Brief 4

The World Bank - Pakistan Poverty Alleviation Fund
Research Partnerships on Participatory Development

PERFORMANCE INCENTIVES IN MULTI-MISSION ORGANIZATIONS

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Context

This study assesses the impact of providing performance-based incentives to front line staff in mission driven organizations such as PPAF. It was designed in conjunction with PPAF (in its second phase) and was implemented by its largest partner at the time, the National Rural Support Program (NRSP).

PPAF main mission is the social mobilization and empowerment of poor households through the formation and strengthening of organizations of the poor at the community level and livelihood enhancement. Like PPAF, NRSP's overarching mission is poverty reduction and community empowerment. To achieve these dual goals, micro credit delivered through Community Organizations (COs) has played an important role.

NRSP's dual focus on social empowerment and microcredit is reflected in its management structure in the branches. Credit Officers (CrOs) are in charge of the microcredit program, while Social Organizers (SOs) handle the inclusion and social mobilization aspects of the program. Field Assistants (FAs), who are at the bottom of this hierarchy, report to the CrO for all issues related to microcredit and to the SO for all issues related to social mobilization and community empowerment. The FA's responsibilities include assisting SOs with CO formation and strengthening, attending CO meetings and processing of loan applications and ensuring timely loan repayment.

During the experiment both PPAF and NRSP were scaling up their microcredit program rapidly, creating two challenges. The first was to maintain portfolio quality while expanding operations to meet their disbursement and client goals. The second was to ensure the quality of the community level institutions that would contribute to the longer-term goal of social inclusion and empowerment. In this context, management was worried that a shift in the mission of the organization towards shorter-term more bottom line goals like repayment at the expense of softer and harder to measure but more overarching goals like empowerment and inclusion could demoralize staff.

To test these potential trade-offs we worked with NRSP to devise two performance-based bonus contracts for FAs. The first incentivized performance on disbursement and loan recovery (the credit bonus) while the second incentivized performance on observable correlates of social empowerment (the social bonus), new CO formation and regular meeting and saving by CO members.

The Experiment

The experiment was implemented as a horse race between two incentive contracts each of which differentially rewarded the FA for one of the two tasks they were assigned to do. The incentive was provided as a simple salary bonus payable each month but with triggers such that in a given month only a subset of FAs would qualify to receive it. Monthly base salary was about Rs. 3000/month at the time (roughly $50/month) and the largest bonus an FA could earn in any month was about Rs. 600.

The bonus contracts were designed to be easily understood, equitable and fair. Each bonus had two triggers. In the credit bonus the first trigger was based on disbursement, measured by the number of active loans

managed by the FA in any month while the second was triggered if the repayment of the installment was made in full by the 20th of the month due. The disbursement trigger could be satisfied at two levels: High (A) or Low (B). If the FA met at least target B for disbursement, she/he qualified for a bonus based on repayment. For a recovery rate of 100% the bonus was 20% of salary if A (15% if B). For a recovery rate less than 100%, the bonus was reduced by 20% for each 1% reduction in the recovery rate. The social bonus also had two triggers, the first was based on the number of COs managed and the second on the level of attendance and savings at monthly CO meetings. If an FA met target B or better for the number of COs created, she/he qualified for a bonus based on CO meeting attendance. For attendance at 85% the bonus was 20% of base salary (15% if B) declining by 20% for each 5% fall in attendance.

The experiment was implemented in all 15 districts where NRSP was active at the time and in all branches or field units (FUs) in these districts. This provided a sample of 162 FAs who were randomly assigned to receive one of the two types of bonus contracts or to continue as before, i.e., with a flat monthly salary. All FAs in an FU were assigned the same bonus contract. The base salary of the control group is also the base pay in the bonus arms. Bonus pay was simply added to base salary if an FA earned a bonus in any month.

Results

Fas assigned to the credit bonus (Cr-FAs) improve repayment by the 20th but there are no differences in repayment at the end of the month. New CO formation and disbursement also increases for Cr-FAs in part driven by a lower rate of loan rejections. This suggests a greater orientation among Cr-FAs to view CO members as potential clients for microcredit rather than for the broader purpose of community mobilization. Because there is no impact on repayment at the end of the month, the new borrowers may come from less risky, better off households contributing to a shift in the composition of borrowers. Social outcomes such as attendance in CO meetings, however, decline significantly. In contrast, FAs assigned to the social bonus (Soc-FAs) improve repayment slightly and in particular improve social outcomes such as CO formation and attendance.

Since a good number of FAs work in a team, we examine the impact of partnership on performance in each of the incentive contracts. We find that un-partnered FAs assigned to the social bonus perform at least as well as those assigned to the credit bonus on almost all financial outcomes, save default at the 20th of the month, and Soc-FAs do significantly better on generating new loans and new disbursement. The overall differences among Cr-FAs and Soc-FAs described earlier thus come entirely from partnered FAs. In particular, partnered Soc-FAs perform extremely poorly on all financial and most social outcomes. Because it is harder link the effort of FAs to social outcomes, there seems to be more free-riding among partners assigned to the social contract. Consistent with these results, partnered Soc-FAs report a large decline in the quality of their relationship with their SO, while all other treated FAs report an improvement in their relationship with their SO.

Policy Implications

These results suggest that providing high-powered incentives on an institution's short-term bottom line need not improve revenues and can come at the cost of longer term, more directly “mission” related goals, and perhaps also at the cost of outreach to poorer microfinance clients. In contrast, a more direct focus on longer-term 'mission' goals through the social bonus does not seem to affect the health of the bottom line in any significant way, while improving the quality of social mobilization. In short, high-powered incentives on credit outcomes tend to create negative spillovers on non-incentivized social outcomes, but the reverse is not true.

The results also suggest more careful attention to team incentives, particularly when individual effort cannot be easily linked to final outcomes, as is the case, in particular, with FA effort on social empowerment related objectives.

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