

THE MFI'S CHOICE OF LOAN METHODOLOGY AND BUSINESS MODEL

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Motivation

- Group lending (solidarity groups or village banking) considered the major microfinance innovation
 - Group lending a method for ensuring repayment
 - Experience from default rates in subsidized agri-loans 50-70ties
 - A major microfinance research area has been the study and modeling of the advantages of group lending
 - But MFIs shift from group lending to individual lending
 - 60% in dataset do mainly individual lending
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What determines MFIs' choice of lending methodology?

- Repayment risk?
 - Market outreach
 - Poverty level of customers?
 - Rural vs urban market?
 - Female customers?
 - MFI's efficiency and sustainability?
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Data

- 290 rating reports with up to four years of observations
 - Advantages of rating reports compared to Mixmarket data:
 - Raw data publically available
 - More variables available
 - Data is not self reported
 - Less large MFI bias
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Loan methodology effect on ROA and PaR

Loan Methodology	<i>ROA</i>			<i>PaR30</i>		
	Mean	Std	N	Mean	Std	N
Village bank	-0.028	0.119	65	0.062	0.094	66
Solidarity group	0.004	0.101	54	0.040	0.051	55
Individual loan	0.031	0.092	142	0.074	0.082	142
Other	-0.015	0.030	2	0.086	0.042	2
Total	0.011	0.104	263	0.064	0.081	265
ANOVA: F-stat.: 5.342; df: 262; Sign.: 0.001				F-stat.: 2.419; df: 264; Sign.: 0.067		

Logit – repayment risk only

Positive = individual
Negative = group

	PaR30
Portfolio yield	
Repayment risk	1.532 ⁵
Operational costs of portfolio	
Average loan	
Urban main market	
Gender bias	
Competition	
Latin America dummy	-0.178
dmafri	-0.420 ⁸
dmena	-0.751 ¹
dmeeca	0.096
Pseudo R2	0.058
N	883

Logit – repayment risk and others

Positive = individual
Negative = group

	PaR30	PaR30
Portfolio yield		2.245 ³
Repayment risk	1.532 ⁵	4.339
Operational costs of portfolio		-2.199 ²
Average loan		0.003 ¹
Urban main market		1.219 ¹
Gender bias		-1.275 ¹
Competition		0.121
Latin America dummy	-0.178	-0.857 ³
dmafri	-0.420 ⁸	0.088
dmena	-0.751 ¹	-0.838
dmeeca	0.096	0.389
Pseudo R2	0.058	0.579
N	883	610

Logit – repayment risk robustness

Positive = individual

Negative = group

	PaR30	PaR30	Writeoff
Portfolio yield		2.245 ³	1.842 ⁷
Repayment risk	1.532 ⁵	4.339	-3.302
Operational costs of portfolio		-2.199 ²	-1.925 ³
Average loan		0.003 ¹	0.002 ¹
Urban main market		1.219 ¹	1.130 ¹
Gender bias		-1.275 ¹	-1.325 ¹
Competition		0.121	0.110
Latin America dummy	-0.178	-0.857 ³	-0.838 ³
dmafri	-0.420 ⁸	0.088	0.079
dmena	-0.751 ¹	-0.838	-0.827
dmeeca	0.096	0.389	0.440
Pseudo R2	0.058	0.579	0.565
N	883	610	585

Conclusion

- ❑ Group lending is associated with rural markets, female customers and smaller loans (poorer customers)
 - ❑ Repayment risk is a poor predictor of loan methodology choice
 - ❑ Lending methodology influences MFI efficiency levels

 - ❑ THE QUESTION FOR THE MFI IS:
 - What to do when group lending is needed to reach poorer customers when it at the same time leads to lower efficiency levels?
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