

Towards a Performance Measurement Framework for Community Development Finance Institutions in the UK

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Abstract

Community Development Finance Institutions (CDFIs) are publicly funded organisations that provide small loans to people in financially underserved areas of the UK. Policy makers have repeatedly sought to understand and measure the performance of CDFIs to ensure the efficient use of public funds, but have struggled to identify an appropriate way of doing so. In this article, we empirically derive a framework which measures the performance of CDFIs through an analysis of their stakeholder relationships. Based on qualitative data from 20 English CDFIs, we develop a typology of CDFIs according to three dimensions: organisational structure, type of lending, and type of market served. Following on from this, we derive several propositions that consider how these dimensions relate to the financial and social performance of CDFIs, and provide the basis for a performance measurement framework.

Towards a Performance Measurement Framework for Community Development Finance Institutions in the UK *

Christoph Kneiding¹ and Paul Tracey²

1. Introduction

Community Development Finance Institutions (CDFIs) are regarded as a key policy tool for community regeneration and development in the UK (Policy Action Team 3, 1999; Social Investment Task Force, 2000; Bank of England, 2000). By providing credit and related services to individuals and enterprises in deprived communities, they tap a market that has largely been ignored by mainstream financial institutions. CDFIs are often seen as the developed world counterparts of microfinance institutions (MFIs) that operate in developing countries, and a key point of discussion has been whether it is appropriate to use the same kinds of measures and techniques in both contexts. In addition to the fact that CDFIs' activities extend beyond microfinance, we believe that the differences between microfinance in developing and developed countries are very significant, and that there is a need for a performance measurement framework that is specific to developed economies. Our aim in this article is to examine the factors that underpin CDFI performance in the UK, taking into account both social *and* financial performance. For this purpose we use stakeholder theory, and link the question of performance measurement to the stakeholder environment of CDFIs.

To date, the CDFI movement has been considered as a rather homogeneous entity by UK policy makers. Beginning in 1997, significant funds were directed towards the sector to promote community development (e.g. via the so-called Phoenix Fund). This mirrored an earlier initiative in the US in 1994, when the Clinton administration established a well-endowed CDFI fund to promote the regeneration of communities with low levels of economic activity and high levels of unemployment (Benjamin et al., 2004). Since the late 1990s the CDFI sector has grown rapidly in the UK, with almost

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half of the 80 CDFIs currently operating established since 2004 (CDFA, 2006). Evaluations of their operations have generally painted a positive picture of the sector, but the validity and reliability of these studies have been questioned (NEF, 2001; NEF, 2006; CDFA, 2006). Insufficient data availability and varying data quality, which are partly a function of the relative newness of the sector, have posed particular problems. More fundamentally, two closely connected issues remain unsolved: (1) current ways of measuring CDFI performance are not guided by a coherent theoretical rationale; (2) public bodies therefore have no proper guidelines to direct further funds into the sector. Based on a qualitative research design, our paper uses a novel approach to address these issues.

We argue that there is no single set of performance measures which can be applied to the sector as a whole. Instead, we develop a performance measurement framework that can be used as a tool to monitor the individual stakeholder relationships of each CDFI. Based on their stakeholder environments, we identify different types of CDFIs according to three dimensions: organisational structure, type of lending (regarding loan size and target group served), and whether the CDFI's primary focus is the client or the funder market. We argue that it is essential to consider these dimensions and to qualitatively describe the nature of the relationships that CDFIs have with their stakeholders when establishing a performance measurement framework. In the discussion section, we derive several propositions to illustrate how these factors might affect the financial and social performance of CDFIs.

Thus, the aim of this paper is not to define a set of performance measures for the CDFI sector, but to lay the foundation for a new way of thinking about CDFI performance. Although the study only pertains to the UK, there are strong grounds for supposing that our framework may have relevance for community finance in other developed countries. First, the CDFI sector in the UK is quite mature compared to other industrialized countries. Second, the financial resources that have been channelled through the Phoenix Fund, and which are unparalleled in the European context, have forced CDFIs to consider carefully how they should account for their financial and social performance. Third, the CDFI sector in the UK is often regarded as a role model for other European countries and may therefore offer valuable insights that facilitate the development of community finance elsewhere.

The article is structured as follows. In the next section we relate stakeholder theory to performance measurement and outline a framework that conceptualizes this link. In the third section we detail our methods, and describe how the data were collected and analysed. Following an account of the results of our interviews in the fourth section, we develop a preliminary framework for the measurement of CDFI performance that incorporates both the social and financial aspects of performance. Finally, we consider the implications of our study for practitioners, policy makers and academics, and suggest directions for future research.

2. Stakeholder Theory and Performance Measurement in the Context of CDFIs

2.1. Main Theories

At the time when Eccles (1991) proclaimed a ‘performance measurement revolution’ and questioned the hegemony of financial data in corporate accounting systems, most firms remained firmly reliant upon a single set of financial measures to gauge their performance. The situation has changed substantially since then, with many firms and other organisations seeking to account for non-financial dimensions of performance in addition to financial ones (Neely, 1999). At the same time, a significant body of scholarship, much of it rooted in stakeholder theory (Freeman, 1984), has proposed ways of including non-financial measures into analyses of corporate performance. Most notably, Clarkson (1995) advocated that corporate social performance could be analysed and evaluated more effectively by using a framework based on the management of a corporation’s relationships with its stakeholders. This led him to define the corporation as a system comprising primary stakeholder groups, these being defined as ‘persons or groups that have, or claim, ownerships, rights, or interests in a corporation and its activities, past, present, or future’ (Clarkson, 1995: 106). Donaldson and Preston (1995) helped to structure the early discussions about the nature of stakeholder relationships by introducing a taxonomy of normative, instrumental, and descriptive stakeholder types.

Building on this work, Atkinson and Waterhouse (1997) extended the performance measurement discussion from a managerial point of view, noting that the systems used by most firms to measure non-financial performance are essentially extensions of their financial reporting systems. While this may or may not be appropriate for corporations, for other organisational forms, most notably non-profit organisations that are

characterised by their double (financial and social) or even triple (financial, social and environmental) bottom lines, this approach to performance measurement is generally deemed insufficient (Pearce, 2003). In order to capture the multidimensional nature of performance, Atkinson and Waterhouse (1997) focus their definition of performance on ‘one output of strategic planning: senior management’s choice of the nature and scope of the contracts that it negotiates, both explicitly and implicitly, with its stakeholders’ (1997: 26). The performance measurement system, in turn, is the tool the organisation uses to monitor these contractual relationships. Within their study, the authors only consider for-profit organisations, but they point out that this does not limit the applicability of their work to organisations with multiple objectives. They distinguish between environmental stakeholders that define the critical elements of a company’s competitive strategy, and process stakeholders that work within the environment defined by the external stakeholders.

When applying this system of performance measurement, one needs to understand the importance that is attributed to the individual stakeholders by a given management team, and to ‘get inside the heads’ of managers (Jones et al., 2007). With respect to this question of ‘who or what really counts’ to organisations, Mitchell et al. (1997) provided much needed clarity through their theory of stakeholder identification and salience. In this typology the three principal determinants of salience – power (the ability of the stakeholder group to bring about outcomes that it desires, despite resistance), legitimacy (the extent to which the stakeholder group’s relationship with the organisation is socially accepted and expected), and urgency (the degree to which the stakeholder group’s claim is time sensitive and of critical importance to the organisation) – combine linearly to produce seven different types of stakeholder groups, each with a predicted level of salience for managers of the organisation in question. In the paper we combine Mitchell et al.’s (1997) typology with insights from Atkinson and Waterhouse (1997) in order to develop a performance measurement framework designed to examine these stakeholder relationships in the context of CDFIs.

2.2. Community Development Finance in the UK

In the UK, CDFIs have emerged in the past ten years to address financial exclusion and problems with access to finance for enterprises (NEF, 2006). During this time policy support for the sector resulted in significant public funding to enterprise-lending CDFIs

through (a) the Phoenix Fund, a development fund to promote innovative ways of supporting enterprise in deprived areas; (b) the establishment of the Community Development Finance Association (CDFA), the trade association of CDFIs; and (c) the Community Investment Tax Relief (CITR), a scheme that encourages investment in disadvantaged communities by giving tax relief to investors who back businesses and other enterprises in less advantaged areas by investing in accredited CDFIs. According to the CDFA, by 2005, CDFIs had financed over 18,000 businesses and people; they claim to have created 11,000 jobs and sustained another 88,000, while the finance provided has helped to lever £285 million of funds from other sources (CDFA, 2005).

The structure of CDFIs in developed countries is far from homogenous. For example, in the US, in contrast to the UK, CDFIs have been able to attract large funds from religious institutions and private individuals (Pinsky, 2001). There is also disagreement within and between countries about their role and effectiveness in facilitating community development (Affleck and Mellor, 2006). However, there is general agreement that CDFIs are independent financial institutions that provide capital and support to enable individuals or organisations to develop and create wealth in disadvantaged communities and/or under-served markets (Derban et al., 2005). The financial products and services that CDFIs provide are not usually available from mainstream lenders and financiers. Many CDFIs augment their loans with a range of counselling and educational services that increase their borrowers' economic capacities and potential (Benjamin et al., 2004).

A key feature of CDFIs is the so-called double bottom line, i.e. their aim to achieve financial *and* social returns on investment (Derban et al., 2005). However, this concept is not unproblematic. Two issues have been particularly contested. First, with respect to financial returns, should performance measurement focus on the extent to which a given CDFI is financially sustainable (i.e., generates enough revenue from interest payments to cover its operating costs and grow its loan programme), or should performance be measured by the extent to which it is successful in attracting external funding from government, foundations, and other sources? Second, with respect to social returns, what is social performance (Clarkson, 1995), and how can social returns be measured in a valid and reliable way (Sinha, 2006; Tulchin, 2003)? The issue of social performance is particularly complex because (1) some kinds of social outcome, e.g., improvements to

an individual's quality of life or a community's standard of living, are not easily amenable to quantification, and (2) CDFIs operate in a diverse range of communities, and the kinds of social issues that they seek to address therefore often differ substantially (Woller, 2006).

More generally, little is known about the interaction between the factors that underpin financial and social measures of performance.³ In order to establish a performance measurement framework for CDFIs it is necessary to describe these interactions. Only then, we suggest, will it be possible to determine if the performance of all CDFIs should be measured according to the same criteria, or if the measures used should be contingent upon the nature of a given CDFI and the market in which it operates. In line with the arguments of Atkinson and Waterhouse (1997), in this article we identify the criteria for measuring performance by analysing the ways in which CDFIs interact with their stakeholders. Subsequently, we establish propositions that seek to explain how these interactions affect the financial and social dimensions of CDFI performance. This is especially important because, as with non-profit organisations more broadly, there is little scholarship that considers how performance measurement might be theorized. This article therefore has the following research objectives:

- (1) To develop a typology for classifying different types of CDFIs;*
- (2) to develop a preliminary framework for gauging CDFI performance that incorporates both social and financial measures and that is able to account for the diversity within the CDFI movement.*

3. Methods

3.1. Data Collection

Data on 20 English CDFIs were collected in spring 2007 via semi-structured interviews (see Table 1 in the Appendix). Credit unions and bigger national organisations such as Charity Bank or Triodos Bank were not included in the sample, as the legal structure of a banking institution, staff size, as well as their turnover volume does not allow for a meaningful comparison against the majority of CDFIs that adopt the legal structures of

³ The only empirical approach towards measuring the performance of CDFIs in the UK focussed on their loan repayment rates, implicitly assuming this to be a 'good' performance measure (Derban et al., 2005). While we appreciate the importance of this measure, we do think it might yield a slanted view of factors influencing performance and accordingly distort the empirical results towards a purely financial interpretation of performance.

Industrial and Provident Societies (IPS), Charities or Limited Companies, and that are staffed with a very small team of employees.

Interviews were conducted with the loan fund manager of each CDFI, who in some cases was also the CEO of the institution. The average interview lasted slightly more than one hour and consisted of two parts. Initially, a topic guide was used to acquire information about the history of the institution as well as its stakeholders. Prepared index cards were shown to the interviewee to represent the CDFI's stakeholders; where necessary these were adjusted to the specific context of the institution during the course of the interview. At the end of the first part of the interview, these records were presented to the respondent to verify the set of stakeholders for the institution.

The second part of the interview aimed to identify the underlying constructs used by the interviewee in order to ascribe meaning to each stakeholder. This was done by utilizing the repertory grid technique, which is based on George Kelly's personal constructs theory (Kelly, 1955). The technique has its origin in clinical cognitive psychology, but has also been applied by a number of economists (e.g., Reger and Palmer, 1996; Hisrich and Jankowicz, 1990). The interviewee is asked to compare three elements (in our case three of the institution's stakeholders), and specify how any two of these stakeholders are alike and thereby different from the third.⁴ In this way, bipolar dimensions used by the respondent to differentiate among the particular stakeholders were elicited. Thus, researcher-imposed structure on subject-cognition was minimized. This procedure continued until it became obvious that no other constructs could be elicited from the interviewee. Finally, three constructs were supplied by the interviewer, which were based on the salience dimensions defined by Mitchell et al. (1997):

- The stakeholder's claims are powerful vs. the stakeholder's claims are not powerful (dimension of power)
- The stakeholder's claims are legitimate vs. the stakeholder's claims are illegitimate (dimension of legitimacy)
- The stakeholder's claims are urgent vs. the stakeholder's claims are not urgent (dimension of urgency)

⁴ This is referred to the "minimum context form" of construct elicitation as opposed to the "full context form" in which the interviewee is asked to select similar pairs out of the whole set of elements (Fransella and Bannister, 1977, p. 14-15).

Informants were then asked to rate all stakeholders on a five-point-scale based on the dimensions they named, with the extreme of the scales being represented by the opposite constructs. For example, ‘1’ indicated best match for the emergent pole, and ‘5’ for the opposite pole. If none of the construct’s poles are predominant, ‘3’ is used (see Figure 1 in the Appendix for an example of a completed grid). In two cases where a loan fund had ceased to operate, we stopped at the second step of the analysis, focused on the reasons for the closure and how they were connected to the stakeholder environment of the institution.

3.2. Data Analysis

The interviews were tape-recorded, and a detailed transcription was compiled for each participating institution. The average length of the typescript was 20 pages. Digital recordings of the interviews were retained for consultation as required. Additionally, the repertory grids that were defined during the course of the interviews were compiled by the interviewer on the basis of the tape recordings and then reverted to the interviewee for completion. The interviewees were sent the repertory grid within two working days so that the discussion was fresh in his/her mind. Eighteen completed repertory grids were received in total (as detailed in Section 3.1., two repertory grids were not compiled as in these cases the loan funds had ceased to operate).

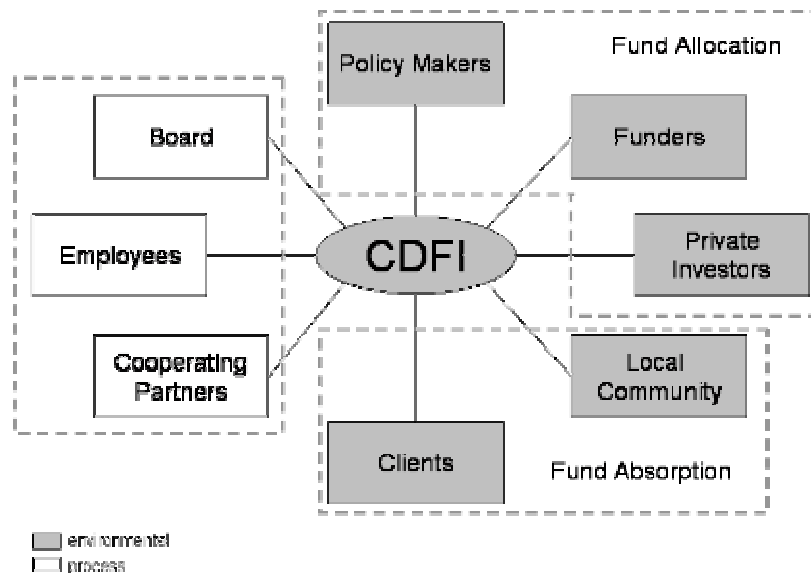


Figure 2: Fully Specified CDFI Stakeholder Map.

For the purpose of our analysis, we adopted Atkinson and Waterhouse’s (1997) definition of performance measurement as a tool to monitor stakeholder relationships.

Based on a review of existing typologies of organisational stakeholders (cf. Sirgy, 2002) we identified in a *first step* a total of eight distinct stakeholders (see Figure 2). According to the typology of Atkinson and Waterhouse (1997), stakeholders can be broken down into process stakeholders (employees, board, and cooperating partners), and environmental stakeholders (policy makers, clients, local community, funders, and private investors). There is a clear separation between the source of funds (policy makers, funders, and private investors), and the use of funds (clients, and local community) for environmental stakeholders. In the following part of this section, we briefly describe each stakeholder:

- *Employees* of a CDFI include the CEO of the organisation, the loan fund manager, loan officers and back office support. In smaller organisations of 2 or 3 employees, this separation is obviously diluted, as the CEO may also act as a loan officer, while back office duties are allocated equally to the remaining employees.
- Although the *Board* typically does not appear in existing stakeholder typologies, it was distinguished by many respondents. Similar to most non-profit organisations, the board comprises unpaid volunteers that generally show a strong attachment to the organisation's mission and feel committed to 'do good' in their local community.
- CDFIs often work closely with *Cooperating Partners* like business support agencies, business advisers, or commercial banks that refer clients to them. In that sense they occupy a supplier role for the CDFI, as they provide them with potential borrowers.
- *Policy Makers* set the policy framework for the operations of CDFIs, either through the control of critical resources (Pfeffer and Salancik, 1978), or through powers attributed by law. Examples of the former group are the Regional Development Agencies that since 2006 control the funds flowing into the sector, private investors like Charitable Foundations and banks that support certain institutions financially. The latter group can be exemplified by the Financial Services Authority (FSA), which regulates all providers of financial services in the UK. As most interviewees considered policy making to go hand in hand with funding, we included this stakeholder to represent fund allocation.
- The *Funders* comprise public sector organisations that act as a source of capital for the CDFI.

- Unlike Funders, *Private Investors* have a private sector background. They invest in the CDFI either by loans on preferential rates (in the case of banks) or by donations (mostly as part of their CSR activity). Sporadically, individual members of the local community may also act as private investors.
- *Clients* of the CDFI include individuals as well as micro, small and/or medium enterprises that are normally located in the geographic area which is served by the institution.⁵ In the case of business lending, most CDFIs require supporting evidence from clients to show their inability to obtain a regular bank loan (e.g., a written rejection of a loan application by a bank).
- CDFIs differ from mainstream financial institutions, as they cultivate specialized knowledge about the *local communities* in which they do business. Local communities are included as stakeholders because they serve as drivers for the creation of the CDFI, which justifies the assumption of an implicit contract relationship between CDFI and community (for a critical view on the role of ‘communities’ in the stakeholder framework cf. Donaldson and Preston, 1995).

There are overlaps and inter-relations between different stakeholders. For instance, it may be hard to separate the policy makers from the funders, as funding by a governmental organisation like a Regional Development Agency is regularly accompanied by regulations and reporting requirements that affect the internal processes of the CDFI. Equally, clients are usually part of the local community and therefore represent a sub-group of this stakeholder. As such, stakeholders should be viewed from a functional perspective; individuals or organisations can occupy more than one stakeholder role. Interestingly, only one of the institutions included in the study had developed a stakeholder map similar to the one detailed above, or had made a systematic attempt to determine the importance of its stakeholders. Nevertheless, all interviewees were open to this approach and were willing to apply the stakeholder framework to their institutional environment.

In a *second step* we conducted a content analysis (Holsti, 1969) to identify the main themes that dominated the relationships within different groups of stakeholders. Three distinct topics emerged, each related to one or more of the stakeholder groups that were identified earlier:

⁵ This does not have to be the case. There are some CDFIs that cover their market by target group, e.g. by focussing on social enterprises or women.

- The organisational structure of the CDFI
- The type of lending (i.e. loan size and target group of lending)
- The orientation of the CDFI towards the “client market” or the “funder market”

In the *third step*, we used Multidimensional Scaling (MDS) for analysing the repertory grids that were established (Bell, 1997). This is a widely applied technique for this kind of data and is included in most statistical packages (in our case we used the SPSS ALSCAL module). MDS enables the mapping of construct variables with the element variables and represents these mappings in spatial terms. The distance between the stakeholders (elements) and their attributes (constructs) show how closely they are related to one another. Therefore, the attributes closest to the stakeholders are those that have the most relevance from the point of view of the respondent.

Fransella and Bannister (1977) note that the use of MDS in conjunction with the repertory grid approach is relatively uncommon. This may be related to difficulties in interpretation. In assessing the extent to which elements and constructs are associated, the distance between co-ordinates is considered. A perfect association would result in an exact match of co-ordinate pairs. However, it is the researcher’s discretion how close data points have to be in order to be deemed associated. For this reason we decided to control our results through both correlation analysis (which allows us to explore relationships among the characteristics being studied) and cluster analysis (which enables the researcher to explore meaningful groupings that exist within a data set). This procedure was also proposed by Fransella and Bannister (1977) in order to reappraise one’s conclusions.

In the following section, the empirical findings are reported. Given the constraints of space and the complexities of individual cases, we have had to be selective when presenting the data. Nevertheless, we consider that the data presented support the arguments posited in a constructive manner. The results of the study are reported in two parts. In the first part, we use our stakeholder analysis to develop a way of classifying CDFIs along three key dimensions. In doing so we highlight that there is considerable variance within the CDFI sector. In the second part, we use this classification to develop a preliminary framework for measuring the performance of CDFIs which seeks to account for the social and financial aspects of performance.

4. A Stakeholder-based Classification of CDFIs

The content analysis generated three major dimensions which govern a CDFI's relationship with its respective stakeholders, and are therefore key when it comes to performance measurement. First, it is important to account for its organisational structure, i.e. if it is a pure CDFI or if the CDFI is embedded in an enterprise agency. Second, one has to distinguish between different types of CDFI lending, i.e. the loan sizes it extends and the target groups it serves. Third, CDFIs differ in their orientation towards the market they serve. While some are focused on the client market and see the funder market as a means to achieve their aims, others are focused on the funder market, and see the client market as a means to achieve their aims. In the following subsections, we discuss the three dimensions in detail and relate them to the corresponding group of stakeholders.

4.1. Process Stakeholders: Organisational Structure

The content analysis revealed a clear divide between CDFIs that are solely extending loans and CDFIs that are embedded in an enterprise agency. The latter institutions are full service agencies that act as one-stop-shops for business development services. Their activities comprise a wide array of non-financial services like training, consultancy and advisory services, marketing assistance, information, technology development and transfer, and business linkage promotion. A distinction is sometimes made between 'operational' and 'strategic' business development services. Operational services are needed for day-to-day operations, such as information and communications, management of accounts and tax records, and compliance with labour laws and other regulations. Strategic services, on the other hand, are used by the enterprise to address medium- and long-term issues in order to improve the performance of the enterprise, its access to markets, and its ability to compete (ILO, 2001). The enterprise agencies we interviewed had already been operating for several years or even decades and had incorporated loan finance as an additional product into their portfolio. Pure CDFIs, by contrast, do not provide any kind of business development services, but rather focus solely on extending loans to certain target groups.

GTR is an example of a CDFI that is embedded in an enterprise agency. The organisation has been operating for over 20 years, and provides skills development

programmes as well as consultancy services for small and micro businesses in the local area. The loan fund manager, a retired bank clerk with 30 years of experience in the commercial bank world, took a clear stance on the relevance of the CDFI within the agency:

If I'm being honest with you, the scenario is: first and foremost, we're an enterprise agency, and secondly we're an enterprise agency with a loan fund. So, yes, we're a CDFI and we're following the remits that are available through that. But in a way – in simple terms – we're an enterprise agency that has got a loan fund and we haven't got that many other whistles and bells and things associated with ourselves as a CDFI.

(Loan fund manager, GTR)

Similarly, the loan fund manager of ADQ, which is also an enterprise agency with a 25-year-history, illustrated how essential the loan fund was to the agency's operations:

If we [the loan fund] were to cease straight and tomorrow, ADQ would cope. What ADQ actually does is business training and advice (), which is quite a big section of our company (). And () the loan fund is just an added product that we can offer.

(Loan Fund Manager, ADQ)

Pure CDFIs, in contrast, naturally take a very different stance towards the provision of additional non-financial services for their clients. GHT is a CDFI that provides loans for businesses as well as personal finance. It is a relatively young institution that was set up as an initiative of several local and regional bodies. When talking about the organisation's purpose, its CEO highlighted that GHT is not interested in pursuing activities that are out with its core mission:

We're not interested in delivering business support. We get asked to do all sorts of things, because we're quite good at delivery. But we're only interested in fulfilling our mission and the people who are gonna be interested in that, and we bring them in.

(CEO, GHT)

These different views reflect a noteworthy discrepancy in the way that CDFIs manage their relationships with their process stakeholders, particularly their employees and their cooperating partners. In some cases, the employees of enterprise agencies are not only involved in managing the loan fund, but also execute tasks that are related to the enterprise agency, such as holding seminars or helping to develop business plans. They tend to see themselves as part of the enterprise agency, and not part of the loan fund. Based on the interviews, this can lead to a very different understanding of what constitutes the mission of the organisation. While the employees of pure CDFIs in many

cases show strong commitment to providing loans to specific target groups, the mission of employees from enterprise agencies tends to focus on the support of small businesses. Loan finance is seen by them as only one alternative within a wider product range.

Furthermore, enterprise agencies have the possibility to cross-subsidise their CDFIs via income streams that are generated through business development services. This allows them greater freedom in choosing their target market as well as the social or financial aims they want to achieve, as external funding can at least partly be substituted internally. Consequently, one might assume that the relevance of funders is considered lower in enterprise agencies compared to pure CDFIs, which are fully dependent on external sources of finance.

Another difference lies in the way cooperating partners are perceived. While enterprise agencies have the opportunity to ‘hatch’ their future borrowers, pure CDFIs need to rely on a well-functioning network of cooperating partners that have the capability of supplying them with investment-ready clients. Pure CDFIs therefore have to take an active stance in managing their relationships with cooperating partners in order to hold up a constant deal flow over time. This does not mean that enterprise agencies can do without their cooperating partners (in fact, they play a vital role for all of the enterprise agencies that we interviewed); nevertheless in situations where the supply of investment-ready clients deteriorates, it can at least partly be substituted internally.

4.2. Environmental Stakeholders

4.2.1. Clients: Type of Lending

When the interviewees were asked to describe the relationships they had with their clients, it became clear that there are two main issues governing these relationships. First, three loan types need to be treated separately: personal loans, microloans, and SME loans. Second, the target group that is served by the CDFI plays a vital role for the nature of the relationship with clients.

With regard to the loan types, personal loans are usually not higher than 1,000 pounds and are intended for various purposes like household expenses, ‘back to work’ expenditures, or personal debt consolidation. In the case of business loans, there is a

broad taxonomic consent within the CDFI sector that microloans are those up to a maximum of 10,000 pounds, while SME loans cover funding needs that lie between 10,000 and 50,000 pounds. The main difference between these loan types, though, does not lie in the amount that is lent, but in the nature of the relationship with the borrower. One CEO reported that his CDFI had been moving away from microloans and focusing instead upon SME loans. His justification for this strategy was as follows:

Micro enterprise lending is really up to [a loan amount of] about 10,000 [pounds]. () It's more about people who think: I would like to work for myself. They're not really thinking about building a business; they think about how can I create through trading opportunities an income for myself? And they're one person bands in the main. And they're very high risk, and they generally need an enormous amount of business support to go alongside the lending, which is why we've chosen to come out of it.

(CEO, SWQ)

A similar argument was also made by the CEO of SFP, a pure CDFI that has been operating for around 10 years. He reasoned the move from the microloan to the SME loan segment by referring to the different costs involved:

We've moved away from the 1,000 to 10,000 [pound segment], because we can't make that pay on our model, it's too costly. We made loans from 10,000-50,000 [pounds] with our original mission of local jobs for local people being paramount.

(CEO, SFP)

Thus a crucial decision for a given CDFI is the target market that it chooses to focus on, as this has important implications for the nature of the relationships with its clients as well as the costs involved in the lending process. As is shown in Table 2, there are two dimensions through which the different target markets can be described: the complexity of the credit assessment process, and the nature of the business support. In the case of personal loans, the credit assessment process tends to be quite quick, and is usually based on very simple formal criteria such as the applicant's age, postcode area, or income. By contrast, decisions about microloans and SME loans are based on the evaluation of business plans that describe the purpose of a given business and the intended use of the loan, which makes the whole process more complex and time-consuming.

While personal loans are not connected to any additional support after they have been approved, CDFIs are expected to provide business support to the recipients of microloans and SME loans for the duration of the repayment period, either themselves

or through cooperating partners. More generally, microloan clients require more intensive support than SME loan clients. This is mainly due to the fact that the businesses of microloan clients tend to be start-ups and typically have less experience than SME loan businesses. As explained earlier, business support is not an issue for pure CDFIs; their main purpose is to identify adequate cooperating partners in order to make their clients investment-ready.

Table 2: Nature of Credit Assessment and Business Support according to loan size.

	Credit Assessment	Business Support
Personal loans	Simple	n/a
Microloans	Complex	high
SME loans	Complex	moderate

Another issue that dominates CDFIs' relationships with clients is the different target groups that they serve. The institutions in the study differ in their focus on specific client groups, the unifying theme being to help overcome financial exclusion. While all have clear geographic restrictions in their lending activities (mostly as a result of the conditions placed on CDFIs by donors), some also confine their borrowing to specific target groups like women, ethnic minorities and disabled people. Others pose certain exigencies towards the types of businesses that can be lent, e.g., by stipulating that the businesses which receive funds must make an identifiable local impact, or have a specific ethical cause. This influences the way in which clients are dealt with, as each target group has specific needs that need to be met. TDF's loan fund manager, for example, emphasised the varying risk perceptions of men and women when taking up loans:

There is a very great difference in dealing with women. Because I would say 90% of the time the advisor team has to convince a woman to apply for more than they were initially going to do. Whereas the opposite is true for men, who always want the maximum [loan amount] available.

(Loan Fund Manager, TDF)

4.2.2. Clients and Funders: Market Focus

The analysis of the repertory grid data through multidimensional scaling (MDS) enabled us to map stakeholders and the constructs that were named by the interviewees in spatial terms based on two dimensions. We found one dimension to be constant throughout most of the repertory grids, namely the divide between the environmental stakeholders

according to their role as fund absorbing or fund allocating entity (cf. also Figure 2). We labelled the former “client market”, and the latter “funder market”. One interviewee commented that serving these two markets simultaneously would pose a fundamental challenge for any grant-funded organisation. On the one hand, the organisation’s mission is aimed at lending to a specific client group; on the other hand, public funds are often tied to conditions that restrict their usage. Thus a central question for CDFIs is: which of these markets constitutes its core mission and what is the mechanism for achieving this mission? One loan fund manager summarized this dilemma in the following way:

Unfortunately, one of the drawbacks with any grant-supported organisation is that in an ideal world is that what would happen is that we would perceive a need and decide how we wanted to address that need, and then approach the funders asking them to fund us. The reality is that we get to hear that there is a new funder or there is funds available and the criteria that the funders set we can adapt or we can use to support our key aims.

(CEO, EAS)

As described above, we included three constructs into the repertory grids that captured the three dimensions which constitute a stakeholder’s salience – power, legitimacy, and urgency (Mitchell et al., 1997). With the help of the MDS procedure, we were able to graphically relate these constructs to particular stakeholder groups, and thereby understand the prioritisation of stakeholders by each individual CDFI. In assessing the extent to which elements and constructs are associated, the distance between coordinates is considered. A perfect association would result in an exact match of coordinate pairs. This analysis revealed two types of CDFIs, which differed primarily in the way they perceived the two market sides they prioritise. While one group of CDFIs had a clear focus on the client market, the other group either had a clear focus on the funder market or did not exhibit any clear focus at all, i.e. they were “lost” between the two markets.

GHT is a typical example of a CDFI that is clearly focused on the client market, which is nicely illustrated by the MDS evaluation of its repertory grid (see Figures 1 and 4 in the Appendix). Dimension 2 clearly represents the client market/funder market divide, while Dimension 1 depicts the nature of the aims that the individual stakeholders pursue (i.e., social vs. financial aims). In this specific case, the local community is seen as part of the funder market, because it was understood by the interviewee as the collectivity of any organisations or individuals from the local area that are financially involved in the

CDFI, but not the recipients of loans. All three salience constructs are closest to the clients, indicating a clear focus on this market, which is also evidenced by the following quotation from its CEO:

And because of our background – the way that we operate is like a private-sector organisation, we're driven in a private-sector manner – so we are uniquely harsh with our donors. I will say to them things like: I will not take this grant unless you do x, y, z.

(CEO, GHT)

HED's repertory grid evaluation (see Figure 5), by contrast, reveals a different perception of funder and client market. Dimension 1 represents the two different market sides, while Dimension 2 could be interpreted as the abstractness of the individual stakeholders, ranging from very abstract (local community) to very tangible (voluntary directors). In the case of Figure 4, the salience constructs are all centred around the funder group, indicating the priority of that market for the CDFI. Its loan fund manager, a former bank clerk with 25 years of commercial bank experience, confirms this interpretation when describing the motivation for addressing specific client groups:

I think [we] have effectively been driven by what money was available and for what purpose by the government. And because that pot of money was available then it happens. And therefore policies were made and driven, totally because the money could be achieved; if you meet these criteria and if you act like this those policies are adopted and therefore that slant has been put on it.

(Loan Fund Manager, HED)

Returning to the question of client and funder market focus, we conclude that one group of CDFIs sees its mission in serving a specific client market. Addressing the funder market is the purpose to achieve this mission. The remaining groups, in turn, see their mission in accessing available funds from the funder market; addressing the client market is therefore the purpose in order to obtain these funds.

5. Towards a Performance Measurement Framework for CDFIs

According to Atkinson and Waterhouse (1997), the notion of primary and secondary performance measures is central in the development any performance measurement framework. In the case of CDFIs, primary performance measures are related to the double bottom line; i.e., its financial and social returns. Typical examples for financial returns are measures like its operational self-sufficiency (i.e. how well costs can be covered through operating revenues), or its portfolio yield (i.e. the gross loan portfolio's ability to generate financial revenue from interest, fees and commissions). Social returns

refer, for instance, to the number of jobs created or sustained through lending activities, or the target group focus, measured by the number of clients that belong to a specific target group in relation to the total number of clients (for a theoretical framework on social returns cf. Navajas et al., 2000).

What the organisation expects or gives to each stakeholder group to achieve its primary objectives are its secondary objectives (Atkinson and Waterhouse, 1997). The basis for identifying these secondary objectives lies in the way that stakeholder relationships are managed by the CDFI. Success is created by monitoring and managing performance on the secondary objectives, which should therefore be the focus of the organisation's performance measurement. As Atkinson and Waterhouse (1997) note, 'improving organisational performance by monitoring financial performance [i.e. a primary performance measure] is as useless as trying to improve a sports team's performance by only reporting the scores of its games.' The focus of attention needs to be on the secondary objectives. As noted above, there are three main dimensions which describe the ways in which a CDFI interacts with its stakeholders: (i) its organisational structure (related to process stakeholders); (ii) loan type and target group; and (iii) client vs. funder market focus (both related to environmental stakeholders). These are the underlying dimensions of the secondary objectives, or the drivers of performance. Figure 3 illustrates this relationship between drivers and measures of performance.

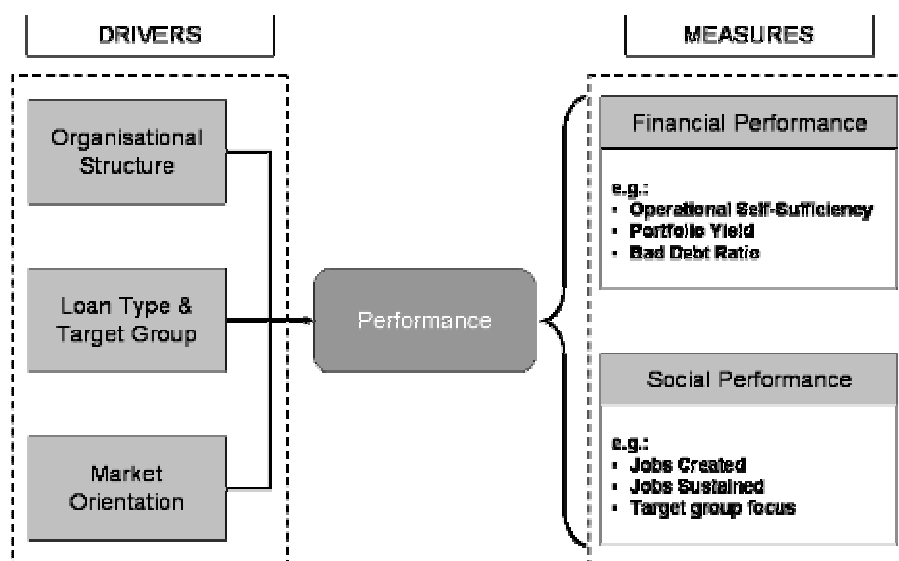


Figure 3: A Framework for Performance Measurement of CDFIs.

At the outset of the analysis (see Figure 2) we defined three distinct groups of stakeholders, namely process stakeholders (employees, board, and cooperating partners), as well as environmental stakeholders. The latter group was divided into source of funds (funders, private investors, and policy makers), and use of funds (clients, and local community). The three drivers of stakeholder management that we have identified cover each of these groups. In accordance with Freeman (1984) we posit that systematic managerial attention to stakeholder interests is critical to the success of a firm. Neglecting the needs and demands of one of these groups will lead to a significant loss of legitimacy, and – in the longer term – failure of the CDFI. Process stakeholders and environmental stakeholders (the latter ones in their roles as fund allocation and fund absorption) act as the three main pillars that support any CDFI's activity. The implicit and explicit contractual relationships with these entities have to be managed simultaneously in order to ensure a balance within the stakeholder system. Therefore, we state in our first proposition:

PI: A CDFI has to manage its relationships with all three stakeholder groups concurrently to excel in social and financial terms. Losing the support from one of these groups is likely to result in the failure of an institution over the medium term.

The drivers of performance that we have identified will probably relate to the financial or social nature of a CDFI's performance. With regard to organisational structure, our results indicate that CDFIs embedded in an enterprise agency tend to be the beneficiaries of cross-subsidising within the agency. This may lead to a softer stance regarding financial viability compared to pure CDFIs that depend solely on their lending activities. Our data support this conjecture, assuming that the interest rates that are charged serve as an indicator: Within our sample, the three organisations that charge the highest interest rates were pure CDFIs. Furthermore, our analysis has shown that CDFI employees of enterprise agencies tend to see their work in a more holistic way compared to their counterparts from pure CDFIs. Enterprise finance is regarded as one element within a wider range of products, which might also contribute to a softer stance towards sustainability. This leads us to our second proposition:

P2: CDFIs that are embedded in an enterprise agency will exhibit higher levels of social performance than pure CDFIs. Pure CDFIs, in turn, will exhibit higher indicators of financial performance.

The picture becomes more complicated when it comes to the loan size and the target market that is served, respectively. Specific target markets are connected to corresponding measures of social performance. A CDFI that is targeting its activities at supporting women's entrepreneurship should be measured along different social performance indicators than a CDFI that supports entrepreneurship within the cooperative movement. Equally, borrowers in rural areas might face completely different obstacles compared to their counterparts who live in urban centres. Social outputs are therefore highly target-group specific, which makes benchmarking across different institutions extremely difficult.

With regard to the loan size, though, a general assumption towards financial performance can be made which is purely based on cost considerations.⁶ As has been described above, the credit assessment process in the case of microloans and SME loans is comparably complex, as it is based on a business plan which then, as a rule, is evaluated by a loan panel. Consequently, the relationship between fixed costs and total loan size will be less favourable in the case of microloans. Furthermore, businesses receiving microloans tend to have no track record as they are usually start-ups, whereas businesses receiving SME loans tend to have some business experience. It is thus easier for a CDFI to assess the risk profile of the latter group compared to the former group. Based on these considerations, we derive our third proposition:

P3: A CDFI's financial performance will be higher if it operates in the SME loan segment compared to operating in the microloan segment.

Consequently, financial performance indicators should take loan sizes into account. It does not seem appropriate to compare financial indicators of an institution that extends microloans with an average of 5,000 pounds to an SME lender whose average loan is

⁶ It is acknowledged that most probably there will be a correlation between target group and loan size, which might make it difficult to treat these two dimensions completely independently from each other. Furthermore, we do not take into account personal lending because of its differing methodology, which has been detailed above.

20,000 pounds. If a CDFI covers loans of different sizes, it is advisable to split the loan portfolio according to loan size, and assess their financial performance separately.

We believe that the most important driver of performance is also the one that is the most difficult to measure, namely the market orientation of the CDFI. Non-profit organisations, like their counterparts from the private sector, need to understand the market they are serving and not only react to the remits that are available through public funding. It is only when the clients become the focus of institutional attention that their needs are liable to be understood. This will allow for a long-term strategy that involves serving a specific market as opposed to a 'patchwork' strategy that focuses mainly on the public funds that are available at a particular point in time. Clearly, this does not allow for the 'systematic attention' to stakeholder interests that Freeman (1984) regarded as essential for organisational success. This leads us to our final proposition:

P4: CDFIs that focus on the client market will exhibit higher financial and social performance indicators compared to CDFIs that are focused on the funder market.

Using the repertory grid technique, we have proposed a strategy designed to assess whether a CDFI is focused on the client market or the funder market. Although the process of acquiring these data was rather cumbersome, by providing a framework to help identify (1) CDFIs that are liable to survive in the long term, and (2) CDFIs that are liable to achieve the greatest social impact, we believe our study makes a substantive contribution and has the potential to help policy makers maximise the efficient use of limited public funds.

6. Conclusions

Applying a stakeholder approach towards performance measurement for CDFIs in the UK has allowed us to develop some important insights into the relationship between the factors that underpin performance and the concept of the double bottom line; i.e., the aim of achieving financial and social returns. Based on their stakeholder environments, we identified different ways of classifying CDFI performance according to three dimensions: organisational structure, the type of lending they pursue, and their focus on the client or the funder market. In advancing our argument we have presented four propositions. To excel in social and financial terms, a given CDFI has to manage its

relationships with all three stakeholder groups (i.e. process stakeholders, use of funds, and source of funds) concurrently. Second, CDFIs that are embedded in an enterprise agency will exhibit higher indicators of social performance than pure CDFIs. Third, a CDFI's financial performance will be higher if it operates in the SME loan segment as compared to operating in the microloan segment. Finally, CDFIs that focus on the client market will exhibit higher financial and social performance indicators compared to CDFIs that focus on the funder market.

6.1. Implications

Our study has a number of implications for actors involved in the CDFI movement. Most importantly, practitioners from the CDFI sector often complain about the multitude of demands that they face from different actors. The framework that we have proposed could be used by individual CDFIs to map the organisation's stakeholders and prioritise their claims. Furthermore, the framework might help to reframe discussions about the double bottom line of CDFIs. The question of which objectives – social or financial – CDFIs should prioritise, and whether both sets of objectives can be reached simultaneously, has been the source of much discussion and debate. Our analysis suggests shifting the focus away from a fixed set of measures, and instead adopting a contingency approach in which different measures are used to assess different types of CDFI. When there is clarity about the factors that underpin the performance of a particular CDFI, one can then begin to discuss the measures. Our propositions – which are certainly open to critical discussion – might serve to guide this process.

Policy makers are interested in identifying CDFIs that use public funds in the most efficient way. As stated in the introduction, recent funding policies in the UK gave the impression that the sector was seen as a rather homogeneous block by policy makers. Peer groups of CDFIs could be created using the three dimensions identified in this article to enable more appropriate comparison. After identifying CDFIs that perform within each peer group, their lending activities should not be restricted to exhaustive rules and regulations (one loan fund manager reported that his funder gave him a detailed list defining the characteristics of financially excluded persons). Rather, they should be supported with sufficient capital to achieve scale (Ratcliffe and Moy, 2004) and be given the opportunity to operate for some years with a minimum of restrictions on their lending activities.

From an academic point of view, we believe that this paper makes a theoretical as well as a methodological contribution. First, the approach towards performance measurement presented could be valuable for the analysis of any non-profit organisation or social enterprise. It highlights ‘who or what really matters’ to the CDFIs – whether the focus is on the funder market or the client market. From a methodological perspective, the repertory grid technique delivered new insights into the motivations of non-profit entrepreneurs. We believe that our methodological approach has wide applicability within the third sector as many non-profit organisations face the fundamental challenge of serving two markets – i.e., clients and funders.

6.2. Directions for Future Research

There are two main limitations to our analysis. First, we did not take into account possible interactions between stakeholders (Neville and Menguc, 2006). The majority of stakeholders that we have defined are in fact interconnected and do not act in isolation. One example is Community Investment Tax Relief (CITR), which has been designed by policy makers to attract private investment to the community development finance sector. These stakeholder interactions add a new layer of complexity to our analysis and suggest many avenues for future research.

A second limitation is the fact that there might be problems of interaction between the factors that underpin performance that we have identified. A certain characteristic of one driver might predispose the characteristic of the other drivers, and therefore weaken our propositions, which assumed that each driver is independent. Within our sample, we did not find any statistically significant correlations⁷, which might also be due to the rather small sample size. Further research will be required to gain more insights into possible interdependencies between drivers.

Finally, our analysis has focused on the CDFI market in the UK. It would be interesting to see if the framework that we have established can be replicated for comparable institutions in other European countries. Additionally, it might be possible to test our propositions empirically through the collection of quantitative data. This would

⁷ Based on a Chi2-Test of independence.

represent an important step in developing our preliminary findings into a genuine performance measurement framework for CDFIs.

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Appendix

Table 1: Summary of the Cases.

Name	Year founded	Gross loan portfolio (in pounds)	Lending Type (b=business; p=personal)	Embedded in enterprise agency
GHT	2003	600,000	b/p	no
JAI	2001	650,000	b/p	no
HED	2003	186,000	b	yes
GTR	2002	1,372,000	b	yes
SWQ	2002	1,000,000	b	no
MBD	2000	360,000	p	no
WSD	2005	390,000	b	no
GVC*	1983	n/a	b	yes
ODE	1998	700,000	b	no
ISD	1992	270,000	b	no
ADQ	2004	740,000	b	yes
DFR	1997	1,500	b/p	yes
LPO	2004	20,000	b	yes
RWE	2005	130,000	b/p	no
EAS	2005	580,000	b/p	no
SFP	1997	2,200,000	b	no
ASL*	2005	n/a	b/p	yes
BCV	1986	460,000	b	yes
TDF	1987	1,166,000	b	yes
HBV	2004	643,000	b/p	no

* ceased operating as CDFI.

Pole 1	Customers	Local Comnity	Employees	Private Investors	Policy Makers	Coop. Partners	Donors	Voluntary Directors	Pole 5
We are experienced with their needs	2	3	1	2	2	3	2	2	We are not so experienced with their needs
Close to us	3	4	1	3	4	3	2	1	Distant from us
Outward-looking perspective	5	4	2	3	3	2	3	4	Inward-looking perspective
Interested in financial return			2	3					Interested in ethical return
Have knowledge on micro-level	2	2	2	4	4	3	3	3	Have knowledge on macro-level
Mission-driven			2	3				1	Results-driven
Motivated by the 'big matter'	5	3	3	2	2	3	1	2	Motivated by the 'single case'
Commit themselves to our agenda	5	4	2	4	4	3	3	1	Have their own agenda
Know what financial exclusion means	4	4	1	3	3	2	2	1	Have no grasp of what financial exclusion means
We have frequent contact with them	1	4	1	2	3	4	3	1	We have intermittent contact with them
Their claims are powerful	1	4	1	2	2	4	2	2	Their claims are not powerful
Their claims are legitimate	1	2	1	2	3	4	2	1	Their claims are not legitimate
Their claims are urgent	1	3	1	3	3	4	3	2	Their claims are not urgent

Figure 1: Example of a completed Repertory Grid (GHT).

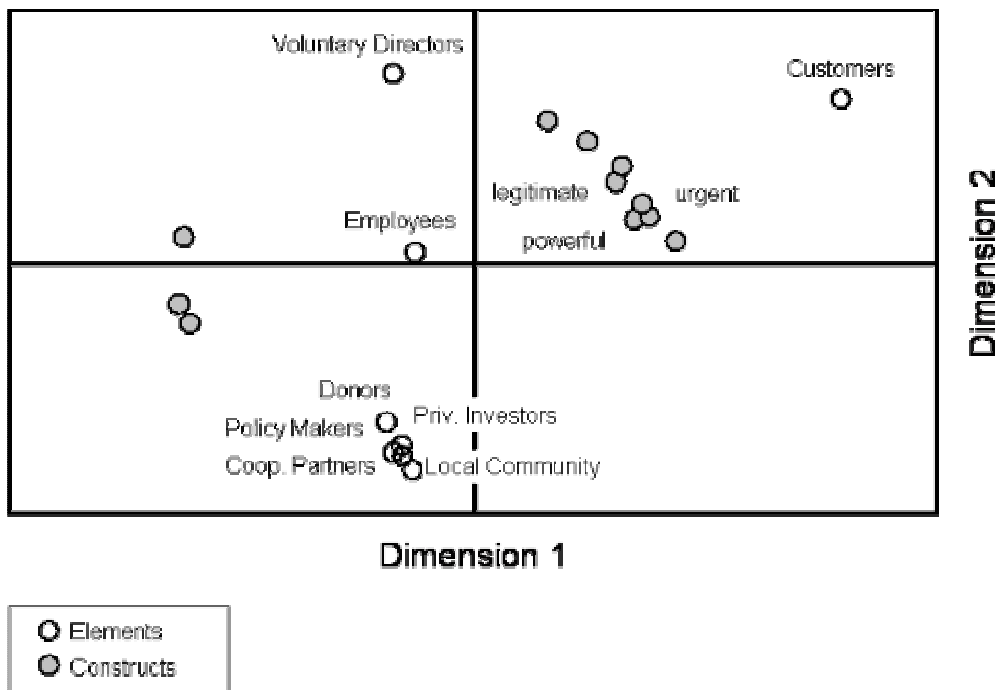


Figure 4: MDS plot of GHT.

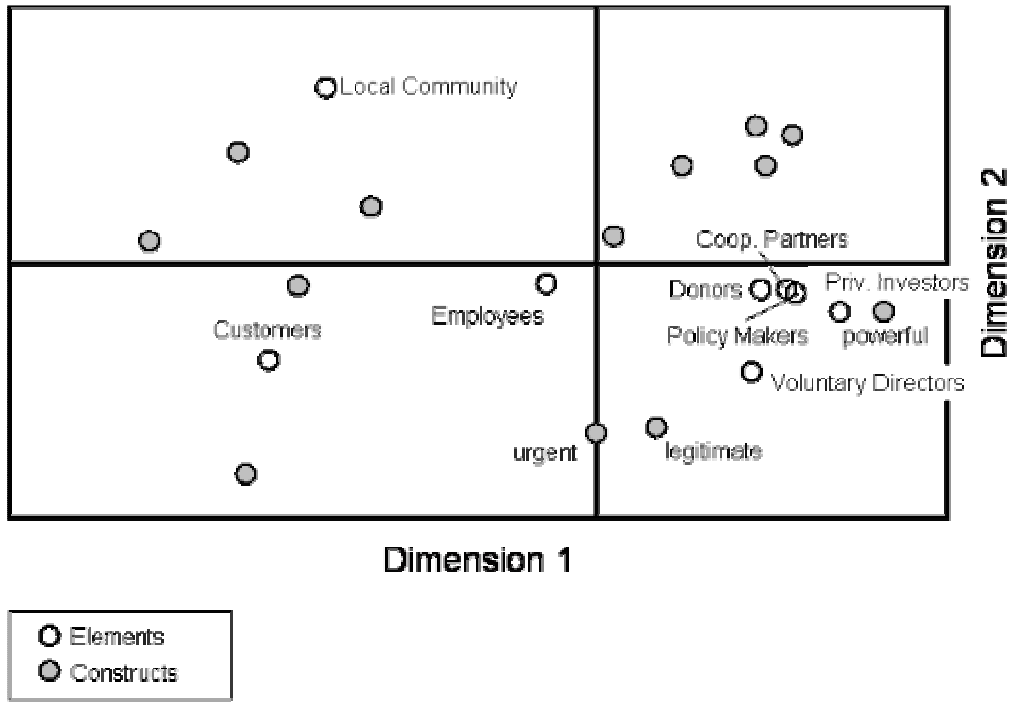


Figure 5: MDS plot of HED.