PMIC Insight - V

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Environment and Social Management Framework - PMIC

PMIC's ESM Framework Objective

Pakistan Microfinance Investment Company Limited has adopted a Triple Bottom Line approach that envisages economic development, social inclusion and environmental sustainability. Accordingly, in addition to financial targets, an ESM Framework has been developed and adopted by the institution that envisages an adequate and appropriate response by PMIC and its borrowers to the challenges and risks associated with environmental and social issues, and risks, within the ambit of microfinance in Pakistan. It identifies and recommends standards and requirements for due diligence in order to mitigate environmental and social risks both at the portfolio and operational levels that apply to all PMIC's activities including lending and investing. The framework is designed with the aim of providing direction and guidance to PMIC and its borrowers in setting up ESM procedures for enhanced risk mitigation.

PMIC's E&S Principles

PMIC has devised five E&S principles which – in a targeted manner – respond to the risks associated with the entire scope of business of PMIC and its borrowers, including credit and otherwise.

E&S Principle 1 – Mainstreaming Environmental and Social Principles within the Governance Structure of PMIC

Ensuring clearly defined E&S management systems are in place that are commensurate with the level of E&S risks associated with PMIC's business activities.

E&S Principle 2 – Reducing Ecological Footprint and Promoting Social Inclusion within PMIC

Having efficient solutions which reduce impact on the environment, specifically water usage, transport fuels, energy and waste generation at the workplace.
Inclusive, responsive, encompassing and non-discriminatory HR policies and procedures

E&S Principle 3 – Managing PMIC Portfolio E&S Risks

Devising ESM Procedures which include due diligence procedures to identify risks and impacts of and on borrowers/investees, enforcement, monitoring and reporting of ESM procedures, external communication and a grievance redressal mechanism for ESM.

E&S Principle 4 – Providing Green and Inclusive Microcredit

Generating a measurable social and environmental impact alongside a financial return. Products may target safe drinking water, improved sanitation, waste management and recycling, sustainable agriculture, medicinal plants, sustainable harvesting and, mother and child nutrition and immunization.

E&S Principle 5 – Investing into E&S Knowledge Economy

Nurturing the E&S risks-related knowledge across the board through designing – and financing – structured training programs in ESM fundamentals, and pictorial resource materials for staff, borrowers and end-clients.

Positive News - Licensing of Private Sector Credit Bureaus

The State Bank of Pakistan (SBP) had introduced the Credit Bureau Act, 2015 to formalize the setting up of credit bureaus in the private sector. After a lapse of almost two and a half years, Aequitas (Pvt) Limited was recently licensed as the first credit bureau in the private sector in Pakistan, following which, Data Check Limited has also received its license. The licensing of private sector entities marks an important milestone for the financial sector eco-system at large and the microfinance sector in particular.

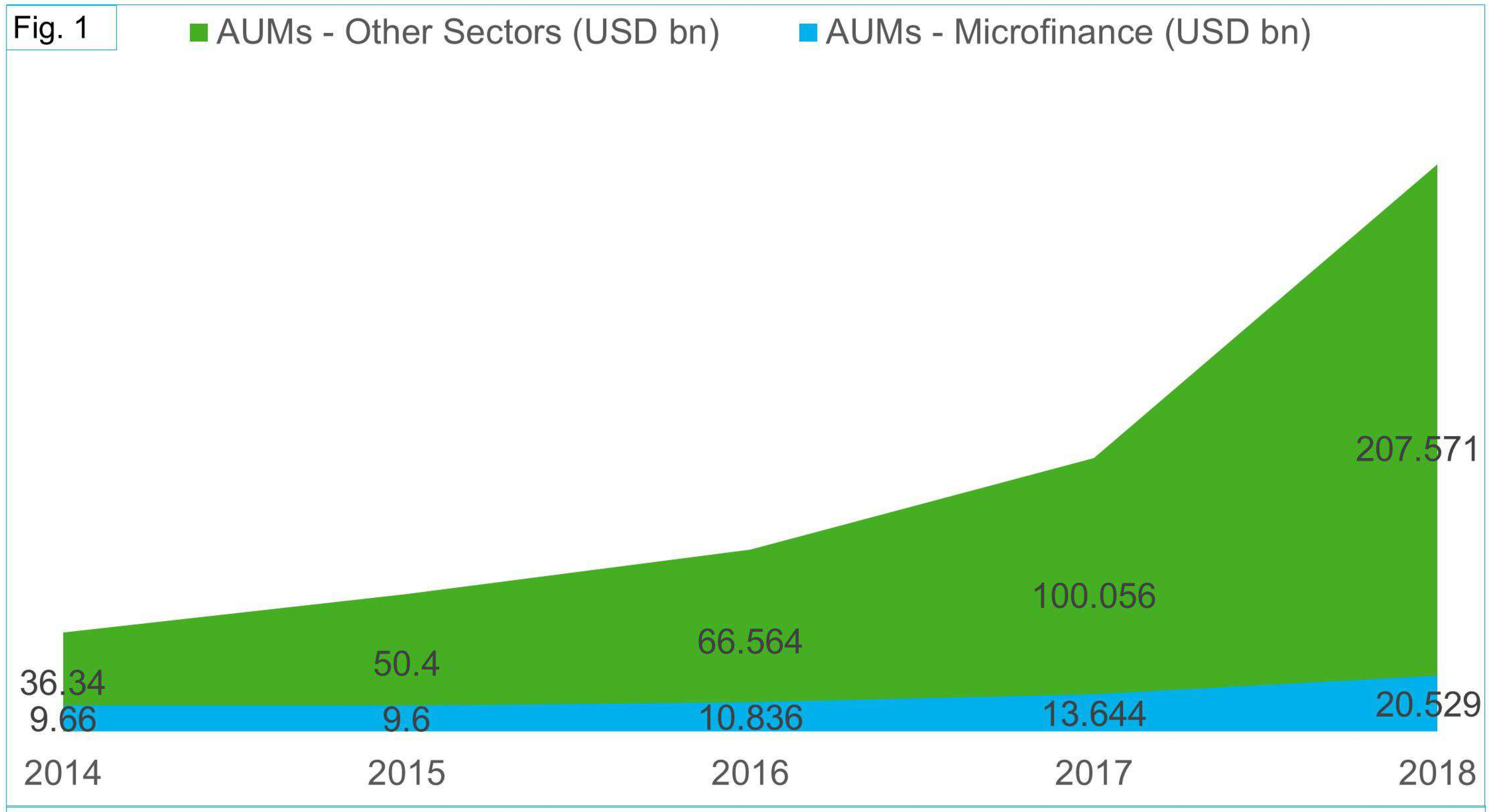
The primary purpose of credit bureaus is to make sure that creditors have the information they need to make lending decisions. In the past three years alone, the gross loan portfolio of the sector has increased almost 4x from Rs. 66.76b at end Dec-14 to Rs. 254.61b by end Sept-18. In the absence of a sector-wide credit bureau, microfinance providers (MFPs) may not be fully aware of the incidence of multiple borrowings, or the extent of leveraging by individual clients, unless such information is accurately disclosed by the clients themselves. In view of this, the sector was running the risk of over-indebtedness.

The setting up of credit bureaus is expected to allow MFPs to make more informed credit decisions. As per the Credit Bureau Act, all credit institutions are required to become members of at least one credit bureau. Given that a credit institution is required to report information to only the credit bureau(s) it is a member of, sector wide consolidation of credit information may still be lacking. An easy fix to the problem would be to require all credit institutions to report credit information to all licensed credit bureaus whereas they may only be required to generate credit report from the credit bureau(s), which they are a member of. In this way, the database of all credit bureaus would be standardized and then the licensed entities can compete on the basis of service quality, pricing and diversity of product offerings. The Act allows for a structured mechanism for credit bureaus to offer value added services such as individual credit scoring and research & analytics on aggregated data.

Focusing Outward

Impact Investing is a rapidly growing industry on the global scale. Based on 81 repeat respondents' answers over the period 2013-2017, the GIIN Annual Impact Investor Survey 2018 reported a 13% CAGR for the AUMs of the industry. As shown below in Fig. 1, total AUMs increased from USD 46b to a high of USD 228.1b over the course of just four years – 2014 to 2018. The graph below also shows that the pace of growth in AUMs has accelerated considerably lately. In fact, Markets and Markets forecast the market to grow from USD138b in 2015 to USD 307b by 2020 implying a CAGR of 17.3%.[1] Mckinsey also predicts the growth of impact investing industry to more than USD 300b by 2020.[2]

Fig. 1



n: 124 145 156 208 226

Other sectors include all those in Fig. 2, except Microfinance

GIIN Annual Impact Investors Surveys (2014 – 2018)

At the end of 2018, almost 9% of the AUMs were allocated to the Microfinance sector; the third highest allocation in terms of sectoral distribution (Fig. 3). However, as also seen in the graph above, impact investing assets allocated to the microfinance sector have not experienced growth commensurate with the increase in overall AUMs. Recent allocations as seen in Fig. 2 indicate a shift in the global impact investing landscape away from general microfinance towards targeted areas of interventions which can be mapped to various Sustainable Development Goals (SDGs). AUMs allocated to the Microfinance sector grew by only 8% over the period 2013-2017. On the other hand, there is an increasing interest in the Education sector (SDG 4) as it has witnessed the greatest pace of AUMs increase. Food & Agriculture (SDG 2 and 12), Energy (SDG 7), Healthcare (SDG 3) and Financial Services (SDG 8 and 10) are some of the other key sectors which have attracted significant funding from impact investors in recent years. While access to finance itself is perceived to facilitate the achievement of at least 8 of the 17 SDGs, recent trends in investment allocation indicate that if microfinance sector is to continue to attract funding from impact investors, sector players may have to re-align their product strategies with specific SDGs to build better cases for attracting funding.

Fig. 2
n: 81 repeat respondents

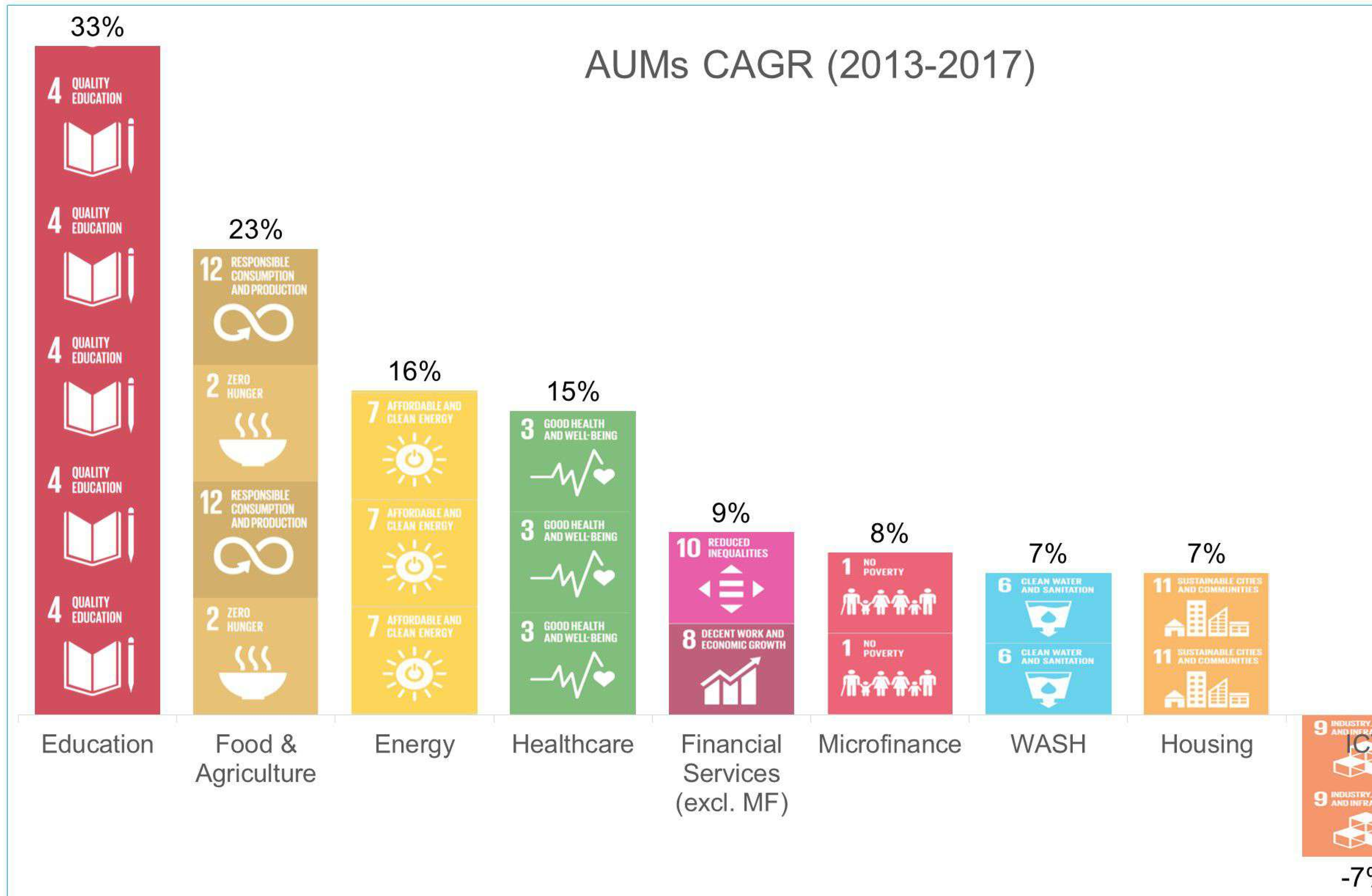
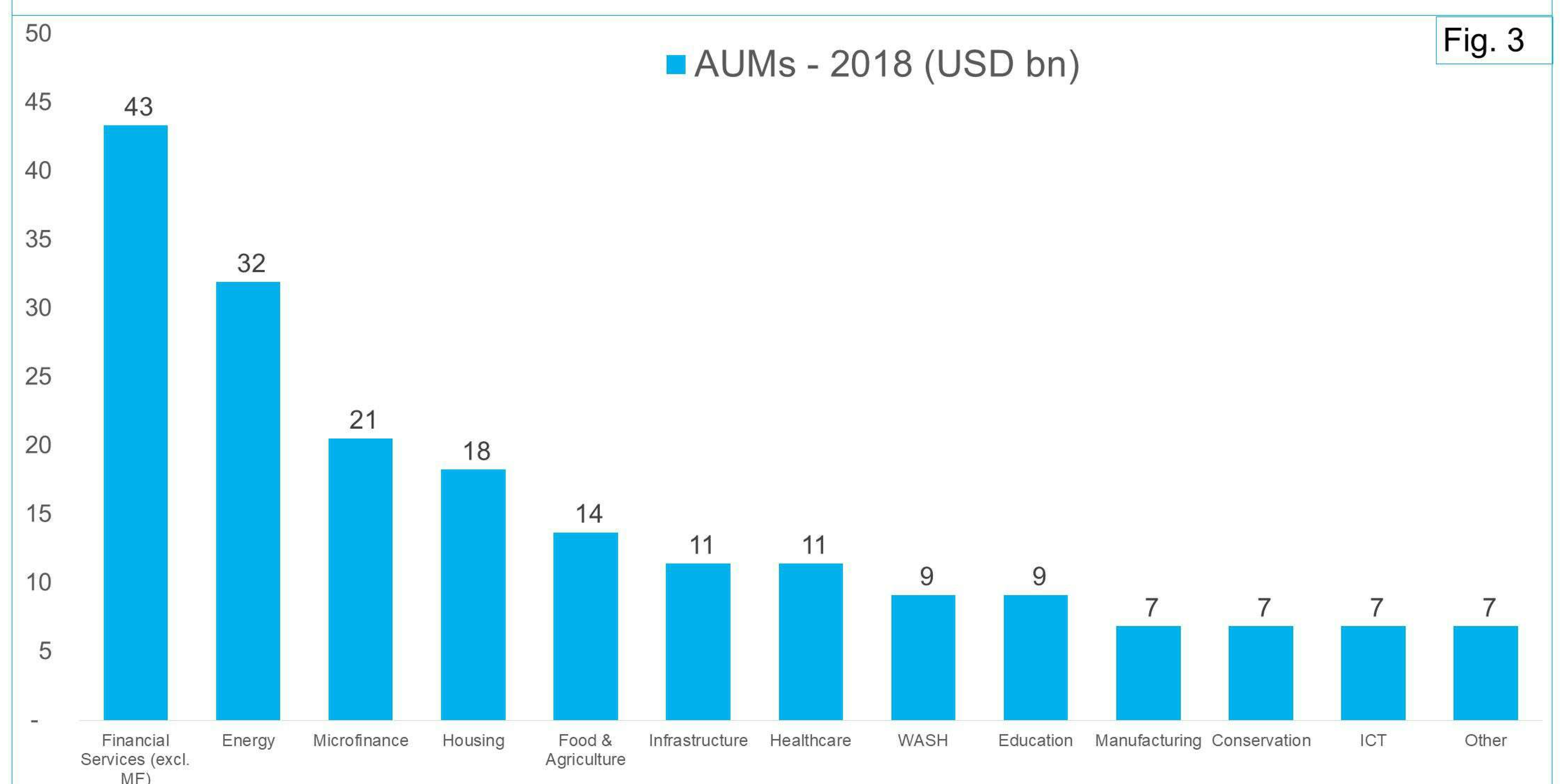


Fig. 3



Other sectors include SMEs, child welfare, commercial goods, transport, retail, tourism, forestry, and commercial real estate.

GIIN Annual Impact Investor Survey 2018

Note: The associations between sectors and SDGs, as depicted in Fig. 2 may not be endorsed by GIIN

[1] Sharma, Prashant, et al. Global Impact Investing: Market Size and Forecast – From 2015 till 2020. gsgii.org/reports/global-impact-investing-market-size-and-forecast-from-2015-till-2020/

[2] Pandit, Vivek, and Toshan Tamhane. "A Closer Look at Impact Investing." McKinsey & Company, www.mckinsey.com/industries/private-equity-and-principal-investors/our-insights/a-closer-look-at-impact-investing.

Acronyms

CAGR ------- Compound Annual Growth Rate
AUMs --------- Assets Under Management
WASH ------- Water, Sanitation & Hygiene

Learning Hub

Topic of the Quarter

Impact Investing

Definition

The Global Impact Investing Network (GIIN) defines impact investments as investments made with the intention to generate positive, measurable, social and environmental impact alongside a financial return.

Global Impact Investing Industry

Growth

- Global impact investing industry has shown stable and significant growth over the years; currently around 229 organizations are managing USD 228.1 billion in assets under management (AUMs) which have grown at 13% per annum.[1]

Geography

- Over 60% of AUMs were allocated to emerging markets in 2015.
- As per the GIIN Annual Impact Investor Survey, 35% of AUMs were allocated to Latin America, Sub-Saharan Africa and South Asia. South Asia however, accounted for only 7% of this allocation.

Sector

- The top three sectors in terms of invested AUMs are financial services (19%), energy (14%) and microfinance (9%).

Instruments

- The greatest share of capital invested is through private debt (41%) followed by private equity (18%) and public equities (14%).

Estimating E&S Returns[1]

Problem

There are no generally accepted analogues for the desired environmental and social returns in dollar terms.

Solution

The six-step methodology developed by The Rise Fund and the Bridgespan Group helps calculate the impact multiple of money invested – it expresses social value as a multiple of investment.

Step 1: Assess Relevance and Scale

Investors first ought to take into account the relevance and scale of a product, service or project for evaluation. The nature of the intervention should be aligned with an institution's social impact investment themes. Similarly, the number of people expected to be impacted – scale – is also to be estimated.

Step 2: Identify Target Social or Environmental Outcomes

Once relevance and scale have been established, identify the envisaged outcomes. Material published by MDRC, J-PAL and Mathematica Policy Research, for instance, can guide an investor in not only verifying if the desired outcomes are achievable and measurable but also estimating a company's impact potential.

Step 3: Estimate the Economic Value of Those Outcomes to Society

After identifying the target outcomes, social impact investors need to find and rely on an "anchor study" in order to robustly translate the target outcomes into economic terms. Such a study should be rigorous, relevant for context, recent, and frequently cited in research literature. Alternatively, guidance from a field expert may also be sought.

Step 4: Adjust for Risks

Values derived from Step 3 are then adjusted for the quality and relevance of the study. An Impact Realization Index is developed with values assigned to six risk categories: quality of study; its link to the intervention; correspondence of the study to the social environment of the project; country income group; and projected usage of the product or service. The calculated index (0% to 100%) is multiplied by the value derived in Step 3 for risk adjustment.

Step 5: Estimate Terminal Value

An estimate needs to be made of the value of impact in the final year of investment. Then, depending on the nature of the intervention, a time period may be assumed for which the output (people reached) and social value are expected to continue undiminished. Probabilities for the undiminished continuation of the two – output and value – are assessed. Final year impact values are then discounted by higher rates for low-probability projects and vice versa, to calculate the terminal value.

Step 6: Calculate Social Return on Every Dollar Spent

Finally, the estimated dollar value of a social/environmental benefit is divided by the total dollar investment. Conducting sensitivity analysis of the impact measurement multiple is also recommended.

Case Study

Acumen Fund – Managing Towards Impact 2018[2]

Impact Management & Measurement

Acumen's governing framework defined impact along three dimensions:

i. Poverty focus – the extent of service to those living at or below the international poverty line.
ii. Breadth – the number of people reached by the business.
iii. Depth – the extent of household or individual welfare.

IMM activities could be broken down into two components: **due diligence** i.e. determination of whether an investment aligns with Acumen's mission and sector priorities; and **managing and measurement** i.e. ascertaining the impact performance over time.

Challenges to IMM Activities

- **Impracticality of Randomized Control Trials (RCTs)**
  RCTs, despite being the "gold standard" of impact measurement involve high costs, time and a narrow focus; Acumen's portfolio enterprises had mostly limited time and resources to assume such measurement exercises.
- **Restricted Data Collection Practice**
  Acumen's practice of only collecting data that investees could readily produce meant that most of it focused on "breadth" of impact i.e. most information pertained to operating output indicators such as number of people served or products sold. This system was not contributing to an improved understanding of impact for Acumen itself.
- **Evolving Business Models of Investees**
  Most of the investees were social enterprise startups; their business models were evolving and it was often not feasible to spend significant amount of time and resources for evaluating inconsistent interventions – also of short spans of time.
- **Perceived Top-Down Imposition of Measurement Requirements**
  Historically, portfolio companies had found impact measurement requirements – including Acumen's – to be imposing and not necessarily designed to help them improve, evolve, and increase their impact.

Lean Data Approach – Strategies & Outcomes

- **Understanding Customers' Lives**
  Acumen's Lean Data approach prioritized downward accountability to understand the lives of customers of its portfolio enterprises and explore how they interacted with the products and services offered by the enterprise. Data emerging via this approach allowed the enterprises improve after-sales support and motivated them to enhance their own capacity to implement Lean Data-style surveys.
- **Simple, Easy and Short Survey Designs**
  Efforts were dedicated to design easy-to-understand and as-short-as-possible questionnaires to elicit responses from the end-clients in order to minimize time spend. For instance, Acumen's Energy Lean Data Baseline Survey – comprising 15 questions took just 16 minutes to complete over the phone. Thus, data were also more readily available to Acumen.
- **Tools of Data Collection**
  Various remote-data collection technologies – in addition to in-person surveys – were employed to conduct the studies such as SMS, Interactive Voice Response (IVR), phone calls, and sensors for tracking certain products' usage. These tools were significantly cost effective as for studies comprising 200-300 people, Acumen could deliver projects for around $20,000-$30,000 including staff time.

1. Addy, Chris, et al. "Calculating the Value of Impact Investing." Harvard Business Review.
2. Cole, Shawn, et al. "Acumen Fund - Managing Towards Impact 2018." Harvard Business Review.

SDG 5: Achieve gender equality and empower all women and girls

Sustainable Development Goal 5

Targets by 2030

- **5.1 –** End (all forms of) discrimination against women and girls.
- **5.2** – Eliminate all forms of violence against women and girls.
- **5.3** – Eliminate all harmful practices such as child, early and forced marriages, and genital mutilation.
- **5.4** – Recognize and value unpaid care and domestic work.
- **5.5** – Ensure women's full and effective participation and equal opportunities for leadership at all levels of decision-making.
- **5.6 –** Ensure universal access to sexual and reproductive health and reproductive rights.
- **5.A –** Undertake reforms to give women equal rights to economic resources, property ownership, financial services, inheritance & natural resources.
- **5.B** – Enhance the use of enabling technology to promote the empowerment of women.
- **5.C** – Adopt and strengthen sound policies and enforceable legislation for the promotion of gender equality.

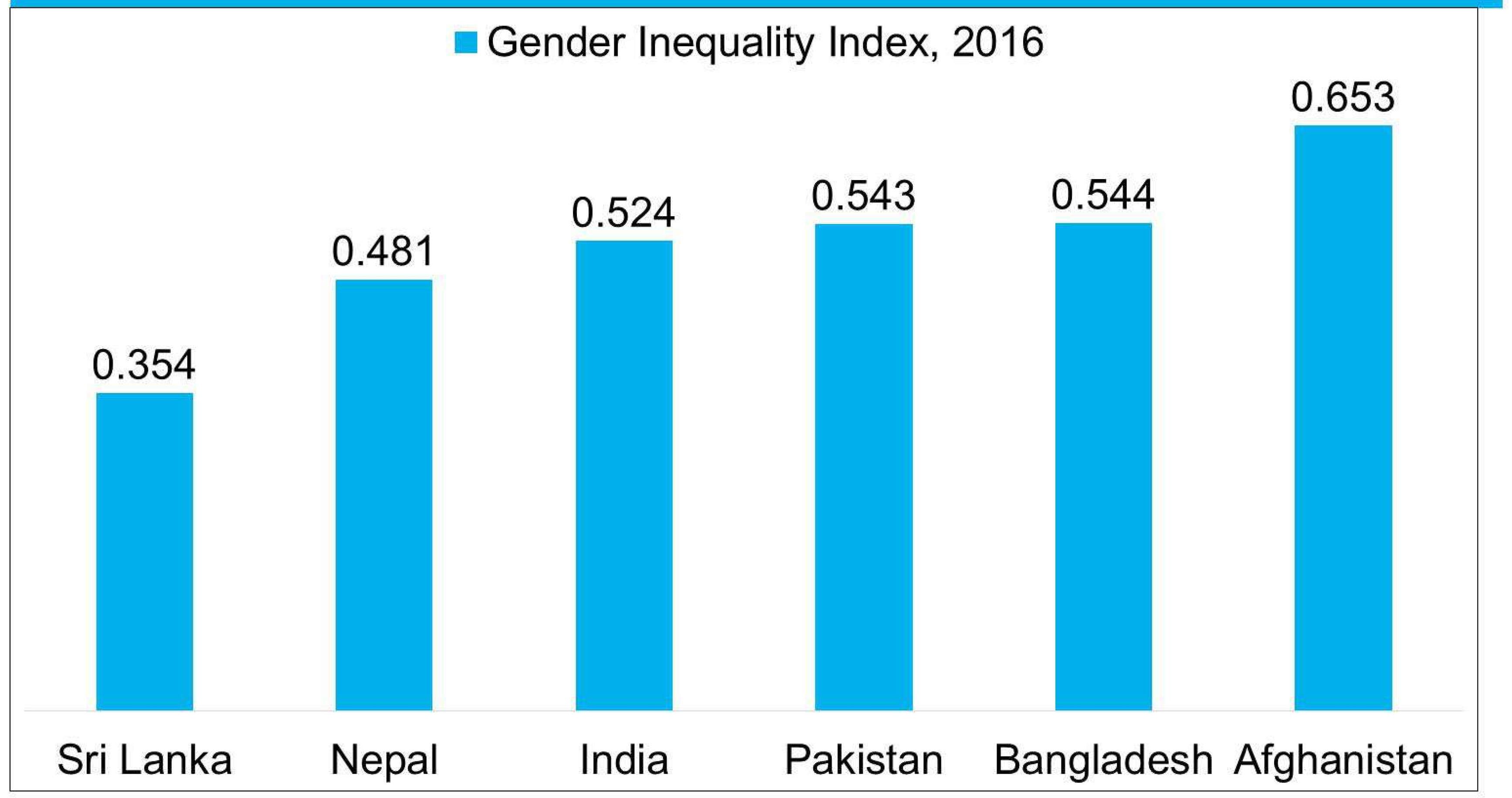
Global Progress – 2018

- Globally, the percentage of women in national parliaments has increased from 19% in 2010 to around 23% in 2018.
- In 2017, one in three girls aged 15 to 19 had been subjected to female genital mutilation in the 30 countries where the practice is concentrated, compared to nearly one in two in 2000.
- Data from 2000 to 2016 from about 90 countries indicate that women spend roughly three times as many hours in unpaid domestic and care work as men.

Pakistan's Status

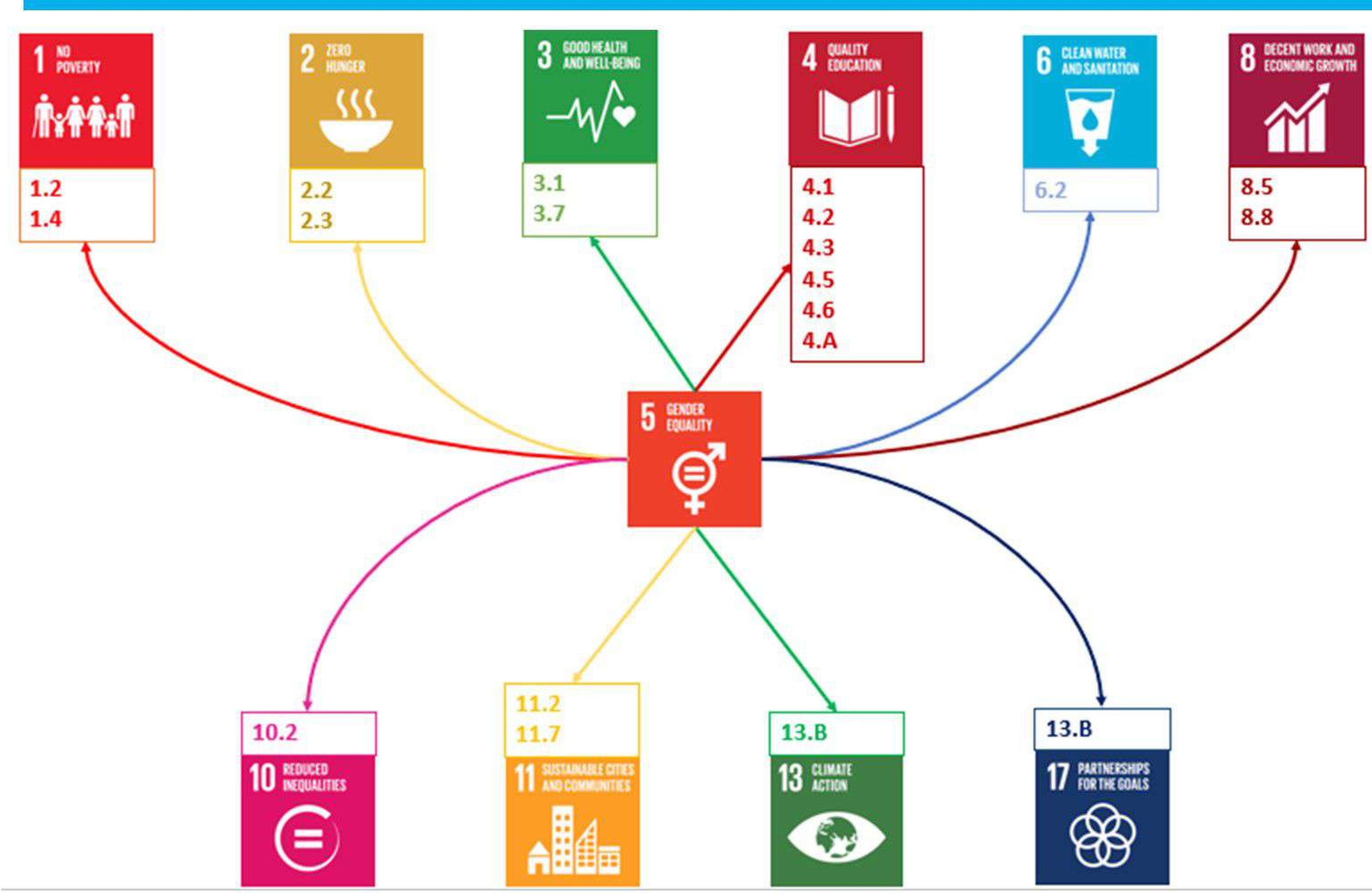
- Pakistan is one of 108 countries which have a non-discrimination clause in the constitution with gender mentioned in it.
- Proportion of seats held by women in national parliament was 20.6% in 2016.
- Literacy rate of adult female population (ages 15 and above) was 44.3% in 2014; the same for adult male population was 69.1%.
- Pakistan is among the six countries farthest from gender parity in work (in Asia Pacific) as per the Mckinsey Global Institute – 2018.*
- In 2013, only 6% of firms in the country had women as top managers.
- Female labor force participation rate was close to 25% in 2017.
- 46.6% of women aged 15 years or older experienced physical or sexual violence from an intimate partner in 2016.
- 2.8% of women aged 20-24 were married before the age of 15 in 2013; the share is 21% for those married before 18 years of age.
- The Gallup World Poll estimated 27% of women had a cellphone in 2016 against 86% of men.

Regional Comparison



GII measures gender inequalities in three aspects of human development—reproductive health, measured by maternal mortality ratio and adolescent birth rates; empowerment, measured by proportion of parliamentary seats occupied by females and proportion of adult females and males aged 25 years and older with at least some secondary education; and economic status, expressed as labor market participation and measured by labor force participation rates of female and male populations aged 15 years and more. Higher the score, greater the inequality; the scale is from zero to one.

Gender Equality – Achieving SDGs



The overarching approach of SDGs involves sustainable development for "all" i.e. irrespective of gender, ethnicity, disability and nationality, among others. However, some targets within each SDG have a gender-specific approach embedded in them which manifests itself in the language of these SDGs. Progress towards SDG 5 will facilitate the achievement of above shown targets in other SDGs and vice versa.

Pro-Women Legislation Landscape - Pakistan

Legislation	Year
The Dowry And Bridal Gifts (Restriction) Act	1976
The Women in Distress and Detention Fund Act	1996
Acid Control and Acid Crime Prevention Act	2010
The Protection Against Harassment of Women at the Workplace Act	2010
The Criminal Law (Amendment) Act	2010
The Prevention of Anti-Women Practices Act	2011
The Women in Distress and Detention Fund (Amendment) Act	2011
The Criminal Law (Amendment) Act (Prevention of Acid crimes incidents)	2011
The Domestic Violence Prevention and Protection Bill	2012
National Commission on Status of Women Act	2012
National Commission for Human Rights Act	2012

Pakistan acceded to the Convention on Elimination of all Forms of Discrimination Against Women in 1996. It is evident from the list that most of the pro-women laws have been enacted post-accession.

Microfinance and Women Empowerment

- Studies on the impact of microcredit in societies where women have traditionally been excluded from the cash economy have found that women's access to credit led to a number of positive changes in women's own perceptions of themselves, and their role in household decision making.[1]
- An increase in the proportion of women accessing microfinance services by only 15% could potentially lead to a reduction of gender inequality, as measured by GII, by half in the average developing nation.[2]
- Using data from 1990-2016, and employing panel spatial econometric models to analyze the changes in women's empowerment over the years, Cetin and Keser observe that the microfinance indicators are statistically and economically effective in promoting women empowerment in both MENA (Middle East & North Africa) and European regions.[3]

Works Cited

1. Kabeer, N. (2001) 'Conflicts over credit: reevaluating the empowerment potential of loans to women in rural Bangladesh', World Development 29(1): 63–84; Kabeer, N. (forthcoming) 'From social exclusion to citizenship: wider social impacts of microfinance', in J. Copestake, M. Greeley, N. Kabeer, S. Johnson, and A. Simanowitz (eds.) Money With A Mission. Microfinance and Poverty Reduction, Rugby: ITDG Publications
2. Quanda Zhang & Alberto Posso (2017) Microfinance and gender inequality: cross-country evidence, Applied Economics Letters, 24:20, 1494-1498, DOI: 10.1080/13504851.2017.1287851
3. Çetin, Işın, and Hilal Yıldırır Keser. "Women Entrepreneurship in MENA and Europe: Empowerment Through Microfinance." Microfinance and Its Impact on Entrepreneurial Development, Sustainability, and Inclusive Growth, by Ramesh Chandra Das, IGI Global, Business Science Reference (an Imprint of IGI Global), 2018.

* Mckinsey&Company also analyzed the financials of 89 European listed companies with the highest level of gender diversity. It was revealed that these companies on average, had outperformed their sector in terms of ROE (11.4% vs an average 10.3%), EBIT (11.1% vs 5.8%) and stock price growth (64% vs 47% over the period 2005-2007) – *Women Matter: Gender Diversity, a Corporate Performance Driver*

The Economics

The Economy

Two developments on the economic front that caught everyone's attention during CY18 were the sharp Rupee depreciation of almost 34% against the USD in addition to almost 425bps hike in the policy rate. In view of the macro-economic challenges confronted by the economy, the banking regulator and policymakers have adopted a tighter fiscal and monetary policy stance. This is expected to slow down the GDP growth in the on-going year; growth can pick up over the long term if the government is able to arrest the imbalances in the external account and shore up some foreign reserves.

As of January 18th, 2019, the SBP's reserves stood at USD 6.6b vis-à-vis USD 16.1b at the end of FY17. SBP's reserves are expected to boost with the help of inflows from Saudi Arabia and China. The Saudis will deposit USD 3b as "BOP Support" (USD 2b already received) and have also offered a 1 year deferred payment facility of up to USD 3b for oil. The federal government also plans to issue dollar-denominated scripless Pakistan Banao Certificate (PBC) for resident and non-resident Pakistanis to generate funds to build the depleting foreign exchange reserves and support the balance of payment.

With regards to the interest rates, uncertainty continues to persist as the market remains divided on the policy action expected in the upcoming monetary policy statement. Pakistan's external debt servicing for the next twelve months is above USD10b, which will exert significant negative pressure on the country's liquid forex reserves. In order to service future debt payments, the government would require more international inflows thereby resulting in a possibility of increasing the policy rate to attract foreign investors. With an increase in inflation, the real interest could come under pressure thereby becoming another factor for the SBP to raise the interest rate further.

Item	Amount
GDP (at current market prices) – Sept'18	$309.68b
July-Dec'18 Trade Balance	($15.55b)
Public External Debt % GDP – Sept'18	24.7%
Total Liquid FX Reserves – Jan 18, '19	$13.26b
CPI – Dec'18 (YoY)	6.2%
6-month KIBOR – Jan 28, '19	10.75%

Commercial Banking Sector

In CY2018, the advances to deposits ratio in the commercial banking sector increased from 53% to 59%, on the back of aggressive growth in advances while the pace of growth in deposits has successively declined in the last few years.

CY2018 also witnessed relatively aggressive expansion in private sector credit to Rs. 4.3tr from Rs. 3.7tr in the preceding year. A larger portion of credit growth in 2018 was witnessed in the first half while rising interest rates had a dampening effect on private sector credit expansion towards the latter half of the year. In view of the prevailing uncertainty in the market, banks adopted a more cautious approach towards lending. Moreover, credit spreads have also widened, reflecting the changes in risk appetite and decline in liquidity levels on the bank's balance sheet.

During previous periods of higher interest rates, banks have been able to enjoy healthy profits by simply placing excess liquidity in high yielding government paper. In the current high interest rate scenario, the benefit of higher interest rates may be muted to an extent as the ADR is relatively on the higher side, which means that a larger portion of assets are deployed in advances. Having said this, CAR is healthy while net infection is under 1%; both factors contribute positively to the soundness of the banking sector.

Item	Amount
Advances – Dec'18	Rs. 7.9tr
Deposits – Dec'18	Rs. 13.4tr
ADR – Dec'18	59%
Net Infection Ratio – Sept'18	0.8%
Risk Weighted CAR – Sept'18	15.9%
Credit to Private Sector % Total Scheduled Banks' Credit – Dec'18	66%
Credit to SMEs % Loans to Private Sector Business – Dec'18	9.0%
Agriculture Credit % Loans to Private Sector Business – Dec'18	6.0%

Microfinance Sector

With lending rates fixed and having room for increase, the sharp rise in interest rates is likely to place significant downward pressure on the spreads of microfinance players, both MFBs and NBMFIs.

In case of MFBs, an increase in deposit rates is already visible as they try to compete with the attractive rates on government saving schemes while commercial banks with much bigger franchises have also jacked up their deposit pricing. In case of NBMFIs, borrowing cost is mostly tied with market benchmark rates and has trended upwards in line with the movement in Kibor.

In either of these structures, the compression in spreads would mean reduced rate of internal capital generation and the need for external capital if these institutions are to continue with their growth momentum. Given the non-profit structures of almost all NBMFIs, external support can only be forthcoming in the form of tier-II capital as absent shareholders in the legal structure, there is no other mechanism for external support. On the other hand, MFBs may look towards their shareholders for equity support while also eyeing the capital markets for issuance of tier-II bonds.

The increasing cost of doing business and inflationary pressures in the economy may also exert negative effect on the repayment capacity of end-borrowers and such trends may need to be closely monitored for impact on portfolio quality.

	Q3-2018	2017	2016	2015	2014
Penetration Rate (%)	32.5	28.3	22.3	13.7	11.5
Active Borrowers (In m)	6.66	5.8	4.6	3.8	3.1
Gross Loan Portfolio (Rs. in b)	254.6	202.7	136.9	93.0	66.8
PAR-30 (%)	2.2%	0.1	1.4	1.4	1.1
Value of Savings (Rs. in b)	204.7	186.9	121.4	64.7	43.5
Number of Policy Holders (In m)	8.14	7.3	5.9	4.6	3.8