The Impact of Internationalization on Micro Finance Institutions' Performance

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Motivation

- Little is known about what drives the performance of providers of Microfinance Institutions (MFIs) – (Cull et.al, 2007)

- Significant international influence among MFIs:
  - Capital providers (donors, debt, equity)
    - 51% international subsidized debt
  - International initiators (Care etc.)
    - 38% international initiator
  - International governance – reporting & board membership
    - 24% international board membership
  - Extensive global networks – Opportunity International, Women's World Bank, etc.
    - 32% members of recognized international network

- But – policy recommendations: "to accelerate innovative *domestic* market solutions" (C-GAP, 2006, p. viii)

Theoretical motivation

- Advantages of international business activities (based on transaction cost and agency theory)
  - (i) economics of scale – especially knowledge (e.g., Dunning, 1977; UNCTAD, 2003),
  - (ii) reduced cross-boarder transaction costs by the means of internalized (within firm) markets (Buckley and Casson, 1976, 1998),
  - (iii) lower cost of capital from global capital (e.g., Stulz, 1999; Bekaert and Harvey, 2000; Oxelheim et al., 2001) and
  - (iv) better corporate governance (e.g., Oxelheim and Randøy, 2003; Coffee, 2002).
- Versus the disadvantage: “liability of foreignness” (Dunning, 2000)
  - Lack of local market knowledge
  - Need to transfer technology and systems
  - Costs of transfer of personnel
- We suggest Microfinance Institutions can benefit from the same kind of advantages.

Microfinance and Internationalization

- MFI can benefit from reduced transaction costs and reduced agency costs by:
  - international knowledge access – having an international initiator (H1)
    - Efficient transfer of skills and competencies
  - international funds access – international debt (H2)
    - Debt as a monitoring mechanism
  - international monitoring – international board member (H3)
    - Increase monitoring and board competencies
  - international network – member of recognized int. network (H4)
    - Provide monitoring and access to competencies

Our Model

- Research question: Does internationalization affect (increase) Microfinance Institution's social and financial performance?

    - MFI **financial** performance = f (international initiator, international debt, international director, international network membership + MFI specific control variables + Country control variables)

    - MFI **social** performance = f (international initiator, international debt, international director, international network membership + MFI specific control variables + Country control variables)

Data and Methods

- Dependent variable: Financial performance (adjusted Return on Assets) and social performance (average loan size)
- Sample: 290 MFIs from 61 countries
- Panel data – 4 years
- GLS – with 3SLS methodology

Significant results:

* p<.05 (two-tailed)
** p<.01 (two-tailed)
*** p<.001 (two-tailed)

	Financial Performance: Return on Assets	Social Performance Average loan size	Portfolio Growth
H1 International initiator		-**	-10%
H2 International debt		-*	
H3 Int. board member			
H4 International network		-10%	

Conclusion

- Main findings
  - Internationalization enhance social performance – but not financial performance
    - Facilitates lower transaction costs of transfer of know-how and funds
    - Facilitates better corporate governance – as agency costs of monitoring is reduced
- Limitations & weaknesses
  - Use of proxies – such as for social performance
  - Does not address the underlying processes – affecting performance
  - Reversed causality?