

Strategic Business Planning

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1. What This Module Covers

This module addresses the need for microfinance institutions to adopt comprehensive business strategies. It presents guidelines that microfinance organizations can follow to successfully create and implement a strategic business plan for their operations. One comprehensive way of thinking about strategy is to consider it as “the pattern or plan that integrates an organization’s major goals, policies, and action sequences into a cohesive whole.”¹ Preparing a strategic business plan forces an organization to think about the goals that they hope to accomplish. Such a plan also requires establishing a realistic timeframe for the completion of specific goals. In order for an institution to succeed, it must carefully lay the proper foundation on which it will grow.² The strategy that an organization follows is determined only after careful assessment of the institution and the environment in which it operates. After working through this module, your organization should have a better sense of this environment, and of the business strategies it will employ.

This module will look in-depth at several important aspects that a microfinance institution should be considering while preparing their business plan, including:

- How to clearly state an institution’s mission and goals
- Identifying the institution’s markets and clients
- Conducting an environmental analysis
- Performing an institutional assessment
- Choosing the appropriate strategy that focuses on maximizing outreach and profitability

¹ Ruocco, Paul and Tony Proctor. Strategic Planning in Practice: A Creative Approach. Marketing Intelligence & Planning. Vol 12 No. 9, 1994 pp 24-29.

² Shirley A. Lunde, Using Microfin 3. A Handbook for Operational Planning and Financial Modeling. http://www.cgap.org/html/p_techincial_guides02new.html

- Defining objectives and general activities

1.1 Strategic Planning – Working as a Team

Strategic planning is a team effort, one that draws on the particular skills and expertise of employees in the organization. Early on in the planning process, the organization should start identifying several key players who will help create the plan. These players should include professionals with experience in the field or region that the institution will find itself in, and who can speak to the particular needs of that area. Incorporating players from all levels of the organization helps determine if the program is appropriate to the social and economic context of the clients and the realities of the informal sector that the program will serve.³ Research has shown that individuals in an organization work harder at achieving a goal when they help in setting the goal.⁴

In other words, the process that a microfinance institution employs in the early planning stages determines the quality of the plan and its final outcome.

Considering the interests and visions of several key stakeholders in order to achieve the goals of the organization, outreach and profitability, is vital. These stakeholders include:

- The institution's board members
- Staff members
- Clients

“Involving those responsible for implementing the plan helps ensure broad endorsement, essential for successful implementation.”⁵ In fact, researchers have discovered several barriers to the effective implementation of strategic business plans. These barriers generally arise from conflicting priorities among managers and staff, but also from poor communication of program goals.⁶

³ United Nations Development Programme. MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme., Chapter 1

⁴ John A. Parnell, Shawn Carraher, and Kenneth Holt. Participative management's influence on effective strategic diffusion. Journal of Business Strategies; Huntsville, 2002

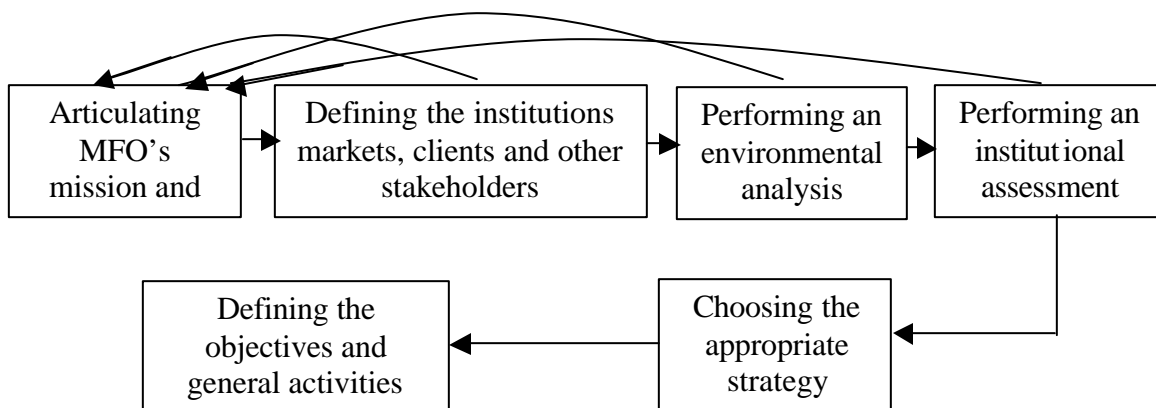
⁵ Shirley A. Lunde, Using Microfin 3. A Handbook for Operational Planning and Financial Modeling, http://www.cgap.org/html/p_technical_guides02new.html

⁶ Wessel, J.R. (1993). The strategic human resource management process in practice. Planning Review, 21, 5, 37-38

Strategic business planning is also helpful (especially in the early stages) in determining which factors are vital to the microfinance institution’s success. While the primary goal of a microfinance institution is to serve client needs, it is also necessary for managers in an organization to determine how to efficiently maximize the resources available to them.⁷ Financial projections can be a very useful operating tool for an institution’s managers. Comparing actual performance results with those projected, managers can determine if the institution is keeping the “right pace” towards the goal reflected in the business plan. Other issues such as the sustainability of the organization and its longevity can be revealed in examining the financial components of a business plan.⁸

1.2 An Ongoing Process

Finally, strategic planning must be viewed as an ongoing process, one that must be revisited periodically and revised as real-life experiences reveal areas of the plan that can be improved upon. When considered as a continuous procedure, an organization can regularly evaluate its stated goals and mission, adjust them as needed, and better respond to environmental and institutional changes.⁹ This idea of a cyclical planning process can be illustrated in the following diagram:



As the model illustrates, the steps taken in establishing a strategic business plan are not linear. As an organization performs the various steps in the planning process, it is important to determine if

⁷ CARE Savings and Credit Sourcebook Chapter 9

⁸ CARE Savings and Credit Sourcebook Chapter 9

the stated mission and goals are appropriate. Revising your strategy when needed is key to a strong business plan.

2. Articulating the Institution's Mission and Goals

Successful management of a microfinance institution requires many business skills. Yet, before these can be put into action, an organization must define its mission and goals. Defining a mission helps to lay the foundation of an organization, providing the basic direction that the institution will follow. In essence, creating a mission statement establishes why the organization exists and what it hopes to accomplish. The mission should succinctly state the target market, objectives, and guiding principles that will be used to reach the objective.¹⁰

The mission and goals should be the basis for all activities that the institution will be involved in. It should be viewed as a source of motivation for its board and staff members, bringing them together with a clear, unifying vision.

2.1 Developing the Mission Statement

In general, when developing a clear and complete mission statement, there are several things that a planning team must consider.

What is the problem that the organization wants to address?¹¹ There are several questions that you can ask that will help you to determine this, these include:

- Is it the lack of access to financial services among rural poor; or the alleviation of poverty?
- Not only does an organization need to determine the problem area, but it also needs to decide on what level they plan to address the issue.
- It is vital that the organization clearly understands the problem and how a microfinance project can help solve it.
- Who is the organization assisting?¹²

⁹ United Nations Development Programme. MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme. Chapter 1

¹⁰ United Nations Development Programme. MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme. Chapter 1

¹¹ McNamara, Carter: Basics of Developing Mission Vision, and Value Statements.
http://www.mapnp.org/library/plan_dec/str_plan/stmnts.htm#anchor519441

¹² CARE Savings and Credit Sourcebook, Chapter 1

- A clear idea of this group cannot be overlooked, as the characteristics of the target group will directly influence the design of the institution's services.
- An organization must have an understanding of the economic activities that the target group participates in, their demographic, and their cultural characteristics. These traits all influence the activities, and therefore the mission of the microfinance organization.
- How will you reach the client, and what services will your organization be providing?¹³
 - Given the particular characteristic of the target group, what outreach method is most likely to engender trust in your organization?
 - What microcredit model is most suitable for this particular group and its needs?
 - Is a solidarity group-lending model more appropriate than an individual lending program?
- What are the institution's ultimate goals?¹⁴
 - What would you like to achieve in five years?
 - How will your organization measure success?
 - Will it be through the number of clients served, repayment rates, or another measure of impact on the client's well being? This should be stated somewhere in your mission.
- Does your organization have a plan for sustainability and self-sufficiency?¹⁵
 - Have you considered ways to reduce your dependency on outside funding sources?
 - Do you have a plan in place that ensures the services you provide to your target group will be available to them for the long term?
 - Are you considering expansion plans to provide your services to a broader range of people?

2.1.1 Mission Statements Motivate and Clarify Purpose

¹³ CARE Savings and Credit Sourcebook, Chapter 1

¹⁴ United Nations Development Programme. MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme. Chapter 1

¹⁵ CARE Savings and Credit Sourcebook, Chapter 1

The importance of a clear, well thought out mission statement cannot be overemphasized. Not only does it force an organization to think critically about its objectives, but it also requires the organization to start thinking realistically about how the objectives will be met. A mission statement can serve as a motivating factor for workers, board members, and funders alike, especially if the goals are clear and attainable. Finally, by working through a series of detailed steps at the start of a program, an organization can begin focusing in on a particular area of work and design solutions that will effectively serve its target group.

2.1.2 Examples of Mission Statements

While the process of developing a mission statement requires that the organization undergo in-depth analysis of its operations, the final statement produced should be simple and to the point. Some examples of mission statements include:

- Rural Finance Facility of South Africa's mission is to
Facilitate investment in rural communities by the provision of professional financial services.
- The Microfinance Capacity Building Programme in Africa (AFCAP) also provides a good example of a succinct mission statement:
*To build a core group of internationally competitive African professional service providers from the private sector who in turn will deliver appropriate, high quality products and services to the microfinance industry.*¹⁶
- The mission of Friendship Bridge is
*To work with mutual understanding and respect to connect persons of the United States with those of Southeast Asia. We hope to promote sustainable healing of the injuries to the body and spirit that were caused by the ravages of poverty, disease, ignorance and war, so that we may all share in peace, joy and hope for our future in the global community.*¹⁷
- Another example of a mission statement is Opportunity International's statement, which is short and precise:
*Our mission is to provide opportunities for people in chronic poverty to transform their lives.*¹⁸

¹⁶ Microfinance Capacity Building Programme in Africa, <http://www.afcap.or.ke/>

¹⁷ The Friendship Bridge <http://www.friendshipbridge.org/mission.html>

¹⁸ Opportunity International <http://www.opportunity.org/international.html>

A microfinance institution's mission statement can be as short or as long as necessary, depending on the desire of the organization, and on the depth of its specialization and commitment. Yet, it should be clear to the reader of the statement, exactly what an organization is trying to accomplish. It should also “define the institutional culture of your organization”.¹⁹ Many missions are hard to accomplish, and the goals of an organization should be phrased in a way that illustrates how your organization plans to make the mission a reality. For example²⁰,

- “to provide access to microfinance services to over a certain number of households by the end of a certain year.
- “to reduce donor dependency of an organization by 50%”

2.1.3 Final Thoughts

Goals will differ depending on the stated timeline, and of course your organization. Through the course of developing a mission statement, the feasibility of meeting various goals may change. It is important to continually review and revise your mission and goals, as further research or experiences reveal that previously determined timelines are not attainable. Your organization may also decide, after spending some time in the field, that there are other areas or issues that it is better able to address. The organization is considered effective if it sets and reaches measurable and attainable goals, not if it adheres to its original mission without revision.

3. Defining the Institution's Markets and Clients

3.1 Understanding Your Clients

Microfinance institutions exist to serve clients, so it is vital that the organization has a clear understanding about the demographics and cultural characteristics of the group that is being served. In addition, recognizing the economic needs of the group, and how your organization can assist them in furthering their goals is an important part of understanding your clients. Once you have identified your target group, members of the group can provide valuable feedback on your products and services, as well as the design of future services. The previous section asked

¹⁹ United Nations Development Programme. MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme. Chapter 1

you to consider your organization's mission and goals; this section will go into further detail on how to identify the market that your organization will operate in, as well as the clients that you will serve within this segment.²¹

3.2 Identifying Your Market

When a microfinance institution decides to operate in a community, it is important to recognize that it is not possible to serve everyone in the community. Instead, an organization should identify a target market within which it will work, and begin focusing its resources there. In order to choose the proper market for the services provided, an organization should consider operating in communities that have the following:²²

- Good access to the services that you are providing
- A demonstrated interest in your assistance
- Committed and capable community leadership that will support your organization's efforts in the community
- An identifiable and real potential for the success of your organization in the community

3.2.1 Market Segments

Markets can be divided into market segments, which are usually classified by location (for example, a particular neighborhood, a semi-rural market town, or the area within a 15-mile radius of a branch office). These can be further segmented according to the economic activities located within them, such as market vendors, producers, or farmers. The potential clients within each segment generally have many common characteristics. As a result, when an organization chooses to operate within a specific market segment, the institution increases the likelihood of reaching its clients and providing its products and services to meet the needs of those particular clients.²³

3.2.2 Market Analysis

²⁰ Shirley A. Lunde, *Using Microfin 3. A Handbook for Operational Planning and Financial Modeling*, http://www.cgap.org/html/p_technical_guides02new.html

²¹ CARE Savings and Credit Sourcebook, Chapter 1

²² United Nations Development Programme. *MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme*. Chapter 1

²³ United Nations Development Programme. *MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme*. Chapter 1

Before an organization decides to enter a new market or expand further into its existing market, the market should be carefully analyzed, and the following factors need to be considered.²⁴

Considering the size of the market and the number of microentrepreneurs that operate in it. The size of the market is important to know in order to do things like forecasting, financial planning and budgeting, and calculating the risks and abilities of other potential MFOs entering this specific market or area.

What is the expected demand for financial services? This is the most important issue in market analysis, because it specifically demonstrates the market potential. Understanding the potential for your services is important for a microfinance institution in order to establish whether it is worth creating an MFO in the area. This information is also vital in determining the size of an organization, and the amount of resources needed in order to start an MFO, or to develop it further. A microfinance institution should track the expected demand in order to be ready to react to changes to it.

What market penetration can be reasonably achieved? In other words, what is the portion of all potential clients in the market that you estimate that your services can reach? This is related to the point above about expected demand. An organization should not expect that it will reach all potential customers, but having a realistic sense about whom you are likely to reach is valuable, especially when you are forecasting revenues and expenses in the budgeting process.

Consider the key market trends, such as the growth in market demand for the goods produced by the entrepreneurs. Tracking key market trends is important to predict the change in demand, economic activity, and economic situation. An organization can use this information in order to adjust its pricing policies, therefore better serving its customers.

How does an organization gather this type of information? There are generally two types of market analysis that can be performed: formal and informal.

- Informal analysis may include a casual discussion with potential or current clients

²⁴ CARE Savings and Credit Sourcebook, Chapter 2

- Formal analysis is usually a more structured process that might involve conducting a detailed market study.

For example, your organization may decide to conduct formal interviews with potential clients, asking them questions about the type of work that they do, to get a sense of the services that they may require. Based on the results of evaluation, the institution can decide whether the market has opportunities for expansion, or may require more in-depth research.²⁵

Where else can one find information about the market? The organization may use primary and secondary sources of information. The local bureaus of statistics, as well as other banks of information, are a valuable source. However, it is possible that this information might not be up to date, as may be the case now in Russia, where the external environment is changing very rapidly. Information that was relevant two years ago may no longer be useful in decision-making today.

3.3 Identifying Your Clients

If a market segment meets the initial selection criteria, the organization will want to conduct a more detailed analysis. This analysis can help the institution understand the economic, social, and personal characteristics of the entrepreneurs that operate within the segment, as well as the kinds of products and services that most appropriately satisfy their needs. The analysis consists of two parts – the analysis of the key economic indicators and of the personal traits of the customers. Economic traits primarily deal with inherent risks. This analysis addresses questions like: Will the customer be able to pay back her loan? How will he or she pay it back (from what sources) in case of an emergency? Does she have enough work experience to manage her business and take on the responsibility of paying off her debts?²⁶

3.3.1 Economic Indicators of Clientele

Key economic traits include:

The nature of the enterprises e.g., relative proportion of commerce, service, production and agriculture. Production and agriculture have historically been fields where microfinancing has

²⁵ UNDP. MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme. Chapter 1

²⁶ UNDP. MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme. Chapter 1

been most prevalent. It was the most popular way of self-improvement among the poorest people with very small businesses; while services were the prerogative of other, larger business units.

The demand for specific financial services, i.e. credit or savings, working capital or equipment loans. Identifying for what purpose clients wish to borrow money is important. Loans for working capital are different from equipment loans with respect to their liquidity and risk. Analyzing the intended use of the loans is suggested, in order to build appropriate loan policies and pricing strategies. This market information might vary greatly in different areas, and organizations would have to encompass different pricing strategies within one area for different client segments.

What are the income and assets of both businesses and households? Understanding the amount of clients' income and assets is important to secure the loans. How will the client be able to repay the loan if he fails in his business? This involves determining if the client will have the ability to pay back the loan.

The diversity of income sources is another economic trait to consider. This economic trait is related to the previous one and is primarily an issue related to risk. If a client's income is based on what she earns from selling handmade matryoshkas and a wage paid at a plant, and she loses her job, will she be able to pay back her loan? Diversity of income sources is one way to reduce risks to both sides – to an MFO and a client. Finally, it is good to consider the presence of other wage earners in the household, which can influence the rate of repayment.

Recognizing the work experience of your client. The more work experience the customer has within her business field the more likely the entrepreneur will be successful in his venture. An organization should analyze the chances that the borrower will be able to pay back his loan.

3.3.2 Demographic Characteristics of Clientele

In addition to the economic indicators, a microfinance institution must also note the demographic characteristics of the clients it will serve. These include:²⁷

²⁷ CARE Savings and Credit Sourcebook, Chapter 2

The gender of your client is an important economic indicator. When considering the design of a credit program, an institution must factor in the gender of the clients that it will serve, for example, women are more likely to use the services provided by a microfinance organization. Social and cultural conditions in many poor countries result in women being generally excluded from the formal and informal financial sectors. Careful program design will include strategies to extend services to women in ways that they will be effective for them, for example peer group lending methodologies.

The age of your client is also an important consideration. If a specific age group is being targeted as a client group, it is necessary to determine any existing barriers to extending loans to them. You will want to consider whether there are laws requiring a minimum age before a person can enter into a loan agreement? Similarly, assessing whether there are any risks involved with loaning money to elderly clients, i.e. a lower life expectancy in an area might lower the chances that your organization will receive repayment.

What is the main language of your client and her level of literacy? What is the literacy rate in the area that you are working? How does this influence how you will deliver your services? If a significant portion of your target group is illiterate, this will influence whether you require written loan agreements. Does the region that you are working in have laws that govern how to deal with legal agreements entered into by illiterate clients?

The citizenship of your clientele may also be a factor that you should be considering. Will your organization have requirements for citizenship or residency in order for a client to be eligible to receive your services? There are practical considerations when determining whether to establish these criteria. Chief among them is the idea that residency or citizenship represents a sense of stability and therefore the greater potential for the repayment of a loan. Your organization may also have determined in its mission statement that it will specifically serve the needs of residents or citizens of the country that you are operating in.

It is important to understand that the nationality of a potential borrower is not an obstacle in communicating with an MFO, but is an important issue that should be used to create special

product mixes for this specific client, to better serve his or her needs. Due to the fact that the Russian social environment is very diverse, an organization will succeed if it takes national and cultural differences into consideration. In other words, a seeming challenge can become an opportunity.

By understanding the economic and personal traits of your clients, you can develop the products and services to effectively meet their needs. However, an organization should not simply identify the key trends in clientele, but also be willing to orient its services toward the needs of the clientele.

4. Performing an Environmental Analysis

Environmental analysis means identifying and assessing the external challenges that an institution might face. All external factors that affect the organization are considered either opportunities or threats. Opportunities are the existence of some preferable situation, which an organization can use to gain an advantage, while a threat is an external challenge that an organization must work to overcome.

An environmental analysis looks at these four factors, which we will explore in more detail below:

- Competition
- Collaborations
- Regulatory policies
- Other external elements

4.1 Competition

Competition might be significant within the market in which the organization operates. While in Russia there is no intense competition yet, organizations should certainly anticipate that competition will become greater in the future. If, in your area, competition is already a significant factor, an organization might choose to carry out a careful review of its current and potential competitors, including:

- Other microfinance institutions
- Moneylenders
- Informal credit schemes
- Clients' suppliers
- Formal financial institutions

4.1.1 Evaluating Competition – Two Methods

An organization should view competition, not just as a threat, but as an opportunity for the organization to determine how it can learn from its competition to improve its own services. Organizations are often encouraged to routinely undergo an assessment of their **Strengths**, **Weaknesses**, **Opportunities** and **Threats** (referred to as a SWOT analysis), that will allow them to identify a strategic area that they might take advantage of. This includes a thorough analysis of the competition, as well as the organization's stated mission and goals.²⁸ Consider developing a matrix like the one below to help you organize your ideas as you brainstorm.²⁹

Factors	Internal	External
Positive	Strengths	Opportunities
Negative	Weaknesses	Threats

²⁸ Robbins, Stephen P. and Mary Coulter. *Management*. New Jersey: Prentice Hall, 1996

²⁹ Matrix format modeled after one found on National Network for Health website www.nnh.org

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An example of items that might arise during a SWOT analysis³⁰:

- Strengths:
 - International collaborative programs
 - Good relationship with local community
 - Responsive faculty and staff, even in times of budget restraint
- Weaknesses:
 - Lack of effective evaluative instruments
 - Reliance on government funding
 - Structure - too few resources; too many programs
- Opportunities:
 - Opportunity for growth
 - Opportunity to capitalize on niche programming
- Threats:
 - Lack of accountability
 - Competition moving in and serving the same demographic

Competition should be considered as a test of an organization's ability to survive, develop, and prosper. It is an opportunity to identify the weak points within the organization, by simply exploring where and why its competitors are successful. The next step is for an organization to try and improve its own services as a means of addressing a competitor's weakness. For example, informal creditors, who often operate where many potential borrowers are located, ask for extremely high interest rates (sometimes more than 50% annually), and require a very large deposit. The competitive advantage of a microfinance institution is that it provides loans at a lower rate, and the loan is made officially compared to communicating with informal creditors or moneylenders.³¹

³⁰ Ruocco, Paul and Tony Proctor. Strategic Planning in Practice: A Creative Approach. Marketing Intelligence & Planning. Vol 12 No. 9, 1994 pp 24-29.

³¹ UNDP. MicroStart. A Guide for Planning, Starting and Managing a Microfinance Programme. Chapter 1

For an organization to stay competitive, it is important to analyze the competition, identify its strengths and weaknesses and to take appropriate actions in order to stay afloat. The organization may use the following table as a tool for analysis:

Key Characteristics	Main Competitors		
	Competitor 1	Competitor 2	Competitor 3
Lending methodology			
Loan amounts			
Loan terms			
Interest rates			
Fees			
Payment frequency			
Guarantee requirements			

The main competitors should be listed across the top, while the first column lists the institution's key characteristics, including lending methodology, loan amounts, loan terms, interest rates, fees, payment frequency, and guarantee requirements. By analyzing this information, an organization can more easily identify its unique market niche.³²

³² Shirley A. Lunde, Using Microfin 3. A Handbook for Operational Planning and Financial Modeling, http://www.cgap.org/html/p_technical_guides02new.html

4.2 Collaboration

After an organization has identified and assessed its competition, it may discover that collaborating with another institution will allow it to reach a larger clientele. This is particularly true if your organization is new to an area where another locally established microfinance organization exists. However, there are several reasons why an organization might want to partner with an existing source of service.³³

The main reason to collaborate is ensuring that the services that an international agency is providing will continue on, even after that agency ends its operations in the country. Partnering with a local institution would allow for a sustainable delivery of service to the clients.

Sharing the development vision with local people who will benefit from the collaborative relationship. Providing opportunities for locals to participate in the process of your organization enables your organization to combine your resources with a local expertise about what services should be provided, and how best to do so. This collaboration can also establish a sense of accountability to more than just the clientele, but also to a local agency that relies on the cooperative effort.

Shared resources are another advantage of local partnership. In particular, local partners are often made up of members of the target group and are therefore able to provide an organization with information that they as 'outsiders' may not be able to collect. Likewise, your organization may have access to information that a local partner might not have, so that partners can complement each other and maximize each other's strengths.

Finally, a local collaboration can result in improved costs and benefits, something that is often sought after in institutions where resources are limited. Start-up costs and other infrastructure investments can be shared between the two organizations, which can free up more of a microfinance organization's money for investment in other program areas.

The type of collaboration an organization enters into depends on its needs. An international network with many helpful technical contacts will be an advantage if the organization seeks

broad-based institutional strengthening. On the other hand, the organization can collaborate with the local bank or another financial organization if legislation prevents the organization from offering certain services.

4.3 Regulatory Policies

As MFOs increase in size they begin attracting more attention and this results in greater attempts by government to regulate their activities. Regulatory policies established in the area where your organization operates can significantly affect the organizational environment. For example, “restrictive interest rate ceilings can impair its ability to charge an effective interest rate sufficient to cover its full costs. [...] The customer may also be affected by other policies, such as regulations on land ownership, registration requirements for microenterprises and price controls on agricultural products.”³⁴ This should also be taken into consideration by an MFO in order to formulate good pricing strategies. When establishing a program, it is essential that your organization determine that the policies in place are “sufficiently conducive both to the growth and stability of small economic activities and to the viability of a savings and credit program.”³⁵

4.3.1 Current State of Regulatory Policies in MFOs

There are many opinions regarding the role of regulation in microfinance organizations. It has been argued that for a microfinance organization to thrive, it should be allowed to operate with little restriction. For example, this “lack of regulation may help to explain why the microfinance sector has developed much further in Bangladesh than in other countries.”³⁶ However, when considering the long-term sustainability of an organization, some form of regulation may be necessary to guarantee that proper accounting and other banking related procedures are in place. The following figure might help you to understand some of the current thoughts on when and who should be regulated.³⁷

³³ CARE Savings and Credit Sourcebook, Chapter 4

³⁴ Shirley A. Lunde, Using Microfin 3. A Handbook for Operational Planning and Financial Modeling, http://www.cgap.org/html/p_technical_guides02new.html

³⁵ CARE Savings and Credit Sourcebook, Chapter 3

³⁶ Asian Development Bank. Role of Central Banks in Asia and the Pacific: Overview. 2000. Manila, Philippines

³⁷ Asian Development Bank. Role of Central Banks in Asia and the Pacific: Overview. 2000. Manila, Philippines

Prudential Regulation and Supervision of MFIs

The argument for regulating and supervising any financial institution rests on:

- the need to protect depositors from loss of their savings
- the need to maintain confidence in, and stability of, the financial system.

This suggests that:

- MFIs that do not collect deposits need not be regulated
- central banks need to decide whether and how nonbank MFIs should take deposits

From: Chapter 6 Regulation of Nonbank Microfinance Institutions

4.3.2 MFO Regulation in Russia

On October 17, 2002, World Bank Moscow, along with CGAP and several Russian (and other) microfinance organizations, hosted a videoconference. The goal of this conference was, among other things, to discuss the role of MFOs in Russia, and to examine the current trends in this growing sector. From this dialogue came several recommendations regarding regulation of microfinance activities in an organization. What follows are a few of these recommendations:³⁸

- Refrain from imposing regulation on ‘credit only’ MFOs
- Reconsider imposing regulation on MFO’s who accept cash collateral only, especially if the MFO will not lend this collateral out to other clients.

4.4 Other External Elements

Governmental influence and overall macroeconomic trends might significantly affect a microfinance institution and its clients. They should also be taken into consideration when building a solid business strategy. Obviously, such things as natural disasters, high rates of inflation, or economic underdevelopment are a threat for both microfinance institutions and

³⁸ Gidasov, Andrey. Current Trends in the Russian Microfinance Sector. December 18, 2002. From the Business Information Service for the Newly Independent States website: www.bisnis.doc.gov/bisnis/isa/021218RusMicroFin.htm

clients. On the contrary, a stable economic environment and political situation provides a positive environment for microfinance institution development.³⁹

5. Performing an Institutional Assessment

Institutional capacity is one of the most crucial factors that predetermine the organization's ability to achieve its goals. Consequently, each organization should pay attention to its internal system and be able not only to identify its strengths and weaknesses, but also to undertake certain steps to influence the situation if needed. Institutional assessment is usually best carried out after a market study and the environmental analysis, so that an organization can evaluate its strengths and weaknesses in light of its ability to meet client needs in the context in which it operates.⁴⁰

There are many ways to evaluate an institution's resources. A well-known and widely used method for organizational assessment is that the organization assesses its performance in key areas of operations through a series of questions, the answers to which indicate whether it is following the kinds of practices shown to be most effective for microfinance institutions.

The institutional assessment evaluates six areas of operations, which we will be discussed in more detail in the following sections⁴¹:

- Credit and savings program
- Board and management issues
- Human resource management
- Administration
- Financing
- Financial management

³⁹ Shirley A. Lunde, Using Microfin 3. A Handbook for Operational Planning and Financial Modeling, http://www.cgap.org/html/p_technical_guides02new.html

⁴⁰ Shirley A. Lunde, Using Microfin 3. A Handbook for Operational Planning and Financial Modeling, http://www.cgap.org/html/p_technical_guides02new.html

⁴¹ Shirley A. Lunde, Using Microfin 3. A Handbook for Operational Planning and Financial Modeling, http://www.cgap.org/html/p_technical_guides02new.html

Management is one of the most important areas. There are five areas of management in which the analysis of internal environment concentrates: human resources, general management, information systems, internal control and audit, planning and budgeting. Some would argue that human resources management is the most important of these. However, paying attention to each of these areas will result in a well-balanced assessment of your institution.

5.1 Credit and Savings Program

When considering your credit and savings program, there are a few questions that you should ask, to ensure that your program is designed to address the needs that you are setting out to address. Below is some discussion about the types of questions to ask.

Are your products appropriate for the market segments that the organization seeks to reach? For example, you should identify if there is a need for savings as well as credit services in the community that you are serving. Another thing to consider is the size of the loans offered, and if they are meeting the needs of your potential clients.

How good is the portfolio quality, as measured by the default rate and portfolio at risk? The financial management modules covered the hallmarks of a high-quality portfolio.

Is there a clear pattern of significant growth and increasing profitability? If not, examining your portfolio might reveal areas where improvements can be made to move your organization towards growth.

Is there a high rate of client retention? If not, understanding why clients are not turning into return clients can help reveal areas of your mission or objectives that might need to be revised.

Are clear and proper credit policies and procedures in place? These policies will make it clear to everyone in the organization what the protocol is for extending credits to clients. In addition, you want to ascertain whether or not your organization monitors the productivity of its loan officers (such as the number of active clients per loan officer)?

Does the credit staff maximize its time with clients relative to the time it spends on administrative work? Your organization should be striving for a proper mix of client time and administrative time.

5.2 Board and Management Issues

If your organization has a board of directors, you will likely rely on them for advice and guidance as you build your organization. They should be expert in the area of microfinance and possess the skills and strengths that your organization is looking to maximize. As you consider your board of directors, the following points may help you to select members who will complement your organization's talents.

The board should provide vision and policy leadership. For example, as you craft your mission and goals, and later revise them, your board members should help you to decide in what direction your organization should be moving. The board should also provide ongoing guidance and advice to the executive director. If at all possible, at least one board member should possess expertise in such key areas as banking, law and accounting. This experience will serve you well should conflicts or problems arise in these areas. Do the board members have the necessary skills and knowledge (such as a strategic perspective, management skills, knowledge of credit and finance, and fundraising ability)?

The roles and responsibilities of the board and management need to be clearly defined, so as to prevent inappropriate intrusion by the board into operational details. Clearly communicating the role of the board and other management early on in the process of planning will help avoid miscommunication of goals and objectives. In a crisis situation, or at other times when you need the input of the board and upper management, these defined roles will assist you in knowing who to approach with your problems. For example, do you want the board members participating in the setup of performance targets and monitoring progress toward them? If so, are you attracting board members who have the knowledge and skills to assist your organization in this capacity/

5.3 Human Resource Management

Aside from your clients, your staff is the most important asset of your organization. Treating employees well is necessary if you want them to continue to perform at their optimal level of performance. There are several issues related to human resource management that can help improve or maintain the smooth functioning of your organization.

Does your organization have an organizational chart and job descriptions for all positions? Clearly defined job descriptions demonstrate that the organization is thinking strategically about the various functions that employees will undertake.

Are you recruiting and training staff to ensure the appropriate skills? When filling positions for credit and finance manager, make sure that you are hiring staff that understands the local regulations and rules related to finance. Staffing these positions with trained staff will help ensure that regulations and other local rules are adhered to.

Is the level of administrative staffing sufficient but not financially burdensome? Adequate staffing allows for the greatest number of clients that can be served. In addition, low staff turnover helps save hiring and retraining costs.

*Are the organization's incentive systems designed to hold staff accountable and to reward them for good performance?*⁴² Incentives and rewards, when possible, encourage employee retention and empower staff to do good work. As greater operational scale is reached, is compensation becoming more competitive with market rates? There should be a clear pattern of promotion from within, if that is the system that you desire. Performance evaluations should be based on mutually developed and agreed upon objectives.

5.4 Administration

There are additional administrative duties performed in an organization that generally fall under the title of administration. A discussion of these duties follows below.

⁴² Robert Peck Christen, *Banking Services for the Poor: Managing for Financial Success* (Washington, D.C.: ACCION International, 1997, pp. 182–89) for a fuller discussion of staff incentive systems.

*The management information system should produce accurate, timely and comprehensive reports for accounting and loan-tracking*⁴³ Investing in MIS includes a large commitment of a MFOs capital. Ensuring that this investment pays off includes receiving useful reports that can improve the operation of your organization. Once these reports are produced, the appropriate reports should be provided to the different levels of users (board, management, staff) within the organization. In addition, be sure that the various users easily understand the reports.

The institution should regularly assess its management information system to ensure that it is sufficient for its needs today and over the medium term. Recall from our earlier discussions that it is a good idea to revisit your mission, to ensure that you are still meeting your goals. Consider revising your MIS plans just as you would your mission.

The chart of accounts must be appropriate to the institution's needs. For example, it should track income and expenses by branch, and separate grant income from earned income

5.5 Financing

When considering the financing of an organization, there are many points to keep in mind. A lot of issues specific to the financing of an organization, as well as financial management, have been covered in more detail in another module. The points listed below are

Is the organization able to mobilize the amount and types of funding it needs for current and planned operations? The mix of funding sources should be appropriate for the needs of the organization? There should be some priority placed by management on moving away from dependence on subsidized funding.

⁴³ CGAP, *Management Information Systems for Microfinance Institutions: A Handbook* (New York: PACT Publications, 1998).

5.6 Financial Management

Again, financial management has been covered in another module, but below are a list of questions that you should consider when thinking about financial management during your strategic planning process.

- Is reliable information available for assessing the organization's financial situation, including trends in performance indicators?
- Are budgets and cash flow projections prepared and reviewed regularly?
- Does the staff conduct periodic analysis comparing projected with actual performance (variance analysis)?
- Do financial statements present an accurate picture of the institution?
- Does key staff have good financial management skills?
- Does the organization have a well-thought-out investment management approach?
- Is the institution moving steadily toward full, subsidy-adjusted profitability?
- Does the organization periodically review its fixed asset base to ensure that it is not becoming obsolete?
- Is there a formal, comprehensive system of internal controls in place to prevent corruption and the misuse of funds?
- Does a reputable accounting firm perform a formal audit each fiscal year?

The main goal of the environmental analysis and institutional assessment is providing the organization a clear idea of “where it needs to focus its attention in order to meet its clients’ needs and enhance its profitability. By systematically assessing past trends and current performance, the analyses lay the groundwork for determining the kind of strategy that will enable your institution to achieve its goals.”⁴⁴

6. Choosing a Strategy

As already discussed, the strategic planning process involves developing and articulating a strategy. The strategy is the key reference point for operational planning, as a link between the

⁴⁴ Shirley A. Lunde, Using Microfin 3. A Handbook for Operational Planning and Financial Modeling, http://www.cgap.org/html/p_technical_guides02new.html

two parts of the business planning process. An organization should review all of its operational decisions in light of whether they reflect its strategy and move further toward its objectives.

The process of identifying a strategy has three parts:

- Choosing what products to offer in which markets;
- Deciding which areas of the institution need to be strengthened to ensure that it can provide the chosen products in the selected markets; and
- Determining clear objectives and activities for implementing the product, market and institutional development goals.

6.1 Product and Market Options

The organization can pursue expansion by offering existing or new products in current or new markets. The product-market mix provides the information for choosing the appropriate development strategy. This strategy must reflect the option that it will pursue first and the sequence according to when it might add others.

6.2 Market Penetration

If current products are commensurate with projected client needs and current markets offer the potential for significant expansion, the appropriate strategy would be to expand existing products in existing markets.

6.3 Product Development

If current markets offer the potential for significant expansion but existing products cannot meet projected client needs, the strategy should be to enhance current products or develop new products for expansion in existing markets.

6.4 Market Diversification

If existing products can meet projected client demand but current markets do not offer sufficient growth potential, the appropriate strategy would be to enter new markets with the current products.

6.5 Product Development and Market Diversification

If existing products are insufficient to meet projected client needs and current markets are insufficient to achieve sustained profitability, the organization must determine which of the first three options to pursue initially and in what order product and market expansion should be pursued.

Product-market mix:

		Market	
		Current	New
Product	Current	Market penetration	Market diversification
	New	Product development	Product development and market diversification

6.6 Institutional Development

To implement an expansion strategy, the organization will likely need to strengthen certain areas of its operations, as identified by the institutional assessment. In building on the strengths and addressing the areas needing improvement, it should focus on the factors that are essential to effective and profitable performance in the current and projected environment. It is also important to choose which areas to start with as developing in all directions is always a challenge. Thus a solid plan of development should be devised. Otherwise, too much talking and little action can prevent an organization from implementing any one of the desired improvements.

7. Example of Strategic Business Planning in a Microfinance Institution

We have talked a lot about what a strategic business plan should include, and when you should conduct one. But, how does this type of planning actually work in an MFO? Friends of Women's World Banking in India conducted a strategic business planning training program to help translate these ideas into actions. The objectives of the training program include:⁴⁵

- Assisting member organizations in developing and following effective business plans that will assist in sustaining their various credit programs.
- Increasing the supply of funds available, increasing clients deposits, and improving service delivery.
- Providing information on MFOs and the training program.
- Replicating the training on local and regional levels to encourage the widespread use of business planning in MFOs.

The results of this strategic training proved promising and include, among other things:

- Many participants had no experience with basic business planning. After the training sessions, 93% of attendees returned to their organization and drafted strategic business plans.
- These MFOs demonstrated enhanced business skills and decision-making abilities. One example from the group is that “after the training, many groups lowered their interest rates for lending to encourage member borrowing, and increased the interest rates for savings to increase deposits.”⁴⁶
- Membership and savings levels increased as these MFOs saw an increase of members as high as 40 to 90% after implementing their strategic plan.

After conducting this training, the general conclusion is that strategic business planning is a valuable tool to help participants learn about financial and other business skills important to a Microfinance organization.

⁴⁵ Training in Strategic Business Planning: A Program for Indian Microfinance Institutions: Friends of Women's World Banking, India. Promoting Women in Development Report-in-brief.

⁴⁶ Training in Strategic Business Planning: A Program for Indian Microfinance Institutions: Friends of Women's World Banking, India. Promoting Women in Development Report-in-brief.

8. Defining Objectives and General Activities

Once the strategy for expansion is selected and the areas that require strengthening are identified, it is often helpful to develop objectives and activities for implementing the strategy. These then become the basis for operational planning.

The objectives should address the major elements of the operational plan, as follows:

- Products and services
- Marketing channels
- Institutional resources and capacity
- Financing and financial management

For each objective, it is necessary to outline activities based on the findings from the strategic planning process. Consequently, these activities are a plan of what should be done in order to implement the strategic plan. The strategic planning process culminates in the task of developing and articulating the strategy. The strategy provides the key reference point for operational planning, serving as a link between the two parts of the business planning process. A microfinance institution should review its operational decisions in light of whether they reflect its strategy and move it further toward its objectives.

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