

December 10, 2010

## **Introduction and background to the Principles for Investors in Inclusive Finance**

A group of investors\* and Her Royal Highness Princess Máxima of the Netherlands, UN Secretary-General's Special Advocate for Inclusive Finance for Development initiated drafting Principles for Investors in Inclusive Finance early 2010. These investors believe that specific principles for investors in inclusive finance, of which microfinance is a part, would strengthen the movement towards responsible finance. The principles have been developed with a broad group of investors together with UNPRI and in consultation with CGAP and other industry players, keeping in mind the Client Protection Principles of the Smart Campaign, as well as other work on social performance and environmental, social and corporate governance (ESG) issues.

The Launch of the Principles will take place at a Responsible Finance Meeting in the Hague, the Netherlands on January 27<sup>th</sup> 2011. A core group of international investors will be the first signatories to these Principles and the event will mark the start of a campaign to increase the signatories to these Principles in the coming year.

On behalf of the working group,  
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\* The working group of investors consists of Goodwell, Oikocredit, PGGM, SNS Asset Management and Triodos Investment Management

## Principles for Investors in Inclusive Finance (December 2010)<sup>1</sup>

Inclusive finance, which includes but is not limited to microfinance, focuses on expanding access of poor and vulnerable populations, micro- and small-enterprises, and those otherwise excluded to affordable and responsible financial products and services. This encompasses a wide range of financial services including savings, credit, insurance, remittances, and payments. These services should be provided by a variety of sound and sustainable institutions. Inclusive finance carries with it the responsibility for all actors in the value chain - investors, retail financial service providers and other relevant stakeholders - to understand, acknowledge and act in accordance with the interests of the ultimate client. Clients are typically low-income and constrained by asymmetries in financial knowledge, power and influence. Access to finance must be provided in such a way that the interests of the clients are protected. The Principles for Investors in Inclusive Finance, aligned with the United Nations Principles for Responsible Investment (PRI<sup>2</sup>) which will pursue this as an active work stream, are signed by direct investors or fund managers and indirect investors investing via designated funds. By signing, direct investors or fund managers as well as indirect investors signal their intent to uphold the principles in their own investments, and to support the actions taken by other actors in the value chain to implement the principles, including retail financial service providers, rating and benchmarking agencies, donors, and government regulators and policymakers.

It is acknowledged though that while indirect investors operate at a distance, direct investors can more directly influence adherence to the Principles. The examples of possible actions under each Principle are therefore especially meant for direct investors or fund managers who, in the value chain of inclusive finance, have the relationship with the financial institutions providing finance to the ultimate clients.

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<sup>1</sup> *These Principles are the initiative of a core group of investors and Her Royal Highness Princess Máxima of the Netherlands, UN Secretary-General's Special Advocate for Inclusive Finance for Development. They developed the Principles with a broad group of investors together with UNPRI and in consultation with CGAP and other industry players.*

## ***Principles for Investors.***

As investors or fund managers investing in inclusive finance, we have a duty to act in the long-term interests of our clients - private and institutional investors. While upholding our fiduciary responsibility, we will commit to adhering to and promoting the following principles of inclusive finance.

**1. *Range of Services.* We will actively support retail providers to innovate and expand the range of financial services available to low income people in order to help them reduce their vulnerability, build assets, manage cash-flow, and increase incomes.**

Possible actions:

- Encourage development and extension of the range of financial services to include savings, loans, insurance, payment services, remittance facilities, pension plans, etc. to low income populations;
- Stimulate providers to develop innovative products tailored to the needs of low income clients;
- Encourage retail providers to expand their service offerings to more remote areas and more vulnerable populations;

**2. *Client Protection.* We believe that client protection in particular is crucial for low income clients. We will therefore integrate client protection in our investment policies and practices.**

Possible actions:

- Endorse the Client Protection Principles<sup>3</sup> publicly;
- Incorporate the Client Protection Principles into investment policies, due diligence processes and possibly financing or shareholder agreements;
- Invest in retail providers that have endorsed the Client Protection Principles;
- Engage with retail providers on an ongoing basis to encourage them to make the Client Protection Principles part of their operations;
- Monitor implementation of the Client Protection Principles through mandatory reporting and regular monitoring and evaluation;
- Report on progress on advancing the Client Protection Principles to investors and other stakeholders.

**3. *Fair treatment.* We will treat our investees fairly with appropriate financing that meets demand, clear and balanced contracts, and fair processes for resolving disputes.**

Possible actions:

- Provide financing in an appropriate currency;
- Provide financing with an adequate tenor;
- Negotiate terms and conditions that are transparent, fair and reasonable, including fair break-up clauses;
- Actively support the building of a diversified funding base;
- Pay special attention to the interests of the ultimate clients in dealing with defaults or forced exit or-restructuring situations.

4. **Responsible Investment. We will include environmental, social and corporate governance (ESG) issues in our investment policies and reporting.**

Possible actions:

- Sign the UN Principles for Responsible Investment (UNPRI)<sup>2</sup> and commit to adopt and implement them;
- Adhere to CGAP MIV Disclosure Guidelines and report annually;
- Use the standards and tools set forth by the Social Performance Task Force<sup>4</sup> for the purpose of measuring and reporting on social performance;
- Assist in developing appropriate references for environmental and corporate governance issues.
- Promote implementation of anti-corruption practices.

5. **Transparency. We will actively promote transparency in all aspects.**

Possible actions:

- Use our influence to ensure that the pricing, terms and conditions of financial products and services offered by providers are transparent and adequately disclosed in a form understandable to clients;
- Fully disclose our own policies, criteria and related conditions of our products and services to our investees and other relevant stakeholders;
- Be explicit about investment objectives, both financial and social, to our investors;
- Endorse MFTransparency<sup>5</sup> a global initiative for fair and transparent pricing in the microfinance industry

6. **Balanced Returns. We will strive for a balanced long-term social and financial risk-adjusted return that recognizes the interests of clients, retail providers, and our investors.**

Possible actions:

- Exercise voting rights when available;
- When investing in equity, develop an engagement capability with investees to achieve a reasonable and fair alignment between the social impact and the financial return requirements of shareholders; i.e focussing on the long-term rather than short-term returns.

7. **Standards. We will collaborate to set harmonised investor standards that support the further development of inclusive finance.**

Possible actions:

- Participate in networks to share tools, information, and resources;
- Develop and support appropriate collaborative initiatives;
- Contribute to advancing benchmarking to include standards and incentives for improvement;
- Contribute and encourage the use of the Impact Reporting and Investment Standards (IRIS) as the language for measuring and reporting social and environmental performance<sup>6</sup>;
- Collectively address relevant emerging issues, particularly on regulation and policy.

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<sup>2</sup> The United Nations Principles for Responsible Investment (<http://www.unpri.org>) read as follows:

### **The Principles for Responsible Investment**

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

#### **1 We will incorporate ESG issues into investment analysis and decision-making processes.**

Possible actions:

- Address ESG issues in investment policy statements
- Support development of ESG-related tools, metrics, and analyses
- Assess the capabilities of internal investment managers to incorporate ESG issues
- Assess the capabilities of external investment managers to incorporate ESG issues
- Ask investment service providers (such as financial analysts, consultants, brokers, research firms, or rating companies) to integrate ESG factors into evolving research and analysis
- Encourage academic and other research on this theme
- Advocate ESG training for investment professionals

#### **2 We will be active owners and incorporate ESG issues into our ownership policies and practices.**

Possible actions:

- Develop and disclose an active ownership policy consistent with the Principles
- Exercise voting rights or monitor compliance with voting policy (if outsourced)
- Develop an engagement capability (either directly or through outsourcing)
- Participate in the development of policy, regulation, and standard setting (such as promoting and protecting shareholder rights)
- File shareholder resolutions consistent with long-term ESG considerations
- Engage with companies on ESG issues
- Participate in collaborative engagement initiatives
- Ask investment managers to undertake and report on ESG-related engagement

#### **3 We will seek appropriate disclosure on ESG issues by the entities in which we invest.**

Possible actions:

- Ask for standardised reporting on ESG issues (using tools such as the Global Reporting Initiative)
- Ask for ESG issues to be integrated within annual financial reports
- Ask for information from companies regarding adoption of/adherence to relevant norms, standards, codes of conduct or international initiatives (such as the UN Global Compact)

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- Support shareholder initiatives and resolutions promoting ESG disclosure

#### **4 We will promote acceptance and implementation of the Principles within the investment industry.**

Possible actions:

- Include Principles-related requirements in requests for proposals (RFPs)
- Align investment mandates, monitoring procedures, performance indicators and incentive structures accordingly (for example, ensure investment management processes reflect long-term time horizons when appropriate)
- Communicate ESG expectations to investment service providers
- Revisit relationships with service providers that fail to meet ESG expectations
- Support the development of tools for benchmarking ESG integration
- Support regulatory or policy developments that enable implementation of the Principles

#### **5 We will work together to enhance our effectiveness in implementing the Principles.**

Possible actions:

- Support/participate in networks and information platforms to share tools, pool resources, and make use of investor reporting as a source of learning
- Collectively address relevant emerging issues
- Develop or support appropriate collaborative initiatives

#### **6 We will each report on our activities and progress towards implementing the Principles.**

Possible actions:

- Disclose how ESG issues are integrated within investment practices
- Disclose active ownership activities (voting, engagement, and/or policy dialogue)
- Disclose what is required from service providers in relation to the Principles
- Communicate with beneficiaries about ESG issues and the Principles
- Report on progress and/or achievements relating to the Principles using a 'Comply or Explain' approach
- Seek to determine the impact of the Principles
- Make use of reporting to raise awareness among a broader group of stakeholders

The Principles for Responsible Investment were developed by an international group of institutional investors reflecting the increasing relevance of environmental, social and corporate governance issues to investment practices. The process was convened by the United Nations Secretary-General.

In signing the Principles, we as investors publicly commit to adopt and implement them, where consistent with our fiduciary responsibilities. We also commit to evaluate the effectiveness and improve the content of the Principles over time. We believe this will improve our ability to meet commitments to beneficiaries as well as better align our investment activities with the broader interests of society.

**We encourage other investors to adopt the Principles.**

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<sup>3</sup> The Smart Campaign (<http://smartcampaign.org/>) is a global effort to unite microfinance leaders around a common goal: institute client protection in all that we do – to better serve clients and strengthen the microfinance industry. The Center for Financial Inclusion at ACCION International, CGAP, and many industry players recognize the need to protect microfinance clients, both for their benefit and the benefit of the industry as a whole. Over the last months, a consensus has emerged around six principles that would comprise the industry’s commitment to client protection:

### ***Client Protection Principles***

- ***Avoidance of Over-Indebtedness.*** Providers will take reasonable steps to ensure that credit will be extended only if borrowers have demonstrated an adequate ability to repay and loans will not put borrowers at significant risk of over-indebtedness. Similarly, providers will take adequate care that noncredit, financial products (such as insurance) extended to low-income clients are appropriate.
- ***Transparent and Responsible Pricing.*** The pricing, terms, and conditions of financial products (including interest charges, insurance premiums, all fees, etc.) will be transparent and will be adequately disclosed in a form understandable to clients. Responsible pricing means that pricing, terms and conditions are set in a way that is both affordable to clients and sustainable for financial institutions.
- ***Appropriate Collections Practices.*** Debt collection practices of providers will not be abusive or coercive.
- ***Ethical Staff Behavior.*** Staff of financial service providers will comply with high ethical standards in their interaction with microfinance clients and such providers will ensure that adequate safeguards are in place to detect and correct corruption or mistreatment of clients.
- ***Mechanisms for Redress of Grievances.*** Providers will have in place timely and responsive mechanisms for complaints and problem resolution for their clients.
- ***Privacy of Client Data.*** The privacy of individual client data will be respected, and such data cannot be used for other purposes without the express permission of the client (while recognizing that providers of financial services can play an important role in helping clients achieve the benefits of establishing credit histories).

<sup>4</sup> In March 2005, a Social Performance Task Force was created (see: <http://www.sptf.info/>). The Task Force is charged with clearly defining social performance and addressing questions about measuring and managing social performance. It consists of over 850 leaders from all over the world from every microfinance stakeholder group: practitioners, donors and investors (multilateral, bilateral, and private), national and regional networks, technical assistance providers, rating agencies, academics and researchers, and others. The participants unite around a common statement of principles in support of social performance.

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## Advancing Social Performance in Microfinance

### As organizations involved in the field of microfinance, members of the SPTF:

1. **Define** social performance as the effective translation of an institution's social goals into practice in line with accepted social values that relate to:
  - Serving increasing numbers of poor and excluded people sustainably (i.e. expanding and deepening outreach to poorer people)
  - Improving the quality and appropriateness of financial services available to target clients through systematic assessment of their specific needs
  - Creating benefits for clients of microfinance, their families, and communities relating to social capital and social links, assets, reduction in vulnerability, income, access to services, and fulfillment of basic needs
  - Improving the social responsibility of our own organizations and the partners we support. This includes consumer protection and gender equity, as well as responsibility to staff, environment and the community.
2. **Recognize** that financial performance alone is insufficient to achieve our goal of serving increasing numbers of poor and excluded people sustainably. Success in microfinance is driven by a double-bottom line: strong financial and social performance, and that these twin measures are mutually reinforcing in the long run.
3. **Further recognize** a growing interest from donors, networks, practitioners, rating agencies, funders, and other stakeholders in testing, applying, and improving new tools for social performance management, assessment, monitoring, and reporting.
4. **Commit** to improving the social performance of microfinance by:
  - Setting clear and specific social objectives for our own organizations and expectations for the organizations we support.
  - Designing, introducing and using systems to manage, assess, monitor, and report on social performance inside our own organizations and the organizations we support.
  - Using information on social performance to improve our own operations.
  - Verifying our social results with external assessments, audits and ratings where appropriate and available.

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- Being transparent about our social performance and promoting transparency of the partners we support through regular reporting to the MIX on its indicators of social performance standards (SPS).
  - Promoting and exchanging ideas, resources, good practices, and other information on social performance.
  - Endorsing the Social Performance Management Principles  
<http://www.spmresourcecentre.net/iprc/index.cfm/spm-principles/>

<sup>5</sup> [www.MFTransparency.org](http://www.MFTransparency.org)

<sup>6</sup> In 2008, the Impact Reporting and Investment Standards (“IRIS”) (see <http://iris.thegiin.org>) were developed to provide a single, consistent language for measuring and reporting the social and environmental performance of investments across a variety of geographies and sectors. The standards are overseen by an independent governance body that provides guidance toward the ongoing advancement of the framework and ensures its alignment with existing best practices. The IRIS standards are consistent and aligned with the standards produced by the Social Performance Task Force.