth" (Cashpor, 2010).

As of approximately 2006, although still encouraging strict and prompt repayment cultures, the ratings begin to acknowledge that there are certain times when a borrower should not be forced to repay her loan and, by extension, that there are cases when the loan should be written off by the MFO. These occurrences are referred to by the raters as "genuine," and the reports exemplify such instances with externalities such as floods and con-

struction projects, as well as with the borrower or her husband passing away.

> "The groups with overdues visited during the field visit seemed to have genuine problems. The group members had either lost their businesses in the flood or had been displaced due to a highway construction project" (GVMF, 2006).

> "Staff behaviour: GK staff behaves respectfully with the clients. Peer pressure and/or group liability is invoked in cases of default. The earlier culture of 'zero tolerance' with respect to defaults has been relaxed a little after the Davangere incident. The staff has been instructed not to insist on recovery in case a household is in distress. The staff maintains a professional relationship with the clients" (Grameen Koota, 2007).

Staff behavior becomes more and more formalized and rule-based over time, as does the behavior of the target constituency vis-à-vis the MFO. In the ratings from 2006, the grey-shaded box "Client protection and transparency" enters the reports temporarily; it is removed in 2007. In this context, the concept of "client feedback" is introduced, and MFOs are expected to provide a formal channel through which the target constituency can articulate any concern or grievance to the MFO.

> "There is also a mechanism through which clients can approach the Head Office in case of complaints against staff. The contact numbers of the Head Office are written on the files maintained with the clients but the facility has not been used so far" (Cashpor, 2006).

> "The clients are encouraged to visit and complain to the senior staff at Branch/Head Office in case of any grievance. Client feedback is solicited at the time of loan disbursement at the Branch Office, and during the meetings attended by the senior staff or the internal audit team. In one of the cases, during the visit of the Area Manager, the clients complained that they were yet to receive their BFL share certificates, and the field staff was directed to issue the certificates to the members which was complied with immediately" (BWDA, 2006).

Template II: Social outcomes

Over time, the concept of who constitutes an eligible microfinance client expands and is no longer limited solely to poor village women in groups; in the 2005-2011 reports, there are also a few examples of urban populations, entrepreneurs, individuals, and people who are far from being among the most impoverished counted as part of the MFOs' respective target constituencies.

> "Though, in most of the state it is still free of competition it is now also targeting more upscale customers to whom the commercial banks also cater, and where competitive threats exist. As a result, GVMFL is now creating a service environment incorporating the following features in order to create an edge over the banks. (…) These factors will help GVMFL to capture the large size loan market for upscale consumers. Though, it would risk drifting away from the original mandate of targeting only the poor, yet it would capture the entrepreneurship from the semi-urban and rural middle class families" (GVMF, 2008).

> "BFL has been experimenting with loans to individual entrepreneurs. It had individual loans of Rs 3.4 crores outstanding as on 31 March 2007. The lending is mainly done in the urban locations. These are higher sized loans ranging from Rs 50,000 to Rs 350,000. The organisation takes collateral and guarantor from the applicant. The loan approval and disbursement is centralised" (BWDA, 2007).

> "SKS Microfinance Pvt. Ltd. targets low-income families through its group loans and plans to introduce individual loans to cater to the needs of the upper poor segment. The organisation does not consider destitute families as its target group as it believes they need a long-term handholding before they can reach a level at which they can borrow. (…) SKS currently serves mostly rural areas and is piloting an urban microfinance model" (SKS, 2006).

For those organizations that offer various development, social, and non-financial activities such as healthcare, training and education (e.g., Mahasemam and SNFL), the raters positively and explicitly acknowledge these activities, contending that they build client loyalty and bonding, as well as provide a source of competitive advantage for the MFO.

> "Staff of SMBTs is still involved in implementing development projects started by ASSEFA which helps SNFL to retain bonding with its customers" (SNFL, 2011).

> "The major competitive edge of Mahasemam is the support from Meenakshi Mission Hospital, which it has also been able to leverage well. (…) In addition, the recent health insurance tie-up with ICICI Bank is aimed at providing free treatment to clients at several hospitals across the state. Apart from tie-ups with hospitals, Mahasemam Trust has also organised eye camps, HIV/AIDS awareness camps and medical check-up camps for the microfinance clients. (…) These steps are expected to improve and maintain client loyalty in the long run" (Mahasemam, 2006).

> "**Credit plus services provided to clients:** MT provides a mix of services to its clients. Not only does it provide microfinance and related training, but linkages with insurance, savings, and healthcare as well as legal services. This differentiates it from its competitors" (Mahasemam, 2009, **bold** in original).

Template II: Financial outcomes

The topic of interest rate setting receives increasing attention in the rating reports over time. As noted in the 2006 report, Cashpor has reduced its interest rate. However, the raters conclude that this measure has led to poor financial performance, including losses and a reduced net worth. This strongly contributed to the relatively low rating grade of β+ given in the "Financial performance" category the same year.

> "**Low capital adequacy:** CMC is expanding at a rapid pace. Its operating expenses are high and it reduced its interest rate to 26% on a declining basis from the financial year 2005-06. This has resulted in huge losses, which has eroded its capital base further. (…) This very low capital adequacy is a substantial risk for lenders" (Cashpor, 2006, **bold** in original).

In 2010, Cashpor decided to again reduce its interest rate. However, this time, the raters are more positive about the decision. The difference between the 2005 and the 2010 interest rate reductions was that in 2010, the raters were content with Cashpor's overall financial performance in terms of its profitable operations, commendable portfolio quality, and future

plans to further reduce costs, and thus argued that the financial situation of the organization allowed for a reduced interest rate.

> "Apart from its good financial performance, CMC has earned a reputation for double bottom line performance through its poverty focus. The Board of Directors of CMC decided to reduce the rate of interest charged from clients from the earlier ~31% to 25.8% from July 1, 2010. This was done after CMC achieved much better profitability during 2009-10" (Cashpor, 2010).

In the 2006 and 2007 ratings of BWDA, the raters acknowledge the organization's strong portfolio quality, low operating costs and profitable performance, scoring the organization an α in the "Financial performance" category for two consecutive years – and BWDA's comparatively low interest rate is cited as an important competitive advantage.

> "The major advantage of BWDA when compared to other MFIs of similar scale in Tamil Nadu is the relatively low interest charged by the organisation. (…) The interest charged by BWDA on its loan products translates into an effective interest rate of 19% pa, which is much lower than other MFIs in the state. Hence, the organisation is less likely to face political pressure for reducing the interest rate" (BWDA, 2006).

There are also instances in which interest rates are considered by the raters to be too low; the following extract from a report on BWDA (2008) indicates that the raters would welcome an increase in interest rate as a means to increase profit margins and enable further expansion of operations.

> "BFL loan products come with an APR of 21% approx, which translates into relatively thin profit margins leaving little scope for utilising high cost borrowings. This has become a bottleneck for expansion and has resulted in a sluggish portfolio growth since the last rating. Weak funds mobilisation position, combined with increase in level of competition has pronounced the risk of significant client drop-out in short to medium term. However on a positive note, (…) as informed by BFL subsequent to the rating visit, interest rate of loans given out to SHGs has also been increased to 18% since 1 November thus easing the pressure on margins a bit" (BWDA, 2008).

One of the main factors that seem to influence the attitude towards interest rates is the organization's financial performance, i.e., if operations are profitable enough and generate the surplus needed to grow. As the issue of competition also becomes more relevant, MFOs operating in competitive environments are expected to maintain an interest rate similar to those of their peers.

In the 2006 reports, excessively high interest rates are discussed in the context of political risk, as authorities in some of the southern Indian states put pressure on MFOs to lower interest rates from 2003-2004 onwards. The adverse external environment even caused raters to downgrade the scores of some organizations.

> "High interest rate: ASA is charging a 12% flat interest rate, coupled with 2% upfront processing fees. This does not seem to be sustainable in light of growing political awareness about rates of interest in Indian microfinance. ASA is still not profitable and, therefore, will have to work hard to generate a surplus in a situation where its effective rate of interest might have to be lowered" (GVMF, 2006).

> "SKS (…) has a rating grade of α- on financial indicators. This is lower than the previous rating grade of α mainly due to the political pressure on interest rates… Profit margins are thin and likely to be wiped out over the next financial year due to rapid expansion and pressure on interest rates from political circles. (…)" (SKS, 2006).

Interest rate levels are also discussed in light of non-financial activities. Up until 2006, the non-financial services offered by Mahasemam are not associated with any negative comments from the raters. However, although not directly discouraging such activities, the 2006, 2008, and 2009 reports highlight the implications for cost control and interest rate setting when offering non-financial welfare services.

> "**High operating expense ratio:** The operating expense ratio of the organization is very high at 24.6% on for 2007-08. This high operating cost has offset the increased yield, thus lowering profitability. The organization also provides non-financial services to its clients" (Mahasemam, 2008, **bold** in original).

> "**Slightly high effective rate of interest:** MT collects 7% upfront interest and 12%p.a. flat during the loan term, on its income generating loans. This reflects a high effective rate of interest (39.1%), compared to the competitors (32-35%). However, the Trust justifies this by indicating that it undertakes provision of credit plus services to clients, which give it a competitive edge over other players" (Mahasemam, 2009, **bold** in original).

As noted in the reports, neither Mahasemam nor SNFL have a clear demarcation between their microfinance operations and their non-financial social development activities. In the 2011 SNFL report, the raters note the increased staff productivity due to the development activities.

> "Issues: Low staff productivity as the field staff is also involved in development projects of ASSEFA" (SNFL, 2011).

One area upon which the raters have focused much attention is operating efficiency and the closely linked staff productivity. There are numerous examples from the rating reports where the raters point to unacceptably high costs and low staff productivity levels; below are some illustrative extracts.

> "The staff productivity of CMC is moderate at 298 borrowers per field staff as on 31 March 2009. Each branch, on an average has 1,247 borrowers and 4 Centre Managers (CM). The productivity has improved significantly since the last rating, but is still lower than that achieved by some of the other MFIs of similar size in the country" (Cashpor, 2009).

> "Operating expenses are relatively high at 33.6% and partly reflect a somewhat low staff productivity at 343 clients per field staff. Keeping in mind the density of population in the areas where MT is operating, staff productivity can go up to as much as 500 clients per field staff. The ratio could be even higher in the urban branches of Chennai" (Mahasemam, 2005).

Along the same lines, the raters place great value on staff productivity, and there are several instances where improved staff productivity contributes to a higher rating.

> "The staff productivity of BFL is good and has further improved since the last rating. It has Borrowers to Field staff ratio of 919, which is very high. The staff productivity shows a sharp jump in last one year" (BWDA, 2007).

> "The grade of CMC on organisation and management is good at α. CMC has improved its performance on management as compared to the previous rating. (…) Staff attrition has reduced and CMC has improved its remuneration policy. Staff productivity has also improved significantly since the last rating" (Cashpor, 2010).

Intriguingly, there is one instance from 2008 where the raters suggest that the staff productivity may be too high within a particular MFO. The argued implication of an excessively high staff productivity ratio is the potential negative effects on the portfolio at risk.

> "Overdue loans are not closely monitored by the field staff. The field staff on most of the occasions is confined in their interaction to Group Animator only, this holds true for both monthly data collection visits as well as visits for overdue tracking. Dependency on Animator and high caseload on staff are the reasons for lack of follow up on overdue loans. (…) Due to a monthly collection model, the productivity levels at BFL are *on the higher side*. The staff productivity is high at 616 borrowers per field staff as on 31 Mar 2008 (45 SHG per field staff)" (BWDA, 2008, *italics* in original).

As part of the push towards higher efficiencies, the raters also encourage MFOs to increase the number of group members that are active borrowers of the MFO. This is seen as one way of increasing efficiency and reducing operational expenses.

> "Adding further to the inefficiency of the expansion strategy is the fact that the number of members was 5.28 lakhs as on the 31 March 2009 whereas the number of borrowers was only 1.49 lakhs. This implies that even though the field staff of SMBT managed 473 SHG members on an average as on 31 March 2009, only 121 members out of these were active borrowers and were productive for SNFL" (SNFL, 2009).

> "With an increase in concentration, the organisation has also increased its total borrowers to total members' ratio significantly. With large number of borrow-

ers in their first cycle, its average loan outstanding has come down sharply" (BWDA, 2007).

There are two organizations in the sample that are described as having explicit poverty-targeting tools; Cashpor and Grameen Koota both have a policy in place restricting their work to efforts focusing on poor women who are identified using the "Cashpor housing index." In the Grameen Koota report from November 2004, the MFO's practices of "poverty targeting" when selecting villages to work with is considered problematic, as it constrains the organization's financial performance. The number of villages covered in a given geographical area of operation is referred to as "horizontal concentration/coverage" in the reports, and the number of individuals covered within a given village is referred to as "vertical concentration/coverage" (or "depth of coverage") in the reports. Rather than suggesting the elimination of the practice of "poverty targeting," the raters suggest that the MFO select the villages it works with more carefully.

"While pursuing rapid expansion, the organisation has mainly grown horizontally, covering large number of villages. However, its vertical coverage within villages has been low. GK had 583 centres across 411 villages on 30 September 2004, which had a significant impact on its costs. The reasons for the low vertical concentration are the small size of the villages and the clear policy of GK of working only with poor clients. As a result, the organisation finds limited target families in one village. However, lack of proper strategy for selection of villages resulted in selection of some unviable villages and the organisation had to withdraw from some such villages later. This contributed to its client drop out rate as well. The organisation has a high client dropout rate of 16.0%, which is a matter of concern" (Grameen Koota, 2004).

In the subsequent Grameen Koota report, the raters commend the organization for having changed its expansion strategy.

"Over the last one year, the organisation has brought a small change in its expansion strategy. Along with spreading the horizontal spread of its operations, it has restricted the operational area of its new branches from 25 km radius to only 10 km radius. This is a good strategy, as the visited areas during the rating visit reflected a reasonable scope for vertical expansion. This would also enable the organisation to curtail its operational cost" (Grameen Koota, 2005).

In the case of Cashpor, the 2006 report highlights the negative effects of poverty targeting on the organization's financial results.

> "CMC focuses on targeting the poor and it has developed a tool (housing index) to assess the poverty among the prospective clients. The organisation has the strategy of working with only poor clients based on its poverty assessment tool and does not work with the non-poor. To motivate its staff to target very poor clients, it offers higher incentives too. However, since CMC operates in regions where the absorption capacity of its clients is low, and it targets only the poor clients, it takes several years for a new district to achieve break-even, since CMC has to motivate and prepare poor clients who are otherwise reluctant to avail loans. As per the organisation's plan, a new district should break-even in the fourth year of its operation; however, it took six years for its first district, Mirzapur, to break-even. Due to the very long time taken by districts to break-even, the organisation's capital has been gradually eroded" (Cashpor, 2006).

Template III: 2012-2014

Template III: Structures

Of the 2012-2014 reports, three reports focus on for-profit and regulated non-banking financial companies, one focuses on a cooperative, and two focus on not-for-profit section 25 companies. In these reports, structural aspects are evaluated along similar lines as in the previous periods, but with a few important additions and revisions.

From 2011 onwards, an appendix containing a board profile is included, with extensive details about each board member, along with his/her present position on the board and year of joining. This reinforces the importance of the individual qualities of board members. Below is an extract from the board profile appendix of ASPL (2013).

Profile of the board		
Board Member	Position on Board	Experience
Mr Deep Joshi	Independent Director*	An Indian social worker and NGO activist. Recognized for his vision and leadership in bringing professionalism to the NGO movement in India. Former Executive Director Professional Assistance for Development Action (PRADAN)
Ms Rupali Kalita	Nominee Director, RGVN	A Rural Development Banker with more than 20 years of working experience in the banking sector who was instrumental in spreading the outreach of the microcredit wing of RGVN

* Though has a token shareholding (Rs 1,000) in the NBFC.

Individuals who are "independent" from the organization, have professional backgrounds, and are associated with well-regarded organizations are considered as assets in the reports. The board members are there in their capacity as individuals, and their eligibility to be qualified as board members is rooted in their personal track records. The ratings also describe the board of RGVN as "diversified," and it remains unsaid if this is due to the fact that that it is headed by a woman.

The issue of member representation on the board, as well as community ownership, is discussed in the case of Annapurna, which is a cooperative, and in the cases of SNFL and RGVN, which are partly member-owned. As in the earlier reports of, e.g., Grameen Koota and SNFL from the previous time period, having members as board representatives is regarded with certain hesitation.

> "Annapurna has a reasonably involved board with community representation. (…) Representatives of the members are elected by the Community Representatives (CR) and changed every three years. Only members in 4th cycle and onwards and those who have been CR for at least 1 year are eligible to be inducted in the Board. (…) The community members' representatives play limited role in the Board. However all important decisions are made after members' approval in the Annual General Meeting" (Annapurna, 2014).

In the case of SNFL, the raters report that the surpluses of the clients are automatically transferred to the books of accounts of SNFL as equity on a

monthly basis. In return, the clients, who are organized into self-help groups, which in turn are organized into mutual benefit trusts (called SMBTs), receive an annual allotment of SNFL shares in return. The raters note, however, that the clients are unaware that their self-help groups formed part of the SMBTs, that they are making a surplus, and that they are shareholders. A similar description is made in the case of RGVN (2012).

> "The clients were not aware of their membership with SMBT. They lacked information about the member surplus due to them/their SHG, which is invested in SNFL. (…) Most of the SMBT members are not aware of the surplus due to them" (SNFL, 2012).

> "17.4% of equity is held by the 7 Mutual Benefit Trusts (MBTs) of clients, with RGVN(NE)'s key staff as their trustees. (…) The MBTs were formed with an objective to empower the members and encourage community ownership in the organisation However, it is difficult to ensure participation of the members and thus RGVN(NE) is now exploring the possibility of discontinuing the MBTs and selling their shares to new investors. The client's/ member's investment will be reimbursed to them along with suitable returns" (RGVN, 2012).

There are no calls from the raters to increase the involvement of the clients in decision-making processes at any level.

Apart from developing strategies, making policy decisions, and monitoring the management, the raters place renewed emphasis on the centrality of having an independent internal audit function that reports directly to the board, circumventing the managing director. The audit procedures are described in detail and at length (the section covers up to two PowerPoint slides in the reports). An addition from earlier reports is the encouragement from the raters to include visits to clients in the internal audit process. Also, the importance of following up on the internal audit findings is emphasized.

> "The unit wise internal audit reports are reviewed during monthly PMC[58] meeting. The Internal Auditor prepares summary report of all units and presents it during monthly review meetings. The Internal Audit findings are not presented to the Board. (…) The Board visits the units annually under the new initiative – DART. They also check the monthly internal audit reports on a random basis" (Guardian, 2013).

> "There is an Internal Audit Committee of three directors which includes an independent Director and the representatives of NEDFI and RGVN (Andhra Pradesh Mahila Abhivruddhi Society). The committee also meets quarterly. (…) Audit findings are shared with the Audit Committee on a quarterly basis with a copy to the Managing Director. (…) The scope of these audits is limited to operations/branches. A quarterly audit plan is approved by the Audit Committee. Audits are conducted as per the detailed Internal Audit manual" (RGVN, 2012).

During the most recent years of the studied sample, the expected board responsibilities are expanded to include an outspoken "social" dimension, and there are instances where the raters note that the board embraces the mission and vision of the organization and that it focuses on social performance (ASPL, 2013; RGVN, 2012).

> "To enhance delivery of credit plus services, RGVN (NE) has registered a different society called Gyanarun, and plans to transfer Rs 20 lakh to it from its profits for the FY 2012-13. (…) The board has also initiated various efforts towards SPM and client protection" (RGVN, 2012).

Template III: Procedures

The accounts and assessments of MFO procedures in the most recent reports resemble, to a large extent, those of the preceding years. The emphasis on explicit rules and norms to guide the staff when dealing with the target constituency is reinforced. The reports note how well the MFOs comply with existing microfinance regulations and Reserve Bank of India norms. The raters also comment on and evaluate how well the MFOs adopt and adhere to codes of conduct and principles, e.g., the code of con-

[58] The project management committee (PMC) comprises the chairman, the chief executive officer, two managers, zonal manager, internal auditor and two unit officers.

duct developed by the two industry associations (i.e., Microfinance Institutions Network and Sa-Dhan) and the global initiative The Smart Campaign. Finally, the reliance on formal rules is manifested in the growing prevalence of written manuals governing procedures in various areas, e.g., human resources and operations.

There are, in the 2012-2014 period, three reports of MFOs that do not fall under Reserve Bank of India regulation since they do not take the legal form of non-banking financial companies, namely, Annapurna (2014), which is a cooperative, and the two reports on Guardian (2012 and 2013), which is a section 25 company. Although the raters acknowledge that the Reserve Bank of India guidelines are not compulsory for these organizations, they still make direct reference to these guidelines in their assessments.

> "Though [Annapurna] does not fall under the purview of RBI guidelines, few modifications in product features were made to adhere to the guidelines. However compliance with income limit, CB check and repayment tenure would have improved its performance on client protection parameters" (Annapurna, 2014).

The Reserve Bank of India rules for non-banking financial companies require that, inter alia, the MFOs make assessments of their clients' indebtedness level, do not levy prepayment or delayed payment penalties, charge interest rates below the cap, present the interest rate on a reducing-balance basis, and only include interest rate, a limited processing fee, and an insurance premium in the price. The raters indirectly refer to many of the Reserve Bank of India rules when assessing MFOs that are run in other legal forms than the non-banking financial company as well, such as in the case of prepayments.

> "Foreclosure and prepayments are allowed with no additional charges however Guardian has not experienced any prepayments so far" (Guardian, 2012).

> "Although there are no pre-payment/ pre closure penalties, in case of Annapoorna the advance interest amount collected upfront at the time of loan dis-

> bursement is not returned for the number of days remaining at the time of prepayment" (Annapurna, 2014).

An entire section that focuses on "client protection" was incorporated into the 2012-2014 reports and covers the following seven principles: "Appropriate product design and delivery"; "Prevention of over-indebtedness"; "Transparency"; "Fair and respectful treatment of clients"; "Mechanism for complaint resolution"; and "Privacy of client data." With the inclusion of this category, the raters assign considerably more space to discussion of these issues. As part of this section, the concept of "client feedback," which was included in the 2006-2007 reports but was not then figured into the final rating grade, has been reintroduced.

> "Annapurna participates/conducts studies to understand and improve its practices. In November 2013, it also started making calls to clients to gauge their awareness and satisfaction levels. It plans to continue this practice with a much larger sample" (Annapurna, 2014).

Another addition is the implementation of a formal mechanism for grievance and complaint resolution, as per Reserve Bank of India guidelines.

> "Mechanism for complaint resolution – moderate
>
> - There is no formal complaints' desk/box at unit/branch and HO. (…)
> - The contact number of the unit office and unit officer are mentioned in the group register. After receiving a compliant, the branch staff is supposed to immediately respond to the client, however, there is no formal process for escalation of complaint.
> - During their field visits, monitoring staff, internal auditor and CEO ask feedback from the members and try to know issues.
> - The BoD has initiated an annual program where they meet the clients of all units and take their feedback on the services provided by Guardian.
> - HO does not maintain any database of complaints received at the branches. Also, there are no checks to ensure proper redressal of clients' grievances by the branches" (Guardian, 2012).

As the target constituency enters into financial contracts with the MFO as borrowers or insurance subscribers, the raters also stress the role of the MFO in clearly and actively communicating the terms and conditions of the agreements, as well as ensuring that these conditions have been understood. Receipts and signatures are prevalent factors of the discussion, communication is preferably carried out in the local language, interest rates are assigned on a declining rate basis, and loan cards or the equivalent are expected.

> "The loan product features are explained during the group formation, collection of loan application and loan disbursement. (…) The loan documents are in the local language. The terms and conditions are also printed on the loan document. A printed repayment schedule is provided to the clients at the time of loan disbursement. Majority of the visited clients were aware about the interest rate, processing fee, insurance fee and instalment amount. The changes in the interest rate and term were communicated to the clients" (Guardian, 2012).

Providing information about the financial contract and/or transaction to the target constituency is, however, not considered sufficient; the raters regard it as the responsibility of the MFO to also ensure that the target constituency fully understands the implications of this information.

> "The staff has not been adequately trained on communicating with the clients to ensure that the clients can understand the terms of the contract, their rights and obligations. However, the pricing mechanisms are clear and do not create confusion on the total costs" (SNFL, 2012).

> "High emphasis on staff training to enable them to explain product features to clients – LMS product certification compulsory for all field staff" (ASPL, 2013).

The phenomenon of loan utilization checks emerges as a frequently addressed concept and even gets its own acronym, "LUC," in 2012.

> "Policy on loan utilisation checks (Pollock and D'Adderio) was not followed strictly. LUC are mostly conducted at the time of collection of first installment. CO/BM ask the members if they have used the loan amount for stated purpose or not and record their findings for the group as a whole in the post in-

> spection survey format. The efficacy of utilisation checks could be improved" (MIR, RGVN, 2012).

Since the introduction of the new category "NBFC-MFI"[59] in 2011, individual loan appraisals are a regulatory requirement for NBFC-MFIs. As I describe in Chapter 6, the framework stipulates that lending MFOs have to ensure that each and every borrower lives up to several conditions related to annual household income levels, total indebtedness, group membership, and other borrowing sources. Such regulatory requirements necessitate individual loan appraisals as opposed to group-level decisions, and a clear shift away from groups toward individuals can be noted.

> "Loan application is prepared by the CO who visits each borrower's house to ensure that all details required in the application are complete and correctly furnished. S/he then gives his/her recommendation regarding the loan estimated on the basis of cash flows of clients household, activity and adherence to financial discipline. At this stage clients are rejected if they do not comply with RBI guidelines on income and indebtedness" (RGVN, 2012).

> "SNFL has now limited its operations in the state of Tamil Nadu and changed its business model from wholesale lending to SMBTs to lending to the individual borrowers directly. This has been done in order to achieve standardisation of operations to allow better monitoring and control" (SNFL, 2012).

However, the reports also assess whether or not Guardian, which is a non-profit section 25 company, has adopted a more individualized approach to the loan process.

> "Loan application is prepared by the COs who visit applicants' houses to ensure that all required details are complete and correct. COs then appraise and propose loans on the basis of income and cash flows of the applicants. Guardian introduced individual loan appraisal format last year to capture data on multiple borrowings and family's income and expenditure" (Guardian, 2012).

In the most recent reports, the raters pay increasing attention to the staff of the rated MFOs. The idea of giving feedback to the executive management

[59] Non-banking financial company microfinance institution.

and the board, which in earlier reports was restricted to the clients, has been expanded to also encompass staff.

> "The Board started Directors Annual Review Tour (Dart) to evaluate the quality of implementation of systems and processes in the field. Feedback from staff and clients are generated which are taken into consideration while preparation/review of business plan and formulation of policies. DART is conducted before the Annual General Meeting (AGM). DART report provides direction to the CEO for future action" (Guardian, 2012).

> "Issues: Scope for improvement in customer and staff feedback system and in audit process to include Wealth Management advice process" (ASPL, 2013).

In the most recent reports, there are also descriptions of client targeting processes being focused on the poor and those living in "challenging" areas, initiatives that seem to be appreciated by the raters.

> "Strengths: Operations in geographically challenging areas" (RGVN, 2012).

> "The MFI plans to start using PPI [Progress out of Poverty Index] score for client targeting by the end of the year, enabling inclusion of underprivileged households. (…) It has included SPM [social performance management] parameters in internal audit and plans to include social performance parameters in staff performance appraisal" (RGVN, 2012).

The reports also begin to address several "social" issues related to staff in the 2012-2014 sample; there are, for instance, examples of the raters commenting on the percentage of staff members who are women, as well as on caps in incentive systems.

> "Staff are eligible for monthly incentive which is based on members added, increase in portfolio outstanding, recovery rate and number of new loans and reloans. Additionally incentive is given on service quality by way of 'files with no remark' and 'no rescheduling/cancellation of disbursement'. Incentive is capped for members added, increase in portfolio outstanding and number of new loans and reloans" (Annapurna, 2014).

> "The main parameters on which the performance of field staff is evaluated are customer enrolment, audit and compliance and wealth management (which should be in tune with household needs). Performance incentive is capped at 20% of [cost to company] and paid to field staff at half yearly intervals. All staff are provided insurance cover (medical, accident and life). Non-monetary incentives like exposure visits for outstanding performers are also provided" (ASPL, 2013).

> "Performance appraisal for all staff is done by respective supervisors. Performance incentive of a [credit officer] is based on quantitative (forming 75% of total, including repayment rates, PAR>30, active borrower and average outstanding) and qualitative parameters (25%, including quality of credit disbursed and recovery, behavior with clients, adherence to code of conduct and other parameters). A proposal to include Social Performance Management parameters in the performance appraisal system is under consideration" (RGVN, 2012).

Template III: Social outcomes

With the introduction of the new heading "Alignment of practices with mission," there is an outspoken expectation that the organization not only deliver on the financial side, but also have a mission in place, which, in the following excerpts, may include components such as poverty targeting, expansion into challenging areas, credit-plus services, and female empowerment.

> "It's vision is 'Serving entire North Eastern region and impacting 2 million lives by the year 2015 and facilitate better access to health, education and livelihood opportunities'" (RGVN, 2012).

> "The mission of SNFL is 'to facilitate easy and timely access to credit and other financial services, for the rural population especially poor women and rural artisans through a network of MBTs located in their vicinity'" (SNFL, 2012).

> "The mission of Guardian is to promote water and toilet facilities which it follows diligently as all the loan products offered are for water and sanitation activities (construction for toilet, connection for water supply, renovation of toilet and water connections, water purifier)" (Guardian, 2012).

> "Annapurna's mission is 'to make the poor and needy women financially and socially empowered and strong and to bring happiness in their lives'" (Annapurna, 2014).

In addition, the raters assess the loan products offered by the MFO and how well they meet the client's needs in terms of, e.g., the intended purpose of the loan and the level of the interest rate.

> "The interest rates on the loan products is also priced lower at APR of 22.4% in comparison to the allowable limits for MFIs (cost of funds + 10%/12% which is in the range of 26% to 28% for the NBFC-MFIs as prescribed by RBI) as Guardian targets the lower income segment" (Guardian, 2013).

> "Issues: Annapoorna loans are of twenty weeks tenure which not only limits its use for productive purposes but also increases the interest burden on clients as in each cycle 1% processing fee is collected" (SNFL, 2012).

> "Loan is provided for various purposes and is not restricted to income generation activities" (Annapurna, 2014).

When it comes to the eligible target constituency in these most recent reports, the focus on the individual as opposed to the group cannot go unnoticed. The new Reserve Bank of India requirements for NBFC-MFIs include an obligation on the part of the MFO to make assessments on an individual basis before extending a loan.

Template III: Financial outcomes

There is a continued pressure on the MFOs to act as market players. This is manifested in an emphasis on operational efficiency, productivity, and cost control; an increasing focus on not only being sustainable but also generating profits; evaluations of strategies to handle risk as well as competition; and assessments of how efficiently the MFO manages its financials. The reports thus maintain that financial sustainability and profitability are central to the rating, and a negative "Return on assets" is treated as an obstacle.

> "Addition of branches in other north-eastern states could result in higher monitoring cost and thereby an increase in OER. (…) OER increased from 7.9%

(annualised) during FY 2010-11 to 9.8% during FY 2011-12 in spite of higher productivity as average personnel cost increased by 50% during the period. With its planned expansion, it would be difficult for the MFI to keep its operating expenses and loan loss provisioning within the margin cap of 10% applicable to NBFC-MFIs with assets > Rs 100 crore" (RGVN, 2012).

"The co-operative society has consistently registered positive returns despite high operational expense ratio as compared to a typical MFI on account of lower borrowings and thus lower financial cost. However during April-September 2013 improved staff productivity has contributed to better efficiency bringing it near to industry standards. The increased efficiency has led to higher RoA of 2.1%; it would have been even higher but for reduction in interest rates. Being a co-operative, Tier I capital adequacy ratio (CAR) is moderate but Tier I+II CAR is good on account of sub-ordinate debt" (Annapurna, 2014).

"**Profitable operations:** RoA for the period April – September 2012 was 3.6% (annualised).The portfolio yield increased from 26.7% in FY 2011-12 to 31.7% in April – September 2012. Interest is charged on flat basis and deducted upfront from disbursement thereby ensuring healthy yield irrespective of the portfolio quality. Further, yield has also increased because of the new loan product – shorter tenure of 20 weeks and an upfront [loan processing fee] of 1% (SNFL, 2012, **bold** in original).

There are also instances where the raters seem to provide a legitimate justification for poor financial figures, e.g., in the case of Guardian's high costs and Annapurna's voluntary cap on staff productivity.

"The operating expenses ratio at 12.8% during 2010-11 seems high if compared with MFI but has to be seen in the context of its different operational model of identifying new borrowers every time and fixed small loan size" (Guardian, 2012).

"Annapurna aims at an average staff productivity of 700 borrowers per loan officer with a cap at 750; as on 30 September 2013 field staff productivity was at 523 and comparable with urban MFIs" (Annapurna, 2014).

Prevalence of key concepts in the templates

One way of supporting the idea of three templates is by showing that a certain terminology also can be associated with each template. As shown in Table 12, it is possible to distinguish a certain type of terminology in each template. As I have elaborated on in the above text, the reports from the early years reflect attempts to create strong and homogenous groups; decision-making is commonly described as participatory; and the "Subsidy dependence index" is typically used to assess the financial standing of the organization. In Template II, the terminology shifts, and while the raters discontinue many concepts, new ones are introduced in their place, e.g., the growing prevalence of discussion of entrepreneurs and return on equity. Although Template III shares much of the terminology used in Template II, certain concepts are especially frequent in the 2012-2014 reports, e.g., independent directors, manuals, feedback from clients and staff, and mission and vision statements.

Table 12. Analysis of prevalence of key concepts

	1999-2004 (24)	*2005-2011 (27)*	*2012-2014 (6)*
Homogenous groups (procedures)	12	1	1
Strong groups (procedures)	28	3	0
Group-level/Internal savings (procedures)	24	8	0
Participatory / Participative decision-making regarding staff and the target constituency (procedures)	12	2	2
Subsidy dependence index (financial outcomes)	70	0	0
Entrepreneurs and entrepreneurship (social outcomes)	0	18	3
Return on equity (financial outcomes)	2	33	3
Independent directors (structures)	1	21	10
Loan utilization check / LUC (procedures)	13	25	22
Manuals, e.g., training, human resources, operations, audit (procedures)	10	13	15
Feedback from clients and staff (procedures)	0	3	19
Mission and vision statements (social outcomes)	0	12	18
Strategic / Business / Five-year plan	13	29	14

Descriptive and normative text

The above discussion revealed considerable changes in how different organizational elements have been evaluated over time, together forming vastly diverging templates for MFOs. This suggests that the rationale for evaluation has undergone transformation and change. However, this does not reveal how articulate and intense the raters are in communicating the template. In this section, I aim at measuring the strength of the template, thereby investigating the following research question: *How does the template change in strength over time? (Question 1c)*.

The methodological choices and considerations are described, at length, in Chapter 4. In short, to operationalize the strength of a text, I have analyzed changes in terms of descriptive and normative text. I coded 14 reports along the metrics of descriptive text, normative value text, and normative prescriptive text. Seven reports were from 1999-2003 and are

referred to as Group 1, and the remaining seven reports are from 2011-2014 and are referred to as Group 2. (A more detailed discussion of the sampling within the larger sample is presented in Chapter 4.)

Until the beginning of 2008, the sample reports include precise lending recommendations in Indian currency.[60] Apart from these lending recommendations, these reports also include "Projected cash flows and financial statements for five years."[61] All reports in the first format, which persisted until 2006, contain the heading "Creditworthiness," wherein the raters elaborate on the rationale for the rating grade and the lending recommendations.

In the first reports from 1999, M-CRIL also gives explicit "Suggestions" to the MFO in the three areas of governance, management and financial performance under a separate heading at the end of the report.

As of 2007, which saw the launch of the second format, the reports include an outlook assessment which is either positive, neutral/stable, or negative. A positive outlook suggests that the organization is expected to improve its rating in a one-year period to move up one level; a neutral/stable outlook suggests that the organization is likely to retain its rating; and a negative outlook suggests that the organization will likely receive a lower rating in the future (see, e.g., Annapurna, 2014).

Normative text from 1999-2003

To impart a better understanding of how the raters evaluate and prescribe MFO structures, procedures, social outcomes, and financial outcomes from 1999-2003, below are some examples. The first two sentences are normative value sentences, and the last is a normative prescriptive sentence. I have underlined the terms that motivated my decision to categorize the sentence as either a normative value or prescriptive sentence. For social outcomes, no sentences could be identified inn Group 1.

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[60] The last report in my sample to have lending recommendations is the report on Grameen Koota from March 2008.

[61] The last report in my sample to have the category "Projected cash flow and financial statements for five years" is the report on SNFL from July 2008.

STRUCTURES

"The board of the organisation is made up of some <u>very eminent</u> professionals who have a <u>reasonably</u> high degree of interest in the activities of the organisation and are also involved in fund raising for SKS" (SKS, 2001).

"The present <u>limited capacity</u> of the internal audit team allows it to visit a small number of groups and branches." (GVMF, 2001).

"Suggestions: (…) Members <u>can be</u> encouraged further to take a more active role in operational issues and transactions at the Centre level" (Cashpor, 1999).

PROCEDURES

"The lack of consolidated information is a <u>weakness</u> in BWDA's microfinance programme" (BWDA, 2001).

"However, the organisation was managing <u>well</u> essentially due to small operations and very few delinquent loans and the sangam manager's follow up on those loans that were delinquent" (SKS, 2001).

"Given the weaknesses in the management system, it is <u>strongly suggested</u> that the loan from SIDBI should be made conditional to the organisation establishing a formal tracking system for overdues" (BWDA, 2001).

FINANCIAL OUTCOMES

"CFTS's operating efficiency ratio is also <u>poor</u> and has been measured at a very high 376% (due to the present outreach and staff structure relationship), though this ratio should improve in the next one year with a rapidly growing portfolio and slower growth (than before) in the operating costs" (Cashpor, 1999).

"In terms of field staff productivity the organisation displays <u>weak</u> performance – the number of active borrowers per member of field staff stands at just over 66" (SKS, 2001).

> "The organisation needs to consider ways to increase its profitability – one clear way is to increase the productivity of staff in terms of numbers of active borrowers and portfolio handled" (BWDA, 2002).

Normative text from 2011-2014

Below are some examples of normative text from the 2011-2014 reports. As above, the first two sentences represent normative value sentences, and the last sentence is a normative prescriptive one. I have underlined the terms that motivated my decision to categorize the sentence as either a normative value sentence or prescriptive sentence.

STRUCTURES

> "The level of participation of the board members in strategic decision making and in exercising oversight is good" (Guardian, 2012).

> "Strong Board with qualified and experienced professionals in the field of banking, microfinance and development" (RGVN, 2012).

> "Compliance of internal audit findings needs to be improved" (SNFL, 2011).

PROCEDURES

> "Well developed operational, HR, accounting and internal control manuals" (Guardian, 2011).

> "Annapurna has a well documented HR manual which integrates guidelines of acceptable code of conduct to be followed by all employees" (Annapurna, 2014).

> "The staff need to be trained on the use of Code of Conduct in their work" (SNFL, 2012).

SOCIAL OUTCOMES

> "Appropriate product design and delivery – WatSan products designed to suit the need of clients" (Guardian, 2013).

> "Issues: Annapoorna loans are of twenty weeks tenure which not only limits its use for productive purposes but also increases the interest burden on clients as in each cycle 1% processing fee is collected" (SNFL, 2012).

> "SNFL will also need to review its products from the perspective of client needs" (SNFL, 2012).

FINANCIAL OUTCOMES

> "Operating efficiency – improved due to better staff productivity" (Annapurna, 2014).

> "Guardian has been incurring operating losses since beginning and but has maintained a good portfolio quality with PAR (>30 days) of 0.1% on 31 March 2012" (Guardian, 2012).

> "Average cash in hand and at the banks during April – September 2012 was 14.05% of the average total assets which is high and there is a scope for more efficient utilisation of funds" (SNFL, 2012).

Analysis of textual investigation

In this chapter, I aim to analyze the main findings of the previous chapter's textual analysis of the rating reports. I have structured the chapter into four sections, each of which deals with one of the four findings from the empirical investigation.

Incorporating and raising the bar for financial performance

When analyzing changes in how the raters categorized and emphasized different headings over the years, several trends can be noted. It appears as if many themes that are discussed in the "Financial performance" category are increasingly also considered under one of the other two rating catego-

ries of "Governance" and "Management." Sometimes the same heading is found under both the "Financial performance" category and "Governance" or "Management," as is the case with "Fund mobilization"/"Mobilization of funds." Other times, one heading is mainly discussed under either "Governance" or "Management," but it has a direct bearing on financial performance; "Staff productivity" and "Operational efficiency" are, for instance, two dimensions that, perhaps surprisingly, have been placed under "Governance" as opposed to "Financial performance." Existing headings that have a direct impact on financial performance figures also come to receive an increasing amount of dedicated space in the reports.

Apart from how headings are organized under the different rating categories, the reports also reflect a tendency to encourage the implementation of governance and management structures and practices that ensure financially sound operations and safeguard the prioritization of efficiency, profitability, and growth. Despite the fact that the raters place less weight on actual financial performance indicators when assigning rating grades, there has been an emphasis on structures and procedures designed to improve efficiencies and reduce costs. The grey boxes in Table 13 indicate headings that have a direct impact on the financial performance of the organization.

The above observation is especially interesting when bringing into the equation the changes in rating weightages over the years. Notably, the "Financial performance" category was reduced considerably in terms of rating weightage, from approximately 50% in the early ratings to 30% in the more recent ones. The category referred to as "Management," however, remained stable in terms of rating weightage at 30%. The rating weightage has thus shifted away from "Financial performance" and toward "Governance," which could indicate that the importance of "Financial performance" has decreased in the ratings. At the same time, there has been a change in how the different rating categories are defined by the raters and where different headings and indicators belong. Several headings that are closely related to the financial performance of the MFO have been introduced into or reinforced in the reports under "Management" and "Governance."

Table 13. Changes in headings and rating weightages

	1999-2006	2007-2011	2012-2012	Change
GOVERNANCE				
Rating weightage	20%	30%	40%	↑
Headings	Strategy for microfinance operations		Operational and growth strategy	
	Experience in microfinance			
			Competition	
			Fund mobilization	
			Board	
			Second line of leadership	
			Alignment of practices with mission	
			Shareholding pattern	
MANAGEMENT				
Rating weightage	30%	30%	30%	↔
Headings	Human resources quality and management		Human resources quality and management	
			Staff productivity	
			Operating efficiency	
	Accounting and MIS		Accounting and MIS	
	Tracking system for overdues		Tracking system for overdues	
	Financial planning and control systems		Financial planning and cash management	
			Internal audit and control	
	Quality of clients/member groups		(Quality of clients/member groups)	
	Infrastructure		Infrastructure	
	Decision making			
			Client protection	
FINANCIAL PERFORMANCE				
Rating weightage	50%	40%	30%	↓
Headings	Credit performance and asset quality		Credit performance and asset quality	
	Mobilization of funds		Capital adequacy	
	Asset, liability and equity composition		Asset, liability and equity composition	
	Sustainability and profitability		Profitability and sustainability	
			Portfolio diversification	
			Margin analysis	

When analyzing changes in indicators, the number of indicators has increased, with a peak during the years 2007-2010, and more "financial" indicators have been introduced. In the early reports, the raters use more soft measures to capture the financial standing of the organization. The "Cumulative repayment rate," for instance, which is a common risk indicator during the early years of the sample, captures the total amount of repayments made so far compared to the total amount due, and thus gives a sense of the repayment pattern over a long period of time. This suggests a rather patient and steadfast approach to repayment from the lender's point of view. The "Cumulative repayment rate" is successively replaced by more short-term, detailed, and accurate indicators, e.g., "Portfolio with arrears 1-30," "Portfolio with arrears 31-60," and "Portfolio with arrears 61-90." When measuring financial sustainability and profitability, there has also been a change in the type of indicators measured from the "Subsidy dependence index" to "Return on equity," which is a commonly used indicator in the financial sector. Around 2003, the raters ceased to track "Group-level savings," which is an indicator that has no direct bearing on the financial results of the MFO. There has been an increase in various indicators and ratios pertaining to growth and size, including the growth in members, clients, active borrowers, staff members, portfolio, and loan size. The reports give increasing attention to efficiency and productivity, and indicators such as "Cost to company per employee," "Cost per borrower," and "Active borrowers per members" are common in the more recent reports.

As shown in Table 11, the benchmarks presented in the reports have changed substantially over the years; from 2001 to 2011, the portfolio at risk decreased from 6% to 0.7% and the operational expense ratio decreased from 20% to 8.6%. This reflects the general trend of Indian microfinance in terms of increased efficiencies. In a rapidly transforming sector such as microfinance, this means that MFOs are constantly being compared against peers. At the same time, M-CRIL makes a distinction between benchmarks, i.e., industry or "top ten" averages, and rating standards. The performance standards employed are not always on par with the industry averages. M-CRIL has indicated that it strengthened its rating methodology in 2001, and did so again as sometime between 2003 and 2005. This means that the minimum requirements for attaining certain rating grades were in-

creased, e.g., in terms of capital adequacy. From this it follows that the same assigned rating grade in the "Financial performance" category in 1999 does not reflect the same performance 15 years later.

In parallel to the above-noted developments, there is also a shift in how the issue of client awareness is categorized, first as a potential default risk and later as an indication of social performance. In the new rating product of 2012, a full section called "Client protection" was added under the "Management" category. The heading "Quality of clients/member groups" is missing from most sample reports. Issues pertaining to client awareness that had been discussed under "Quality of clients/member groups" are after 2012 discussed under the new "Client protection" section. However, discussion of issues pertaining to the quality and dynamics of the group have been abandoned completely. What this suggests is that there has been (1) a shift in the rationale for discussing client awareness from a potential risk of default to social performance; and (2) an exclusion of a discussion on group quality and dynamics.

The heading "Decision making" is also gradually removed from the reports and is completely removed after 2006.

As discussed, M-CRIL's rating instrument has changed in several substantial ways since the inception of the ratings. Despite the decreased weight of the "Financial performance" category, financial indicators, along with organizational features that safeguard the financial performance of the MFO, have been incorporated into the other rating categories. As the sector has become commercialized, indicators, benchmarks, and standards used by the raters have also followed suit, thus raising the bar in terms of financial results.

Three sequential templates

When investigating and analyzing the sample reports based on (Suchman, 1995) organizational elements, I gradually began to discern three different approaches to assessing MFOs in terms of their structures, procedures, social outcomes, and financial outcomes. It appeared as if some organizational features were considered important during some periods of time, while others were left out of the assessments. More importantly, the rationale, or

underlying logic, in the assessments changed over time. I defined a "change in the template" as having occurred when the evaluation rationale for assessing at least one of the organizational elements underwent a substantial and enduring change that was apparent in several reports. To avoid repetitions, a more thorough analytical discussion about the actual changes in the template contents is provided in Chapter 6.

The time periods of the three templates should not be treated as precise, but rather as indicative of when one rationale for assessing MFOs more or less had been overridden by a new rationale. The years 2003-2005 should, for instance, be seen as a grey-zone transition period during which the rationale for evaluating structural and procedural elements gradually changed. To support the idea of three sequential templates, I also conducted a simple word count analysis to show that certain terminology was associated with certain time periods in the ratings (see Table 12).

Notably, changes in the reports do not generally happen suddenly, but instead are commonly preceded by smaller events and telltale signs that indicate what is about to happen. Similarly, when elements leave the reports, traces and fragments often remain. In the case of client protection and transparency, for instance, this was included as a non-rated section in the year 2006 and thereafter disappeared, only to reenter the reports in 2012, this time weighing in the rating grade.

Table 14 summarizes the three sequential templates identified in the above investigation. The shift from the first to the second template mainly occurs in terms of structural and procedural elements, while the evaluation of outcomes remains relatively stable. In Template II, several changes can be noted in how the raters evaluate structural and procedural elements compared with the earlier years. The reports from 2012-2014 (i.e., Template III) use a similar approach to evaluating organizational structure as was in the previous template, although some aspects have been revised. The evaluation of procedural elements in Template III emphasizes transparency, fair treatment, responsible practices, and formalization in the relationship with the target constituency. The evaluation of social outcomes has changed from being implicit in the first template to being explicit and clearly articulated in the third template. The most stable and constant organizational element as reflected in the templates is that of financial outcomes.

From the start of ratings until 2014, the raters have been relatively consistent in their push towards improved efficiency and sustainability/profitability.

Although the Indian microfinance sector as a whole, as well as the sample used in this dissertation, exhibits heterogeneity and fragmentation in terms of legal form, general orientation, organizational size, microfinance delivery models, and other factors, the reports do not consider such individual differences in their evaluations. Instead, organizations are evaluated against the same measuring stick, with one template active at a time.

When the transformation process from trusts and societies into non-banking financial companies gains momentum, the non-banking financial company form quickly becomes the preferred legal form among raters. For those MFOs operating as, e.g., trusts and societies, the legal form is discussed and enshrined as an important issue. The non-banking financial company represents the only legal form whose microfinance activities are regulated. The governance model that is both implicitly and explicitly promoted draws on the corporate governance model.

In the third template, all MFOs are more or less assessed based on how well they comply with the new Reserve Bank of India regulation, although this regulatory framework is mandatory for the new category of "NBFC-MFIs"[62] only. Other examples in which the evaluators rely on the regulatory framework in their assessments are in their discussions about satisfactory levels of capital adequacy. From a different perspective, in Template III, all MFOs are evaluated based on how well their practices are aligned with their mission, implying that even for-profit corporations such as non-banking financial companies are expected to have more than financial goals.

[62] Non-banking financial company microfinance institution.

Table 14. Summary of the three sequential templates

STRUCTURES	*PROCEDURES*	*SOCIAL OUTCOMES*	*FINANCIAL OUTCOMES*
Template I (1999-2004)			
Mixed legal forms Community ownership as dominant idea for non-banking financial companies Board is to guide and support Executive management and board "on par" with one another Local experience is valued Presence of target constituency on board is welcomed Groups expected to make their own decisions	Poverty targeting Careful group formation processes Homogenous, strong, and independent groups Groups engage in recordkeeping Internal savings mobilization and circulation Staff participate in operational decision-making Zero-tolerance policies vis-à-vis arrears Incentive systems based on repayment and managed portfolio Management and information systems and accounting systems in place	Vision and mission statements lacking The target group consists of poor, rural, women organized into homogenous groups Non-financial services common	Financial sustainability High repayment rates High staff productivity and low costs Geographically concentrated operations; optimizing horizontal and vertical coverage Interest rate set after financial sustainability Clear cost allocation
Template II (2005-2011)			
Non-banking financial company as preferred legal form Microfinance operations in separate legal entity Private equity investors Board monitors organizational performance	Strategies to manage competition Reaching the many Targeting the unbanked Focus on internal MFO processes, e.g., group audits, loan assessment procedures Formalization and	Vision and mission statements largely lacking Widened definition of the eligible microfinance client to also include urban, entrepreneurs, individuals, the unbanked Non-financial services justified as a competitive ad-	Profitability High repayment High staff productivity (but should not affect the portfolio at risk) Geographically diversified portfolio Interest rate set based on political sentiment, competi-

Independent directors and experienced professionals as board members Executive management and board separated Target constituency on board is seen as problematic due to lack of relevant expertise Organograms	standardization of client-MFO relationship Zero-tolerance policies relaxed; rule-based cases of genuine distress Incentives consider adherence to policies and compliance with processes Written manuals and codes of conduct; staff decisions based on formal rules	vantage and as a means to retain clients	tiveness, and financial sustainability
Template III (2012-2014)[63]			
(Socially engaged board) (Diversified board)	Focus on individuals, not on groups Further formalization and standardization of client-MFO relationship Written manuals Industry codes of conduct Formal regulation Incentives have caps and consider social performance parameters	Explicit vision and mission statements Target group consists of the poor, the unbanked, and individuals Loans for relevant/useful purposes Consideration of client needs in product design Interest rate set low to benefit client	Continued focus on profitability Instances of bounded financial performance; e.g., capped staff productivity and high OER for a social cause Interest rate set to reach profitability but within Reserve Bank of India cap

Explicating and mediating tensions

During the analysis of the reports, a number of explicit tension-infused situations within the same rating report are identified. In many of these cases, it is unclear what the raters' verdicts are, as they adopt a considered tone

[63] Parenthesis implies that the observation only was made in one or a few reports.

and weigh positive aspects against negative ones without stating which is preferred.

To start with, in the reports from 1999-2003, the strong emphasis on financial performance combined with more socially oriented structural and procedural elements gives rise to a number of emerging tensions and conflicts. More specifically, accounts depicting an MFO's quest to target socioeconomically weak sections of society do not always mesh with the raters' push for financially sustainable operations. There is a direct tradeoff between only targeting the poorest villages in a given geographical area of operation or focusing on as many villages as possible in the same area, and thus increasing scale and efficiency. There is also a tradeoff between only targeting the poorest individuals within a given village, or attempting to assist as many individuals as possible, without considering their socioeconomic profile. Another area that indirectly prompts tension is when the raters assess the mobilization and circulation of group-level savings. Since these savings never end up in the account books of the MFO, but instead cause reductions in staff productivity indicators, they may be difficult justify from a financial performance perspective.

In Template II, examples of confusing messages in terms of the tradeoffs between financial outcomes and social outcomes are articulated in the ratings of Mahasemam and SNFL. In the case of Mahasemam, the raters note that the organization offers non-financial services such as healthcare and education to its target constituency. The raters acknowledge that these differentiate the organization from its competitors and help build client loyalty and retention. These credit-plus services are partly cross-subsidized by the income from the interest rate paid on loans. While the raters applaud Mahasemam for providing credit-plus services and perceive this as one of the organization's four "positive highlights," they also note that the organization's high interest rate due to the provision of credit-plus services is one of four "negative highlights." A high interest rate, it is argued, makes the organization less competitive. A similar explicit tension is found in the 2011 SNFL report. The raters see ASSEFA's field-level development activities as a key strength of SNFL. At the same time, they single out the low staff productivity as a significant weakness and explain it as be-

ing due to the field staff's involvement in the development activities of ASSEFA.

The earlier instance of tension between the socioeconomic status of the target constituency, on the one hand, and the financial performance of the MFO on the other (as found in Template I) has been resolved in the second template. In the ratings of Cashpor and Grameen Koota, i.e., the two organizations in the sample that are described as employing systematic poverty targeting methods, the raters clarify that financial performance aspects such as low costs are prioritized over "poverty targeting."

The most recent reports from 2012-2014 contain a number of explicit tensions, some of which are even articulated on the same page in a single report. One such tension pertains to interest rate. The same report that endorses low interest-rate levels as a means to benefit the target constituency also condemns the organization for not being able to cover its costs and thereby failing to attain financial sustainability. Another tension can be found in the product design. Guardian offers a one-time loan for sanitation, which is treated as a relevant and purposeful loan. The raters acknowledge the social dimension of such a loan, but at the same time, they criticize the fact that Guardian does not offer second-cycle loans in order to retain its clients.

Table 15. Explicit tensions in the templates

Template	*STRUCTURES*	*PROCEDURES*	*SOCIAL OUTCOMES*	*FINANCIAL OUTCOMES*
Template I	LOCAL RESPONSIVENESS AND COMMUNITY OWNERSHIP	BUILDING SOCIAL CAPITAL Targeting the poorest villages Targeting the poorest individuals within the village Mobilizing savings	SOCIAL AS PART OF THE ORGANIZATION'S IDENTITY	TOWARDS FINANCIAL SUSTAINABILITY Low costs High staff productivity
Template II	TOP-DOWN GOVERNANCE	FORMAL	MISSION FOR FINANCIAL CAUSE Non-financial services	FINANCIALIZATION Low costs High staff productivity Competitive interest rate
Template III	(SOCIALLY RESPONSIBLE) TOP-DOWN GOVERNANCE	FORMAL AND TRANSPARENT	EXPLICIT MISSION FOCUS Low interest rate Relevant products with a social impact	BOUNDED FINANCIALIZATION Profitability Client retention Low costs

Changes in template strength

The above analysis of M-CRIL's rating instrument suggests that the rationale for evaluating different organizational elements has changed in important ways over the years, creating an organizational template in constant transformation. When analyzing changes in the template and the rating instrument, I have also considered the concept of strength, operationalized as the amount of descriptive and normative text.

As summarized in Table 16, the strength of the organizational template has changed vastly when comparing reports from the early years to those from more recent years. The template was very strong during the initial

years, i.e., Template I. In the 2011-2014 sample, which more or less covers the third template, the number of normative statements has decreased considerably both in relative and absolute terms. These findings suggest that the language in the reports has changed from firmly instructing and articulating desired behavior, to more passive, descriptive, and factual language.

Table 16. Amount of descriptive, normative value, and normative prescriptive text

MFO	*Total characters*	*Normative value text characters (%)*	*Normative prescriptive text characters (%)*
GROUP 1 (2001-2003)			
GVMF (1999)	18,405	2,337 (13%)	2,649 (14%)
Cashpor (1999)	23,674	4,518 (19%)	3,349 (14%)
GVMF (2001)	41,393	7,149 (17%)	1,062 (3%)
SKS (2001)	38,106	7,990 (21%)	3,217 (8%)
BWDA (2001)	26,019	4,541 (18%)	2,370 (9%)
BWDA (2002)	38,028	4,719 (12%)	3,395 (9%)
Grameen Koota (2003)	38,620	4,577 (12%)	1,306 (3%)
TOTAL GROUP 1			
Characters	224,245	35,831	17,348
Characters per report (%)	32,035	5,119 (16%)	2,478 (8%)
GROUP 2 (2011-2014)			
Guardian (2011)	37,340	6,599 (18%)	452 (1%)
SNFL (2011)	30,960	3,358 (11%)	603 (2%)
RFVN (2012)	50,907	3,923 (8%)	1,401 (3%)
Guardian (2012)	45,174	4,765 (11%)	303 (1%)
SNFL (2012)	43,565	2,927 (7%)	1,249 (3%)
Guardian (2013)	46,515	5,883 (13%)	474 (1%)
Annapurna (2014)	52,472	4,590 (9%)	534 (1%)
TOTAL GROUP 2			
Characters	306,933	32,045	5,016
Characters per report (%)	43,848	4,578 (10%)	717 (2%)

This table shows that there has been a change over time in the amount of normative value text and normative prescriptive text. The reports in Group 2 contain, on average, almost 12,000 characters (without spaces) more than the reports in Group 1. Despite the fact that Group 2 reports are considerably lengthier, there has been a substantial decrease in the absolute as well as relative amount of normative value text, as well as normative prescriptive text, from 1999-2003 to 2011-2014. In four of the most recent reports from 2011-2014, the normative prescriptive text was only around 1% of the total text, while in two of the reports from 1999-2003, the equivalent figure was 14%. Noteworthy, prior to March 2008, the reports also contained credit recommendations, but these were thereafter removed. What the above suggests is thus that, with time, narrative text became increasingly pertinent.

Notably, descriptive text may change in meaning if removed from its spatial and temporal context; the same sentence may prove to be positive for one type of organization at one specific point in time, but negative for another. The mobilization of savings is, for instance, evaluated in positive terms during the early years of rating (see, e.g., GVMF, 2001) and is regarded as a major risk in more recent reports due to a stricter regulatory environment (see, e.g., Mahasemam, 2009).

Chapter 6

Contextualizing rating practices

As I demonstrate in the preceding chapters, the evaluative practices of Micro-Credit Ratings International Limited (M-CRIL) have undergone much change over the years. M-CRIL has, e.g., made formal revisions in its microfinance rating instrument and introduced new rating products. The analysis has also revealed three distinct and sequential organizational templates of the Indian microfinance organization (MFO) from 1999-2014; Table 17 summarizes the content of these. In addition, when investigating the strength of the templates, I found that early reports contain more normative and prescriptive text, as opposed to descriptive text, when compared to more recent reports.

In this chapter, I make an attempt at contextualizing M-CRIL's evaluative practices and the templates that the reports project by discussing the macro as well as the meso level contexts. While the macro level relates to more broad currents and events in the Indian microfinance sector, the meso level focuses on the situated vantage point, market position, and perceived role of M-CRIL. Through this analysis, I aim to approach my final research question: *How do changes in rating practices and in the templates projected through these relate to trends and events in the sector, as well as to the rater's market position? (Question 2)*

The above question seeks to understand how rating practices and the templates, as projected by M-CRIL, correspond to sectoral trends and events, as well as how changes in rating practices and in the template relate to the market position of M-CRIL. The question is broader and more diffi-

cult to delimit than the previous questions I have posed in this dissertation. It is not, however, my aim to explain the causal relationship behind changes in evaluative practices and in the template. Rather, I want to shed light on whether M-CRIL's projected templates converge with and reflect trends and events in the microfinance sector, and whether changes in the templates correspond to changes in M-CRIL's market position.

Table 17. Summary of the three templates

	STRUCTURES	*PROCEDURES*	*SOCIAL OUTCOMES*	*FINANCIAL OUTCOMES*
Template I	LOCAL RESPONSIVENESS AND COMMUNITY OWNERSHIP	BUILDING SOCIAL CAPITAL BRINGING IN SYSTEMS	SOCIAL AS PART OF THE IDENTITY	TOWARDS FINANCIAL SUSTAINABILITY
Template II	TOP-DOWN GOVERNANCE	FORMAL	MISSION FOR FINANCIAL CAUSE	FINANCIALIZATION
Template III	(SOCIALLY RESPONSIBLE) TOP-DOWN GOVERNANCE	FORMAL AND TRANSPARENT	EXPLICIT MISSION FOCUS	BOUNDED FINANCIALIZATION

Contextualizing rating practices from 1999–2004

Rural indebtedness, credit cooperatives, and social banking

It is not my aim here to undertake a thorough analysis of how and why Indian microfinance came into being. However, a brief retrospective of the history of rural indebtedness, rural banking policies, and financial inclusion agendas in India is needed in order to provide context for the emergence of microfinance ratings and, by extension, the content of the first template.

Rural populations in India have long been impacted by poverty, indebtedness and agrarian crises. As formal financial institutions have failed to reach out to much of India's rural regions, usurious moneylending practices have instead become the norm. Coupled with the oppressive caste system, this has served to further reinforce the exploitation and marginalization of the poor (Mishra, 2008).

Until the late 1960s, the credit delivery system in rural India was largely dominated by the cooperative segment. Although India's cooperative credit structure constitutes one of the largest rural financial systems in the world, it has never realized its full potential according to most observers. One reason that is commonly put forth to explain the lackluster performance of the cooperative movement is poor governance, where, e.g., elite groups have come to dominate the boards and used the cooperatives to their own advantage (Shah, Rao, and Shankar, 2007; Sriram, 2005).

From 1969 to 1991, a series of measures were taken to reach rural areas and redress existing inequalities. During this period, also known as the bank nationalization era, many of the largest commercial banks were nationalized, the network of regional rural banks was established, and the National Bank for Agriculture and Rural Development (NABARD) was set up as an apex bank to increase the credit flow to rural populations. The Reserve Bank of India strived to influence the sectoral orientation of bank lending with the introduction of "priority sectors," which stipulated that a certain proportion of the total net bank credit be deployed in given sectors, e.g., agriculture and small-scale industries. In 1989, as a response to distressed farmers, the government also issued its first nationwide loan waiver, an initiative which is unique to the Indian context (Shah et al., 2007; Radahakrishna, 2007).

Despite these efforts, numerous weaknesses have been identified in the rural financial institutions, particularly poor efficiency and profitability, as well as insufficient repayment discipline, and new strategies for the rural credit delivery system were welcomed. The 1991 Reserve Bank of India Committee on the Financial System became the blueprint for the new agenda. As part of the concurrent broader trend toward liberalization, the committee suggested deregulation in the banking sector and took a clear stand against using the credit system for redistributive purposes. Instead,

the committee argued for the phasing out of earlier efforts, e.g., directed credit, branch networks, and subsidized credit. It was argued that Indian banks should be made competitive, and developments in the banking sector should be driven by profitability and market principles (Mohan, 2006; Shah et al., 2007; Sriram, 2005). As a result of the new approach, the number of rural bank branches started to drop, and the share of agricultural and rural credit fell substantially. It was in this context of deregulation and liberalization that the microfinance project was born (Shah et al., 2007).

Deregulation and the birth of the self-help group movement

In the mid-1980s, Indian non-governmental organizations started experimenting with the formation of women's group, referred to as self-help groups, based on traditional South Indian savings and credit groups. In 1992, NABARD initiated a pilot project with 500 self-help groups together with the well-known non-governmental organization Mysore Rehabilitation and Development Association (MYRADA) (Sriram, 2004). Encouraged by the positive results, NABARD catalyzed the Self-Help Group Bank Linkage Program, which was formally launched in 1992 and which is often described as the origin of large-scale microfinance in India. During the 1980s and 1990s, several important apex organizations were also set up with a focus on providing credit to organizations supporting poor women, e.g., Friends of Women's World Banking India in 1982, Rashtriya Mahila Kosh (the National Credit Fund for Women) in 1993, and the Small Industries Development Bank of India (SIDBI) Foundation for Micro Credit in 1999.

Non-governmental organizations, primarily trusts and societies, came to play key roles as facilitators in the NABARD-initiated Self-Help Group Bank Linkage Program. These organizations often had experience in implementing social welfare programs (e.g., sanitation, health, and education) in a particular geographic area. As part of the Self-Help Group Bank Linkage Program, the facilitating organization mobilized poor rural women to form self-help groups, provided capacity-building and training, and linked the self-help groups to the formal financial system. The bank lent to the groups after the incubation period, thus bearing the entire credit risk. The facilitating organizations typically met their expenses by way of external

grants, small contributions from the bank, and payments from the groups (Ananth, 2005).

During the 1990s, many of the facilitating organizations engaged in the Self-Help Group Bank Linkage Program also began launching microfinance operations themselves, most of which operated on a nonprofit basis. These organizations – here referred to as "MFOs" – were no longer simply facilitators that helped link self-help groups to the mainstream banks; rather, they started offering financial services themselves.[64] During these early years, the organizations received funds for on-lending from international donors as well as from Indian apex organizations such as NABARD, Friends of Women's World Banking India, and the SIDBI Foundation for Micro Credit. In these cases, the MFO bore 100% of the credit risk on the portfolio, and the bank's incentive was directed to ensure the solvency of the MFO (Ananth, 2005; Sarkar and Singh, 2006; Shah et al., 2007). The Self-Help Group Bank Linkage Program and the MFOs have come to constitute the two main channels for the provision of microfinance services in India.[65]

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[64] Microfinance services in India are mainly channeled through groups, i.e., self-help group (SHGs) and joint liability groups (JLGs), also referred to as Grameen groups. The Self-Help Group Bank Linkage Program builds on self-help groups, while MFOs use self-help groups, joint liability groups and individual lending. Self-help groups are commonly bigger groups with 12-20 members from homogenous socioeconomic backgrounds. In a typical self-help group, the members make regular small savings deposits, and the group uses its accumulated savings as a pool for internal circulation, or it may open a savings account with a nearby bank. Since 1993, the Reserve Bank of India has allowed unregistered groups to open savings accounts with banks (Goenka and Henley, 2010, p. 53). The self-help groups are also capacitated to undertake relatively extensive bookkeeping within the group. The joint liability groups are smaller in number, record-keeping is typically performed by the MFO, and the focus on savings is less salient. It has been argued that self-help groups create better savings habits and stronger group cohesion, while joint liability groups have more stringent monitoring, as well as faster loan processes, bigger loan amounts, and shorter loan durations (Duflo, Tripathi, and Walton, 2007; Harper, 2002). Another highlighted distinction is that, when lending to self-help groups, the MFO lends to a group, but when lending to joint liability groups, loans are recorded in the names of individual borrowers (Ghate, 2006, p. 57). Many of the larger MFOs have adopted mixed models and approaches (CRISIL, 2009).

[65] For the most part, with the exception of the Self-Help Group Bank Linkage Program and MFOs, cooperatives and regional rural banks provide small loans. However, although the portfolios of the cooperatives and the regional rural banks have a focus on agriculture and allied activities, they predominantly lend to large-scale farmers and small businesses, while low-income clients constitute a very small portion of their portfolios. In 2009, these two channels jointly disbursed more than twice the amount disbursed by the Self-Help Group Bank Linkage Program and MFOs (Intellecap, 2009).

During the years that followed, several policy changes were made by the Reserve Bank of India that contributed to the growth and evolution of the Indian microfinance sector, including both the Self-Help Group Bank Linkage Program and the MFOs. Perhaps most importantly, the Reserve Bank of India classified loans to self-help groups as "priority sector" lending, meaning that banks could link up with non-governmental organizations and channel funds to self-help groups through them, thereby reaching their "priority sector" targets. In 2000, the Reserve Bank of India also exempted nonprofit organizations (mainly trusts, societies and section 25 companies) engaged in microfinance from registering as non-banking financial companies, which is an arduous and costly affair.[66] In addition, many development schemes targeted to women were also routed through self-help groups. In 1998, the largest meta-association (in terms of number of member organizations) was established in India under the name Sa-Dhan.

In parallel to these developments, microfinance also started receiving increased attention from global players, e.g., the World Summit for Social Development in 1995 and the World Micro Credit Summit in 1997. Some of the most influential global microfinance support and advocacy initiatives were also formed during this time period. One of these was the Consultative Group to Assist the Poor (CGAP), which is a donor consortium launched by the World Bank in the mid-1990s with the goal of supporting the development of financially sustainable microfinance. Organizations such as CGAP raised hopes that microfinance would create a "virtuous cycle" of economic growth from the grassroots up based on the idea of "giving a fishing-rod instead of fish." In 2003, a CGAP report asserts that:

> "[f]inancial services thus reduce poverty and its effects in multiple concrete ways. And the beauty of microfinance is that, as programs approach financial sustainability, they can reach far beyond the limits of scarce donor resources" (Littlefield, Morduch, and Hashemi, 2003, p. 9).

In 1998, CGAP launched a project that grew into the largest publicly available microfinance database and information clearinghouse, MIX Market, whose core purpose was to increase transparency in the sector.

[66] Notably, this did not extend to for-profit companies.

M-CRIL's challenge: Creating order from chaos

One organization that came to play an especially important role in the Indian microfinance sector during this formative period was M-CRIL. M-CRIL was one of four specialized microfinance rating agencies that came into being during the years 1997-2001. In 1998, M-CRIL carried out the first rating of an Indian MFO after an 18-month period of methodology testing and development funded by the Ford Foundation. Prior to the establishment of the SIDBI Foundation for Micro Credit in 1999, SIDBI decided to test M-CRIL's microfinance rating product, and in the same year, M-CRIL obtained its first bulk contract with the SIDBI Foundation for Micro Credit for rating its MFO customers (Chetan et al., 2003). Since then, SIDBI has been the top client of M-CRIL in terms of number of ratings commissioned.

When M-CRIL began operations, the agency saw its chief responsibility as facilitating the provision of financial services to the millions of poor and rural Indians who were excluded from the formal banking system.

> "The number and size of microfinance institutions in India is small in relation to the numbers of poor people in the country. MFIs in India cover no more than 2% of the 60 million poor families in the country" (M-CRIL, 2000, p. 8).

However, at that time, M-CRIL deemed the situation in the microfinance sector to be mediocre, especially when it came to the quality of the staff, systems and procedures, and financial performance.

> "Like all development activities in the region, the disease of mediocrity at the staff level also plagues microfinance" (M-CRIL, 2000, p. 28).

> "Performance is poor and the overall scenario is bleak but there are enough good experiences to hold out some hope that the sector can, in the future, become a dynamic and sustainable component of the poverty reduction effort in the region" (M-CRIL, 2000, p. 2).

M-CRIL understood its role in the larger plan to scale up the Indian MFO project as having two chief components: (1) to bring order to a chaotic sec-

tor plagued by "the disease of mediocrity," as well as a lack of (or unreliable, inconsistent or irrelevant) data; and (2) to reduce information asymmetries by helping prospective investors and banks to understand the potential in the microfinance sector and increase their knowledge about MFOs.

The large corporate raters were, according to M-CRIL, not able to take on the task of rating MFOs, since they lacked an in-depth understanding of the specifics of microfinance; further, their systems and procedures were regarded as not being well suited to rate MFOs (M-CRIL, 2006b, p. viii; e-mail with Alok Misra, 7 September 2014). The former executive director of SIDBI and the founder of the SIDBI Foundation for Micro Credit, Brij Mohan, explains that although the perceived credibility was higher with the Standard & Poor's-controlled Credit Rating Information Services of India Limited (CRISIL), which was an established actor in the mainstream financial market at the time, the advantages of employing a specialized rater like M-CRIL outweighed CRISIL's perceived superiority in terms of credibility.

> "The effort level was higher with M-CRIL, but the credibility level was higher with CRISIL" (interview with Brij Mohan, 25 May 2012).

A perceived problem at the time was that there MFOs had no standardized ways of generating data; the first step in bringing in order to the sector was thus to produce the necessary data.

> "…the systems employed by most MFIs are relatively unsophisticated and, not only is the availability of data inadequate, its reliability is often also open to question. (…) [The] authenticity of an MFI's reporting system is first determined by a snap system audit and, if its reliability is found to be unsatisfactory, data is physically reconciled from base level records. In an average, small-medium Asian MFI with 3,000-4,000 loan accounts, this could entail examining all the loan ledgers to get accurate portfolio information" (M-CRIL, 2004, p. vi).

Another perceived problem was that there were no systems in place to monitor and analyze the data. M-CRIL thus encouraged MFOs to implement financial control systems, and management and information systems.

> "Management information systems in use are improving but still often inappropriate, and the concept of portfolio quality is only now beginning to be understood. Accounting and other microfinance management issues also need attention" (M-CRIL, 2004, p. ii).

If the chaotic situation on the ground was one side of the coin, the other side was the massive information gap, as well as a pervasive lack of awareness of and/or misconceptions about the microfinance sector among potential investors and banks, according to M-CRIL's assessment at the time. To bring in the investors and the commercial banks, M-CRIL intended to design, communicate, and make comprehensible standardized ratios, national and global benchmarks, and best practices through analysis, sectoral reviews and updates. One way of standardizing the Indian microfinance sector was via the creation of "the M-CRIL top 10" from M-CRIL's MFO database. This type of benchmark reflects the performance of the ten best Indian MFOs and is present in the M-CRIL reviews.

During the first years of the 21st century, M-CRIL was the sole rater in the Indian microfinance space, and the agency's microfinance rating was the only rating product on the market. In 2001-2002, Standard & Poor's CRISIL launched a microfinance grading product, making it the world's first mainstream rating agency to develop a separate methodology and scale to assess MFOs (CRISIL, 2009). This product can be compared to M-CRIL's microfinance rating. However, as indicated in Table 18, CRISIL remained a minor player for several years; meanwhile, M-CRIL dominated the market and undertook a vast proportion of the total ratings conducted during these early years.

Rating practices from 1999–2004 and Template I

As I describe above, the Indian microfinance sector was born after a long period of state-sponsored attempts at building a wide-reaching cooperative movement, followed by the implementation of socially focused banking policies and subsidized credit. Notably, although none of the 1999-2004 sample organizations are either cooperatives or community-owned, there are remnants of cooperative ideas in the ways that structural aspects of MFOs are evaluated during the first template regime. The early reports

demonstrate a measure of tolerance vis-à-vis legal status, and in cases of transformation into a non-banking financial company, the raters express a certain degree of uncertainty and hesitation. A dominant idea that emerges during this time is that the new organization will be owned partly or wholly by the community via so-called mutual benefit trusts.

The organization of formal governance is to a large extent implicit in the first template, with accounts of an integrated model that values the active participation of different stakeholders in policy decision-making, and which sees governance as a collaborative and participatory effort. The board generally is expected to guide or provide input on policy and strategic issues, whereas management is expected to take operational decisions; however, areas of overlap in this relationship are not regarded as problematic. Instead, the reports describe a relationship in which the two entities ("the board" and "executive management") are integrated, and where the boundaries separating the two are indistinct. Furthermore, in this early period, the raters seem to have no objection when executives fill a role on the board. The microfinance movement, to a large extent, grew out of non-governmental organizations that focused on social welfare activities. The organizations were typically small and had close ties to the communities they served. In line with this, localness is deemed to be a positive quality in the early reports, and as such, the integration of the board and the executive management is natural and to be expected.

The inclusion of women in various domains was also a priority for Indian governments during the 1990s. This is, e.g., reflected in how the raters react to members of the target constituency serving as directors on MFO boards. During this period, having representatives from the target constituency on the MFO board is regarded as positive because the target constituency may be able to provide unique perspective and insight at the field level. In addition, the inclusion of representatives from the target constituency is seen as important from the perspective of enhancing the representational nature of the organization.

The evaluation of procedural elements in Template I recalls sociopolitical empowerment movements wherein the aim is to identify, build the capacity of, and empower those who are seen as voiceless and powerless. As an example, the raters describe, in great detail, the procedures employed by

the MFO when it is identifying the area as well as the individuals to be targeted, which commonly involve: socioeconomic considerations; forming and strengthening homogenous groups; ensuring the quality of groups in terms of recordkeeping abilities and internal savings mobilized; assessing groups and determining their eligibility for external loans; and even facilitating the linkage of groups to mainstream banks. The "social" aspects of Template I are oftentimes inherent in the accounts depicting the organization, the organizational genesis and history, and the MFO's objectives in addressing microfinance. MFOs were thus judged not only for their microfinance activities, but also for how well their groups are doing in terms of solidarity and social cohesion.

The raters' approach to the above issues is largely consistent with historic trends, and the template as encoded by M-CRIL reflects broadly held expectations and demands on the Indian microfinance project. However, when it comes to assessing the internal procedures and financial outcomes of MFOs, the raters adopt a proactive, and at times even aggressive, approach. In Template I, the reports encourage ambitious and rapidly deployed growth strategies, increased efficiency and productivity, and improved financial performance indicators. The raters also promote strict discipline regarding repayment and stringent monitoring and tracking of loans, and incentive systems for staff are seen as innovative and interesting initiatives.

On one hand, such measures should be considered in light of the poor repayment rates then facing many cooperatives and an Indian repayment culture that was threatened after a nationwide loan waiver that risked demoralizing borrowers. Also, at this time, global advocacy groups such as the World Bank saw significant potential in microfinance, regarding it as the first financially sustainable, scalable and bottom-up development intervention, and the project was being used to substantiate the popularly held claim that some of our most pressing social ills could be solved through the financially viable yet socially oriented "social enterprise," as opposed to through big state-funded programs.

On the other hand, the Indian sector was dominated by nonprofit entities, and donations, grants, and savings constituted a large part of the funding for these organizations. The sector had yet to be permeated by private

equity and financially oriented investors that demand satisfactory financial performance and ongoing improvements. Although global microfinance advocates had started to push for financially sustainable microfinance, I suggest here that the push for efficient systems and positive financial results, as reflected in M-CRIL's template, diverges from the Indian field context.

M-CRIL's unique position in the Indian rating space bestowed a sense of confidence on the agency, granting it the self-assurance necessary to make explicit judgments about and attempt to shape the future direction of the sector, especially in the domain of financial outcomes such as growth and efficiency and in terms of procedures such as zero-tolerance policies and staff incentives. This is also reflected in the fact that the template during these early days was strong in terms of its normative and prescriptive tone as compared to later on. M-CRIL saw it as its responsibility to guide and lead MFOs on the right track towards financial sustainability and even profitability.

Contextualizing rating practices from 2005–2011

Endorsements, transformation, and growth

The years that followed were characterized by a structural transformation of the Indian microfinance sector, as well as a period of unprecedented growth. This period also saw many large global players endorsing microfinance: the year 2005 was proclaimed as the international year of microcredit by the United Nations; the Nobel Committee awarded the Peace Prize to microfinance in 2006; and in 2008, microfinance was identified as one of four tools that had been proven to work in achieving the first of the Millennium Development Goals, namely, eradicating extreme poverty and hunger.

In the Indian context, M-CRIL also declared that the agency was satisfied with the status in the sector; Indian MFOs had come a long way in terms of financial performance, efficiency, and productivity, M-CRIL contended. This judgment is also reflected in the *M-CRIL Microfinance Review 2005*:

> "Performance has improved dramatically and the leading MFIs in India are now amongst the most efficient worldwide; further improvement can be expected as the level of competition increases" (M-CRIL, 2006b, p. i).

> "There has been a revolutionary change in the thinking of the average Indian MFI CEO in relation to aspects like sustainability and relatively few now argue that welfare considerations make it difficult to exercise financial discipline. With this change of attitude the considerable management experience of the CEOs comes into play, helping to improve the efficiency of MFIs" (M-CRIL, 2006b, p. ii).

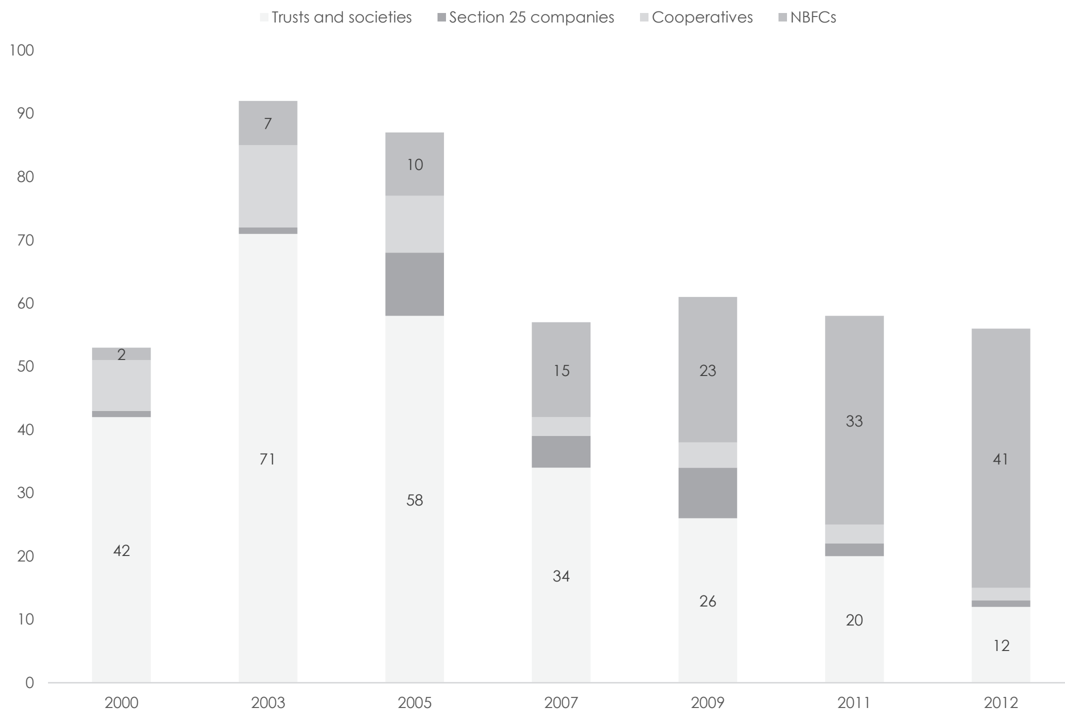
> "During [a 7-year period up to December 2005], the message of sustainability has become substantively accepted by the microfinance sector in India. Interaction with MFIs shows that the advent of rating has made a substantial contribution to this process" (M-CRIL, 2006b, p. 47).

During this period, many of the nonprofit MFOs (i.e., trusts, societies, and section 25 companies) began transferring their microfinance activities to regulated, for-profit, non-banking financial companies, and many notable new microfinance ventures commenced operations under non-banking financial company licenses (Intellecap, 2007, p. 359). From 1999-2010, Indian microfinance commercialized and underwent a structural transformation (Sriram, 2010). In 2008, nonprofits accounted for the majority of MFOs in terms of numbers (approximately 95% of the estimated 1,000 Indian MFOs[67]), but they only accounted for 10%-15% of the total outstanding loan portfolio. The remaining 82%-90% of the total outstanding loan portfolio was channeled through the 46 to 50 for-profit non-banking financial companies (Sa-Dhan, 2014; Microfinance Institutions Network, 2014). Although not representative for the entire Indian microfinance sector, Figure 8 gives an illustration of how M-CRIL's sample has changed in terms of legal structure over the years. The number of MFOs with a gross loan portfolio

[67] Comprehensive statistical data on the Indian MFO population is limited. According to a unique inventory survey commissioned by the German Society for Technical Cooperation (GTZ) and NABARD, there were, in March 2008, about 1,000 MFOs operating in India; 786 of these were captured in the survey. The survey defined an MFO as an organization of any institutional type that delivered financial services to either a minimum of 500 saving members and/or 1,000 borrowers (Regulagedda, 2009).

greater than INR 1 billion,[68] categorized by the Reserve Bank of India as "systemically important," also increased from seven in 2007 to 17 in 2009 (Intellecap, 2009).[69]

Figure 8. Transformation of the legal structure of MFOs in M-CRIL's sample



The figure has been derived from (M-CRIL, 2012).

From 2006-2010, the Indian microfinance sector as a whole grew at an exceptionally fast pace, expanding by 71% in terms of the number of active

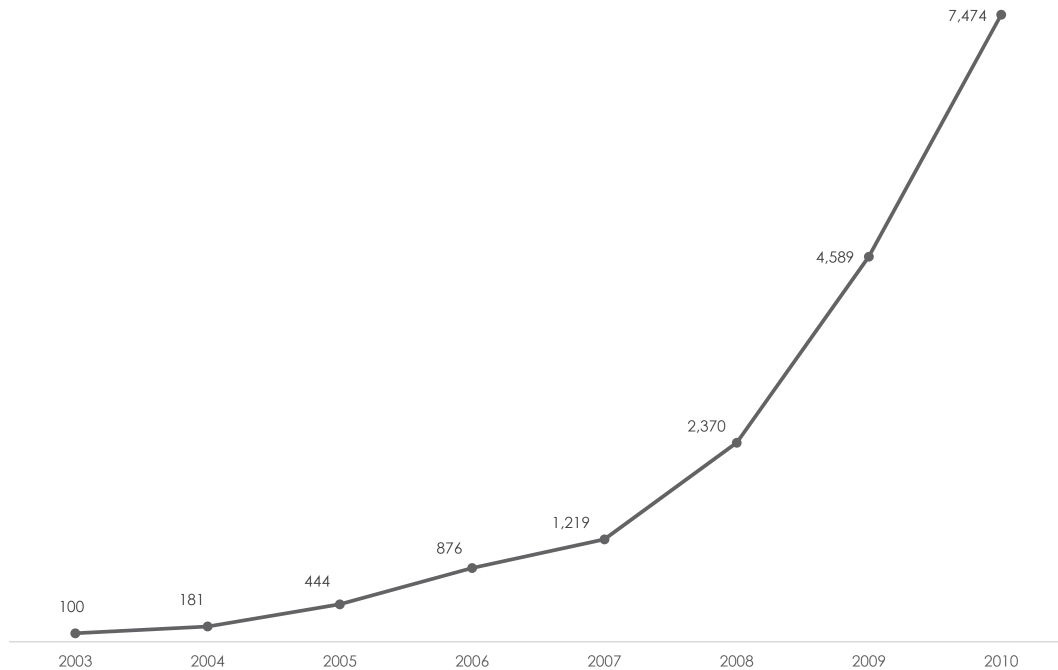
[68] From 1999-2014, the INR/USD exchange rate has fluctuated from 39-68 (Free Currency Rates, n.d.).

[69] In a Reserve Bank of India notification from December 2006, all non-banking financial companies with an asset size of INR 1 billion or more were considered to be "systemically important," and a specific regulatory framework involving prescription of capital adequacy and exposure norms was put in place from 1 April 2007 (Intellecap, 2008).

clients and by 225% in terms of total outstanding loan portfolio.[70] In 2010, the active client bases of the Self-Help Group Bank Linkage Program and the MFOs were 62.5 million and 31.4 million, respectively, and their respective total outstanding loan portfolios amounted to INR 306 billion and INR 208 billion (Srinivasan, 2012); Figure 9 demonstrates the growth in M-CRIL's sample.[71] Commercialization, growth, and economics of scale also brought increased profitability and productivity; in 2009, the seven largest non-banking financial companies, together managing 65% of the total portfolio, had a "Return on assets" of 4.4%, and a "Return on equity" of 28% (Intellecap, 2009).

[70] Figures derived from (Srinivasan, 2012).
[71] Figures are unadjusted for overlaps.

Figure 9. M-CRIL's growth index 2010 (2003 = 100)



The figure has been derived from (M-CRIL, 2010).

The entrance of mainstream rating products and M-CRIL's lack of accreditation

The funding structure of MFOs has also changed radically, shifting from a dependency on grants and donations towards more commercial sources and financial markets. Until 2008, the financing pattern of microfinance in India increasingly focused on debt, growing from 34% of total liabilities in M-CRIL's 2003 sample to 75% in the 2007 sample (M-CRIL, 2010).[72] Although the Indian microfinance project started off as a savings-driven movement, the share of client savings declined from 25% in 2003 to less

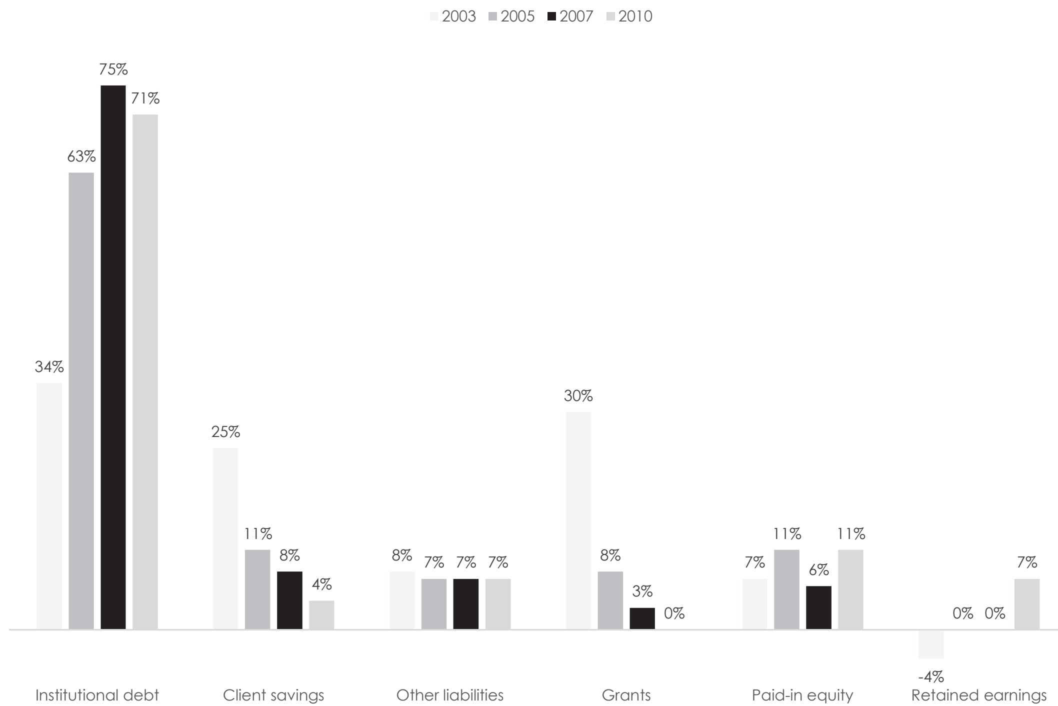
[72] Commercial banks in India, both public and private, are required to direct 40% of their net credit to designated "priority sectors," of which microfinance constitutes one.

than 4% in 2010. MFOs that operate under non-banking financial company licenses are, according to the Reserve Bank of India, strictly prohibited from offering deposit facilities (M-CRIL, 2010). In 2004, the Reserve Bank of India also reiterated that MFOs are not permitted to accept public deposits unless they comply with the extant regulatory framework, implying that trusts, societies, and section 25 companies would face regulatory risk if they were to accept public deposits (Reddy, 2005). There was also a halt in the flow of grants into Indian MFOs, falling from 30% in 2003 to a negligible amount in 2010. The year 2008 saw the entrance of mainstream private equity players, which, together with private individuals and microfinance-focused funds that significantly increased their asset base, contributed to the rising share of equity (Srinivasan, 2009b).[73] During 2006, USD 6 million was invested as equity in Indian MFOs, but in 2010, the annual equity investment amounted to USD 390 million (Arunachalam, 2010).

From 2006 onwards, securitizations of portfolios, structured-debt instruments, portfolio buyouts and even bond issues are some of the liability products that have been under development for MFOs, thus representing an additional means of delivering credit to these organizations. Such products, however, are only available to the larger MFOs (Srinivasan, 2009a).

[73] The legal framework allows for restricted foreign direct investment in non-banking financial companies. However, comprehensive figures on equity from foreign sources are lacking at the time of writing (Kline and Sadhu, 2011).

Figure 10. Sources of funds for microfinance operations in M-CRIL's sample



The figure has been derived from (M-CRIL, 2010).

In India, the Securities and Exchange Board of India is the primary regulator for rating agencies in the mainstream capital market. Those agencies that are registered with the board are referred to as eligible credit rating agencies, and only these credit rating agencies are eligible to conduct credit ratings. With the exception of M-CRIL, all of the rating agencies that are active in the Indian microfinance space and which offer microfinance rating products are credit rating agencies.[74]

Another particular type of mainstream rating that has become relevant for Indian MFOs is bank loan ratings under Basel II, a revised framework on capital adequacy that was adopted by the Reserve Bank of India in

[74] Brickwork and SMERA only received their registrations with the Securities and Exchange Board of India in 2008 and in 2011, respectively.

2007.[75] Under the Basel II framework, banks are required to assign a 150% risk weightage for all unrated exposures to MFOs in excess of INR 100 million. Ratings under the Basel II norms, also called bank loan ratings, are only deemed eligible, however, if they are conducted by a Reserve Bank of India-accredited credit rating agency.[76] If the MFO portfolio has been rated by an accredited credit rating agency, the risk weightage could be set lower based on the level of rating that had been awarded. The cost of higher capital requirements to exposures that are unrated or have a lower credit rating will commonly be passed on by the banks to the borrower, here the MFO (Reserve Bank of India, 2007; Reserve Bank of India, 2008; Srinivasan, 2009a; Fitch Ratings, 2008). M-CRIL is the only agency active in the Indian microfinance sector that lacks accreditation to conduct bank loan ratings.[77]

From 2004-2009, M-CRIL and CRISIL were the main agencies active in the microfinance sector; however, M-CRIL dominated the business with a large share of the market until 2007-2008. Through 2008, M-CRIL had carried out microfinance ratings on 335 Indian MFOs (M-CRIL's own database). Between 2007 and 2009, the three mainstream agencies SMERA,[78] ICRA, and CARE entered the microfinance sector by offering microfinance grading products but their respective market shares were modest.

M-CRIL's revenue model for microfinance ratings in India can be divided into two phases: In the period 1999-2008, the "investor pays" model was followed, and from 2008 onwards, the "issuer pays" model dominated. According to M-CRIL, through 2008, 90% of the funds for the agency's ratings were provided by SIDBI,[79] which typically paid for approximately

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[75] The Reserve Bank of India has also started the implementation of Basel III capital regulations in India.

[76] Such agencies are referred to as "external credit assessment institutions" (ECAIs).

[77] CRISIL, CARE, ICRA, and Fitch became eligible to conduct ratings under the Basel II norms in 2007, and Brickwork and SMERA received approval in 2012.

[78] SMERA was initially an exclusive rating agency for the micro, small and medium enterprises sector and, as such, accredited by the National Small Industries Corporation Ltd. under the "Performance and Credit Rating Scheme for Small Industries," approved by the Ministry of Small Scale Industries, Government of India. SMERA only received its registration with the Securities and Exchange Board of India in 2011.

[79] SIDBI has been the leading wholesaler in Indian microfinance for an extended period of time. The bank requires ratings of all its MFO partners, and through 2008, it was estimated that SIDBI had accounted for 70% of the rating demand in India (Appui au Développement Autonome, 2008). SIDBI's scheme to finance microfinance ratings was part of the National Microfinance Support Project from

90% of the rating exercise, while the lender paid for the remaining 10%. After 2008, when SIDBI's microfinance rating scheme began to ebb, the situation changed drastically; Alok Misra, M-CRIL's chief executive officer, estimates that 80% of the ratings were financed by the individual MFO and 20% by various foreign institutions (interview with Alok Misra, 30 April 2012).

As indicated in Table 18, M-CRIL's market share in microfinance ratings started to decline as of 2007-2008. Several factors may have contributed to this. Around this time, the mainstream corporate raters, with CRISIL in the lead, started winning some market share in microfinance gradings. Also, in 2008, the SIDBI rating scheme ended, as discussed above. A third factor, which is put forward by M-CRIL as the main explanation for the drastic decline, is the agency's lack of recognition by the Reserve Bank of India under the Basel II norms (e-mail with Alok Misra, 7 September 2014). One direct implication of this has been that banks extending loans to MFOs are unable to reduce their risk weightage with an M-CRIL rating; to do so, they have to turn to one of the mainstream credit rating agencies.

Since 2008, there has been no change in the regulatory status of M-CRIL and formal regulation continues to be designed after and intended for the mainstream financial system and credit rating agencies, and not for the microfinance sector and specialized microfinance raters like M-CRIL. Sanjay Sinha states that the ratings of the specialized agencies are accepted by development investors and development banks, microfinance investment funds, and donors, yet not by traditional financial investors, investment/pension funds, and companies (Sinha, 2008a). He elaborates further on this topic in a well circulated paper:

> "However, the main reason MFIs may increasingly use public credit risk rating services is that the ratings of the specialised agencies are not accepted by international commercial investors and by regulators. The response to this situation so far by the international microfinance support agencies (…) has been to devote development resources to encourage the traditional corporate agencies to rate MFIs… Yet, the commercial logic of this strategy of luring traditional raters to cover MFIs is doubtful. (…) It is difficult to see the corporate agen-

2002-2009 was funded by the International Fund for Agricultural Development and the Department for International Development United Kingdom (International Fund for Agricultural Development, 2013).

> cies treating microfinance rating as anything more than a niche service offered for 'social' rather than commercial reasons… For specialised agencies, on the other hand, microfinance is their main or unique area of specialization ensuring that they make an intensive, undiluted effort to understand microfinance and its risk profile. (…) Furthermore, while the specialised rating agencies have the knowledge, skills and commitment to microfinance to develop new products like social ratings, corporate raters have neither the specialised knowledge nor the incentive to innovate in this way" (S. Sinha, 2006, pp. 14-16).

According to a 2012 interview with Alok Misra, the agency still sees ratings as its core competence and looks at other markets such as Asia and Africa (interview with Alok Misra, 30 April 2012). M-CRIL recognizes that it needs to remarket itself and regain the confidence of the bankers in order to "win the war" and "persuade the banks" (interview with Brij Mohan, 25 May 2012). One strategy to tackle increased competition and lacking regulatory support among the specialized rating agencies has been to cooperate with the aim of developing a universal approach to microfinance rating, with a standard rating scale and a common reporting format for global use and comparison. As an attempt at harmonization, M-CRIL and MicroRate entered into a "strategic alliance" that was referred to as MicroRating International. This effort materialized in a new joint microfinance rating product that was launched in 2007 (M-CRIL and MicroRate, 2007; M-CRIL, 2008).

Local crises and social initiatives

While the microfinance sector grew rapidly during its initial years, it also underwent a period of unforeseen turmoil and instability. One of the first incidents in India occurred in 2003-2004 in the southern Indian state of Tamil Nadu, where the state government decided to group MFOs and the illegitimate and oftentimes blacklisted moneylenders together by introducing an act that capped the interest at 12% for all unsecured loans from such providers. The act was, however, stayed by the Madras High Court (Ghate, 2006).

One initiative that aimed at responding to emerging social concerns in microfinance sectors was the SEEP Network. In 2001, after incidents in Bolivia and South Africa when clients perceived that they had been treated

unfairly by MFOs, SEEP initiated a discussion about consumer protection and transparency issues, and in 2002, a working group was formed. In 2004, the working group launched the six SEEP Client Principles: (1) quality of service; (2) dignified treatment; (3) truthful and transparent information; (4) appropriate pricing; (5) protection from unethical and illegal practices; and (6) privacy of client information.

According to a study from January 2006 by the Andhra Pradesh Mahila Abhivruddhi Society, starting in 2003-2004, local media in Andhra Pradesh has repeatedly reported negatively about the activities of MFOs, criticizing MFOs for charging exorbitant interest rates, having rigid repayment mechanisms, and for callous delinquency management procedures (Andhra Pradesh Mahila Abhivruddhi Society, 2006). A more widely recognized crisis that shook the Indian microfinance sector occurred in the Krishna district of Andhra Pradesh in March 2006, when the Andhra Pradesh government closed down 54 branches of two of the leading MFOs. The incidents had widespread media coverage, with articles alleging that ten borrowers committed suicide when they could not repay their loans. As a result of the incident, borrowers were given the impression that they need not repay MFO loans and repayment rates fell to 10%-20% (Shylendra, 2006; The Consumer Protection Working Group, 2006). The 2006 *State of the Sector Report* comments on the root causes of the events in Krishna.

> "One of the longer term causes was clearly the 'quest for numbers' relating to outreach and profitability that is the main motivation of many MFIs. (…) [The] crisis serves as a useful reminder that there are other just as important client-centered consumer protection objectives such as transparency in dealings with borrowers (…) These are goals that apply equally to minimalist as well as more holistic microfinance" (Ghate, 2006, p. 64).

In responding to the Krishna crisis, Sa-Dhan began developing a code of conduct that was issued in January 2007. Global interest in the social impact of microfinance also increased during this time period. In 2005, CGAP initiated the Social Performance Taskforce, which developed into a multi-stakeholder work process aiming at addressing questions about measuring and managing social performance. M-CRIL acted as chair of the subcommittee for social rating and reporting appointed by the taskforce (F.

Sinha, 2006). In 2004-2005, M-CRIL was also the first agency in the world to launch a social rating product, and the first such rating was of BWDA.

A few years later, in 2009, antagonistic encounters between microfinance clients and MFOs were reported again in the media, this time from Kolar in Karnataka. The main drivers of the crisis have been identified as a combination of competition, over-supply of credit, irresponsible lending practices, religious intervention, and low levels of customer awareness (EDA Rural Systems, 2010; Jayaram, Umapathy, Gopinath, and Champatiray, 2011).

The above events coincided with the founding of the Microfinance Institutions Network as a self-regulatory organization of the for-profit non-banking financial companies in 2009, as well as the release of a code of conduct and the establishment of the first microfinance credit bureau (Microfinance Institutions Network, n.d.). During this time, several global initiatives were also launched. One of these is the Transparent Pricing Initiative, which aims to compile and present the interest rates of all MFOs in a standard format, making the results publicly available and readily comparable by rendering them as an annual percentage rate paid on a declining balance as opposed to a flat interest rate. Another initiative is The Smart Campaign, which seeks to position "clients as the driving force of the industry" (The Smart Campaign, n.d.) with the help of seven client protection principles: (1) appropriate product design and delivery; (2) prevention of over-indebtedness; (3) transparency; (4) responsible pricing; (5) fair and respectful treatment of clients; (6) privacy of client data; and (7) mechanisms for complaint resolution.

Furthermore, although researchers around the world have directed much attention and effort at trying to capture the impact of microfinance on various social and economic issues, the social impact debate reached a new level in 2009-2010 with the release of the results of two well-researched and rigorous randomized controlled trials conducted by Banerjee, Duflo, Glennerster, and Kinnan (2013) and Karlan and Zinman (2009). The studies, which focused on Hyderabad, India, and Manila, the Philippines, respectively, were released to mixed responses; some media outlets even declared the microfinance project to be a failure (Bennett, 2009).

Rating practices from 2005–2011 and Template II

Around 2005, it is possible to distinguish a new approach to evaluating MFOs beginning to emerge. The shift from the first to the second template mainly occurs in terms of structural and procedural elements, while the evaluation of outcomes more or less remains similar to those seen in earlier years. In 2007, during the time period of Template II, M-CRIL also launched a new rating product along with MicroRate.

While in Template I, structural aspects of the MFO are not a topic that receives much explicit deliberation, the second template emphasizes the organization of control and power, and governance in particular becomes a frequently discussed concept in the reports. As the seemingly irreversible process of transformation into non-banking financial companies unrolls in the sample as well as in the sector as a whole, the raters push for corporate governance principles such as the separation of the board and the executive management, an independent internal audit function that reports directly to the board, and independent directors as board members. What is particularly noteworthy is that all MFOs are assessed according to a similar template, without much consideration as to whether or not they are run under non-banking financial company licenses.

Including the target constituency as part of the board, e.g., is increasingly seen as problematic, as these women are deemed to be underqualified and ill equipped to govern a regulated entity. Instead, independent experts are called upon to serve in the boardrooms of MFOs, and the role of the board as a provider of administrative oversight is emphasized.

With rated organizations growing in terms of staff, clients, and portfolio size, the raters also pay increasing attention to how MFOs are organized and controlled in areas such as internal hierarchies and internal audits. Not only are the MFOs' internal audit mechanisms discussed in more detail and at greater length, but there is also a change in terms of what the raters believe the internal audit exercise should include and how it should be organized internally. In the reports from the period 2005-2011, the scope of internal audits is not limited to the MFO branches and the women's groups, but also includes head office departments; the internal auditor or audit team is expected to report directly to the board (excluding the execu-

tive management from the process); and there is increasing discussion about how audit reports are implemented and followed up on.

At the same time, the previously popular idea of community-owned non-banking financial companies begins to be challenged by the raters, who point to several challenges with such structures, such as the lack of awareness and understanding of the target constituency vis-à-vis their roles as investors and shareholders, the inabilities of the rated MFOs to handle such large numbers of shareholders, as well as the regulatory uncertainties surrounding these issues. Five of the eight MFOs in the 2005-2011 sample are partly or fully owned by the target constituency at some point during the given time period, yet there are no instances in the reports where the raters characterize as a potential weakness the fact that the target constituency, as majority owners, lack board representation.

The M-CRIL template also reflects a separation of microfinance activities from other types of activities and ambitions in order to make an accurate evaluation of these, thus narrowing down the definition of what constitutes microfinance. In light of BWDA transferring its microfinance operations to the non-banking financial company BFL, it is, for instance, worth recalling that group formation and training are not treated as intrinsic parts of the microfinance model but rather as activities that can be separated from the "microfinance activity" and outsourced by the MFO, thus contributing to a winnowing down of the working definition of microfinance and its terms and conditions.

In Template II, several changes can be noted in how the raters evaluate procedural elements. When the concept of competition enters the reports, the accounts change from attempts to identify the most marginalized villages and mobilize the poorest women to strategies aimed at mitigating and managing competition. This involves first-mover advantages, competitive edge, targeting untapped and unsaturated markets, and offering products that will stand out among those of competitors. In this sense, the reports very much reflect the broader expansion and growth trends in the sector, which critics have claimed spurred many of the recurring crises in the microfinance space. Much of the assessment centers on the rated MFO's ability to navigate and expand in an increasingly competitive environment. There is thus a shift in the conceptualized role of the MFO, moving from

providing microfinance services to the poor or the unbanked, to building competitiveness in order to sustain operations.

Accounts of how groups are mobilized and strengthened are sparser and briefer, and the concept of group quality is completely absent from some of the reports. The evaluation of internal savings circulation is also eliminated. The example of BWDA (2008) demonstrates the raters' instrumental approach to recordkeeping; it is regarded as a functional activity that needs to be performed with accuracy, as well as being closely controlled by the head office. Whether the activity is performed by the group or by MFO staff is no longer considered to be important in the reports; instead, the focus is on whether or not the records are comprehensive, reliable, and verified. Such approach stands in stark contrast to the previous template, where the process of recordkeeping had an innate meaning, as it contributed to the cultivation of strong and independent groups. The heightened focus on the quality and cost of the financial reports diverts attention away from the conceptualization of recordkeeping as an intrinsically empowering process.

The diminished emphasis on group formation and training processes in the Template II reports does not necessarily mean that the MFOs followed suit and were paying less attention to group formation and training during this period. On the contrary, this could just mean that the ratings no longer value such activities as relevant to the rating exercise. An alternative explanation could be field maturity; in other words, that such activities have become taken-for-granted elements of conducting microfinance by this stage and a detailed analysis is thus rendered redundant.

In what can be understood as an attempt at creating a level playing field, Template II reports include accounts of increasingly formalized and standardized loan processes, which include receipts, signatures, and formal loan applications. Evaluation of how staff decisions are made is not included in these reports. Instead, there are accounts describing staff behavior as rule-based and informed by written manuals and policies. The reports expect the MFO to ensure that the target constituency is fully aware of and understands the implications of the loan contract. A shift away from describing the group's readiness for an external loan and toward descriptions of the internal organizational procedures of the MFO when it comes to

processing loan applications is apparent. The focus is thus shifted from the external women's groups to the internal dynamics and processes of the MFO.

Although poor women in rural areas are still considered the primary target constituency, there are examples of a broadened definition of who constitutes an eligible microfinance client, with examples of MFOs approaching an urban "middle class" of entrepreneurs with individually based business loans. When rated organizations are described as offering non-financial welfare services such as healthcare and education, these are considered in terms of giving the MFO a competitive edge and increasing client retention.

Many of the changes discussed above can be explained as a movement towards mainstream banking and a more financial, or banking, logic entering the reports and guiding the template. As I describe above, this period also saw a dramatic shift in the flow of funds to the microfinance sector from donations to bank debt and private equity. In addition, as the regulated and for-profit non-banking financial company legal form came to be increasingly dominant in the Indian microfinance sector in terms of portfolio outstanding and number of clients, the raters gradually begin to regard this as the superior legal form under which microfinance activities should be conducted. At the same time, MFOs that are not operated under non-banking financial company licenses are evaluated using the same measuring stick as non-banking financial companies.

The Indian microfinance sector underwent two crises during this time period: Krishna in 2006 and Kolar in 2009. External jolts such as these may have impacted the ratings in several ways. In 2006, all sample reports included a section on client protection and transparency that by and large drew on the SEEP Client Principles that had been suggested in 2004. After the Krishna crisis, the emphasis on corporate governance and board accountability started to intensify as a central theme in the reports. The earlier policy of zero tolerance for defaults begins to be relaxed, and instead, loan officers are expected to make exceptions for clients that are in genuine distress. Incentive systems are expected not only to be based on repayment rates and the size of the portfolio, but also to take into consideration adherence to policies and compliance with processes.

Notably, in 2004-2005, before any major crises in the Indian microfinance sector had occurred and before critics had begun to charge that the commercialization of the sector had gone too far, M-CRIL piloted a social rating report as part of a global collaborative effort. Although the interest in social ratings has been limited, this serves as an example of how M-CRIL's global embeddedness has introduced global ideas into the Indian microfinance context.

Contextualizing rating practices from 2012–2014

An initial public offering and the Andhra Pradesh crisis

The period of the third template, 2011-2014, was marked by a great deal of turbulence: a major crisis that came to affect microfinance outside India and around the world; a controversial initial public offering; and the formalization of a unique legal category for MFOs with a strict regulatory framework. The commercialization trend reached its apogee in the autumn of 2010, when the largest MFO in India, Hyderabad-based SKS Microfinance, raised USD 358 million to become India's first listed MFO ("SKS prices IPO at top end, raises $358 min," 2010). Several investors from major US and European banks bought shares in the listing (Gaul, 2010).

Beginning in 2010, a series of instances of harassment and suicide were reported in the southern Indian state of Andhra Pradesh.[80] A number of the largest commercially oriented and regulated MFOs were alleged to have played a role in most of the cases ("Rising suicides force AP ordinance to check microfinance firms," 2010). Accusations centered on "mission drift," the questionable ethicality of earning money from severely impoverished and marginalized groups, exorbitant interest rates, and over-indebtedness due to careless lending practices, as well as alleged threats made by loan officers seeking repayment. Many Andhra Pradesh clients refused to repay their loans, and default rates soared.

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[80] A report was prepared by the Gender Unit of the Society for Elimination of Rural Poverty that listed the victims of MFOs in Andhra Pradesh. Out of the 123 alleged cases of harassment, there were 54 deaths in less than eight months. According to the list, some of the largest MFOs are accused of malfeasance in many of the cases (Microfinance Focus, 2011).

The events in Andhra Pradesh took place in the same general timeframe as the listing of SKS Microfinance, which spurred an upsurge of criticism regarding the commercialization of the sector from various quarters, adding fuel to the fire in Andhra Pradesh (Sriram, 2010). Nine months after the successful initial public offering and well into the crisis, the SKS shares were down 70% from the listing price (Strom and Bajaj, 2010; Mader, 2013). Some industry observers argued that the chief factor causing the crisis was the unadulterated greed of the executives, consultants, directors, and investors involved in the MFO sector (Arunachalam, 2014).[81]

In a widely read article published during this tumultuous period, Sanjay Sinha expressed his concerns about developments in the rating business after the Andhra Pradesh crisis, and he accused the mainstream rating agencies of being too optimistic in their ratings of MFOs.

> "The incursion of the large corporate rating agencies into the world of microfinance must bear part of the responsibility for the current mess in the Indian microfinance industry" (Unnikrishan, 2011).

The events in Andhra Pradesh had huge impacts on the growth and performance of Indian microfinance. Low repayment rates for MFOs with operations in Andhra Pradesh led to significant losses and, as a result, banks stopped lending to MFOs all over India (M-CRIL, 2012).

A regulatory framework

Indian MFOs can be divided into two categories: (1) MFOs whose microfinance activities are outside the aegis of the financial sector, namely, trusts, societies, section 25 companies, and cooperatives, and (2) MFOs that are regulated by the Reserve Bank of India, namely, non-banking financial companies. It can be argued that the Indian microfinance sector, up until this point, had evolved in a regulatory void, meaning that specific micro-

[81] The listing of SKS also serves as an illustrative example of the contagious nature of (il)legitimacy. As shown by Jonsson, Greve, and Fujiwara-Greve (2009), when the legitimacy of one organization is damaged by an isolated act, it is likely that similar organizations perceived to belong to the same category also will suffer legitimacy losses.

finance regulation had been lacking, pending, or excluded (M-CRIL, 2006a). In the aftermath of the crisis, the Reserve Bank of India assigned the Malegam Committee with the task of studying a broad range of issues pertaining to the regulation of MFOs in the form of non-banking financial companies (Malegam, 2011). In its *Monetary Policy Statement for 2011-2012*, the Reserve Bank of India accepted the broad framework of regulations recommended by the Malegam Committee (Subbarao, 2011), and in 2011, the Reserve Bank of India created a separate category for non-banking financial companies that are engaged in microfinance. Organizations in the new category, referred to as "NBFC-MFIs,"[82] are held to specific prudential and non-prudential norms and customer protection regulations. Further, only NBFC-MFIs are designated as a "priority sector," thus excluding trusts, societies, and section 25 companies (Kline and Sadhu, 2011; Reserve Bank of India, 2011b; Reserve Bank of India, 2012c).

The capital requirements for transformation into a non-banking financial company are stringent,[83] and to register an NBFC-MFI, the Reserve Bank of India requires that a minimum of 70% of the loan portfolio must be engaged in income-generating activities, and 85% of the MFO's total assets must be "qualifying assets." A "qualifying asset" is a loan that fulfils certain requirements pertaining to, inter alia, the client household income, the client's degree of indebtedness, the loan size, the loan conditions, and the repayment conditions. In addition, for NBFC-MFIs, the interest charged should be calculated on a reducing-balance basis, and the price charged can only include interest rate, a limited processing fee, and an insurance premium. For bank loans to NBFC-MFIs to be recognized as "priority sector" lending, a margin cap has been set by the Reserve Bank of India (Reserve Bank of India, 2011a).

In June 2014, the Microfinance Institutions Network was formally recognized by the Reserve Bank of India as the self-regulatory organization for non-banking financial companies engaged in microfinance. This means that the oversight of compliance with consumer protection and grievance redressal issues of NBFC-MFIs has been outsourced to the network ("RBI accords self regulatory organisation status to MFIN," 2014).

[82] Non-banking financial company microfinance institution.
[83] The minimum entry capital is INR 50 million and the capital adequacy must be 15%.

In addition to the above, NBFC-MFIs have to comply with Reserve Bank of India corporate governance policies. Since 2005, the Reserve Bank of India has issued several directives with corporate governance instructions for non-banking financial companies, which have included, inter alia, requirements on non-banking financial companies to constitute an audit committee; a nomination committee that appoints directors with "fit and proper" credentials; as well as the formation of a risk management committee (Reserve Bank of India, 2012a).

To address issues pertaining to MFOs that do not fall under the supervision of the Reserve Bank of India – trusts, societies, section 25 companies, and cooperatives – the Finance Minister introduced the *Micro Finance Sector Development and Regulation Bill 2007* in Lok Sabha in 2007, but the bill was never approved. *The Microfinance Institutions (Development and Regulations) Bill 2012* is an updated version of the 2007 draft. The current bill has been redrafted several times and is, at the time of writing in November 2014, being considered by the Parliamentary Standing Committee on Finance (Kline and Sadhu, 2011).

In the post-crisis period, the focus on consumer protection intensified. First, the Reserve Bank of India introduced mandatory consumer protection directives contained in the fair practice code for NBFC-MFIs (Reserve Bank of India, 2012b), and the Reserve Bank of India guidelines were issued as a follow-up to the Malegam Committee recommendations (Reserve Bank of India, 2011b). Second, several soft law consumer protection initiatives, some of which had been launched before the crises, gained additional momentum. Two such global initiatives are the Transparent Pricing Initiative and the seven Smart Campaign client protection principles. In the Indian context, the Microfinance Institutions Network and Sa-Dhan agreed on a merged joint code of conduct in December 2011. The code includes integrity and ethical behavior, transparency, client protection, governance, recruitment, client education, data sharing and feedback/grievance redressal mechanisms (Kurian, 2011). Many lenders to MFOs, including SIDBI, started including a "code of conduct assessment" as covenants in their lending agreements (Puhazhendhi, 2013, p. 8). These are assessments of how well the MFO complies with and has implemented the Sa-Dhan and

Microfinance Institutions Network code of conduct. M-CRIL was one of the partners in this initiative.

Plummeting demand and a global partnership

According to the 2012 *State of the Sector Report*, the large non-banking financial companies began to gain momentum in terms of outreach and loans outstanding during the year, and bank credit again began to ease for other types of MFOs, as well as for the Self-Help Group Bank Linkage Program (Puhazhendhi, 2013). More recently, the sources of funding have shifted anew for the large MFOs; securitizations have come to represent the main source of funding for NBFC-MFIs and microfinance issuances are now the largest asset segment in the Indian securitization space, after commercial loans, both by value and number of transactions. Such deals are also categorized as "priority sector" lending, according to the Reserve Bank of India (CRISIL, 2014).

For M-CRIL, the period from 2011-2014 was especially challenging, since demand for the agency's microfinance ratings decreased drastically, while demand for mainstream credit ratings and bank loan ratings was on the rise. During the post-crisis years, M-CRIL's market share hit an all-time low with 11%-12% of the total ratings (see Table 18).

In 2011, the Multilateral Investment Fund (a member of the Inter-American Development Bank) initiated a collaborative effort among the four specialized microfinance rating agencies M-CRIL, MicroRate, Planet Rating and MicroFinanza Rating, aiming at developing a global, uniform rating product. The process resulted in the new rating product entitled "Microfinance Institutional Rating" (MIR) in 2012, as well as the production of a rating guide and a comparability table (The Rating Initiative, 2012).[84] The "Microfinance Institutional Rating" has been described as follows:

> "…a holistic assessment, covering all aspects of a financial rating (Governance, Management Systems and Financial Profile) with the seven principles of client

[84] MIR was preceded by a pilot rating product called the "Responsible Microfinance Rating" that was tested once by M-CRIL in 2011 but never adopted.

> protection and other key social aspects such as mission alignment. The new framework therefore captures all dimensions of an MFI functioning which have a bearing on its sustainability. Integration of key social issues into the rating framework also addresses public policy concerns on institutional practices in lending to the poor" (M-CRIL, n.d.).

Apart from attempting to meet the demands of international investors, the development of the "Microfinance Institutional Rating" product was initiated as a response to the microfinance crisis that had hit some countries (Abrams, 2012), and perhaps especially the Andhra Pradesh crisis, which had repercussions that reached far beyond India. In the first publicly available publication with comparisons of specialized microfinance rating grades, the author describes the motives behind this process.

> "The raters wanted to brand the specialized microfinance rating more clearly in the ratings market to differentiate it from a traditional credit rating. In addition, they wanted a microfinance ratings comparability table to enable clients to compare their different agencies' ratings. Ratings equivalence tables comparing mainstream rating agency credit rating grades of Fitch Ratings, Moody's, and Standard & Poor's are readily available" (Abrams, 2012, pp. 3-4).

Other rating innovations in the social domain included the global launch of Moody's social performance assessment in 2012 (Moody's, 2012), which was pilot-tested on an Indian MFO in 2013. Also, in 2010, CRISIL included social indicators in its microfinance grading product, but it is unclear whether these indicators have a rating weightage, as they have not been incorporated in CRISIL's MICROS framework.

Rating practices from 2012–2014 and Template III

The shift between the second and third templates mainly involves the ways that procedures and outcomes are evaluated. The evaluation of structural elements in reports from this period is similar to the previous template, but certain features are highlighted and emphasized by the raters. Biographies of board members are more detailed, and the internal audit function is further underscored with visits to clients and thorough follow-ups. There are

also examples of more social considerations when it comes to board responsibilities; diversity is regarded as a positive feature in one of the sample report's description of board composition, and the board is expected to take an interest in the organization's social performance.

The evaluation of procedural elements in Template III follows a similar rationale to Template II, although the later reports exhibit a greater emphasis on transparency, fair treatment of clients, responsible practices, and a further formalization in the client-MFO relationship. The perceived importance of written and formal rules in guiding staff and the organization has increased, references to various manuals are more frequent, the raters note how well each MFO follows industry codes of conduct, and assessments on MFO compliance with the new formal regulation for MFOs under non-banking financial company licenses are made. The concept of groups has fallen further in importance, and instead, assessments are made on an individual basis.

However, in the Template III reports, the MFO is expected to be responsive towards the target constituency, which is asked for feedback and encouraged to share complaints and grievances. The target constituency has thus moved out of the structural elements, where she was found as a board member in Template I, and into the procedural domain.

On first reading, the move in Template III towards transparency and client protection can seem like a revival of the socially inclined ideas that informed Template I. There are, however, fundamental differences in the conceptualization of social issues that is present in the evaluation of structures and procedures in Template I versus that of Template III. The conceptualization of social issues in the first template calls on democratic ideals, solidarity, and community mobilization, implying that the target constituency is more of a political and collective actor. By contrast, the social issues in the third template are conceptualized in a way that is more reminiscent of consumer protection legislation, and the members of the target constituency are seen as being able to be transformed into empowered consumers who are well aware of their rights and are able to assert those rights in a marketplace that steadily improves over time.

The renewed interest in the social aspects of microfinance can be understood as a response to the Andhra Pradesh crisis, which was the most

dramatic event to have hit the microfinance sector both in India and around the world, suggesting that evaluative practices are affected by external jolts. As noted, in the aftermath of the crisis in 2012, the new "Microfinance Institutional Rating" was introduced as the result of a global collaborative effort. There are several examples of global influences in Template III, such as attempts at standardizing interest rates into the effective interest rate format and assessments of adherence to the seven client protection principles of The Smart Campaign.

One area where the raters fluctuate is when it comes to the setting of interest rates. In Template I and even more so in Template II, it is implied that interest rates should take into account the financial sustainability of the organization, the prevailing political sentiment in the area of operation, and the interest rate levels of competitors. In Template III, the raters applaud MFOs that keep their interest rates low, and the raters assess the MFO's engagement in generating social results and impacts. The social intentions of the Indian MFO are no longer taken as a given; instead, the reports explicitly describe and evaluate MFOs' "mission and vision statements" and assess each organization's capability and readiness to implement them. Loans are expected to be for relevant and useful purposes (e.g., income-generating activities), and it is expected that the MFO should consider client needs when designing products.

The most stable and constant organizational element in all three templates is that of financial outcomes. From the advent of the ratings through 2014, the raters are relatively consistent in their push towards improved efficiency and sustainability/profitability. This includes controlling costs, minimizing portfolio risk, increasing staff productivity, expanding operations, and strengthening the capital base. However, in Template III, there are indications that something has changed in the evaluation of financial outcomes. Although there is a continued focus on profitability, the reports also contain instances of voluntarily capped staff productivity levels, and the raters assess how well the MFOs comply with the interest rates cap as imposed by formal regulations, thus suggesting a kind of bounded financialization.

Formal regulation also seems to play an important role in the ratings. The only legal form whose microfinance activities are sanctioned by the

Reserve Bank of India is the non-banking financial company form. In the early years, this is also a reason given by the raters for promoting this form. In Template III, the formal rules that regulate NBFC-MFIs are also applied in the evaluation of non-NBFC-MFIs.

As to changes in terms of the strength of the reports, the third template is weak in comparison to the first one, meaning that there is relatively less explicitly normative and prescriptive text in the later years. There are several possible explanations for this observed change. First, the strength of the template may vary with M-CRIL's position within the sector. It may be plausible, for example, that the stronger the challenge posed to M-CRIL by mainstream raters, the weaker the template produced by M-CRIL. Another way of explaining the weakening in the template is field maturity. In other words, as the sector became more mature over time, it became less important to assess the minutia of microfinance operations, and thus the amount of prescriptive and evaluative text in the reports decreased over time.

The next, and final, chapter discusses the findings of this dissertation in relation to earlier empirical studies and the theoretical understanding of how organizational templates are constructed in institutionally complex and ambiguous settings. It also considers different potential explanations for the above-noted changes, as well as future directions for research.

Table 18. Ratings in the Indian microfinance sector from 1998-2014[85]

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	1998-2009	2010	2011	2012	2013	2014	2010-2014	1998-2014
	Microfinance ratings																			
M-CRIL	5	22	34	43	37	53	65	70	65	80	59	36	569	33	17	19	16	0	85	654
CRISIL				3	16	10	16	18	28	42	70	82	285	119	61	74	56	15	325	610
CARE										3	13	20	36	18	18	14	23	38	111	147
SMERA												10	10	10	9	8	3	2	32	42
ICRA												1	1	1	6	4	10	13	34	35
TOTAL	5	22	34	46	53	63	81	88	93	125	142	149	901	181	111	119	108	68	587	1 488
M-CRIL's share	100%	100%	100%	93%	70%	84%	80%	80%	70%	64%	42%	24%	63%	18%	15%	16%	15%	0%	14%	44%
	Credit ratings, Basel II ratings and gradings of initial public offerings																			
CRISIL								2	2	1	1	9	15	14	18	22			54	69
CARE													0	2	6	4	9	16	37	37
SMERA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
ICRA												1	1	6	15	15	19	19	74	75
Brickwork													0				1		1	1
Fitch												1	1	1		1			2	3
TOTAL	0	0	0	0	0	0	0	2	2	1	1	11	17	23	39	42	29	35	168	185
	Social ratings																			
M-CRIL	0	0	0	0	0	0	0	4	9	1	0	4	18	8	3	2	2	0	15	33
	Total ratings in the Indian microfinance sector from 1998-2014																			
M-CRIL	5	22	34	43	37	53	65	74	65	80	59	36	569	33	17	19	16	0	85	654
TOTAL	5	22	34	46	53	63	81	94	104	127	143	164	936	212	153	163	139	103	770	1 706
M-CRIL's share	100%	100%	100%	93%	70%	84%	80%	79%	63%	63%	41%	22%	61%	16%	11%	12%	12%	0%	11%	38%

[85] The table has been derived from the following sources: M-CRIL's own database; e-mail correspondence with CRISIL (11 June 2013 and 4 July 2014); e-mail correspondence with CARE (1 August 2014) (figures based on financial year April to March); SMERA (n.d.); e-mail correspondence with ICRA (21 July 2014); Brickwork Ratings (n.d.-a); Brickwork Ratings (n.d.-b); e-mail correspondence with Brickwork (10 June 2013); e-mail correspondence with Fitch (1 August 2014). Figures until May 2014.

Chapter 7

Discussion and conclusions

In this dissertation, I have investigated evaluative practices and the templates encoded in them in an environment characterized by complexity and transformation. I have focused on rating practices to capture the processual aspects of how idealized images of organizations – templates – are given form and modified. Inspired by Suchman's (1995) taxonomy of moral legitimacy, I have sought to capture expectations pertaining to how organizations are to be governed and controlled, what practices and processes they ought to adopt, and what financial and social goals to pursue. The textual analysis has also included an assessment of changes in the strength of the template. Finally, I have aimed at investigating how the content of the encoded template reflects sectoral trends and events, as well as how changes in the template correspond to the rater's position in the field.

As an empirical focus, I have chosen the crises-ridden, fragmented, and heterogeneous Indian microfinance sector, wherein rating agencies have come to play an important role in directing resources. The Indian microfinance sector is especially interesting since it represents the world's biggest market in terms of the number of borrowers. To investigate changes in the organizational template and in the rating instrument, I have employed a predominantly qualitative single case study method of the only specialized microfinance rating agency in India, Micro-Credit Ratings International Limited (M-CRIL), and its rating practices from 1999-2014. During this time period, much has happened with the market position and perceived role of M-CRIL; state-accredited, mainstream credit rating agencies have,

for instance, entered the microfinance scene and have started to challenge M-CRIL's existence. At the same time, the Indian microfinance sector has undergone a transformation process that has been characterized by vast growth, uncertainty, and controversy.

From my analysis, I was able to deduce several important findings. First, the rating instrument used to evaluate microfinance organizations (MFOs) has undergone a somewhat contradictory change over the years. The weightage of non-financial rating parameters has increased, while financial rating parameters have decreased in the calibration of the final rating grade. This would imply that the raters are placing less and less importance on actual financial results. However, during the same period, organizational aspects that have a direct bearing on the financial performance of MFOs have gradually been incorporated into the non-financial rating categories. This means that, although the rating weightage for the "Financial performance" category has decreased over the years, systems, procedures, and structural arrangements that aim at ensuring and safeguarding the commercial aspirations of the MFO have been encouraged by the raters and have crept into the evaluation of other, non-financial, rating categories. The reports promote business-like processes, practices, and structures, such as introducing fund mobilization strategies, implementing procedures to increase staff productivity, and inviting experts and professionals onto the board. Thus, although the pressure to generate profit has lessened, I conclude that the reports in practice push MFOs to embrace efficiency and leadership models that traditionally appear in the corporate world.

Second, from a more theoretical perspective, much has happened in terms of how the conceptual elements of structures, procedures, social outcomes, and financial outcomes are evaluated. In the 15 years' worth of rating that took place from 1999-2014, three distinct templates encoded in the rating reports can be identified: Template I from 1999-2004; Template II from 2005-2011; and Template III from 2012-2014. Each template is composed of constellations of organizational elements that draw on different rating rationales and underlying expectations.

Third, my analysis also revealed several tensions within the templates. By displaying an idealized image, evaluators such as M-CRIL explicate ten-

sions and can potentially guide organizations embedded in complex and contradictory environments in terms of how to prioritize among competing demands. The above suggests that M-CRIL exposes tensions and, at times, provides solutions for organizations that are stuck between conflicting expectations. The solutions suggested by M-CRIL indirectly (i.e., being encoded in the templates) are not permanent and constant, but rather temporary and fluctuating.

These two last conclusions imply that organizations in fields characterized by institutional complexity and pluralism have to deal with a constantly evolving idealized image. For the individual MFO, this means having to constantly grapple with changing definitions of what is considered "good" microfinance, rendering it challenging to hold on to long-term strategies and visions.

Finally, the strength of the template has changed dramatically when comparing early ratings with more recent ones. When microfinance ratings were a new phenomenon, the reports were more explicit in terms of normative and prescriptive statements. In more recent years, the reports are more factual and descriptive. With the weakened template, the user of the reports (e.g., investors), not the reporter (i.e., M-CRIL), becomes the one responsible for drawing conclusions and determining creditworthiness (Lipartito, 2013, p. 676).

Relating back to my discussion about triangulation in Chapter 4, my first specific research question – *How does the microfinance rating instrument change over time in terms of factors such as rating categories and sub-categories, indicators, and weightages? (Question 1a)* – was answered by drawing on the 57 sample rating reports and interviews with M-CRIL, as well as material produced by M-CRIL over the years. The findings related to Question 1b and Question 1c – *How does the template change in content over time?* and *How does the template change in strength over time?* – emerged after the in-depth textual analysis of the reports. These findings were also verified during interviews with M-CRIL.

In the introductory text, I asked how the idealized images projected in microfinance ratings unfold over time as the field undergoes change and transformation, as well as what role the specific vantage point and market position of the evaluator play in changes to evaluative practices. Thus, as a

second step, I investigated how the content of and changes in the encoded template correspond to the macro and meso contexts, more specifically: *How do changes in rating practices and in the templates projected through these relate to trends and events in the sector, as well as to the rater's market position? (Question 2).* By iterating between the template, the meso level and the macro level, I analyzed how changes in rating practices and in the template corresponded to trends and events in the microfinance sector, as well as to the position and role of M-CRIL in the field. The analysis resulted in several findings.

Although M-CRIL's templates reflect broader trends in the microfinance sector, there are also several instances where M-CRIL's encoded template diverges from sectoral expectations and demands. One such example is in Template I, where M-CRIL pushes for both procedures and financial outcomes that bring about efficiency, expansion and positive financial results, even during a period in which the sector was funded primarily by donations and grants and most organizations were being run as nonprofits. Another example is when M-CRIL introduced a social rating product in 2004-2005, although there was no explicit call or demand for such product in the Indian context. This suggests that evaluators may play a role as institutional entrepreneurs (see, e.g., Munir and Phillips, 2005) through the templates that they project, thus introducing new ideas and guiding the development in the field in a certain direction.

Ratings also seem to react to external jolts such as sectoral crises. In the M-CRIL template, this is reflected in a call for client protection and transparency, as well as improved governance and accountability after the 2006 Krishna crisis and the launch of a completely new rating product with social aspects in 2012 after the Andhra Pradesh crisis. However, as elaborated on by Munir (2005), a critical event such as a perceived crisis should be seen as being interwoven with broader change processes that only become significant as actors bring them to public attention and "theorize" around them, referring to the "process whereby organizational failings are conceptualized and linked to potential solutions" (Greenwood, Suddaby, and Hinings, 2002, p. 58). This means that jolts such as the Krishna and the Andhra Pradesh crises do not necessarily trigger change in the institutional environment and, specifically, in the template projected by M-CRIL, but rather that they enable actors such as M-CRIL to theorize.

As to M-CRIL's market position and perceived role in the sector, this also seems to have an effect on the template and on M-CRIL's rating practices. In the early years, when M-CRIL was the sole player in the Indian rating space, the template was strong and M-CRIL saw it as its role to change the course of development in the burgeoning MFO sector. As M-CRIL's share of the Indian microfinance rating market shrunk and as the sector matured, the template weakened. The launch of a new rating product in 2012 may be understood as an attempt at regaining market share. The new rating product has an explicit social orientation and incorporates social evaluative aspects in an unprecedented way. This type of product differs from the other rating products available in the Indian microfinance space and can be seen as a way for M-CRIL to position itself as a microfinance specialist, in contrast to its competitors that are mainstream credit rating agencies.

In the introduction, I argued that it is plausible to suggest that some evaluators encode templates that do not necessarily reflect broader societal expectations, but instead creatively and perhaps provocatively attempt to alter expectations and demands held by other important audiences. I have in this dissertation shown that prominent evaluators such as M-CRIL play a dual role. First, ratings inform organizations about the template by codifying what is "out there." In this way, they signal to organizations what is legitimate and what is expected of organizations, thus explicating institutional pressures. But intermediaries are more than just communicators of institutional pressures; they also actively contribute to the construction of templates and thereby suggest which organizations and organizational features should be bestowed with legitimacy. While previous studies have implicitly treated evaluators and their evaluations as mere mirrors, focusing instead on the evaluated organization, I suggest that these types of intermediaries are potentially important for understanding field-level change.

Further, the construction of the template seems to be more noticeable in the early years when the field was emerging and the rules of the game still remained to be determined. This may come as a surprise, as it, in theory, may have been less risky for M-CRIL to project a weak and factual template initially, and then, as the field matured, to adopt an increasingly normative and prescriptive tone.

The theoretical contribution

The results of this dissertation contribute to extant literature on institutional logics, and, more specifically, to the growing number of studies that take an interest in contestation, complexity and ambiguity in the institutional environment. Earlier studies have shown that organizations and individuals operating under multiple logics can mix aspects of different logics in innovative, creative, and useful ways (McPherson and Sauder, 2013; Binder, 2007; Voronov, De Clercq, and Hinings, 2013). Instead of treating each logic as prescribing a set of non-separable organizational components, thus specifying an all-encompassing template for organizations, a few recent studies have attempted to disentangle and dissect institutional logics into prescriptions pertaining to distinct organizational elements. Such an approach opens up the possibility of configurations of organizational elements that draw on different logics.

Pache and Santos (2013), for instance, investigate how hybrid organizations internally incorporate different elements of the competing logics that they embody. The authors make a comparative case study of four social enterprises embedded in competing social welfare and commercial logics and analyze which organizational elements of institutional logics that the different organizations adopt. The organizational goal is taken as given – endogenous – to the model, as it is sanctioned by the state, and the other elements are organizational form, exertion of control, and professional legitimacy. The authors argue that hybrid organizations selectively couple intact elements prescribed by each individual logic, and thereby are able to project legitimacy to external stakeholders. Common to this and other related studies is their within-the-organization perspective; they are concerned with actual logic enactments and strategies employed by the acting organization in attempts to render itself legitimate. This stream of research has to a large extent focused on the internal responses and strategies of organizations that face competing and contradictory identity claims and institutional demands, thus painting a picture of the hybrid organization as especially dynamic, creative and active in its dealings with competing logics.

My dissertation builds on this line of enquiry but focuses on the complex institutional environment and the "antagonisms in the organizational

arrangements required by institutional referents" (Pache and Santos, 2010, p. 457). While extant studies have been able to demonstrate that the hybrid-type organization is relentlessly grappling with the internal problems caused by different tensions, these have largely taken the legitimacy of the studied organization as a given, without questioning changes over time in the sources of legitimacy. Thus, rather than assuming that the institutional environment of the hybrid organization is heterogeneous yet stable over time, I here suggest that the template informing organizations operating in environments characterized by numerous and sometimes contradictory expectations is a constantly moving target, as audiences such as external evaluators are able to encode templates with many different logic constellations. This implies that organizations operating in such environments continually have to adapt to and modify structures, procedures and outcomes, not only to overcome internal tensions but also to be consistent with the fluctuating template.

Continuing in the neo-institutional track, I also contribute to the growing field of enquiry that has been labeled "institutional work" and which acknowledges the role of individuals and collectives in purposively creating, maintaining, and disrupting institutions (Lawrence and Suddaby, 2006). The institutional work literature includes both studies on institutional entrepreneurship and studies on deinstitutionalization. Extant research has shown that certain resourceful actors, e.g., professional associations, play especially significant roles in legitimating change (Greenwood et al., 2002). Others have pointed at enabling factors in the organizational environment; Greenwood and Suddaby (2006) discuss institutional entrepreneurship in a mature field, while Maguire, Hardy, and Lawrence (2004) discuss the same in an emerging field. I here argue that significant evaluators such as rating agencies potentially guide the normative environment of organizations in the field via encoded templates, either as conservators and defenders of the current system or as challengers of the status quo.

The agencies also constitute a source of legitimacy, implying that organizations obtaining high ratings are associated with higher degrees of social acceptance. Rating agencies generate normative, prescriptive assessments of the rated organization and its perceived structures, procedures, and outcomes, thus contributing to the development of the field both materially

and in terms of ideals and values. At the same time, not all MFOs choose to be rated; those MFOs which mainly are dependent on donations, member savings or government grants are, for instance, less likely to obtain a microfinance rating. These types of organizations may instead be more interested in social ratings and social impact assessments. Although some would argue that such organizations are less affected by the verdicts of microfinance ratings, extant reasoning based in the neo-institutional tradition and using the organizational field concept would posit that even non-rated MFOs are embedded in the same institutional environment and thus influenced by the same templates.

I also tap into extant literature pertaining to external evaluations. With the exception of Schultz et al.'s (2001) ranking study, research has not explored changes over time in the mechanics and underlying rationales of rating. Instead, extant literature on external evaluations has focused on demonstrating the effects on organizations and fields. Further, most evaluation research has had well-established fields, wherein the template has already been known, as its empirical settings. In this research, I have been interested in how external evaluations unfold in contexts characterized by complexity, ambiguity and contestation.

The study also opens up the discussion about mediators and mediated markets (Zuckerman, 1999). In mediated markets, intermediaries play a dominant role in organizing transactions and deciding on the flow of resources. I argue that mediators can play an especially interesting role as stabilizers, translators, and points of reference in complex and turbulent sectors. Extant studies commonly assign a distinct logic to the evaluating audiences, or institutional referents, which perform the judging and evaluative work. Reay and Hinings (2009), for instance, analyze the professional logic of medical doctors and the business logic of managers, and Purdy and Gray (2009) examine the social services logic of public policy agencies. In contexts such as the Indian microfinance sector, it is, however, likely that some intermediaries, such as M-CRIL, operate under multiple and competing logics, and thus mediate more than one logic in their assessments.

Through my operationalization, I also bring forward a more nuanced view of the concept of legitimacy. By studying the template as encoded by an intermediary, the encoded template can be used as a proxy for determin-

ing what is legitimate. The notion of a significant encoded template as a proxy for legitimacy challenges the tendency within the neo-institutional tradition to conceptualize legitimacy in binary terms as either legitimate or illegitimate (Cloutier and Langley, 2013; Vergne, 2010). By studying a template that is projected by a significant intermediary, it is possible to deduct which organizational elements, as opposed to which organizations, are regarded as legitimate in a given context.

Finally, I contribute to the growing stream of studies that uses microfinance ratings as empirical context to better understand the microfinance sector. Although microfinance activities touches the lives of millions of people in the world, most of whom are poor and live in so-called developing countries and most of whom are women, studies conducted by management scholars have to date been sparse (Khavul, Chavez, and Bruton, 2013, pp. 57-58). Instead, previous studies have been based in quantitative traditions within the fields of economics and finance. As the first study to employ a qualitative and longitudinal approach, the current research brings to light hitherto unexplored aspects of the evaluative instruments used to rate MFOs. By using a qualitative approach, I have been able to gain an in-depth and contextualized understanding of evaluative practices.

The empirical contribution and implications

This dissertation explores the developments in the Indian microfinance sector as seen from the perspective of an important and deeply embedded evaluator. The study provides several empirical insights. To start with, I confirm and extend earlier studies that have shown that microfinance sectors are subject to strong financial influences (see, e.g., Khavul, Chavez, and Bruton, 2013), which have also come to permeate the evaluation of organizations in terms of structures, procedures and goals. As I have shown in this dissertation, the Indian microfinance sector is infused with a variety of tensions, and the most notable one is finding a balance between achieving a social mission and obtaining strong financial results. As suggested by many others, a financial/market logic has started to permeate different types of social arenas in substantial ways. My research supports this observation and suggests that evaluators such as rating agencies project idealized images of

organizations that endorse profit, growth, and efficiency. In addition, evaluators confirm, reinforce, and contribute to the acceleration of a trend towards more business-like structures and practices (Maier and Meyer, 2010, pp. 32-33), e.g., professionalization (Hwang and Powell, 2009), the development of marketing strategies (Shoham, Ruvio, Vigoda-Gadot, and Schwabsky, 2006); (Helmig, Jegers, and Lapsley, 2004), demonstrating impact in terms of quantifiable and measurable results (Gledhill, 2004), the adoption of corporate governance practices (Alexander and Weiner, 1998), and an emphasis on both internal and external audits and evaluations (Roberts, Jones III, and Fröhling, 2005; Townsend, Porter, and Mawdsley, 2002; see also Wijkström and Einarsson, 2011). The reports further project a perspective which, in Desai and Imrie's words, "regard[s] social and political issues as technical and/or procedural issues, that is, matters to be managed" (1998, p. 636).

As discussed above, the rating practices and the templates reflect a widespread trend toward financialization. While acknowledging that nonprofit organizations such as MFOs operating as societies, trusts, and section 25 companies may receive several benefits from these developments, e.g., in terms of stable resource streams, innovation, and efficiency, Eikenberry and Kluver (2004) point at the greater risks to democracy and civil society that are associated with the marketization of nonprofit sectors such as the Indian microfinance sector during its early years (see also Kaldor, 2003; Anheier, 2007). First, the role of civil society as guardians of values may be lost due to intensified competition, mission drift, and a focus on staff productivity. Second, civil society is also seen as the builder of social capital, working to generate social cohesion and create a robust and resilient society. Yet, due to practices such as the recruitment of board members who are not from the target community and a focus on the bottom line instead of on strengthening social capital, this role may disappear over time. A third manifestation of the function of civil society is service delivery and advocacy. However, when market logic enters into the equation, organizations risk losing sight of the poorest and most vulnerable members of society and their actual needs as opposed to "client demand." My findings thus come with a note of caution regarding the increasing reliance on professional evaluators and auditors in the microfinance sector. What type of ide-

als and models do these actors promote, and what type of organizations and ways of organizing may be lost?

Through my study, I hope to provide evaluators with an enhanced understanding for their potential role in reaffirming, as well as creatively constructing, templates to guide organizations in the field. I have concerned myself with the underlying mechanics of and rationales for rating practices and have shown how the rating instrument has undergone considerable change over a relatively short period of time. Although still limited, this supports the finding from other recent studies; Collet and Vives (2013), for instance, show that rankings have changed over time. Although revising and making adjustments in the evaluating instrument is a necessity in a constantly changing environment, evaluators should be aware of the constraints that such changes impose on the evaluated organizations. Evaluators should try to identify, analyze, and reflect on changes over time in their own evaluation approach and attempt to understand the expectations and pressures that they are placing on the evaluated organizations and how these evolve over time.

Although the Indian microfinance sector (as reflected in the sample used herein) is heterogeneous in terms of legal forms, organizational size, and delivery models, raters use one template to evaluate all types of organizations. This implies that ratings lead to the reinforcement of one ideal model of organizational structures and practices. A different approach to rating MFOs would be to categorize MFOs into different subgroups depending on their legal form, delivery model, and profit orientation, and thereafter assess these subgroups according to different rating rationales. This way, a local nonprofit would be assessed according to one specific rationale and a listed MFO with shareholders and profit-seeking investors would be evaluated according to another.

Although expectations from, for example, financially driven investors and banks to show positive financial results explain why the raters embrace the for-profit non-banking financial company form over other forms, regulators may also find this dissertation of interest, as it suggests that raters place a great deal of emphasis on the existence of any type of formal rules or regulatory framework. For the Indian microfinance sector, this has, for instance, resulted in the regulated, and also for-profit, non-banking finan-

cial company form taking precedence over other legal forms whose microfinance activities have remained outside the purview of the Reserve Bank of India. Given the complexity of the Indian microfinance sector, having a legislative framework to lean on and refer to renders the process of evaluation easier and more straightforward; this may be one reason why raters seem to prefer regulated legal forms over non-regulated ones. This implies that policymakers, by refraining from regulating the microfinance activities of not-for-profit trusts, societies, and section 25 companies, also render these forms less legitimate from an evaluation perspective. To encourage pluralism in legal forms, regulators should aim to include the microfinance activities of several different types of legal forms under the legal framework.

There are many types of assessments and evaluations available for investors and donors. To balance the focus on financialization in form and content, those interested in supporting MFOs should rely not only on microfinance ratings, but also on social ratings and audits as well as other forms of assessments that aim at capturing the social impact of the MFO. At the same time, investors and donors should keep in mind that easily quantifiable and measurable indicators are not always the most suitable way of assessing organizations whose aims include building social capital, altering inequitable social and economic structures, and reaching out to the most disadvantaged.

For the evaluated MFO, this study shows that expectations from intermediaries such as rating agencies fluctuate over time and are far from constant. Attempting to conform to an ever-evolving template may be a formidable challenge for the MFO. Instead of chasing a constantly moving idealized image, MFOs should, as proposed by Kraatz and Block (2008), strive to be true to their mission, and reflect consistency, character, and trustworthiness.

Future research

This dissertation has provided answers to several questions related to evaluative practices and the templates projected through these in complex environments. The rapidly changing, globalizing, and increasingly complex

world leaves no one unchallenged and the role and function of evaluators such as credit rating agencies and university rankings have been severely criticized. The seemingly endless supply of mediating organizations and systems – many of which are still nascent – which seek to measure and order other organizations, reveals a certain level of competition and a need to build reputation and legitimacy among the mediators themselves.

In the credit ratings literature, several quantitative studies have looked at the relationship between credit cycles and changes in rating standards (Amato and Furfine, 2004; Altman and Rijken, 2004). However, with a few exceptions (Collet and Vives, 2013), management researchers have not studied how macro level changes impact evaluation instruments and their underlying rationales. Instead, the focus of these scholars has been on the effects of evaluations on the evaluated organizations. At the same time, altering rating criteria and processes as a response to external threats may pose other challenges to the legitimacy of the evaluator, as the credibility of evaluative criteria to a certain extent builds on the fact that these are perceived to be principally consistent and stable over time as opposed to opportunistic and evolving (Kraatz and Block, 2008). In the case of credit rating agencies, for instance, it has been suggested that these follow a reputational model, meaning that users will only hire those agencies whose credit ratings carry weight with investors, and further implying that too many downgrades may alter this credibility (Mathis et al., 2009). In this light, future research needs to ask what factors serve to legitimize evaluators, how evaluators legitimize themselves, and how the legitimating efforts of evaluators impact their products.

A more critical approach would be to investigate sectors wherein several templates battle for space and attention and to study which templates survive and why. Are some sectors more commonly characterized by several competing templates? It is likely that the structure of the field is an important factor for understanding template development. Fields that are structured into clusters with clear internal hierarchies, often referred to as fragmented centralization (Besharov and Smith, 2013), are, for example, likely to contain several competing templates. An analysis of the flow of resources in the field would also clarify the critical actors and their respective logics which the organizations have to oblige in order to secure re-

sources. Further, when there are multiple institutional logics at play and several templates that compete, why are some templates more likely to become enacted by organizations? When assessing which template is likely to survive over others, another question that arises is which institutional referents "have the capacity to mobilize and confront" the organizations (Meyer and Scott, 1983, p. 201). What are the roles of resourceful actors and power asymmetries in these processes? What determines which templates will prevail and which will die out?

In this research, I have shown that rating reports of MFOs include several tensions. One way in which these are dealt with by the raters is to reveal how best to prioritize and address certain issues. My analysis has not, however, gone into detail about how the raters make sense of these tensions. The paradox perspective provides a complementary approach to analyzing tensions that should engage future scholars (Smith and Lewis, 2011).

Concluding remarks

In this dissertation, I set out to investigate how rating practices are constructed and operate. By studying the evaluative practices of a prominent rating agency over time, as well as the templates that are projected through these in the complex and rapidly changing context of microfinance, I have sought to contribute to the understanding of how such practices are constructed and change. I have also shed light on how codified templates correspond to trends and events in the microfinance sector, as well as how changes in the same can be related to the situated vantage point, market position, and perceived role of the evaluator. Addressing gaps in the literature that explores evaluative practices and change, I investigate empirically how a prominent evaluator both reflects and constructs templates for organizations in the field of Indian microfinance. I have with this dissertation added to the growing stream of literature on the role of evaluators and evaluative practices.

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Appendix 1: Sample reports

Name as in report	*Name used*	*Year*	*Update*	*Grade*	*G*	*M*	*F*	*Borrowers*	*Portfolio (million INR)*[86]	*Staff*	*Borrowers per staff*	*Return on assets*	*Legal form*	*Delivery model*
Cashpor Financial and Technical Services Pvt Ltd	Cashpor	1999	0	β+	NA	NA	NA	NA	2	112	NA	NA	Private limited company	JLG
Activists for Social Alternatives (ASA) – Grama Vidiyal	GVMF	1999	0	α-	NA	NA	NA	NA	10	63	NA	NA	Trust	JLG
Bullock Cart Workers Development Association (BWDA)	BWDA	2001	0	β	α-	β-	β+	1,455	3	57	26	-119%	Society	SHG
Activists for Social Alternatives (ASA) – Grama Vidiyal	GVMF	2001	1	β+	α-	α-	β+	18,141	46	156	NA	-5%	Trust	JLG
Swayam Krishi Sangam	SKS	2001	0	β+	β	α-	α-	1,810	5	45	NA	-47%	Society	JLG
Spandana	Spandana	2001	0	α	α-	α	α+	7,742	28	33	300	10%	Society	SHG and JLG
Bullock Cart Workers Development Association (BWDA)	BWDA	2002	1	β+	α-	α-	β+	3,627	11	82	40	-48%	Society	SHG
Mahasemam Trust	Mahasemam	2002	0	β+	α-	β+	β+	692	2	44	NA	-75%	Trust	SHG and JLG
Sarvodaya Nano Finance Lim-ited/SMBTs	SNFL	2002	0	α-	α-	β+	α-	7,744	27	8	NA	0%	NBFC	SHG
Spandana	Spandana	2002	1	α	α-	α-	α+	21,331	93	66	323	10%	Society	SHG and JLG

[86] From 1999-2014, the INR/USD exchange rate has fluctuated from 39-68 (Free Currency Rates, n.d.).

Grameen Koota	Grameen Koota	2003	0	β	α	α-	β	2,719	8	60	60	-27%	Trust	JLG
Activists for Social Alternatives (ASA) – Grama Vidiyal	GVMF	2003	2	β+	β+	α-	β+	41,753	118	221	189	-2%	Trust	JLG
Mahasemam Trust	Mahasemam	2003	1	β+	α-	α-	β+	5,244	15	140	37	-18%	Trust	SHG and JLG
Swayam Krishi Sangam	SKS	2003	1	α-	β+	α-	α-	11,496	40	51	180	-12%	Society	JLG
Swayam Krishi Sangam	SKS	2003	2	α-	β+	α-	α-	20,190	51	80	293	-5%	Society	JLG
Sarvodaya Nano Finance Lim-ited/SMBTs	SNFL	2003	1	α	α-	α-	α+	22,890	68	34	673	3%	NBFC	SHG
Spandana	Spandana	2003	2	α+	α	α	α+	50,254	232	103	488	12%	Society	SHG and JLG
Bullock Cart Workers Development Association (BWDA)	BWDA	2004	2	α-	α-	α-	α-	8,293	33	65	128	0%	Society	SHG
Bullock-cart Work-er's Development Association (BWDA) and BWDA Finance Ltd (BFL)	BWDA	2004	3	α-	α-	α-	α	26,375	56	68	388	2%	Society and NBFC (2003)	SHG
Grameen Koota	Grameen Koota	2004	1	β	α-	β+	β	10,341	37	83	125	-8%	Trust	JLG
Activists for Social Alternatives (ASA) – Grama Vidiyal	GVMF	2004	3	β+	α-	α-	β+	62,413	158	204	339	-1%	Trust	JLG
Mahasemam Trust	Mahasemam	2004	2	β	β+	β+	β	11,840	24	133	90	-13%	Trust	SHG and JLG
Swayam Krishi Sangam	SKS	2004	3	α-	α-	α-	α-	51,672	306	201	257	3%	Society	JLG
Spandana	Spandana	2004	3	α+	α	α	α+	115,742	441	181	639	12%	Society	SHG and JLG
Cashpor Micro Credit	Cashpor	2005	1	β+	β+	α-	β+	68,229	270	438	156	-13%	Section 25 company (2003)	JLG
Grameen Koota	Grameen Koota	2005	2	α-	α-	β+	α-	22,367	114	120	186	2%	Trust	JLG
Activists for Social Alternatives (ASA) – Grama Vidiyal	GVMF	2005	4	α-	α	α	α-	55,566	163	241	231	10%	Trust	JLG
Mahasemam	Mahasemam	2005	3	β+	β+	β	α-	36,342	124	235	155	3%	Trust/NBFC (2004)	SHG and JLG

Trust/Semam Microfinance Investment Literacy and Empowerment Pvt. Ltd. (SMILE Pvt. Ltd.)														
Swayam Krishi Sangam	SKS	2005	4	α	α	α	α	73,635	332	290	254	1%	Society	JLG
Sarvodaya Nano Finance Lim-ited/SMBTs	SNFL	2005	2	α	α-	α-	α	47,282	241	614	78	0%	NBFC	SHG
Bullock-cart Work-er's Development Association (BWDA) and BWDA Finance Ltd (BFL)	BWDA	2006	4	α	α	α-	α	47,308	427	176	324	2%	Society and NBFC (2003)	SHG
Cashpor Micro Credit	Cashpor	2006	2	β+	α-	α-	β+	123,359	510	626	197	-16%	Section 25 company (2003)	JLG
Activists for Social Alternatives (ASA) – Grama Vidiyal	GVMF	2006	5	α-	α-	α	α-	73,368	253	361	203	0%	Trust	JLG
Mahasemam Trust/Semam Microfinance Investment Literacy and Empowerment Pvt. Ltd. (SMILE Pvt. Ltd.)	Mahasemam	2006	4	β+	β+	β+	α-	143,926	261	637	225	3%	Trust and NBFC (2004)	JLG
SKS Microfinance Pvt. Ltd.	SKS	2006	5	α-	α	α	α-	332,663	1,290	1,710	195	3%	NBFC (2003)	JLG
BWDA Finance Ltd (BFL) and Bullock-cart Worker's Development Association (BWDA)	BWDA	2007	5	α	α	α-	α	206,734	759	167	713	2%	Society and NBFC (2003)	SHG
Grameen Koota	Grameen Koota	2007	3	β+	β+	β+	α	73,123	305	361	202	5%	Trust	JLG
Activists for Social Alternatives (ASA) – Grama Vidiyal	GVMF	2007	6	α-	α-	α	α	181,328	803	675	300	1%	Trust	JLG
BWDA Finance Ltd (BFL)	BWDA	2008	6	α-	α-	β+	α	210,721	851	456	616	2%	NBFC (2003)	SHG
Grameen Koota	Grameen	2008	4	α-	α	α-	α-	117,647	826	560	NA	2%	NBFC (2007)	JLG

	Koota													
Grama Vidiyal Micro Finance (P) Ltd	GVMF	2008	7	α	α	α	α+	224,105	1,156	1,018	220	6%	NBFC (2007)	JLG
Mahasemam Trust	Mahasemam	2008	5	β+	β+	β+	β+	73,002	328	632	231	0%	Trust	JLG
Sarvodaya Nano Finance Lim-ited/SMBTs	SNFL	2008	3	α	α-	α-	α	154,772	894	NA	128	2%	NBFC	SHG
Cashpor Micro Credit	Cashpor	2009	3	α-	α-	α-	α-	314,203	1,811	NA	NA	0%	Section 25 company (2003)	JLG
Gramalaya Urban and Rural Devel-opment Initiatives and Network (Guardian) -	Guardian	2009	0	β	β	β	β	3,642	15	21	173	-7%	Section 25 company	SHG and JLG
Grama Vidiyal Micro Finance (P) Ltd	GVMF	2009	8	α	α	α	α+	360,466	2,025	1,596	224	4%	NBFC (2007)	JLG
Mahasemam Trust	Mahasemam	2009	6	α-	β+	α-	α-	71,666	340	774	334	2%	Trust	JLG
Sarvodaya Nano Finance Limited	SNFL	2009	4	β+	β+	β	β+	149,556	934	NA	109	-1%	NBFC	SHG
Cashpor Micro Credit	Cashpor	2010	4	α	α	α	α-	417,039	2,674	NA	NA	3%	Section 25 company (2003)	JLG
Gramalaya Urban and Rural Devel-opment Initiatives and Network (Guardian)	Guardian	2011	1	β	β	β+	β	10,784	53	30	359	3%	Section 25 company	SHG and JLG
Sarvodaya Nano Finance Limited	SNFL	2011	5	β+	β+	β	β+	104,485	481	NA	116	1%	NBFC	SHG
Gramalaya Urban and Rural Devel-opment Initiatives and Network (Guardian) -	Guardian	2012	2	β	β+	β+	β	11,944	64	33	360	1%	Section 25 company	SHG and JLG
RGVN (North East) Microfinance Ltd.	RFVN	2012	0	β+	α-	β+	β+	147,954	1,090	349	424	4%	NBFC (2003)	SHG and JLG
Sarvodaya Nano Finance Limited	SNFL	2012	6	β	β	β	β+	74,567	387	118	109	4%	NBFC	SHG/Individual
Ankur Securities Private Limited	ASPL	2013	0	NA	NA	NA	NA	NA	23	678	NA	4%	NBFC	JLG

(ASPL)														
Gramalaya Urban and Rural Development Initiatives and Network (Guardian) -	Guardian	2013	3	β	β+	β+	β	15,962	83	58	270	0%	Section 25 company	SHG and JLG
Annapurna Mahila Cooperative Credit Society	Annapurna	2014	0	β+	β+	β	β+	34,543	393	152	227	2%	Cooperative society	JLG

Unless otherwise stated, all figures originate from the reports. They have not been modified, as the intention is to reflect the figures used by the raters when doing their assessment.

NA = This figure is not available in the report and cannot be derived from existing data given in the report. "NA" does not necessarily mean that the data is missing completely, but that it is presented in a different form than the one used here and the above form/ratio cannot be derived thereof. For reasons of comparisons, such data has not been included.

Appendix 2: Interview questions for M-CRIL

General questions

- What is the history of M-CRIL?
- What is your role in M-CRIL?
- What is the role of M-CRIL?
- Is M-CRIL different from other rating agencies? Which, how, and why?
- Are the clients different?
- How has M-CRIL funding been structured over the years?
- Is there ever a conflict of interest issue? When and how? How do you address this?
- How do you see M-CRIL working in the future? Will your role change?
- What is the purpose of M-CRIL's reviews and reports?
- What is the purpose of all the articles that you write?

Questions pertaining to the rating reports

- Tell me about the revisions made in the report format. How do they differ?
- What were the reasons for these changes?
- What are the lessons learned?
- There are several types of rating reports. Why? How do they differ?
- What role do benchmarks have in the rating?

- Please comment on the changes that I have observed in the reports so far. Do you agree? Were they intentional? If not, why do you think they occurred? If so, what was the reason behind?
    - Context factors and the political environment
    - Regulation
    - Social performance
    - Decision-making
    - Legal status and model of operation
    - Staff productivity" and "Operating efficiency
    - Financial performance
    - The role of the governing board
    - Organograms
    - Chart with ownership shares
    - Charts with growth rate
    - Interest rate
    - Geographical, horizontal, and vertical coverage
    - Suggestions
    - Projected cash flows and financial statements for five years
    - The role of savings
    - Client protection and transparency
    - What is important when it comes to the board members?
    - MFO visions and missions

Appendix 3: List of interviews

M-CRIL				
No	*Name*	*Designation*	*Date and place*	*Documentation*
1	Sanjay Sinha	Managing director and member of the board	Gurgaon, 12 Oct 2011	Notes were taken
2, 3	Sanjay Sinha Alok Misra	Managing director and member of the board Chief executive officer and member of the board	Gurgaon, 30 April 2012	Audiotaped and transcribed
4	Brij Mohan	Member of the board, former executive director of SIDBI and founder of the SIDBI Foundation for Micro Credit	Gurgaon, 25 May 2012	Extensive notes were taken
5, 6	Gunjan Groover Swetan Sagar	Senior vice president Chief operating officer	Gurgaon, 25 May 2012	Extensive notes were taken
7	Revathy Menon	Analyst	Gurgaon, 25 April 2013	Audiotaped and transcribed
8	Gunjan Groover	Senior vice president	Gurgaon, 25 April 2013	Audiotaped and transcribed
9	Swetan Sagar	Chief operating officer	Gurgaon, 25 April 2013	Audiotaped and transcribed
10	Shraddha Jha	Senior analyst	Gurgaon, 25 April 2013	Audiotaped and transcribed
11, 12	Sanjay Sinha Frances Sinha	Managing director and member of the board Managing director, EDA Rural Systems, and member of the board	Gurgaon, 24 May 2013	Audiotaped and transcribed

OTHERS					
No	*Name*	*Designation*	*Organization*	*Date and place*	*Documentation*
1	Vipin Sharma	Chief executive officer	ACCESS Development Services	New Delhi, 12 Oct 2011	Notes were taken
2	Alok Pande	Director	Ministry of Finance, Government of India	New Delhi, 12 Oct 2011	Notes were taken
3	Harihara Mohapatra	Assistant manager	Sa-Dhan	New Delhi, 12 Oct 2011	Notes were taken
4	Alok Prasad	Chief executive officer	Microfinance Institutions Network	New Delhi, 13 Oct 2011	Notes were taken
5	R Ramakrishna	Senior program specialist	GIZ	New Delhi, 13 Oct 2011	Notes were taken
6	Vivekanand N Salimath	Member of the board	AKMI	Bangalore, 31 Oct 2011	Notes were taken
7	B S Suran	Chief general manager, Inspection depart-ment	NABARD	Mumbai, 11 Nov 2011	Notes were taken
8	Sanjay Kher	National sales manager, Special products	SMERA	Mumbai, 12 Nov 2011	Notes were taken
9	Ravi Kumar Dasari	Manager, MFI Division	CARE Ratings	Mumbai, 12 Nov 2011	Notes were taken

Appendix 4: Examples of rating report covers

Micro-Finance Capacity Assessment

Cashpor Financial and Technical Services Pvt Ltd (CFTS)
Mirzapur, Uttar Pradesh (India)

Rating grade β+ **beta plus** Composite score: 59.5 %	**Assessment**: Recommended, reasonable safety, good systems, needs monitoring

Visit dates: 16-18 March, 1999
Operational head: Mr Md Ahasan Bhuiyan

Maximum validity of rating*: till 18 March 2000

Rating

CFTS has strong organisational and managerial performance though only a moderate financial performance.

In M-CRIL's view on account of the rapidly expanding operations, good management systems and trained workforce, CFTS can absorb - through SIDBI - additional loan funds to the extent of Rs 50 lakhs in 1999-2000 for on-lending to its borrowers from all its branches. **This rating is valid, subject to no other substantial inflows of funds into CFTS beyond the limits specified here** and to no other significant changes in the organisational structure and external operating environment. Monitoring of outreach and financial performance is recommended.

- for M-CRIL division, EDA Rural Systems Pvt Ltd

Sanjay Sinha, Executive Director

***Validity** This rating is valid till the next loan proposal made by CFTS to any financial institution or till any other significant change in the structure of the loan programme or in its external environment. A **review** of this rating is recommended whenever such changes take place or at the end of **one year** from the date of this assessment, whichever is earlier.

Liability The rating assigned is a professional opinion of the assessors and M-CRIL does not guarantee the information and cannot accept any legal responsibility for actions arising out of the recommendations made.

MicroRating International

rating review of an **NBFC**

Grameen Koota – ***fourth update***

NBFC – a unit of GFSL Pvt. Ltd

Bengalooru, INDIA

Rating review as on 31 March 2008 *Report valid until end-January 2009*

Contacts

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CREDIT RATING	**α–**
RATING OUTLOOK*	*positive*

*M-CRIL's viewpoint (positive, neutral or negative) of the future prospects of the organisation

Date of visit	**29 Jan-1 Feb 2008**
Date of previous rating	January 2007
Previous rating	β+

Investment Grade			
Above	α++		
	α	α+	
		α	
		α–	
	β	β+	
		β	
Below		β–	
	γ	γ+	
		γ	

Main Performance Indicators	Mar-06	Mar-07	Mar-08
Gross Portfolio (Rs cr)	13.9	42.8	82.6
Managed Portfolio (Rs cr)	8.3	3.1	-
No. of active borrowers	39,628	82,562	1,17,647
Return on Assets	0.3%	4.3%	2.0%
Portfolio Yield	35.5%	32.6%	27.9%
Portfolio at Risk$_0$	0.0%	0.0%	0.0%
Operating Expense Ratio	22.1%	16.1%	15.6%
Average Loan O/s (Rs)	5,594	5,569	7,025
Borrowers per field staff	200	277	286

Synopsis

From October 2007, Grameen Koota (GK) has been functioning as an NBFC, Grameen Financial Services Private Ltd (GFSL). Meeting the equity requirements of the new entity has enabled GK to enhance its capital adequacy. Operations and management systems continue to be of reasonable standards. With respect to human resources, efforts are being made to build a strong middle management by bringing in ex-bankers. The attrition rate of field staff is high. The management plans to curtail the attrition rate by modifying HR policies. With respect to the size and expansion plans of the organisation, internal audit is moderate and follow-up and compliance mechanisms need to be improved. The profitability of the new entity has declined but is expected to improve over time. Governance has substantially improved with the establishment of a new, stronger and more independent Board.

In M-CRIL's view, on account of a significant institutional presence, overall good performance, as well as considering the growth plans of the organisation, GK can absorb loan funds of up to Rs110 crores till February 2009.

Highlights

Positive

- Stronger governing Board
- Qualified management staff
- High quality and efficiency of field operations
- Good management systems including loan appraisal and recovery systems, staff incentive system, MIS and tracking system for overdues
- Good asset quality and diversified portfolio
- Comfortable capital adequacy

Negative

- Moderate internal audit
- High attrition rate at field staff and client level

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RGVN (North East) Microfinance Ltd. {First rating}

Guwahati, Assam, India – **NBFC MFI** September 2012

Microfinance Institutional Rating

Investment Grade			
Above	α	α+
		α
		α–
	β	β+
		β
Below		β–
	γ	γ+
		γ

RATING	β+
RATING OUTLOOK*	*positive*

Dimensions rated	Grade
Governance & strategy	α–
Organisation & Management	β+
Financial performance	β+

*M-CRIL's viewpoint (positive, neutral or negative) of the future prospects of the organisation

Visit: 3-6 September 2012

M-CRIL

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Appendix 5: Summary of indicators and ratios

	1999 (7 indicators)	*2001-2003 (28 indicators)*	*2005-2007* (32 indicators)*	*2007**-2010 (46 indicators)*	*2012 (35 indicators)*
PORTFOILIO QUALITY	Cumulative repayment rate	Cumulative repayment rate	Cumulative repayment rate		
			Current repayment rate	Current repayment rate	
	Portfolio at risk (60)	Portfolio at risk (60)	Portfolio at risk (60)	Portfolio at risk (60)	Portfolio at risk (60)
				Portfolio at risk (30)	Portfolio at risk (30)
				Portfolio at risk (>0 days) / Gross loan portfolio	
				Portfolio at risk (30) / Gross loan portfolio	Portfolio at risk (30) / Gross loan portfolio
				Portfolio with arrears >50 weeks, 26-50 weeks, 5-25 weeks, no arrears	Portfolio with arrears 1-30, 31-60, 61-90, 91-120, 121-180, 181-365, >365
		Loan loss provisioning ratio	Loan loss provisioning ratio	Loan loss provisioning ratio	Loan loss provisioning ratio
				Write-offs / Average gross portfolio	Write-offs / Average gross portfolio
				Loan loss reserves / Portfolio at risk	Loan loss reserves / Portfolio at risk
CAPITAL ADEQUACY AND SOLVENCY		Asset composition	Asset composition		
		Debt and equity composition	Debt and equity composition		Debt to equity
		Liability and net worth composition	Liability and net worth composition		
		Capital adequacy ratio	Capital adequacy ratio	Capital adequacy ratio	Capital adequacy ratio
	Total savings	Group level savings	Client savings		
SUSTAINABILITY AND PROFITABILITY		Operating self sufficiency	Operating self sufficiency	Operating self sufficiency	Operating self sufficiency
		Financial self sufficiency	Financial self sufficiency	Financial self sufficiency	Financial self sufficiency
		Return on assets	Return on assets	Return on assets	Return on assets
				Return on equity	
		Subsidy dependence index			
				Net operational income	
				Net operating margin	Net operating margin
		Other financial income to average portfolio outstanding	Other financial income to average portfolio outstanding	Other financial income to average portfolio outstanding	Other financial income to average portfolio outstanding
		Total expenses to average total assets	Total expenses to average total assets		
		Income and expense distribution	Income and expense distribution		
GROWTH AND SIZE			Branches	Branches	

				Groups	
				Staff	Staff
				Field staff	Field staff
	Cumulative loans disbursed	Cumulative loans disbursed	Cumulative loans disbursed		
			Loans disbursed in current year		
				Gross (own) loan portfolio	Gross (own) loan portfolio
	Loans outstanding	Loans outstanding	Loans outstanding	Loans outstanding	Loans outstanding
		Outstanding borrowings	Outstanding borrowings	Outstanding borrowings	Outstanding borrowings
		Portfolio		Portfolio	Portfolio
		Members		Members	
		Active borrowers	Active borrowers / Clients	Active borrowers	Active borrowers / Active clients
				Client growth rate	Client growth rate
				Portfolio growth rate	Portfolio growth rate
			Managed portfolio	Managed portfolio	Managed portfolio
			External funds		
	Future outreach outstanding portfolio, total branches, total clients				
ASSET / LIABILITY MANAGEMENT		Yield on portfolio	Yield on portfolio	Yield on portfolio	Yield on portfolio
			Weighted average cost of funds	Weighted average cost of funds	Weighted average cost of funds
		Financial cost ratio	Financial cost ratio	Financial cost ratio	Financial cost ratio
			Loans / Total assets	Loans / Total assets	Loans / Total assets
		Yield to APR ratio	Yield to APR ratio		
				Cash and liquid assets / Total assets	
				Cash and liquid assets / Total deposits	
				Average cash and bank balance / Average portfolio	Average cash and bank balance / Average portfolio
EFFICIENCY AND PRODUCTIVITY		Operating expense ratio	Operating expense ratio	Operating expense ratio	Operating expense ratio
		Active borrowers / Staff	Active clients/borrowers / Staff	Active clients/Borrowers / Staff	Active clients/Borrowers / Staff
		Active clients / Field staff		Borrowers / Field staff	Active clients/ Borrowers / Field staff
				Cost / Borrower	
				Active borrowers / Members	
	Average loan size	Average loan size	Average loan size	Average loan size	Average loan size
				Average loan disbursed	Average loan disbursed
				Average outstanding loan size	Average outstanding loan size
				Gross loan portfolio / Field staff	
			Cost to company / Employee		

* First report format
** Second report format

Appendix 6: Summary of changes in the structure of the reports

1999-2006		2007-2010	2011-2014	
1999-2003	*2004-2006*		*2011*	*2012-2014*
(Untitled initial section)	**(Untitled initial section)**	**(Untitled initial section)**	**(Untitled initial section)**	**(Untitled initial section)**
Rating grade and rationale	Rating grade and rationale	Rating grade and rationale	Rating grade and rationale	Rating grade and rationale
Summary of performance	Summary of performance	Summary of performance	Summary of performance	Summary of performance
Strengths and weaknesses	Strengths and weaknesses	Strengths and weaknesses	Strengths and weaknesses	Strengths and weaknesses
		Country and state overview (1)		
Organizational background and microfinance operations	**Organizational background and microfinance operations**	**Microfinance operations**	**Introduction**	**Introduction**
Sources of funds (table) (2)	Sources of funds (table) (2)			
Microfinance policies	Microfinance policies	Microfinance policies	Microfinance policies	Microfinance products and policies
Savings products	Savings products	*Savings*		
Loan products	Loan products	Loan products	Loan products	
Insurance products	Insurance products	Insurance products	Insurance products	
	Organogram	Organogram	Organogram	Organizational structure
	Growth (table) (6)	Growth (table) (6)		
First rating category: Organizational aspects	**First rating category: Governance and operational strategy**	**First rating category: Governance and strategic positioning**	**First rating category: Governance and strategy**	**First rating category: Governance and strategy**
Strategy for microfinance operations	Strategy for microfinance operations (6)	Operational and growth strategy (6)	Operational and growth strategy (6)	Operational and growth strategy (6)
Experience in microfinance				
	Competition	Competition	Competition	Competition
	Fund mobilization (2)	Fund mobilization (2)	Fund mobilization (2)	Fund mobilization (2)
	Board	Board	Board	Board

	Second line of leadership	Second line of leadership	Second line of leadership	Second line of leadership
	NBFC transformation	Legal status		
	Product development	Products promotion and pricing		
	Equity mobilization (2)	Equity mobilization (2)		
	Growth and expansion/competition			
	Interest rate structure			
	Political environment/risk (1)			
		Investor relations		
		Member dropout		
		Social performance		
				Alignment of practices with mission
				Shareholding pattern
	Client protection and transparency (3)			
Second rating category: Managerial aspects	**Second rating category: Managerial factors**	**Second rating category: Organization and management**	**Second rating category: Organization and management**	**Second rating category: Organization and management**
Human resource quality and management	Human resource quality and management	Human resource quality and management	Human resource quality and management	Human resource quality and management
		Staff productivity (4)	Staff productivity (4)	Staff productivity (4)
		Operating efficiency (5)	Operating efficiency (5)	Operating efficiency (5)
Accounting and MIS	Accounting and MIS	Accounting and MIS	Accounting and MIS	Accounting and MIS
		Loan write-off		
		Analysis of accounting policies		
Tracking system for overdues	Tracking system for overdues	Tracking system for overdues	Tracking system for overdues	Tracking system for overdues
Financial planning and control systems	Financial planning and control systems	Financial planning and cash management (7)	Financial planning and cash management (7)	Financial planning and cash management (7)
		Internal control systems	Internal audit and control	Internal audit and control
Decision making				
Quality of clients/member groups	Quality of clients/member groups	Quality of clients/member groups	Quality of clients/member groups	*Quality of clients/member groups (8)*
Infrastructure	Infrastructure	Infrastructure	Infrastructure	Infrastructure
				Client protection (3) (8)
Third rating category: Financial performance	**Third rating category: Financial performance**	**Third rating category: Financial performance/profile**	**Third rating category: Financial profile**	**Third rating category: Financial profile**
Credit performance and asset quality	Credit performance and asset quality	Credit performance and asset quality	Credit performance and asset quality	Credit performance and asset quality
Mobilization of funds (2)	Mobilization of funds (2)	Mobilization of funds, equity and capital adequacy (2)	Capital adequacy (2)	Capital adequacy (2)

Asset, liability and equity composition (7)	Asset, liability and equity composition (7)	Asset, liability and equity composition (7)	Asset, liability and equity composition (7)	Asset, liability and equity composition (7)
Sustainability and profitability (4) (5)	Profitability and sustainability (4) (5)	Profitability and sustainability (4) (5)	Profitability and sustainability (4) (5)	Profitability and sustainability (4) (5)
		Loan utilization pattern		Portfolio diversification
				Margin analysis
Conclusions	**Conclusions**			
Strengths	Strengths			
Weaknesses	Weaknesses			
Suggestions				
Creditworthiness	**Creditworthiness**			
		Future plans and prospects	Future plans and prospects	Future plans and prospects
Financial statements	**Financial statements**	**Financial statements**	**Financial statements**	**Financial statements**
Balance sheet and income statements	Balance sheet and income statements	Balance sheet and income statements	Balance sheet and income statements	Balance sheet and income statements
Projected cash flows and financial statements for five years	Projected cash flows and financial statements for five years	*Projected cash flows and financial statements for five years*		
M-CRIL's microfinance rating symbols	M-CRIL's microfinance rating symbols		M-CRIL rating grades	M-CRIL rating grades
Glossary	Glossary	Glossary	Abbreviations and glossary	Abbreviations and glossary
			Profile of the board	List of board members
				Microfinance policies and products

Added (shaded in grey)	*Only there in a few sample reports (italicized)*	*Added but only there in a few sample reports (shaded in grey and italicized)*