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Master Thesis

Subsidy Dependence of Microfinance Institutions

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Abstract

Faculty of Economics, Business Administration and Information Technology
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Masters of Banking and Finance

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by Morgan O'Hana

Microfinance is defined as an innovative tool to fight global poverty and a financially sustainable business. Indeed, it reaches out to people who were previously excluded by traditional financial providers. However, forty years after an experiment in rural Bangladesh, the industry is still highly subsidised.
This paper investigates the roots of subsidy dependency in South Asia, Latin America, and Sub-Saharan Africa. Moreover, this study aims to understand which factors result in an institution not being financially viable and investigates which macroeconomic aspects could influence these different indicators in our three target regions. Through an analysis of the institutional setting, we introduce the idea of a locational advantage between the regions, where microfinance institutions would reach profitability more easily.
We conducted a T-test to highlight which indicators are significant in making or breaking the profitability of the "average institution" in each region. The microfinance institutions were divided into two subgroups, respectively the financially sustainable institutions with and without subsidies. Key indicators were then selected from these subgroups and tested from 2007 to 2011. The empirical results revealed that the strength of a microfinance institution in one region can be the weakness of another, such as the case of deposits in Africa and Latin America. However, with the institutional analysis, we understand that financial sufficiency is reached rather with a combination of microfinance industry characteristics and the overall environment than with stand-alone strengths, such as in Latin America. Namely, the region presents itself as a favourable location through the quality of its global and macro layer whereas South Asia and Africa, on average, present greater stand-alone strengths.