Questions to Consider When Setting Desired Profitability Ratios and Ranges

- How does your pricing compare to market prices? Do profitability targets allow your institution to remain competitive relative to other players in the market?
- What is the minimum pricing to ensure full coverage of your product expenses? If you are setting a lower price (one that does not cover costs) on a product for social purposes, how sustainable is the “subsidy” from more profitable products or subsidies from other sources?
- How does each product and service contribute to your institution’s financial goals? Social goals? Which products/services can be justified based on their social benefits to clients, though they are not profitable in the short- or medium-term? How would termination of a product or service impact clients?
- Can you be viable without needing large profits from the more profitable loans? If you establish a policy of targeting cost recovery and profit from the full range of products, evaluate whether the higher cost of smaller loans is within the means of those clients to pay.
- Can you set lower profitability targets that support the sustainability of the institution and attract new investors while at the same time enabling clients to retain a greater share of their income?
- How much of your institution’s growth—whether scaling up or developing new programs—should be borne by new investor capital vs. financed through retained earnings/interest rate income provided by clients? What level of profitability is needed to attract adequate investor capital? Yield targets might be higher if excess income is used to benefit clients. Such examples include investments in: market research/product design/product testing so that products fit better with clients’ needs; client monitoring; improved client protection practices (e.g., creation of a client complaints mechanism or revision of loan contracts to improve their transparency); improved staff training on customer service; or extension of services into unbanked geographic locations. If high profits mainly benefit shareholders above the levels justified by the operating context (e.g., after accounting for inflation, country risk, etc.), then your profit/profit targets are most likely inconsistent with your social goals.