FOUR ESSAYS ON MICROFINANCE BOARDS

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Four Essays on Microfinance Boards

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My husband-Gibson

My children-Matthew, Michelle and Magnus

Whatever you do, work at it with all your heart, as working for the Lord, not for men
Colossians 3:23

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PREFACE AND ACKNOWLEDGMENTS

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Neema Mori
October 17, 2012
Kristiansand, Norway

INTRODUCTION AND SUMMARY OF THE ESSAYS

1.0 INTRODUCTION

Microfinance institutions (MFIs) provide financial services to poor people in order to reduce poverty and help the poor to set up income-generating businesses (Hermes, Lensink, & Meesters, 2011). These organizations typically have the dual objective of reducing poverty (social objectives) and being financially sustainable. Over the last decade, this industry has grown and attracted international attention due to, among other things, 2006 being named the UN Year of Microcredit, and the Nobel Peace Prize being awarded to Mohammad Yunus and Grameen Bank in that year (Galema, Lensink, & Mersland, 2012a; Labie & Mersland, 2011). Most people around the world are now aware of microfinance, and thousands of international stakeholders, such as NGOs, politicians and celebrities, are advocating its use, motivating more actors to become involved (Mersland, Randøy, & Strøm, 2011).

As the industry comes of age with so many stakeholders being involved, claims that MFIs need to improve their boards of directors (boards) as part of corporate governance[*] – have proliferated (Centre for the Study of Financial Innovation [CSFI], 2011; Hartarska & Mersland, 2012). However, apart from policy papers that suggest how MFI boards should be set up, there is little scientific knowledge about what constitutes an effective board and how influential boards are. The essays in this dissertation respond to this gap by investigating the structure, role and influence of the boards of MFIs.

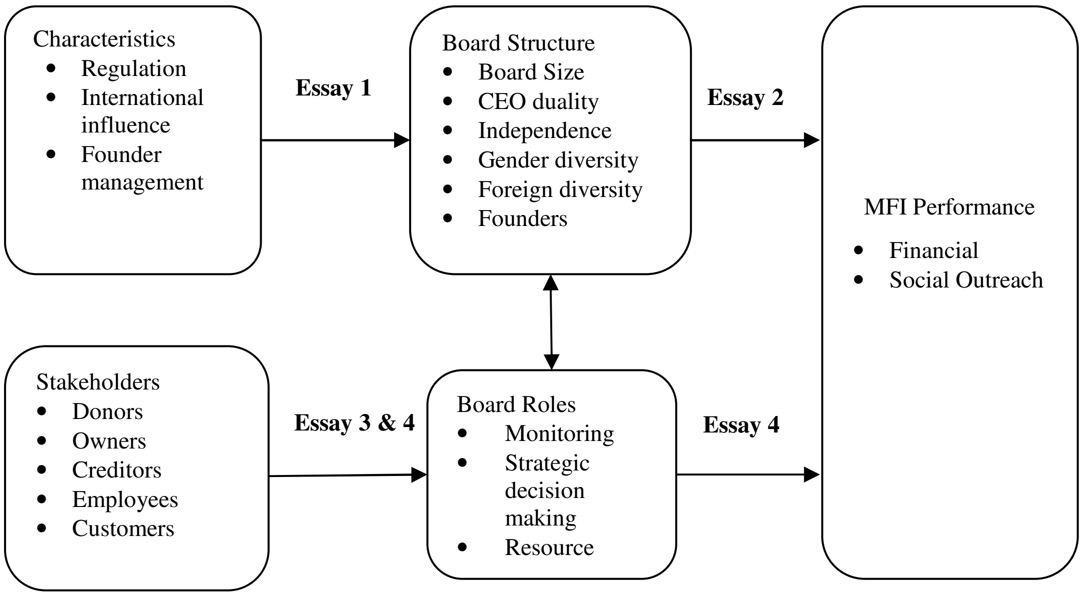
The first essay examines the determinants of board structure in MFIs. The essay is based on the literature that suggests that boards should be structured in response to organizational characteristics (Adams & Mehran, 2005; Linck, Netter, & Yang, 2008). It identifies the unique characteristics of MFIs and examines whether these characteristics determine the structure of their boards. Building on the first, the second essay examines the influence of board structure/composition on the performance of MFIs. The high involvement of different stakeholders in the microfinance industry (Labie & Mersland, 2011; Mersland, 2011) motivated the third and fourth essays, which examine the extent to which stakeholders are represented on MFI boards and their influence on strategic decision making, board structure and the performance of MFIs.

Overall, the four essays show that board structure is important for adherence to MFI board roles and the performance of MFIs. The dissertation shows that enhancing MFI board

[*] I borrow the definition of corporate governance from Thomsen & Canyon (2012), who defines it as the control and direction of organizations by boards, ownership, incentives and other mechanisms.

diversity is a means of enhancing the board's understanding of diverse customer needs (including the desperately poor) and providing strong linkages to resource providers such as international donors, national opinion leaders, fund providers and decision makers. The dissertation gives further evidence of the strong influence on MFIs of CEO founders and local and international stakeholders. The content and format of the essays are summarized in Figure 1.

Figure 1: Overview of the dissertation



Why are boards an interesting subject for this dissertation and why the boards of MFIs in particular? MFI boards are important because they are the strategic decision control systems (CSFI, 2011; Galema, Lensink & Mersland, 2012b). They are also instruments for dealing with the MFIs' external environment and enable MFIs to minimize their dependence on others and gain resources (Council of Microfinance Equity Funds [CMEF], 2005; Dorado & Molz, 2005). The MFI board therefore has a key function as it decides on the strategic direction of the MFI, oversees, monitors and advises the managers, and makes sure that organizational goals are met (Campion & Frankiewicz, 1999).

Microfinance policy papers such as those by Conger, Finegold, and Lawler (1999) and CMEF (2005) have suggested that MFI boards should be structured in such a way that their members are able to carry out their roles effectively. CMEF (2005), for example, argued that an MFI board should consist of a diverse group of members from both inside and outside the MFI. Outsiders are valuable as they provide the board with independent mindsets and experiences that can be shared with other members (Wagner III, Stimpert, & Fubara, 1998). Internal members provide the benefit of MFI-specific knowledge. This was further emphasized by Hartarska and Mersland (2012), who suggested that MFI boards should be composed of a mixture of (1) independent members, (2) insiders with a monetary interest in the MFI, and (3) representatives of stakeholders who represent different interests.

As can be seen from Figure 1, all the essays study the composition, structure and influence of the MFI board. First, the dissertation looks at the characteristics of MFIs and then examines them in relation to the board structure and MFI performance. Second, the dissertation identifies various MFI stakeholders and examines their representation on boards and their influence on (1) the strategic decision-making process and (2) board structure and MFI performance.

This introductory chapter is therefore organized accordingly: First, it gives an overview of microfinance and MFI boards in section 2. Then, section 3 provides the theoretical foundation for the essays. Section 4 elaborates on the data used and section 5 summarizes the essays.

2.0 OVERVIEW OF MICROFINANCE

2.1 The Context of Microfinance

Microfinance is acknowledged as an industry that plays an important role in creating economic and social development from the grassroots level (Maes & Reed, 2012). It is recognized as an important instrument in the struggle against poverty (Sengupta & Aubuchon, 2008). Maes and Reed (2012) reported that the number of customers reached by MFIs worldwide was more than 200 million as of December 2010 and that 56.5% of these customers were among the poorest people in the world when they took out their first loan.

The major regions offering microfinance services and those with the highest outreach are Asia and the Pacific, Latin America, Eastern Europe and Africa (Maes & Reed, 2012). The African region is shown to have the next biggest market for microfinance after Asia. Within Africa, East Africa, which is also the focus of this dissertation, is recognized as the fastest growing market (Consultative Group to Assist the Poor [CGAP], 2009). According to Maes and Reed (2012), 5.3 million East Africans were borrowing from MFIs as of December 2010.

Across these regions different types of MFIs are providing financial services to the poor. These include commercial banks, credit unions, non-bank financial institutions (NBFIs), and non-governmental organizations (NGOs) (Galema et al, 2012a). However, in most regions, the most common providers of microfinance are socially oriented NGOs (Galema et al, 2012b). Regardless of type, MFIs normally pursue a dual objective: financial sustainability and poverty reduction (Mersland et al, 2011). The goal of financial sustainability (the financial objective) focuses on the importance of the MFI being able to cover all of its operational costs from the income it generates from the outstanding loan portfolio (Hermes et al, 2011). The poverty reduction goal (the social objective) stresses the idea of the MFI being able to offer financial services to the poor and helping them to set up their own income-generating businesses (Hermes et al, 2011).

Banks and NBFIs tend to have less of a focus on social objectives and more on financial sustainability, due to factors such as ownership structure (Mersland, 2009), financing (i.e. fewer donations, more commercial debt) (Galema et al, 2012a) and banking regulations (Hartarska & Nadolnyak, 2007). NGOs focus more on social objectives than on financial objectives (Hermes & Lensink, 2011). NGOs have, for a long time, been pioneers in the industry and are often the first to start offering services to the poor in a particular region. They are often supported by donors, who focus mainly on social objectives, and are thus better able to serve the poorest segments of the population.

In line with their dual objective, MFIs (of all types) tend to offer a variety of services. The main focus of most MFIs is on providing financial services such as micro-loans, deposits and money transfers. In addition, MFIs offer other services such as vocational training, marketing and technical assistance, technology access, product design, and accounting and legal services (Galema et al, 2012a). Other services include raising customers' awareness of health practices, the use of formal health care, and the availability of micro-health insurance (Maes & Foose, 2006).

The different types of MFIs, their dual objective and the variety of services offered make this industry unique. This has also made the industry attractive internationally and has led to the involvement of many international stakeholders (Mersland et al, 2011). Table 1 provides a summary of the types of MFIs, their main focal areas and the services offered.

Table 1: MFI Forms, Objectives and Services

	NGOs	Cooperatives/Credit Unions	NBFIs	Banks
Definitions	Registered as non-profit for tax purposes or other legal charter.	Registered as a non-profit, member-based financial intermediary.	An institution that provides similar services to those of a bank, but is licensed under a separate category.	A licensed financial intermediary regulated by a state banking supervisory agency.
Objectives	Dual objective	Dual objective	Financial objective	Financial objective
Regulation	Unregulated	Unregulated	Partly regulated	Regulated
Services	Credit; non-voluntary deposit taking; social services	Credit; deposit taking; social services	Credit; voluntary deposits; limited social services	Deposit taking; credit; payment services; money transfers; no social services
Profit distribution	Non-distribution	To members	To owners	To owners

Adapted from Galema et, al. (2012a, 2012b)

2.2 The Boards of MFIs

Given the popularity of the industry, corporate governance, specifically that of MFI boards, is currently at the forefront of the microfinance policy debate (CSFI, 2011; Galema et al, 2012b). The literature gives several reasons for the importance of having good boards and corporate governance in MFIs. First, the high growth rate of MFIs translates into more customers who need to be served by well managed structures (Coleman & Osei, 2008). Second, MFIs have evolved from focusing on a single product to offering a wide range of financial services (Labie & Mersland, 2011). Third, there has been a rise in the number of local depositors and international microfinance investment vehicles (MIVs), who are spurring on microfinance and becoming important stakeholders of MFIs (Urgeghe & Mersland, 2011). Fourth, previous neglect of the industry by public authorities is being replaced by more proactive policies, and regulatory frameworks are being created all over the world (Labie & Mersland, 2011).

Despite their importance, however, the CSFI (2011) has reported that poor boards and corporate governance as one of the top five risks that MFIs face. The report also showed that the quality of the board is fundamental to an MFI's business and that only the MFI itself can address this. The focus of concern here is not only on the individual quality of each MFI board member, but also on the risk of conflicts of interest, the lack of independence, poor representation and poor accountability. The CSFI (2011) particularly highlighted that, across Africa, including East Africa, boards are a major problem (ranked as the second most common risk). Weak boards create management problems and thus increase the chance of incurring high credit risks.

These challenges and their importance have motivated several studies to analyze the contribution of boards and other corporate governance mechanisms to MFIs. Hartarska (2005), for example, examined the link between governance mechanisms and the performance of MFIs in Central and Eastern European countries. The results showed that smaller boards lead to better performance, boards with employee representation result in poorer performance and those with a higher proportion of donors have better social performance. Similar results were obtained by Soltane (2009), who conducted a similar study in the Mediterranean countries. Mersland and Strom (2009) studied whether different governance measures, such as international board members, board size, competition and regulation, affect MFIs' financial performance and outreach. Their results indicated that an MFI's financial performance improves when its board is informed by local members and it has internal auditors.

Hartarska and Mersland (2012) studied which governance measures promote efficiency in reaching poor customers. They found that MFIs with large boards and with creditors on their boards were efficient and those with employees and donors on their boards were less efficient. Focusing on Africa, Coleman and Osei (2008) studied the impact of governance measures on the performance of MFIs in Ghana. They found that independence of the board and clear separation of the positions of CEO and board chairperson have a positive correlation with MFI performance. They further argued that boards play a critical role in the making MFIs successful.

These studies are few, however, and do not provide a detailed picture of MFI boards. Given the unique nature of the industry, there is a lack of knowledge on what determines the structure of an MFI board and how that structure contributes to the board's strategic roles and performance. There is also a gap in the knowledge about stakeholders' influence on different types of MFIs. In addition, past studies have examined many governance mechanisms simultaneously and mainly use one theory at a time. This dissertation departs from that approach by focusing solely on boards and using a wide range of theories to shed more light on MFI boards and their effect. The dissertation also shows that MFI boards should not remain static because the evolution of the sector requires boards of high calibre. The microfinance environment is currently one of the more challenging ones there is; the international exposure of the sector and the growing complexity of the industry necessitates better and carefully structured boards, based on an examination of various theoretical angles.

3.0 THEORETICAL FOUNDATION

As mentioned earlier, MFIs are of various types but, as Fama and Jensen (1983) suggest, the board should be a mechanism for directing the organization, regardless of type. The microfinance literature indicates that the MFI board has several roles. First, it oversees the various constituencies served by the MFI. Second, it makes strategic decisions for the MFI. Third, it attracts and mobilizes resources and expertise. Fourth, it oversees and monitors the management of the organization. Finally, it assists in identifying the MFI's core mission and works to keep it on track (Campion & Frankiewicz, 1999; Dorado & Molz, 2005). The board structure is a mechanism that helps the board to perform these roles (CMEF, 2005; Linck et al, 2008). This dissertation makes use of various theories to help explain how board structure and composition is conducive to the attainment of the MFI board's roles and the enhancement of its performance.

The agency theory (Jensen & Meckling, 1976), a dominant theory in corporate governance research, assumes that the owners of an organization (principals) and those who manage the organization (agents) have different interests. According to this theory, the board has the role of monitoring the management. The microfinance literature indicates the necessity of monitoring by boards (Hartarska, 2005; Mersland & Strøm, 2009). Soltane (2009), for example, suggests that such board monitoring and control mechanisms are necessary in microfinance because the managers and providers of funds may have diverging preferences and objectives. Mersland and Strøm (2009) argue that large MFI boards induce members to free-ride in monitoring the CEOs. Similarly, Hartarska (2005) shows that diverse MFI boards are better at monitoring. Three essays in this dissertation (1, 2 and 4) use the agency theory for explaining board structure and its influence on both its monitoring role and MFI performance.

Other board roles suggested by the microfinance literature (Campion, 1998; Campion & Frankiewicz, 1999; Dorado & Molz, 2005) include strategy formulation and resource management, which members bring from both external and internal sources. A supportive board structure is needed for this. I used the resource dependence theory (Pfeffer & Salancik, 1978) to explain how resources are drawn from external sources and the resource-based theory to explain how they are drawn from internal sources. The resource dependence theory views organizations as depending crucially for their survival on other organizations and actors, from which they obtain resources. As a result, they need to find different ways of managing this dependence and ensuring they get the resources and information they need.

On the other hand, the resource-based theory suggests that the performance of the organization is enhanced when it explores its distinctive and idiosyncratic resources and capabilities and/or its ability to deploy resources (Barney, 1991). These theories complement each other with regard to access to resources and, therefore, the board should be structured in such a way that it gives the MFI control of critical resources. Based on them, it should be able to build a competitive advantage. Essays 1 and 4 use the resource dependence theory and essay 2 uses the resource-based theory.

Stakeholder representation is important in the microfinance industry (Lapenu & Pierret, 2005; Mersland, 2011). The stakeholder theory suggests that including stakeholder representatives on boards is a formal mechanism that acknowledges the importance of their relationship with the organization (Mitchell, Agle, & Wood, 1997). This mechanism may increase the organization's linkages with important external and internal contingencies. In addition, stakeholders' representation on boards enables them to be more independent (Hillman et al, 2001) because the managers are not only responsible to the owners but also respond to the various concerns of other stakeholders (Cornforth, 2003; Mersland, 2009). Essays 3 and 4 use this theory. Table 2 summarizes these theories, showing the assumptions they make about boards, and giving examples of other microfinance (MF) studies that have applied them and how they are used in this dissertation.

Table 2: How the theories are used in the dissertation

Theories	Assumptions of Boards	MF studies which use the theory	How they are used in the dissertation
Agency	Monitor and control management Provide strategic direction for the organization	Hartarska (2005) Coleman and Osei (2008) Mersland and Strøm (2009) Soltane (2009) Hartarska and Mersland (2012)	Essay 1:Explaining how the board structure is conducive to board monitoring roles Essay 2: How does monitoring enhance MFI performance? Essay 4: Stakeholders' monitoring results in structure and performance
Resource dependence	Provide a variety of resources Advise and counsel management	None	Essay 1: Explaining how the board structure is conducive to board resource roles Essay 4: Stakeholders' resource sharing results in structure and performance
Resource-based view	Board's valuable resources enhance competitive advantage	None	Essay 2: How resource availability enhances competitive advantage and performance of an MFI
Stakeholder	Stakeholders protect their interests Stakeholders have capabilities that enable them to fulfill board roles	Mersland and Strøm (2009) Hartarska and Mersland (2012) Labie and Mersland (2011) Mersland (2011)	Essay 3: Types of stakeholders and how they influence boards' strategic decision-making processes Essay 4: Where in MFIs are different stakeholders represented and how do they influence structure and performance?

4.0 DATASETS

Two datasets are used. The first is global and is used in essay 4. These data were obtained from secondary sources; they were compiled from rating reports available at www.ratingfund2.org and were previously used by Mersland (2009). The rating reports were collected by major microfinance rating agencies (MicroRate, Microfinanza, Planet Rating, Crisil and M-Cril) and contain information from 2001 to 2008. Each of the rating agencies is approved to rate and assess MFIs according to the Rating Fund of the Consultative Group to Assist the Poor (CGAP), which is a branch of the World Bank. The methodologies used by these agencies were compared and there were no major differences in their MFI assessments. The information included in the dataset comprises governance variables, financial statements and risk management by MFIs. It pertains to 379 MFIs from 73 countries worldwide.

However, the global dataset does not contain detailed information on board structure variables or board members' demographic information. Furthermore, it contains many contextual variances since it covers more than 70 countries. This dissertation goes deeper, not only theoretically, but also empirically; in order to understand microfinance boards at this level, there must be less contextual variance. Because of this, the researcher constructed a new and more detailed dataset covering MFIs in the three East African countries of Kenya, Tanzania and Uganda. This region was selected for four main reasons. First, it is among the regions in Africa in which microfinance is most developed, as reported by CGAP (2010). Second, as Table 3 shows, most of the East African MFIs have international affiliations. This may influence their corporate governance as we know that international organizations involved in MFIs are likely to specify how the board should be made up (CMEF, 2005).

Third, there are more founder CEOs and founder board members in this region than in the global dataset, which makes it an interesting area for the study of corporate governance. It may be that corporate governance in the region is affected by the presence of so many founder CEOs. Fourth, the region also has many regulated MFIs, which is important for corporate governance. Usually, regulatory authorities provide specifications regarding how the boards of regulated MFIs should be composed. One of the regulatory specifications is in regard to the maximum timeframe for CEOs and board members. The question of interest then is how can this region have so many regulated MFIs, such extensive international influence and still so many founder CEOs and founder board members? This puzzle led to two of the essays focusing on this region. Overall, the East African dataset is unique and provides more insights into the corporate governance of MFIs.

The East African data were hand-collected by the researcher between January and August 2010. The researcher contacted umbrella microfinance associations in each of the countries selected for the study, and received MFI directories containing the names of MFIs, their CEOs, the number of customers of each MFI and their contact addresses. The MFIs selected from the directories were visited and the CEOs were asked if they would answer some questions on governance, board members' demographics, and MFI operations. The researcher also collected audited financial statements from 2004 to 2009. Other MFIs were also identified and visited using snowball sampling (Saunders, Lewis, & Thornhill, 2003). Furthermore, the researcher conducted face-to-face interviews with selected board members of the MFIs visited. The data collection process led to a dataset containing a total of 63 MFIs, board demographic information on 465 board members, interview results of 30 board members and financial information for six years.

Table 3: Comparison of MFIs in the two datasets

Variables	**East African Dataset**	**Global Dataset**
	Mean	**Mean**
Regulated MFIs	0.39	0.25
Asset size (USD)	7,984,000	6,031,000
Age (years)	9.69	9.00
International influence	0.66	0.33
Board diversity (proportion of females)	0.25	0.28
Founder CEOs	0.54	0.38
Board size	7.18	7.23
Operational self-sustainability	1.04	1.14
Number of customers	35,742	14,978
Average loan per customers (USD)	348	751
Number of MFIs	63	379
Year-observations	343	2,200
Period	2004-2009	2001-2008
Number of countries covered	3	73

5.0 THE ESSAYS

All of the essays have been presented at different conferences and gone through a blind review process to improve their quality. Essay 3 has been published and Essay 4 accepted for publication in peer-reviewed journals. Essay 1 and essay 2 are currently under review.

5.1 Essay 1: Determinants of board structure in MFIs

This essay argues that the microfinance industry is unique in terms of its newness, the diversity of its organizations, because they include those that are both for-profit and not-for-profit, and because its dual objective, both financial and social, with the social objective focusing on both women and the poor. The essay investigates the association between MFI characteristics and board structure. It uses the agency and resource dependence theories and the East African dataset. The results show that the presence of regulations and international influence in MFIs is associated with larger boards, while the presence of founders is associated with small boards and less board independence. There is also evidence of a higher level of gender diversity and nationality diversity on the boards of MFIs managed by founders and those that are internationally influenced. The paper concludes that MFIs should select board structures that are adapted to their unique governance environment in order to enhance their resource access and monitoring ability.

5.2 Essay 2: Board Composition and Outreach Performance of MFIs

Essay 2 is an extension of Essay 1 and looks at the effect of board structure on the performance of MFIs. Since MFIs are known to serve poor people, the paper only looks at the social performance of MFIs. In order to develop hypotheses for this paper, the researcher first conducted personal interviews with board members in East Africa. The hypotheses were developed based on the theories and the interview responses, and then tested on the same East African dataset. This mixed-methods approach was used to link board composition (independence, female, nationality and founder representation) with three dimensions of outreach performance: number of customers, percentage of female customers and average loan size. The findings suggest that poverty outreach (social performance) is enhanced when MFI boards have independent, international and/or female members. The paper concludes that, given the relative newness of microfinance, and the importance of entrepreneurship in the industry, the social mission of MFIs is enhanced by greater board diversity. Board independence appears to improve the quality of board members' monitoring and their ability to provide resources to the MFI. International board members typically bring strong capabilities and access to unique resources. Also, given the fact that there are more desperately poor women than men, having female board members might help MFIs to better understand the needs of these poor women, and also build the trust of female customers.

Essays 3 and 4

These essays were motivated by the interview responses gathered in the course of researching Essay 2. During the interviews, we observed that some board members sit on boards because they regard themselves as stakeholders, and they represent other stakeholders. These essays respond to the need for more knowledge on how stakeholders influence MFIs. For example, Labie and Mersland (2011) argue for a more stakeholder-based approach to determining "who" and "what" really count in the governance and performance of MFIs.

5.3 Essay 3: The Influence of Stakeholders on Strategic Decision Making of MFIs

This essay identifies the local and international stakeholders on MFI boards, and discusses their roles and involvement in strategic decision-making processes (SDMPs). Based on the stakeholder theory, the paper lists five stakeholder groups: customers, employees, creditors, owners and donors. Guided by the strategic decision-making literature, the paper discusses the influence of stakeholders on two aspects of SDMPs – information gathering/usefulness and political behaviour. Based on the review of the literature, the paper argues that when stakeholders serve on MFI boards both information gathering/usefulness and political behaviour occur simultaneously during SDMPs. Stakeholders are a source of useful information, which benefits MFIs by leading to high-quality strategic decisions. However, they also bring costs due to conflict, debate and disagreements, which are a source of poor-quality decisions. Furthermore, their involvement in SDMPs enables MFIs to make a trade-off between their two main objectives. Propositions and a model are developed to guide future empirical studies in this direction. The paper concludes that stakeholders are important but they also introduce costs into MFIs' SDMPs. To benefit from them, MFIs should identify their primary stakeholders, and involve them in their activities.

5.4 Essay 4: The Boards of MFIs: How do Stakeholders Matter?

Essay 4 empirically analyzes the influence of stakeholders on MFI board structure and organizational performance. The paper looks at three issues: the representation of stakeholders across different types of MFIs, the extent to which stakeholders affect an MFI's board structure (board size and CEO duality) and the influence of stakeholders on an MFI's performance (social and financial). This paper uses the global dataset mentioned in section 4 and is supported by the stakeholder, agency and resource dependence theories. The results show that donors and employees are better represented in NGOs, creditors in banks and customers in cooperatives. Also, donors appear to be associated with small boards, non-duality and better performance. Employees are associated with large boards, while customers are associated with duality and good financial performance, and creditors with duality and better social performance. The study concludes that stakeholders, specifically donors and creditors, should take a more active role in their partnership with MFIs and should sit on boards more often, rather than simply providing funding.

5.5 Conclusion

These four essays contribute to the corporate governance literature on microfinance institutions. They provide a broader understanding of microfinance board structures and the results of stakeholder influence on these organizations. While each essay answers the questions it set out to answer, there are still many unanswered questions relating to the theories and the microfinance industry that need to be examined.

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Collection of Essays

Essay 1

Determinants of Board structure in Microfinance institutions

Neema Mori and Trond Randøy

Essay 2

Board Compositions and Outreach Performance of Microfinance Institutions

Neema Mori; Sougand Golesorkhi; Trond Randøy and Niels Hermes

Essay 3

Stakeholders in MFIs: Exploring Their Involvement in Strategic Decision Making

Neema Mori

Essay 4

Boards in Microfinance Institutions: How do Stakeholders Matter

Neema Mori and Roy Mersland

ESSAY 1

DETERMINANTS OF BOARD STRUCTURE IN MFIs

Determinants of Board Structure in MFIs

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Board Structure; Microfinance Institutions; East Africa; Corporate governance.

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ABSTRACT

This study investigates the association between the unique characteristics of microfinance institutions and board structure. The agency and resource dependence theories provided the theoretical guidance for this study. Using a panel dataset of 63 microfinance institutions in East Africa, we found that the presence of regulations and international influence is associated with larger boards, while the presence of founders is associated with small boards and less board independence. There is a higher level of board gender diversity in microfinance institutions managed by founders. There is greater diversity of nationalities in microfinance institutions that are internationally influenced. The implications for practice and theory from this study are further discussed.

1.0 INTRODUCTION

With the coming of age of the microfinance industry, it has recently been highlighted that microfinance providers need to improve their corporate governance structures (CSFI, 2011). As suppliers of financial services to poor people, microfinance institutions (MFIs) are under pressure to improve their performance and a better governance structure is one way of achieving this objective (Labie & Mersland, 2011). In this paper, we address how board structure serves as one such governance mechanism.

In order for board-members to oversee and advise the organization's managers (Hillman & Dalziel, 2003), they need a structure that supports such roles (Jackling & Johl, 2009). However, little is known about MFI boards and what determines their structure. Microfinance policy papers (e.g. CMEF, 2005; Conger, Finegold & Lawler, 1999) suggest how MFI boards should be composed and structured, but we lack knowledge on how these boards are actually structured and what factors determine the choice of a certain structure. This study addresses this knowledge gap by examining the relationship between MFIs' unique characteristics and their board structure. Specifically, our research question is: What determines the board structure of an MFI?

The unique characteristics of MFIs are related to a number of aspects. First, MFIs are characterized by their combined commercial and social goals. Their objectives are therefore to be financially sustainable while reaching out to poor people (Mori and Mersland, in press). These objectives have brought them to the attention of international aid agencies and philanthropic investors (Mersland, Randøy & Strøm, 2011). Second, the international affiliations of MFIs give the industry another unique characteristic. Mersland et al (2011), for example, found that the internationalization of MFIs leads to better organizational performance. Third, MFIs vary in operational form. Some MFIs operate as regulated bank-like entities, with a profit motive, others as unregulated non-for-profit ones. Lastly, the microfinance industry is young and—to a large extent—managed by its founders. For example, in our East African dataset, 54 percent of the Chief Executive Officers (CEOs) of MFIs are also their founders. These characteristics are our motivation for this study; we argue that they partly determine MFI board structure.

Steier (1998) found that board structure in for-profit organizations is set in a way that supports the specific demands of the industry. In relation to the microfinance industry, Conger et al (1999) provide guidelines for a desirable MFI board structure. The authors suggest that MFI boards should be composed of a mixture of members with different skills, especially expertise in social and financial issues. Based on the agency and resource dependence theories, board roles are divided into two main categories: monitoring and advising (Hillman & Dalziel, 2003). The theories suggest that the ability of a board to undertake these roles effectively depends on how they are structured (Linck, Netter & Yang, 2008). CMEF (2005) further suggests that MFI boards should be structured so that their members are beneficial to the organization's attainment of their dual objective.

We examined the determinants of board structure in East African MFIs (Kenya, Tanzania and Uganda). There are two reasons why we were motivated to study this region. First, Africa is recognized as the least developed continent in terms of microfinance, but has the biggest potential market for it (Consultative Group to Assist the Poor (CGAP, 2010)). Within Africa, East Africa is shown to be the most developed region in terms of microfinance. For example, CGAP (2010) reports that 30 percent of borrowers in Africa are from East Africa. Second, microfinance policy papers indicate that most international funding is channelled into East Africa (CGAP, 2010). We expected that this significant influence of international donors and capital providers would push MFIs in the region into having an effective governance and board structure.

We examined the association between three MFI characteristics (regulatory status, international influence and founder management) and three board structure dimensions (board size, board independence and board diversity). Hypotheses were tested using an unbalanced panel dataset of 63 MFIs, obtained through a survey conducted between January and August 2010. The data were analyzed using a mixture of analytical procedures. We used random effects estimation as the main analytical tool and regressed single measures of each board structure variable in relation to the MFI variables. To check robustness, we did joint estimations, using seemingly unrelated regression analysis, and to tackle endogeneity challenges, we performed a two-stage least squares regression with instrumental variables.

The results indicate that the structure of MFI boards is indeed determined by the MFI's unique characteristics. We found that large board size was determined by whether the MFI is regulated and whether it is exposed to international influence. These findings suggest that highly influential stakeholders, such as owners or international funders, have the power to be included on boards, which is a way for them to reduce agency costs. We showed that Founder-managed MFIs are associated with small boards. Regulated MFIs are shown to be associated with highly independent boards, while MFIs that are internationally influenced and those managed by founders have less independent boards. The results further showed that MFIs that are internationally influenced are associated with a greater diversity of nationalities, while those managed by founders are associated with higher gender diversity on their boards.

To our knowledge, this is the first study to address the determinants of MFI boards. We see this paper as providing a contribution in three areas. The first is in relation to boards and governance in MFIs, as little is known about MFI boards. Labie and Mersland (2011) suggest that governance structure is among the most important factors that help MFIs to sustainably offer financial services to the poor. Our study shows the factors that lead to a given choice of governance structure and, based on the agency and resource dependence theories, we suggest ways of improving that structure. Second, we contribute to an understanding of board selection and board members' roles in non-profit and mission-driven organizations. We show the roles played by board members in this industry and how they are achieved through a given structure. Third, we contribute to research on corporate governance in emerging markets, as the focus of our empirical study is East Africa.

The paper proceeds as follows. Section 2 presents the background to microfinance in East Africa. Section 3 presents the theoretical background, followed by section 4 which presents our hypotheses. Section 5 presents the data and methodology used. We present and discuss the results in section 6 followed by conclusions and implications in section 7.

2.0 MICROFINANCE IN EAST AFRICA

The East African countries chosen for this study were Kenya, Uganda and Tanzania. These countries share significant similarities in their legal and regulatory regimes (La Porta, Lopez-de Silanes & Shleifer, 2008) but are heterogeneous in terms of the development of their national microfinance industry. This combination of cross-country institutional similarity with industry variations makes East Africa a suitable environment for microfinance research, particularly in relation to other English common-law countries.

Microfinance operations in East Africa officially started in the 1990s (Randhawa & Gallardo, 2003) but there were microfinance-related activities before then. For example, the Uganda Finance Trust was established in 1984, and the Kenya Female Finance Trust in 1982. The number of microfinance activities and operators has increased dramatically over the last twenty years. CGAP (2010) reports that 3.3 million East Africans were borrowing from MFIs reporting to the MIX database, as of December 2009. The current major providers of microfinance services in East Africa can be divided into four institutional forms*: banks, non-bank financial institutions (NBFIs), cooperatives and non-profit MFIs, which are commonly referred to as non-governmental organizations (NGOs). Cooperatives have vastly different ownership forms and structures and are therefore not included in this study (Hartarska, 2005). For example, cooperative members vote for board members, who must be cooperative members themselves. This implies that the board structure of cooperative MFIs cannot be compared to those of other MFIs.

Another characteristic of the microfinance industry in East Africa is the existence of both domestically and internationally-funded/owned MFIs. MFIs with international partners, or those with international networks, have access to international funding and/or technical assistance in various areas. Commonly, fund providers influence the governance of these MFIs. For example, some funders specify how the board should be organized before they provide funding. Since the region receives extensive international attention, one might expect the governance structure of its MFIs to be more "developed" than that in regions with less international involvement.

The level of government regulation in East Africa is more extensive than in other African regions and this again makes the MFIs of this region particularly interesting. We argue that this adds to the pressure to put an effective governance structure in place. In terms of regulatory regime, for-profit MFIs are regulated by central banking authorities, while non-profit MFIs are not regulated. All MFIs are required to have boards. Furthermore, the boards of all regulated MFIs must satisfy certain requirements. As Table 1 shows, for the boards of regulated MFIs in Kenya, at least two-thirds of the members must not be affiliated to the MFI. In Kenya and Uganda, regulated MFIs are required to have at least five board members. Board diversity is not specified in the regulations, although there are general specifications about the roles, skills and expertise needed on boards.

* In these forms, banks and NBFIs are regulated by central banks and operate on a for-profit basis. NGOs are not regulated and operate on a not-for-profit basis. Cooperatives are regulated by a council of cooperatives and operate on a for-profit basis; we do not include these in our study.

Table 1: Requirements for Boards of Regulated MFIs

Aspects	Kenya	Tanzania	Uganda
Board size	Minimum: 5 members	Minimum: 2 members	Minimum: 5 members
Independence	Two-thirds of members not affiliated	Not specified	Not specified
Diversity	Not specified	Not specified	Not specified
Skills/expertise	Not specified	Banking, finance and support skills	Business-related skills
CEO=Chair	Not allowed	Not allowed	Not allowed
Roles	Monitor management activities and approve/review strategies	Provide direction, guidance and oversight	Ensure good corporate governance and organizational performance
Meetings per year	Minimum: 4	Minimum: 4	Minimum: 4

Source: Bank of Tanzania (2006), Bank of Uganda (2003), Central Bank of Kenya (2006)

Despite the guidelines, there is still significant flexibility in terms of how MFI board members are appointed (CSFI, 2011). Regulators only approve members who have been appointed by MFIs (CMEF, 2005). In Uganda, five of the biggest MFIs became regulated between 2005 and 2007, with the founder remaining the CEO in some cases. In Kenya and Tanzania, similarly, more than half of the MFIs are managed by their founders.

Unregulated non-profit MFIs in East Africa come in a mixture of sizes and also vary in terms of whether their founders are local or international. Locally-founded, non-profit MFIs are typically still managed by their local founders and, since they are unregulated[*], these founders have a great deal of influence over who sit on their boards. Internationally-founded non-profit MFIs have board structures that vary depending on where the MFI was originally based. It is common to find non-profit MFIs in Tanzania whose board-members are CEOs (or board members) of the same MFI in other countries.

Table 2 compares MFIs in East Africa with MFIs worldwide. The global data were obtained from the rating agencies at www.ratingfund1.org and include MFIs from 73 countries.

[*] In our dataset, 60 percent of unregulated (non-profit) MFIs are managed by founders (have founder CEOs).

Table 2: Comparing MFIs from Global Rating Reports with our East African Data

	Global Data: 379 MFIs (Mersland et al, 2011)		East African Data: 63 MFIs (our dataset)		
	Mean	Std. Dev	Mean	Std. Dev.	t-test diff
Regulated	0.25	0.43	0.39	0.49	-4.88**
Asset size (ln)	14.58	1.78	15.58	2.52	-6.96**
Age (years)	9.00	7.14	9.69	6.96	-1.65
International influence	0.33	0.47	0.66	0.47	-11.72**
Board diversity: Female- ratio	0.28	0.42	0.25	0.23	1.82
Founder Management-CEOs	0.38	0.52	0.54	0.49	-5.38**
Board size	7.23	3.57	7.18	2.24	0.33

** $p < .05$

Table 2 shows that, on average, MFIs in East Africa are somewhat similar to those worldwide in terms of age, gender diversity and board size. However, other characteristics are significantly different. In the East African industry, 66 percent of MFIs have international affiliations, a larger proportion than in the global dataset. A larger proportion of East African MFIs, 54 percent, are managed by founders, compared to 38 percent of the global dataset. Finally, there are significant differences between regulated MFIs in East Africa and those in the rest of the world.

3.0 THEORETICAL BACKGROUND

From the management and finance literature we know that boards serve two roles (Hillman & Dalziel, 2003). First, they advise managers on the organization's strategies, which is referred to as the resource and advisory role. Second, they monitor and control the performance of managers (Hermalin & Weisbach, 1991), which is referred to as the monitoring role. Similarly, in MFIs, board members are expected to fulfil a mixture of roles and responsibilities.

Looking at microfinance boards, Campion and Frankiewicz (1999) and Dorado and Molz (2005) suggest that MFI boards undertake the following roles simultaneously. First, the board oversees the various constituencies served by the MFI. Second, it establishes the reputation of the MFI, thereby helping to ensure external legitimacy. Third, the board attracts and mobilizes resources and expertise. It oversees the management, including the selection and removal of top managers. Finally, it assists in identifying the MFI's core mission and works to keep it on track. In addition, the microfinance literature suggests that the board itself is expected to change according to changing organizational priorities and environmental demands (Dorado & Molz, 2005). We grouped the first three roles together as resource and advisory roles, grounded in the resource dependence theory (Brown, Hillman, & Okun, 2011; Pfeffer & Salancik, 1978). The final two roles come under monitoring, which was guided by the agency theory (Fama & Jensen, 1983; Pant & Pattanayak, 2010). We used these theories to complement one another since they guide MFI board roles and help to explain the board structure that is most suitable for the fulfilment of these roles.

The premise of this paper, therefore, is that an appropriate board structure is necessary if MFI boards are to carry out their roles effectively. These ideas are highlighted in the microfinance practitioner literature, such as in Conger et al (1999) and CMEF (2005), both of which provide guidelines on MFI board structure in terms of composition, representation and size. Regarding composition, this literature suggests that board members should have social and commercial expertise, strategic and operational abilities, and legal and communication abilities. Furthermore, it suggests that these skills can be provided by a diverse group of board members, from both inside and outside the MFI. Outsiders (independent members) are particularly valuable as they provide the boards with an independent mindset and experiences they can share with other members (CMEF, 2005). Internally-recruited (dependent board members), like employees, and closely-related stakeholders (i.e., from sister organizations), and provide the benefit of MFI-specific knowledge (Dorado & Molz, 2005). Regarding board size, Conger et al (1999) argue that MFIs should balance the need for skills and resources with the logistical advantages of small boards. These suggestions imply that board structure matters in MFIs in order for members to undertake their roles effectively and to enhance the attainment of MFIs' dual objective. Based on these suggestions, theories and other arguments from past corporate research on board structure (e.g. Jackling & Johl, 2009; Linck et al, 2008), we chose to address three dimensions of board structure: board size, board independence and board diversity.

3.1 Board Size

Board size is an important dimension, as past research indicates that it influences board effectiveness. The literature suggests that large boards are associated with higher coordination costs and free-rider problems (Jensen, 1976; Yermack, 1996). These agency-theory-based arguments imply that relatively small boards operate more effectively, for example by being better at monitoring the CEO. For instance, Lipton & Lorsch (1992) argue that "when a board has more than ten members it becomes more difficult for them all to express their ideas and opinions". Similarly, Jensen (2010) conjectures that "keeping boards small helps improve their performance". In contrast, resource dependence scholars suggest that large boards are the source of various resources (Hillman, et al, 2009; Pfeffer & Salancik, 1978). From this perspective, board size is a measure of an organization's ability to form environmental links with secure critical resources. With different kinds of expertise more likely on large boards, CEOs will obtain better advice and resources.

Within the microfinance industry, we argue that board size should be determined in a way that facilitates attainment of MFIs' dual objective. A large board may enhance MFIs' access to resources while being weaker at monitoring the CEO. Microfinance policy papers advocate boards that are large enough to provide adequate monitoring and resources (CMEF, 2005; CSFI, 2011). Hartarska and Mersland (2012) indicate that MFIs with large boards are associated with better social performance. They argue that MFIs can benefit from having large boards although the effect can change after some time. Their results are consistent with the literature on banks and non-profit organisations, whose boards are found to be larger than conventional ones.

However, Mersland and Strom (2009) state that larger boards in the microfinance industry may induce members to free-ride in their monitoring responsibility, allowing CEOs greater independence. Similarly Hartarska (2005) shows that MFIs with small boards have better performance. She argues that, through their ability to monitor management, small boards contribute to better results. These studies provide evidence that MFIs can benefit from having both small and large boards, but there are some trade-offs between effective monitoring enhanced by small boards, and resource abundance enhanced by large ones. Since MFI board members fulfil both roles simultaneously, we argue that MFIs with large (small) boards benefit more (less) in terms of resources but are less (more) effectively monitored.

3.2 Board Independence

Board independence is important as it affects the ability of the board to monitor and provide resources to the management. The agency theory suggests that independent boards provide better monitoring and can better protect stakeholder interests (Fama, 1980). Jensen (2010) further suggests that, because inside (non-independent) board members are likely to be ineffective at monitoring and evaluating the CEO, the only inside member on the board should be the CEO. The resource dependence theory argues that independent boards are more likely to reduce uncertainties and bring linkages and resources such as funding, skills, information and access to key constituents like policy decision makers (Hillman et al, 2009). Raheja (2005) developed a model that takes into account both the monitoring and resource provision roles of the board and found that independent boards are beneficial to organizations.

On the other hand, Harris and Raviv (2008) demonstrate that, when insiders have important information relative to outsiders, insider-controlled boards are preferred. Insiders can be better sources of internal information but weak at monitoring. Baysinger (1990) demonstrated that insiders contribute to boardroom discussions in ways that external board members cannot because the former have knowledge of the organization's operations and capabilities.

In a young and entrepreneurial industry like microfinance, various stakeholders value clarity and strategic direction. Roche (2009) suggest that young entrepreneurial organizations need more legitimacy and greater acquisition of resources than mature organizations. Similarly, we argue that most MFIs are at the development stage where the need for resources is great (in line with the corporate governance life-cycle arguments of Filatotchev, Toms & Wright (2006) and Roche (2009). Also, as indicated in boards' roles, MFIs, regardless of their age, need board members that can oversee management and help the MFI mission to be on track.

This means MFIs can benefit from more independent boards, not only for better monitoring, but also because of the greater variety of resources that can be brought by outsiders (Dorado & Molz, 2005). Insiders, due to their specific knowledge, are also important and can better assist CEOs with defining and maintaining a strategic focus for the MFI. However, Hartarska (2005) and Hartarska and Mersland (2012) found that MFIs with boards dominated by insiders are not beneficial. This implies that the level of board independence is important for an MFI and should be determined so that it benefits in terms of resources and monitoring.

3.3 Board Diversity

Board diversity relates to a combination of attributes, characteristics and expertise that individual board members contribute to the board's activities. Similar to Walt and Ingley (2003), we define board diversity as the mix of human capital that a board comprises collectively and draws upon in undertaking its roles. This diversity is made up of age, gender, nationality, culture, religion, professional background, knowledge, technical skills, expertise and experience (Walt & Ingley, 2003). Both the agency and resource dependence theories advocate diverse boards (Brown, Hillman & Okun, 2012; Walt & Ingley, 2003). According to the agency theory, diverse boards are better able to monitor CEOs. The resource dependence theory suggests that diverse boards are better at linking the organization to external resources such as access to funding, and connections with competitors and the market. We focused on diversity in terms of gender (Adams & Ferreira, 2009) and nationality (Ruigrok, Peck & Tacheva, 2007) as these aspects contain a mixture of human capital.

Similarly, the microfinance literature advocates diverse boards (CMEF, 2005; Hartarska, 2005; Strøm, D'Espallier & Mersland, 2010). Gender diversity is especially important because of females constitute the main market for microfinance (Kyereboah-Coleman, 2006: Strøm et al, 2010). The objective of the Microcredit Summit Campaign, which plays a central role in promoting microfinance, is "to ensure that 175 million of the world's poorest families, especially females, have access to financial services" www.microcreditsummit.org. Mersland and Strøm (2009) also report that 73 percent of the customers in their global dataset are female. Similar to Mattis (2000), we suggest that there are benefits to increasing the number of women in leadership and board positions for organizations that market their products to women. Women's ability to contribute to boards may also be attributable to their different leadership styles. Strøm et al (2010), meanwhile, suggest that gender-diverse boards are important for the effectiveness of MFIs, and not only as a means of promoting democracy and equality.

In addition, past microfinance research highlights that female representation on boards can enhance MFIs' understanding of female customers' needs (Mersland & Strøm, 2009). Strøm et al (2010), for example, argue that female leadership and board members create a competitive advantage for MFIs due to their market orientation (i.e., females make up the majority of the MFI market). The authors further explain that female leaders may more easily tap into local information sources and help the MFI to create products that are better suited to its customers. Female leaders may also simply have better business acumen. Therefore, we expect MFI boards to be gender-diverse, so that MFIs can benefit not only from gender equality but also from the expertise, skills and experience of both genders.

Because of the high level of involvement of international organizations in the microfinance industry (Mersland et al, 2011), we see diversity of board members' nationalities as advantageous to MFIs. Board members from other countries (than the MFI's home country) are likely to possess a diversity of cultural values and preferences (Caligiuri et al, 2004). Diversity of nationalities provides the board with a broader range of information resources, skill sets and cultural capital.

4.0 HYPOTHESES DEVELOPMENT

The above review highlights that board size, level of independence and diversity matter and are important dimensions of MFI board structure. The question is, then, what are the factors that determine the choice of a certain board structure? Past corporate governance literature helps us to identify possible factors (Lehn, Patro & Zhao, 2009). Factors that have been widely studied are the organization's size, legal status and age (e.g. Alonso, Palenzuela & Merino, 2009; Linck et al, 2008). Since these factors are generic and mostly based on research in the corporate sector, we included them as control variables. Our contribution is to examine factors that we argue are unique to the microfinance industry, and subsequently we hypothesized and tested the relationship between these factors and board structure dimensions. We focused on three factors: regulatory status, international influence and founder management.

4.1 Effect of Regulatory Status

MFIs are either regulated by central banking authorities or are unregulated. Regulated MFIs have defined shareholders and operate on a for-profit basis (CMEF, 2005). Unregulated MFIs are NGOs and operate on a not-for-profit basis. Governance literature shows that non-profit organizations have large boards due to the fact that they lack owners with a monetary incentive to monitor their investments (Speckbacher, 2008). For example, Alonso et al (2009) showed that the average board size of a sample of non-profit organisations is eleven members.

Similarly, regulated organizations, such as banks, are shown to have large boards. Studies by Adams and Mehran (2003, 2008), for example, reported that the average size of a bank board is eighteen members. Regulated organizations have large boards due to the fact that they have a number of important constituencies who, according to the agency theory, sit on the boards to protect their interests (Adams & Mehran, 2008). Constituents can be shareholders, deposit holders, or other independent board members (who indirectly "help" regulators). Similarly, the resource dependence theory suggests that large boards are beneficial due to the resources that each member brings (Pfeffer & Salancik, 1978). Board members, in this case, are a tool for managing external dependencies and reducing uncertainties (Hillman, Cannella & Paetzold, 2000). Furthermore, the regulatory requirement in East Africa for example, see Table 1, requires boards to have at least five members, but sets no limit. Based on the above arguments, we suggest that regulated MFIs need to appoint more board members than non-regulated MFIs in order to protect shareholders' interests, and increase support for the organization by including key stakeholders that can be co-opted. Thus:

Hypothesis 1a: Regulated MFIs have larger boards than non-regulated MFIs

Unlike unregulated MFIs, regulated MFIs have defined shareholders who need to protect their interests by having independent boards who will monitor the management. Also, regulated MFIs have greater flexibility over leveraging and seeking funding from various sources (Hartarska & Nadolnyak, 2007). This means that regulated MFIs need to have board members who can support and assist them with leveraging and accessing funds. Hillman et al (2000) further argue that regulated organizations need the expertise and skills of independent members such as business experts, influential members of the community and support specialists, such as lawyers, in order to manage external dependencies. Furthermore, regulated MFIs in East Africa, for example, are required to have non-affiliated board members. Adams and Mehran (2008) examined banks' boards and showed that they are highly independent. This suggests that regulated MFIs, because they need to monitor management, attract outside resources and comply with regulatory requirements, will opt for more independent boards. Thus:

Hypothesis 1b: Regulated MFIs have greater board independence than unregulated MFIs.

Unregulated MFIs have been shown to focus more on social goals through serving female customers (Cull, Morduch & Demirguc-Kunt, 2009). The suggestion of Mattis (2000) and Strøm et al (2010) that industries that serve females need to have more females on their boards implies that unregulated MFIs may have more female board members than regulated MFIs. Furthermore, international donors provide more support to unregulated MFIs since these are non-profit organizations and to a large extent focus on social objectives (Mori &

Mersland, in press; Mersland et al, 2011). When international donors provide funds to MFIs, they monitor the usage of these funds by sitting on their boards (Mori & Mersland, in press). Steane and Michael (2001) provide further evidence that the boards of non-profit organizations are more diverse than corporate boards. Since unregulated non-profit MFIs focus more on social goals, and have more international donors than regulated for-profit MFIs, we expect their boards to be more diverse. Furthermore, regulated MFIs face regulatory requirements which prescribe board members' skills. This implies that regulated MFIs have less incentive to recruit diverse board members; they only recruit members who match the skills specified by the regulator. Therefore:

Hypothesis 1c: Regulated MFIs have less board diversity than non-regulated MFIs.

4.2 International Influence

There is a high level of international influence in the microfinance industry, which comes in various forms, such as networks, funding providers and international knowledge transfers (Mersland et al, 2011). CGAP (2010) reported that East African MFIs are strongly influenced by international partners (also see Table 2). International business research shows that the internationalization of organizations brings about better performance (Lu & Beamish, 2004; Mersland et al, 2011). This is achieved through, among other means, the provision of resources by international partners and better governance mechanisms (Ruigrok et al, 2007). Similarly, Sanders and Carpenter (1998) suggest that internationalization is a way of strengthening access to resources and the interdependence of organizations. Furthermore, Barroso, Villegas and Perez-Calero (2011) show a positive association between internationalized organizations and board size. We therefore suggest that MFIs that are influenced by international partners (who are members of international networks) are more likely to have larger boards, as this facilitates the transfer of resources such as funding, networks, information and skills by their international partners.

Hypothesis 2a: MFIs that are internationally influenced have larger boards than those that are not.

Typical international partners in the microfinance industry are large international NGOs, such as CGAP, FINCA international, Accion international and so forth (Rhyne, 2005). These partners play the role of initiating, funding and owning MFIs. They also participate in selecting MFIs' board members. Sanders and Carpenter (1998) argue that complexities, such as cultural differences and information asymmetries, arise from being associated with international partners. These complexities have implications for the agency relationships between the MFIs and their partners, enhancing the need for monitoring. In this case, we would expect international partners to require their partner MFIs to have more independent boards, hoping they would provide enhanced monitoring and better access to resources/networks. We further expect the internationally influenced MFIs to be more exposed to the governance practices of their international partners. Based on the above arguments we suggest that:

Hypothesis 2b: MFIs that are internationally influenced have greater board independence than those that are not.

Since most international networks and supporters of microfinance come from the developed world, they prefer MFIs to have diverse boards, as advocated by the political and social forces in their countries. CMEF (2005) provides guidelines for MFIs that collaborate with international partners. Among other things, they recommend that boards should be diverse in terms of gender and cultural background. As mentioned earlier, international affiliations bring cultural complexities, and board members with diverse backgrounds could help to reduce these complexities and enhance monitoring. Ruigrok et al (2007) further suggest that increased internationalization of organizations leads to a higher demand for diverse board members who possess the necessary knowledge and contacts in both local and foreign markets. We therefore expect internationally influenced MFIs (MFIs which are members of international networks) to have more diverse boards, since this could enhance monitoring and facilitate better access to resources.

Hypothesis 2c: MFIs that are internationally influenced have greater board diversity than those that are not.

4.3 Founder Management

Anecdotal evidence, as in the case of Muhammed Yunus and the Grameen Bank, indicates that founder CEOs are critically important organizational players in MFIs. The importance of founders could be due to the relatively young age of the industry (Boeker & Karichalil, 2002). Our East African dataset shows a median MFI age of eight years (Table 2). The implication is that a large number of founders are still present, and they exert a significant influence (Alonso et al, 2009). We argue that founder CEOs have a tendency to treat the organization as their “baby” and want to hold on to it and control it for as long as possible. This was further exemplified in the recent struggle between the Bangladeshi government and Muhammad Yunus, regarding whether the latter should hold on to a board position within Grameen Bank (Burke, 2011).

Corporate research shows that organizations with active founder CEOs have different agency issues, and that such CEOs have an influence over the choice of board structure (Boeker & Karichalil, 2002; Randøy & Goel, 2003). This is due both to their formal position and their history within the organization. Wasserman (2003) suggests that founder CEOs exert power through board seats and over strategic decision making. The agency theory advocates small boards since they are better monitors of CEOs (Yermack, 1996). Monitoring might not be in the interests of founder CEOs, but they opt for small boards in order to exert greater control over board decisions (Daily & Dalton, 1993). The literature also provides evidence that founder-managed for-profit organizations are associated with small boards due to their founders’ attachment and need to control the organization (Certo, Covin, Daily & Dalton, 2001). We therefore suggest that founder CEOs do not want to lose their control, power and influence and thus opt for small boards.

Hypothesis 3a: Founder-managed MFIs have smaller boards than non-founder managed MFIs.

Corporate research in developed countries suggests that inside board members are an important complement to CEOs (Certo et al, 2001). Founder CEOs believe that inside board members can provide organization-specific information that outside board members may lack (Certo et al, 2001). This is in line with resource dependence theorists, who claim that insiders are valuable for supplying the board with specific information about the firm’s competitive environment (Hillman et al, 2000). However, founder CEOs are likely to be less objective in assessing their organizations. Similarly, as founder CEOs need to maintain their influence and power, they are more likely to opt for more insider board members, whom they can control more easily (Boeker & Karichalil, 2002). Daily and Dalton (1993) posit that insiders are unlikely to aggressively monitor and evaluate CEO actions due to their subordinate position in the organization. Similar to the corporate world, we argue that CEO founders in the microfinance industry want to maintain their power, influence and control, and therefore opt for less independent boards. This influence can be seen in Table 2. Nelson (2003) further shows that organizations managed by founders are less independent, which results in less monitoring and a high degree of CEO influence. We thus expect MFIs with founder CEOs to have more insiders on their boards as this facilitates the CEO-board influence and access to organization-specific resources.

Hypothesis 3b: Founder-managed MFIs have less independent boards than non-founder-managed MFIs.

Diverse boards might enhance monitoring since the CEO is less able to control the board's decision making. In order to maintain his influence, a CEO founder might opt for a less diverse board. As Johannisson and Huse (2000) argue in relation to family-based organizations (many of which can be compared to other founder-influenced organizations), "it is the CEO, not the shareholders, who recruit board members, and when you recruit people, you recruit people in your own image, people you trust and can easily communicate with". This implies that founder CEOs use their connections and invite people from their networks onto their boards. Founder CEOs are also likely to invite members they think will be easy to influence, so that decisions can be made in their favour. Diverse board members will be less dependent on the CEO and could provide contrasting views and discipline the management as needed (Walt & Ingley, 2003; Fama & Jensen, 1983). Despite the benefits brought by diverse boards, we expect to find that the boards of MFIs managed by their founders are less diverse, as this enables CEOs to maintain their control, power and influence.

Hypothesis 3c: Founder-managed MFIs have less board diversity than non-founder-managed MFIs.

Table 3 below summarizes the stated hypotheses and their expected signs.

Table 3: Summary of the Hypotheses

Board Structure variables	MFI Characteristics		
	Regulated	Internationally-influenced	Founder-managed
Board Size	+	+	-
Board Independence	+	+	-
Board Diversity (gender & nationality)	-	+	-

5.0 METHODOLOGY

5.1 Sample and Data Collection

The major source of data for this study was a hand-collected survey, conducted by one of the researchers between January and August 2010. The researcher contacted umbrella associations of MFIs in the respective countries and obtained MFI directories. These directories included information on MFI and CEO names, MFI locations and addresses. The researcher identified all of the MFIs listed in the directories, excluding cooperatives. Then, she contacted the CEOs of the identified MFIs and, out of 103 MFIs contacted, 49 (47.6 percent) were willing to participate. The MFIs that were unwilling to participate gave reasons such as the following: the CEO needed permission from the board chair in order to approve our visit (which he/she was not willing to do); others said that their information was confidential and could not be shared for research purposes.

The researcher visited the headquarters of the MFIs that were willing to participate, and the CEOs provided information based on the checklist of questions about governance, board demographics and MFI operations. The researcher further requested audited financial statements for the years 2004 to 2009 from each of the MFIs visited. Additionally, the researcher used the snowball sampling technique (Saunders, Lewis & Thornhill, 2003), whereby, when visiting an MFI, she asked the CEO to provide contact details of another MFI, which could have been on our original list or not. The researcher visited any MFIs that fitted her categorization (i.e., that were not cooperatives and had audited financial statements).

The researcher also visited the websites of some of the MFIs that publish information on governance and audited financial reports. To further check the quality of our information, we compared the information from these websites with that obtained from the CEOs. The data collection process led to a total of 63 MFIs (a mixture of local and international), board demographic information, and financial information for six years. Some MFIs did not have all the information needed and therefore our dataset is an unbalanced panel of 63 MFIs, with 343 observations in total (Wooldridge, 2006).

These MFIs probably represent between a quarter and a third of MFIs in the region. We recognize that, since most of the data were based on MFI directories, it is possible that some were left out and that we have some sample bias. However, we argue that our sample of MFIs represents the major and most established players in the region’s microfinance industry.

5.2 Variables and Measures

Dependent Variables

The dependent variables are based on three board structure dimensions and measured at the end of each year. ***Board size*** is measured as the logarithm of the number of board members (Linck, et al, 2008). ***Board independence*** is measured as the proportion of board members who are not current or former employees (or initiators) of the MFI or members of their families (Wagner III et al Linck et al, 2008; 1998). We measured board diversity using two variables: ***gender diversity***, defined as the ratio of female members to the total number of board members (Adams & Ferreira, 2009) and ***diversity of nationalities***, measured as the ratio of foreign members to the total number of board members (Caligiuri et al, 2004). Data on these variables were compiled from CEOs' responses to questions about board members' demographics and, in some cases, the MFIs' websites.

Independent Variables

The independent variables are the MFIs' characteristics. Data on these variables were obtained from the CEOs' responses. ***Regulated*** was measured as a binary variable equal to one if the MFI is regulated and zero otherwise. Here, we asked the CEOs whether the MFI was regulated by central banking authorities and if so when it began to be regulated. ***International influence*** was measured as a binary variable equal to one if the MFI is a member of any international network or organization that is based outside the MFI home country and zero otherwise (Mersland et al, 2011). The CEO here was asked whether the MFI was a member of any international organization or network, and for what purpose. ***Founder management*** was measured as a binary variable equal to one if the CEO of the MFI was also the founder of it (Boeker & Karichalil, 2002). The data here were obtained from the CEOs, by asking whether or not they were a founding CEO.

Control Variables

As mentioned earlier, and in line with previous studies on corporate governance, we included control variables that also affect board structure. Since organization size relates to possible economy of scale effects, we controlled for ***MFI size***, measured as the logarithm of total assets (Al-Najjar, 2011). Age is related to changes caused by organizational life-cycle changes (Filatotchev et al, 2006) and therefore we included ***MFI age***, measured as the number of years since the MFI began providing microfinance services. We also controlled for ***legal status***, using a binary variable, equal to one if the MFI is an independent legal organization or a branch of another organization abroad and zero otherwise (Mori & Mersland, in press). Data for these variables were obtained from the audited financial statements and CEO responses. We also employed ***country dummy*** and ***time dummy*** variables in order to capture variations in economic development and time.

5.3 Data Analysis

Since our dataset was an unbalanced panel over six years, we could have used either a fixed effects or a random effects model, depending on the time invariance of the variables (Greene, 2008). A fixed effects regression should be used when one wants to control for omitted variables that differ between cases (MFIs) but are constant over time. It allows the variables to change over time so that one can estimate the effects of the independent variables on the dependent variable (Wooldridge, 2006). Some omitted variables may be constant over time but vary between cases, and others may be fixed between cases but vary over time. To tackle this challenge, one can use random effects in order to take both situations into consideration and obtain efficient estimators. To choose between the two models, we ran a Hausman test (Hausman, 1978) to test the null hypothesis that the coefficients estimated by the efficient random effects estimator are the same as those estimated by the consistent fixed effects estimator. The results (unreported) of this test failed to reject the null hypothesis. We therefore used the random effects model, with the generalized least squares (GLS) estimation methodology as the main analysis technique.

6.0 RESULTS

6.1 Descriptive Results

Table 3 presents summary statistics of the variables used. On average, an MFI has seven board members; the minimum number of members is two and the maximum is fourteen. The average proportion of independent board members is 37 percent, which implies that most boards are less independent and dominated by insiders. In terms of board diversity, we see that 25 percent of board seats are held by females and 23 percent by foreign members. Regulated MFIs make up 39 percent of the MFIs in our sample, while 66 percent are under some form of international influence, either in terms of their main donor/funder or other key relationships. The results also show that 54 percent of the MFIs are managed by founders. The average age of the MFIs is 9 years and 76 percent of them have their own legal status. Kenyan MFIs make up 34 percent of the sample, Ugandan MFIs 30 percent and Tanzanian 36 percent.

Table 4: Descriptive Statistics

Variables	Mean	Std. Dev.	Min	Max	N
Dependent variables					
Board size	7.18	2.24	2.00	14.00	331
Board size (ln)	1.92	0.35	0.69	2.64	331
Board independence-ratio	0.37	0.26	0.00	1.00	325
Board diversity: female-ratio	0.25	0.23	0.00	1.00	320
Board diversity: nationality-ratio	0.23	0.33	0.00	1.00	331
Independent variables					
Regulated	0.39	0.48	0.00	1.00	328
International influence	0.66	0.47	0.00	1.00	343
Founder management	0.54	0.49	0.00	1.00	315
Other variables					
MFI size (ln assets)	15.58	2.51	8.41	24.90	255
Age (years)	9.69	6.96	2.00	31	311
Internationally-initiated	0.27	0.44	0.00	1.00	343
Legal status	0.76	0.39	0.00	1.00	330
Operating self-sufficiency	104.35	42.41	6.42	521.87	256
Number of customers	35742	74917	2.00	715969	220
Number of customers (ln)	9.47	1.56	3.13	13.48	220
Kenya	0.34	0.47	0.00	1.00	343
Uganda	0.30	0.45	0.00	1.00	343
Tanzania	0.36	0.49	0.00	1.00	343

Table 4 presents the correlations between the variables. First, we looked at correlations between the board structure variables. Although we argue that these variables are separate constructs, it is not surprising that they are significantly related, as they are all measures of different aspects of board structure. In the multivariate tests, we ran separate regressions for each dimension (Table 6), but also, as a robustness check, we performed a joint test using all variables simultaneously (Table 7).

The correlates provide a first simple test of our hypotheses and we see that a number of them are consistent with our hypotheses. For example, the variable for *regulated* MFIs is positively and significantly correlated with *board size* (coefficient: 0.35, $p<0.01$), while the variable for *founder-managed* MFIs is negatively correlated with both *board size* (coefficient: -0.31, $p<0.01$) and *board independence* (coefficient: -0.23, $p<0.01$), as hypothesized. We also see significant correlations between board structure and control variables. For example there is a positive correlation between *board size* and *age* (coefficient. 0.49), between *board size* and *MFI size* (coefficient. 0.41) and between *board independence* and *MFI age* (coefficient. 0.32). Because of these significant correlations, we controlled for these variables in the regression models.

As we prepared for the multivariate tests, we turned to the question of multicollinearity among the independent variables. Correlation coefficients among the independent variables were rather low, with the highest being between *regulated* and *legal status* (coefficient: 0.51, $p<0.01$). Kennedy (2008) holds that correlations need to be above 0.7 to detect multicollinearity between the two variables. None of the coefficients were this high but significant coefficients are a warning signal that multicollinearity problems may arise. Therefore, variance inflation factors (VIF) are used to test for multicollinearity. The results, as shown in Table 4, range between 1.27 and 2.21, suggesting that multicollinearity was not a problem in our study (Neter, Kutner, Nachtsheim & Wasserman, 1996).

Table 5: Pearson Correlations for Variables in the Regression Model

Variables	N	1	2	3	4	5	6	7	8	9	10	11	12	VIF
1. Board size (ln)	331	1.00												
2.Board independence	325	0.41**	1.00											
3.Diversity: gender	320	0.12*	-0.34**	1.00										
4.Diversity: nationality	331	0.01	0.32**	-0.21**	1.00									
5.Regulated	328	0.35**	0.09	-0.04	0.12*	1.00								2.21
6.International influence	331	0.24**	-0.09	0.17**	0.19**	-0.04	1.00							1.38
7.Founder management	315	-0.31**	-0.23**	0.04	0.04	-0.13*	-0.13*	1.00						1.27
8.Age	311	0.49**	0.32**	0.36**	-0.08	0.45**	0.12*	-0.27**	1.00					1.93
9.Size	255	0.41**	0.03	0.04	0.03	0.46**	0.06	-0.30**	0.50**	1.00				1.73
10.Legal status	330	0.17**	-0.13*	-0.07	0.08	0.51**	0.03	-0.04	0.23**	0.46**	1.00			1.98
11.Kenya	343	0.03	0.13*	0.06	-0.19**	-0.08	-0.02	0.17	0.19**	0.09	0.26**	1.00		1.79
12.Uganda	343	-0.02	-0.01	-0.06	0.08	0.10	-0.01	-0.09	0.01	0.02	-0.18**	-0.47**	1.00	1.47

*** p < .05 ; ** p < .01**

6.2 Regression Results and Discussion

Table 5 reports the regression findings for the random effects estimations. Model 1 reports the results for board size, model 2 for board independence, model 3 for gender diversity and model 4 for diversity of nationalities.

MFI Regulatory Status

The first hypothesis concerns the effect of regulatory status on board structure. Table 5, model 1 provides support for hypothesis 1a, which relates regulation to board size. Regulated MFIs have larger boards than unregulated MFIs (coefficient: 0.09, $p<0.05$). Interestingly, this is in line with Adams and Mehran's (2003, 2008) findings for US banks. Despite the fact that unregulated MFIs have a broader set of stakeholders, regulated MFIs need larger boards to assist them by bringing intellectual knowledge to improve decision making, increase support for the MFI, and in turn boost organizational performance (Jackling & Johl, 2009).

Model 2 provides support for hypothesis 1b, which deals with board independence (coefficient: 0.06, $p<0.10$). This is in line with the corporate literature that argues that regulated organizations need the expertise and skills of independent board members (Hillman et al, 2000). However, we do not know whether these independent board members *really* add expertise and skills, or whether they merely make the MFI "look good" in the eyes of the regulators.

We found evidence of partial support for hypothesis 1c, stating that regulated MFIs have less diverse boards. In regard to gender diversity, model 3 shows support (coefficient: -0.02, $p<0.10$) while diversity of nationalities is not supported in model 4 (coefficient 0.08, not significant). This suggests that regulated MFIs have fewer female board members. One possible explanation could be that regulated MFIs need to comply with regulatory requirements (banking and business expertise) that are less prevalent among female board candidates. This is also in line with studies from the corporate sector in developed countries, that a lack of high-level business experience reduces women's chances of being appointed to boards (Ruigrok et al, 2007). The evidence, however, contradicts the agency and resource dependence theory, which advocate board diversity as a better tool for organizational performance (Walt & Ingley, 2003). From these results we argue that regulated MFIs have less incentive to recruit diverse board members.

International Influence

The second set of hypotheses looks at the relationship between international influence and board structure. Hypothesis 2a, addressing the relationship between international influence and board size, is supported in model 1 (coefficient: 0.16, $p<0.01$). This suggests that, when international actors from the global North are substantially involved in an MFI, they opt for larger boards. We deduce that they do so in order to provide the funding, skills, networks, technical assistance and information needed for long-term MFI survival (Mersland et al, 2011). Furthermore, as international supporters provide resources to MFIs, they also need to sit on their boards to control the usage of their resources, which therefore enlarges board size.

Contrary to the prediction in hypothesis 2b, model 2 shows a significantly negative effect of international influence on board independence (coefficient: -0.09, $p<0.05$). One possible explanation for the lower level of board independence when the MFI has international partners could be that MFI board insiders could be helpful in providing organization-specific information and enhanced decision making (as argued in the case of the corporate sector by (Wagner, Stimpert & Fubara, 1998). Secondly, the results suggest that MFIs that are influenced by international actors could potentially also be influenced by their CEO founders and, therefore, these CEOs prefer insider-dominated boards. To cross-check this, we reran the regression to test whether there is an interaction effect between *international influence-founder CEO* and *board independence.* The results show that, out of the 66 percent of MFIs in our sample that are internationally influenced, 38 percent are managed by founders. By rerunning the model with this interaction variable (unreported), the regression results support the existence of such an effect (coefficient: -0.06, $p<0.05$). We therefore conclude that internationally-influenced MFIs have less board independence, possibly due to the information advantage of board insiders and the CEO founders' strong position within MFIs.

Hypothesis 2c, regarding the relationship between international influence and board diversity, is partially supported. Model 3 does not show significant results in regard to gender diversity (coefficient: 0.06, not significant). This is surprising, as we expected international partners to advocate gender-balanced boards, as suggested by the literature and investors from the global North (CMEP, 2005; Rhyne, 2005). Model 4, however, provides statistically and economically significant results in relation to diversity of nationalities (coefficient: 0.23, $p<0.001$). This is in line with the corporate literature, suggesting that international board members help to reduce cultural complexities and enhance monitoring (Aguilera & Jackson, 2003).

Founder Management

Hypothesis 3 addresses the relationship between founder-managed MFIs and board structure. Model 1 provides support for hypothesis 3a, that founder-managed MFIs are associated with small boards (coefficient:-0.06, $p<0.10$). In line with the findings in the corporate literature (Boeker & Karichalil, 2002; Certo et al, 2001), we argue that founder-managed MFIs are associated with small boards due to their founders' attachment to the organization and their ability to control the organization. One possible reason why founder CEOs opt for small boards could be that it is easier for them to influence small boards and be accountable to fewer board members. For example, when a CEO seeks the board's consent, it is easier for him to speak informally to a small number of individual members.

Regarding the relationship between founder-managed MFIs and board independence, model 2 provides evidence in support of hypothesis 3b (coefficient: -0.07, $p<0.01$). One explanation could be that founder CEOs believe that inside board members provide an additional source of MFI-specific information, which outside board members would not. Another possibility could be that founder CEOs prefer less board independence, as this makes it easier for them to maintain their power, influence and control (Boeker & Karichalil, 2002). This was also shown by Nelson (2003), who found that corporate organizations managed by founders prefer less board independence, which results in less vigilant board monitoring and greater CEO influence.

Regarding the relationship between founder-managed MFIs and board diversity, model 3 provides evidence contrary to the relationship we propose in hypothesis 3c. We expected that founder-managed MFIs would be negatively associated with gender diversity. However, our findings show a significant positive relationship (coefficient: 0.05, $p<0.10$). This suggests that founder-managed MFIs prefer board gender diversity, which could be explained by the founder's desire to achieve the social goal of the MFI; he/she thus uses female board members' skills to emphasize female outreach (Strøm, et al, 2010; Mersland and Strøm, 2009). The high level of openness to female board membership could also be a reflection of the high proportion of female founder CEOs in the industry. It is possible that female founder CEOs want to maintain their influence, and find this easier to achieve if they invite their female friends onto their boards. To check this further, we ran a regression with an interaction variable for *female-founder CEO and gender diversity*. The unreported results (coefficient:

0.23, p<0.001) show similar results to those described above, namely that female-founder CEOs are positively associated with board gender diversity.

In line with our prediction, model 4 provides evidence that founder-managed MFIs are associated with less board diversity in terms of nationalities (coefficient: 0.05, p<0.05). Since diversity of nationalities might bring more independent monitoring of the CEO, and potentially more complex and slower decision making, a powerful founder CEO might not see it as in his or her interests to advance international board membership.

Table 6: Results of Random Effects GLS Regression

Variable	**Board Structure**							
Independent Variables	**Model 1: Size**		**Model 2: independence**		**Model 3: gender**		**Model 4: nationalities**	
	Coef	**Z**	**Coef**	**Z**	**Coef**	**Z**	**Coef**	**Z**
Regulated	0.09*	1.74	0.06+	1.32	-.02+	-1.51	0.08	1.09
International influence	0.16**	2.02	-0.09*	-1.83	0.06	0.98	.23***	3.54
Founder management	-0.06+	-1.07	-0.07**	-2.65	0.05+	1.45	-0.05*	-2.40
Control variables								
Size	0.02	1.32	-0.01	-0.94	-0.01	-1.04	-0.02	-0.97
Age	0.02**	3.71	0.02**	2.46	0.02**	3.09	-0.01	-0.85
Legal status	0.01	0.12	-0.08	-1.29	-0.04	-0.68	0.08	1.09
Kenya	-0.16+	-1.64	0.04	0.50	-0.01	-0.04	-0.16	-2.00
Uganda	-0.14	-1.52	-0.05	-0.69	-0.04	-0.49	-0.03	-0.43
Year dummies		Yes		Yes		Yes		Yes
R^2		0.39		0.24		0.21		0.25
Chi^2		42.16		24.09		18.00		34.25
N		235		235		231		235

+ p < .10; * p < .05; ** p < .01; *** p < .001

In summary, our results show that there are multiple associations between the unique characteristics of MFIs and their board structures. We found evidence that internationally influenced and founder influenced East African MFIs tend to produce a board structure that is more suitable for accessing resources mainly from insiders than for monitoring and accessing resources from outsiders. This is not the case for regulated MFIs. We also showed the significant impact founder CEOs have on board structure, which suggests that these leaders have substantial power within the organizations and with their key stakeholders. These findings might reflect the youth of the industry and organizational life-cycle effects (Filatotchev et al, 2006; Roche, 2009) suggesting that as the industry matures the effect might change. As is also evidenced from the effect of our control variables, age is positively associated with board independence and board diversity.

We also saw this effect of founder CEOs and MFI life-cycle effects when we cross-checked and reran the regressions (unreported), after dividing the sample into two subsamples based on the median MFI age of eight years. The CEO-founder effect is stronger in the sub-sample of MFIs under eight years old than it is in MFIs over eight years old. This implies that, as MFIs grow older, CEO founders are more likely to step down and MFIs will tend to attract more independent and diverse boards.

6.3 Robustness

As part of our robustness checks, we reran the models. First, we used panel data estimation with the seemingly unrelated regression (SUR) methodology (Greene, 2008; and was previously applied to microfinance by Mersland et al, 2011), a procedure that takes account of possible correlations among dependent variables. We also performed a Breusch-Pagan test to check the extent to which the residuals in the SUR regression were independent. The results are reported in Table 6.

A common challenge in corporate governance research is the issue of possible reverse causality. Our second robustness check was to rerun all models using instrumental variables with a two-stage linear regression (2SLS). The methodological concern here was the possibility of an omitted unobservable variable that affects both independent and dependent variables (Adam & Ferreira, 2009). The literature shows that many of the variables of interest in corporate governance investigations are not truly exogenous, that is they are determined completely outside the model systems but are endogenous (Hermalin & Weisbach, 2003). Carter et al (2010) suggest that we can use lagged performance variables as instruments even though they are not completely outside the system of equations. We followed their suggestions and use lagged variables of MFI performance. We used lagged operational self-sufficiency[*] and lagged number of customers[†] as our instruments. We tested the correctness[‡] of these instruments (Cheung, Connelly, Limpaphayom & Zhou, 2007) and ran a 2SLS (Wooldridge, 2006). The results are presented in Table 7.

The results in both Table 6 and Table 7 are to a large extent similar to the main results of most of the hypothesized relationships. We showed that regulated MFIs are associated with large boards and a lack of board gender diversity, and that internationally-influenced MFIs have larger and less independent boards. Also, international influence has no significant association with board gender diversity, but does have a positive relationship with diversity of nationalities. Overall, we highlight that our results show that there is a need to address the three dimensions of MFI board structure individually, and that our random effects model is efficient.

[*] Operational self-sufficiency (OSS) is a financial performance measure that is widely used in the microfinance literature. It measures the ability of the organization to cover its operating costs using interest income. It is computed as operating revenue / (financial expenses + loan loss provisions + operating expenses). High OSS means better financial performance.

[†] Number of customers is used as a proxy for measuring the social performance of MFIs. Many customers means greater outreach to the poor and better social performance.

[‡] Following Cheung et al. (2007), we test for the correctness of the instrument as follows. We first run OLS for each dependent variable with independent variables. Then we estimate residuals for each dependent variable. Afterwards, we correlate the residuals with the endogenous-independent variables and suggested instruments. The results show that the instrument variables correlate significantly with the endogenous variables but not with the dependent variables' residuals.

Table 7: Results of Seemingly Unrelated Regression

Variable	Board Structure							
	Model 1: Size		**Model 2: Independence**		**Model 3: Gender**		**Model 4: Nationalities**	
Independent variables	**Coef**	**Z**	**Coef**	**Z**	**Coef**	**Z**	**Coef**	**Z**
Regulated	0.16***	3.54	0.09**	2.27	-0.08*	-2.02	0.06	1.13
International influence	0.19***	5.52	-0.09***	-3.13	0.04	1.42	0.24***	5.12
Founder management	-0.06+	-1.60	-0.08***	-3.26	0.09***	3.11	-.07+	-1.72
Control variables								
Size	0.02	1.73	-0.01	-1.60	-0.01*	-1.94	-0.01	-1.36
Age	0.01***	4.98	0.01***	3.87	0.02***	5.80	-0.01	-2.05
Legal status	-0.14**	-3.05	-0.13**	-3.35	0.00	0.01	0.11	2.10
Kenya	-0.06	-1.28	0.11*	3.00	-0.05	-0.33	-.19***	-3.80
Uganda	-0.15	-3.62	-0.00	-0.04	-0.01	-0.31	-0.09*	-1.83
Year dummies		Yes		Yes		Yes		Yes
R^2		0.46		0.28		0.25		0.26
Chi^2		197.84		91.41		75.26		80.69
N		231		231		231		231

Correlations of Residuals

	Board size	Board independence	Gender diversity	Diversity of nationalities
Board independence	0.35			
Gender	-0.06	0.34		
Nationalities	-0.09	-0.28	-0.28	
Breusch-Pagan Chi^2 (3)	93.99			

+ p < .10; * p < .05; ** p < .01; *** p < .001

Table 8: Results of a Two-Stage (2SLS) Regression

Variable	Board Structure							
	Model 1: Size		**Model 2: Independence**		**Model 3: Gender**		**Model 4: Nationalities**	
Independent variables	**Coef**	**t**	**Coef**	**t**	**Coef**	**t**	**Coef**	**t**
Regulated	0.84**	2.05	0.33	1.12	0.04	0.13	-0.29	-0.70
International influence	0.31^{+}	1.60	-0.25^{+}	-1.67	0.28	0.79	0.52^{+}	1.99
Founder management	-0.15*	-2.04	-0.10*	-1.97	0.06^{+}	1.53	-0.07	-0.99
Control variables								
Size	0.01	0.20	-0.09*	-1.73	-0.06	-1.8	-0.01	-0.25
Age	0.01	0.13	0.01^{+}	0.11	0.03***	3.19	-0.01	-0.27
Legal status	-0.51***	-2.23	-0.28^{+}	-1.32	-0.08	-0.53	0.29	1.21
Kenya	0.19	1.40	0.22*	1.40	-0.01	-0.06	-0.28*	-2.11
Uganda	-0.20	-2.42	-0.05	-0.90	-0.06	-1.01	-0.08	0.36
Instruments	Operational self-sufficiency; number of customers							
R^2					0.14			
F stat	4.82		4.38		4.06		3.40	
N	163		163		163		163	

+ p < .10; * p < .05; ** p < .01; *** p < .001

7.0 CONCLUSIONS AND IMPLICATIONS

This study examined the determinants of board structure in MFIs. Guided by the agency and resource dependence theory, we examined three unique characteristics of MFIs: regulation status, international influence and founder management. Using a sample of 63 East African MFIs, we showed the relationship between these characteristics and three dimensions of board structure: board size, board independence and board diversity (gender and nationality). We used a mixture of analytical procedures to obtain valid and robust results.

The results showed that there are significant associations between MFI characteristics and board structure. We found that MFIs that are regulated have larger boards, high board independence and less gender-diverse boards. The lower diversity in regulated MFIs might be due to the expertise demanded by the regulators (see Table 1), or it could reflect discrimination against females. This needs to be further explored in future studies. Similarly, MFIs that are internationally influenced have larger boards, more international boards, and less independent boards. Past research highlights that MFIs' international partners establish connections with MFIs in order to provide them with resources, such as funding, and international experience, through technical assistance and advice (Mersland et al, 2011). Founder-managed MFIs show similar characteristics to those demonstrated in the corporate founder-CEO literature (Certo et al, 2001). These results have various implications.

7.1 Implications for Theory

In this study, we applied the agency and resource dependence theories as complementary theories in studying the microfinance industry. Past studies on board structure mostly applied these theories in relation to large for-profit organizations in developed countries (Jackling & Johl, 2009; Linck et al, 2008). We showed that these theories can be applicable to research on a young entrepreneurial industry like microfinance, about which corporate governance research is still very limited (Mersland & Labie, 2011).

To our knowledge, we are among the first to highlight the relevance of the resource dependence theory for examining corporate governance in MFIs, though several studies have used the agency theory (Hartarska, 2005; Mersland & Strøm, 2009). The resource dependence theory is particularly useful for understanding microfinance, due to the common dual objective of MFIs (financial sustainability and having a social mission), and the need for MFIs to obtain access to key stakeholders (fund providers, community leaders, etc.). As stated by Pfeffer and Salancik (1978:1), "to understand the behaviour of an organization you must understand the context of that behaviour". This means that to understand the behaviour and structure of MFIs, there is a need to first understand the context and environment of the microfinance industry.

Agency-theory-based studies commonly suggest that small and independent boards are better at monitoring organizations, particularly their CEOs. We found that CEO founders do not like such "controls" and that the CEOs' ability to affect the choice of board structure indicates that they are able to exercise power over MFIs. We therefore argue that, despite the commonly emphasized monitoring benefits of having small and independent boards, the social mission attachment of the founder CEO might make "strong" monitoring less necessary, as is the case in founder-managed for-profit organizations (Randøy & Goel, 2003).

There is still relatively little corporate governance research from emerging economies and Africa in particular (Rossouw, 2005). This study indicates that the agency theory and resource dependency theory are useful for understanding boards in an emerging market context such as East Africa.

7.2 Implications for Practice

The CSFI (2011) reported that corporate governance is one of the major challenges facing African MFIs. One highlighted challenge is the lack of board independence. We found this lack in both internationally-influenced and founder-influenced MFIs, but we argue that this lack of board independence is due to the industry's newness and we suggest that this will need to change as MFIs grow. As the CEO of one East African MFI put it, "four years ago, the board's role was largely advisory. Now, stakeholders expect it to take a more active role, especially in monitoring and risk control. We need to draw more on the specialized expertise of outside members" (CMEF, 2005). MFIs should also be aware that board insiders are a source of organization-specific information (Wagner et al, 1998) and help with the strategic direction of the MFI. However, we suggest that their presence on boards should not be so overwhelming as to make monitoring difficult.

Another practical implication relates to regulation. Currently, some public policy suggests that MFIs should change from operating as NGOs on a not-for-profit basis to being regulated and operating on a for-profit basis (Hartarska & Nadolnyak, 2007). MFIs should be aware that this type of change will have implications for the board structure, not only through regulatory requirements (see Table 1), but also because the owners/trustees (or other legal bodies in charge) will have to focus on recruiting board members who can assist with monitoring and provide access to resources.

In this study, we found evidence of the strong influence of CEO founders on MFI board structure. We urge MFI founders, as their organizations grow, to make room for independent boards, so that the CEO does not limit the MFI's access to new people with new ideas (Boeker & Karichalil, 2002). There is some evidence in the corporate literature that some founders might stay on too long (Filatotchev et al, 2006; Wasserman, 2003), and the owners/trustees of MFIs should be aware of this challenge and be ready to replace CEO founders if necessary.

With the financial crisis in the global North, the ability of international partners to support MFIs might diminish and MFI governance structures should reflect this risk. Specifically, MFIs should seek to recruit board members who provide strong links with multiple stakeholders, so that they can work more independently from past or present major donors/owners.

7.3 Limitations and Direction for Future Research

This study has several limitations. First, we used only a few dimensions of board structure. There are other board structure dimensions that we did not consider, and which probably would be useful to consider when researching microfinance. Dimensions such as the education, age and expertise of board members (e.g. in Ruigrok et al, 2007) and CEO duality could be considered in future studies.

The independent variables (regulations, international influence, and founder management) chosen for this study might be explored in more detail: for example, the cultural and institutional distance between the MFI and its international partner/network, the specific background of the CEO founder, the content of the regulations, and finally, a more detailed picture of the MFIs' customer environment. In addition, there might be other determinants of board structure that should be considered in future studies, for example the nature of the corporate governance environment (such as the legal regime), and the level of financial development of the country.

In this study we found, surprisingly, that international influence brings less board independence. Corporate governance policies, in general and also in the microfinance context, advocate *greater* board independence in order to reduce information asymmetries between owners/trustees and management. Future research should therefore address this paradox.

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ESSAY 2

BOARD COMPOSITION AND OUTREACH PERFORMANCE OF MFIs

Board Composition and Outreach Performance of Microfinance Institutions

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ABSTRACT

Microfinance institutions (MFIs) provide financial services to poor customers living in poverty. This study addresses the relationship between MFI board composition and the poverty outreach (social performance) of MFIs. In particular, we investigated whether the proportion of independent, international, female and/or founding board members is associated with measures of outreach performance. We used data from a survey, containing information about the boards of 63 MFIs in Kenya, Tanzania and Uganda. Our findings suggest that outreach performance is improved when MFI boards have a higher share of independent, international and/or female members, which supports the hypothesis that board composition is important in helping MFIs to achieve their social objectives.

1.0 INTRODUCTION

Past research suggests that board decisions have an impact on the (broadly defined) performance and/or mission of organizations (Dalton, Daily, Ellstrand, & Johnson, 1998; Zahra, Filatotchev, & Wright, 2009). Furthermore, the significant interest in board issues, within both academic and policy circles, is partly driven by the fact that board decisions and board behaviour are believed to be affected by board composition and board diversity (e.g., Van, Gabrielsson, & Huse, 2009). Policy makers have looked at the role of boards in discussions about corporate governance best practices, which in many cases have been developed into corporate governance codes and in some cases into law (e.g. the Sarbanes-Oxley act in the United States). In the academic literature, a large number of studies have analyzed the relationships between various board characteristics – such as board member demographics, board diversity, and board processes – and organizational performance. These studies almost exclusively focus on for-profit firms. Much less is known about the role that the boards of non-profit, mission-driven organizations play in attaining organizational goals.

This paper looks into the role the boards of microfinance institutions (MFIs) play in the attainment of organizational goals. In contrast to formal banks, most MFIs have a dual objective of outreach to poor customers (i.e. outreach (or social) performance) and covering long-term costs (i.e. financial performance, sometimes referred to in the industry as self-sustainability) (Mersland, Randøy, & Strøm, 2011). The question is how and to what extent the boards help them to reach these objectives.

From a practitioner's perspective, it has been stressed that the governance of MFIs should receive more attention. Only recently has it been acknowledged that good governance may make an important contribution to the achievement of the objectives of these institutions.

As an example of this emerging trend, in 2011 the BBVA Microfinance Foundation, in collaboration with the Inter-American Development Bank (IDB), published a guide for the adoption of good governance principles in MFIs. According to this guide, "good corporate governance contributes to efficient management and to considering stakeholder interests, boosting the microfinance institution's reputation and integrity and fostering customer trust" (p.7). Moreover, the Banana Skins report – published by the Centre for the Study of Financial Innovation (CSFI, 2008) –listed weak corporate governance and management quality among the ten most important risks confronted by the microfinance industry during the last few years. Inarguably, the recent attention paid to the governance of MFIs is related to the increasing interest of private investors in financing these institutions. Transparency and trust in the internal operations of MFIs are key elements in the funding decisions of these private investors.

Previous studies on the relationship between MFI governance and performance have mainly analyzed the impact of leaders, in particular female leaders (Strøm, D'Espallier, & Mersland, 2010) or governance mechanisms, such as competition, regulation, board size and stakeholders (employees, donors and creditors) (Hartarska, 2005; Mersland and Strøm, 2009; Soltane, 2009) on the financial performance of MFIs. As an alternative, Hartarska and Mersland (2012) employed the cost efficiency concept from the banking literature and modified it to capture the duel objectives of MFIs. Our study theoretically and empirically embodies different strands of literature and methodology.

To our knowledge, no other study to date has examined MFI boards in detail, and specifically the impact of board characteristics on achieving the MFI's social mission. As mentioned above, the governance mechanisms of MFIs and their implications have received wide attention in the industry. Therefore, this study addresses the industry's call for good practices and the theoretical shortcomings of previous studies (for example, Hartarska and Mersland, 2012, failed to capture the poverty level of MFI clients) by examining the detailed characteristics of MFI board members and the extent of their influence on the attainment of the MFI's social mission, focusing on both the breadth and depth of outreach to customers. Examining board impact is important due to the MFI board's role of monitoring and guiding it to attain its mission (Galema, Lensink, & Mersland, 2012).

This study therefore contributes to the microfinance literature by focusing on MFI board composition and its impact on MFI social performance. We did this by first identifying the key board members who arguably have a direct influence on the outreach mission of these institutions. MFIs operate in environments where the social mission of serving the poor is commonly highlighted as the most important objective (Cull, Demirguc-Kunt, & Morduch, 2009). Therefore, understanding the relationship between boards, as a governance mechanism, and social performance is particularly important.

The microfinance industry is also argued to be an entrepreneurial industry. with a focus on developing innovative strategies that will better serve the poor (Strøm et al, 2010). This justifies basing our arguments about board composition on the entrepreneur literature and adapting them to the context of MFIs. This helped us to identify the factors that significantly affect the MFI governance structure, and enables MFIs to achieve their social mission. This is an important consideration given the potential role MFIs can play in facilitating development and alleviating poverty. In particular, we emphasized composition by examining to what extent boards include independent (or external) board members, international members, female members and/or founding members and how these characteristics of boards are related to outreach performance.

A further contribution of this paper is its focus on sub-Saharan Africa, a region that is considered the poorest in the world, with one of the largest markets for microfinance (CGAP, 2009). We used this context to investigate the link between an MFI's board composition and its potential to help the poorest in the community. The empirical analysis is based on information on the board characteristics of 63 MFIs in Kenya, Tanzania and Uganda. The information was collected by conducting detailed surveys of the boards of these institutions. The information we collected covers the period 2004-2009. We found support for the fact that boards with a higher proportion of independent, international and/or female board members perform better in terms of both the depth and breadth of their outreach. These results suggest that MFI board composition is indeed important for the achievement of social objectives. There are practical policy implications in terms of advising the boards of MFIs on the selection of new board members.

The remainder of this paper is structured as follows. In section 2 we discuss the theoretical framework supporting the general hypothesis that board characteristics are related to the social performance of MFIs. In section 3 we develop hypotheses relating different board characteristics to MFIs' social performance based on the theoretical framework discussed in section 2 as well as on information about board members' behaviour and incentives obtained from several in-depth interviews. Section 4 discusses the data and methodology. In section 5 we present the descriptive statistics, after which we discuss the results of the multivariate analysis in section 6. We end with the implications and contributions of our research, its limitations and directions for further research in section 7.

2.0 THE IMPORTANCE OF BOARDS: A BRIEF REVIEW OF THE THEORY

Literature on the board has traditionally focused on large listed companies owned by a large number of minority shareholders (e.g., Daily, Dalton, & Cannella, 2003). In this literature, explanations of the board-performance relationship are rooted in two widely applied theoretical models, the agency theory and resource-based theory. The agency theory emphasizes that the separation of management and stakeholders leads to a divergence of their respective interests. Thus incentives and controls have to be provided to induce managers (agents) to maximize organizational goals. According to the agency theory, boards play an important role in screening, monitoring, and enforcing contracts with managers. These board roles may safeguard the organization from the misuse of resources by managers, which reduces the agency costs in both for-profit and non-profit firms (Dalton et al, 1998; Dalton, Daily, Johnson, & Ellstrand, 1999; Fama & Jensen, 1983; Speckbacher, 2008).

The resource-based theory suggests that the performance of the organization is enhanced when it explores its distinctive and idiosyncratic resources and capabilities and/or its ability to deploy resources (e.g., Barney, 1991; Kogut & Zander, 1993; Peteraf, 1993). Applying this theory to the question of the importance of board composition, it suggests that board members provide access to resources that are critical for the organization's performance. These resources may be (1) gathered through board members' networks that grant the organization access to, for example, external finance or contacts with governmental organizations, (2) advice, for example with respect to strategic decision making, or (3) knowledge or information about regulations or clients.

Thus, based on these two theoretical models, boards serve two main roles. First, they monitor and control the performance and accountability of managers on behalf of the shareholders, keeping them focused on their goals (Hermalin & Weisbach, 1991). Second, they advise and inform managers on issues relating to business strategy (Pfeffer & Salancik, 1978) and provide access to resources. This is referred to as the resource and advisory role of boards (Hillman, Nicholson, & Shropshire 2008). In undertaking both roles, boards guide and motivate managers to accumulate resources, effectively configure and bundle them, and leverage their use to create a competitive advantage. This holds for profit organizations and non-profit organizations such as MFIs.

One recently emerging research stream emphasizes the role of boards for young entrepreneurial organizations (see, e.g., Certo, Daily, & Dalton, 2001; Zahra & Filatotchev, 2004; Zahra et al, 2009). For these organizations, a board's role should be geared more to helping them to overcome the liabilities of their newness and small size. The argument is that a board can add significant value by providing access to resources and strategic advice. Since MFIs have emerged relatively recently, we therefore expect the resource-providing role of boards to be particularly important for their performance. Being successful in attaining organizational objectives is positively associated with having access to and/or acquiring a wide array of resources, which may help to improve managerial skills and expertise.

The corporate governance literature recognizes that the individual characteristics of board members, such as age, gender, experience, nationality, etc., can be predictors of their ability to monitor and provide access to resources (Hillman & Dalziel, 2003). More specifically, it highlights several dimensions of board composition as being important for carrying out these two board roles, including board size (Yermack, 1996), board diversity (Adams & Ferreira, 2009), board leadership (Rechner & Dalton, 1991), board stakeholder representation (Luoma & Goodstein, 1999) and international board members (Riahi-Belkaoui, 1998). Following on from the corporate governance literature, a few studies have looked at MFI boards together with other governance mechanisms, and have identified the (potential) impact of board characteristics, such as board size, stakeholder representation and the existence of female leadership on the performance of MFIs (Hartarska, 2005; Hartarska & Mersland, 2012, Strøm et al, 2010).

The importance of the governance of MFIs has also been on the agenda of practitioners in microfinance. As mentioned in the introduction, the CSFI (2011) listed inadequate corporate governance as one of the most important risks currently faced by the microfinance industry. Moreover, several policy-oriented studies have advocated the importance of having a mixture of skills and experience among the members of MFI boards (Council of Microfinance Equity Funds [CMEF], 2005). These studies have generally argued that, since the industry provides poor people with financial services, it is necessary for board members to have a mixture of social and business skills and experience (Campion, 1998; Campion & Frankiewicz, 1999). For example, CMEF (2005) suggested that, when selecting new board members, MFIs should target individuals with the ability and willingness to devote time and talent, who are seen as independent, bringing skills and objectivity, and who are influential and can assist with political issues, tap funding, and help the organization to build a positive public image.

Moreover, CMEF stressed the need for a diverse board (in terms of gender, ethnicity and/or cultural background) to ensure a broad perspective. The advice provided by this institute stresses the importance of both the monitoring and advice/resource access roles of the boards of MFIs. Finally, the 2011 guidelines published jointly by the BBVA Microfinance Foundation and the IDB, referred to earlier, stress, among other things, the importance of having independent board members with the financial, legal and social knowledge to achieve the MFI's goals, who are committed to being actively involved in attaining these goals, and who will provide input into strategic decision making. Moreover, the guidelines stress the importance of optimal board size, board diversity and CEO/chairman duality. These best practices developed for MFIs are very similar to those described in the corporate governance literature and corporate governance codes.*

3.0 HYPOTHESES

So as to analyze the relationship between board composition and MFIs' outreach performance, we derived several hypotheses explaining how specific board member characteristics may contribute to the attainment of the social mission of these institutions. In developing these hypotheses, we were guided by two sources. First, our hypotheses were grounded in the theoretical models discussed in the previous section, the agency theory and resource-based theory. Second, we carried out detailed interviews with 30 board members from 20 MFIs in the three focal countries. These interviews helped us to establish what motivates individuals to serve on the boards of MFIs and what board member characteristics are perceived as being potentially important for achieving better social performance. In particular, the interviews focused on how the board members were recruited, what motivated them to accept the position and to stay on as a board member, how their background/competencies related to their contribution to the MFI's mission, and whether they felt they influenced the key decisions and performance of the organization.

Combining the theory-based arguments with the information gathered from these interviews, we identified four characteristics of board members that may be instrumental in promoting better social performance of MFIs: independence, nationality, gender and the presence of the founder on the board.

* The BBVA Microfinance Foundation/IDB guidelines, for example, take the OECD Principles of Corporate Governance as their point of departure.

3.1 Independent Board Members

Independent board members have no affiliation to the organization on whose board they are sitting. In the corporate governance literature, board independence is seen as an important dimension of board composition as it determines the ability of the board to monitor the management and provide a greater variety of resources. Having no affiliation to – and thus no direct interest in – the organization increases a board member's objectivity and ability to safeguard the organization from the misappropriation of resources. This reduces agency costs, which contributes to better organizational performance (Fama & Jensen, 1983; Hillman et al, 2008; Speckbacher, 2008). Moreover, it has been argued that independent board members bring new skills and capabilities that may be instrumental in whether organizations obtain their goals (Raheja, 2005; Zahra et al, 2009; Zhang, Baden-Fuller, & Pool, 2011).

Past research suggests that the independence of board members is also important for the social performance of MFIs. Hartarska (2005) found that the outreach performance of MFIs whose boards contain a higher proportion of internal members is worse. Galema, et al, (2012) further argue that MFI board members are generally independent persons who simply wish to support these organizations. Our interview findings are in line with these observations. Independent board members, who commonly have more "outside" exposure and experience, appear to be motivated to serve on boards in order to contribute to MFIs' social outreach mission. They indicated that they are willing to do this by monitoring management, as well as by using their skills and experience. Many outside board members revealed that they were recruited to serve on MFI boards in the hope that they would use their experience and networks to help the MFI gain access to resources that would contribute to its outreach mission. We therefore hypothesized that independent board members enhance the outreach performance of MFIs due to their ability to effectively monitor, provide skills and experience, and enable access to valuable resources:

H1: A higher proportion of ***independent*** *board members is positively associated with the outreach performance of MFIs.*

3.2 International Board Members

International board members are those who do not come (originally) from the country where the organization is located. The corporate governance literature indicates that organizational performance may improve when boards are international. For example, Oxelheim and Randøy (2003) found that the internationalization of the boards of publicly traded firms enhances firm performance as international board members have more experience and are better at monitoring management. In particular, they may facilitate the transfer of value-enhancing corporate governance practices. International board members can also take a more independent role in monitoring as they will often have less vested interests in the organization, which helps to reduce agency costs and forces the organization to be more performance-oriented. Finally, international board members are perceived as having more extensive networks, which may at least potentially better link the organization to valuable resources.

Similar arguments may hold for international MFI board members. They may facilitate the transfer of international competencies and may contribute to better monitoring and resource provision, thereby enhancing MFIs' outreach performance (Mersland et al, 2011). For example, they may link the institution with international partners, investors and organizations such as CGAP and ACCION international (Mersland et al, 2011; Rhyne, 2005). Links with international networks can also be established if the board members in question represent the international organizations that were involved in starting the MFI in the first place. This is actually the case for a number of institutions in our sample of East Africa MFIs (Hospes, Musinga, & Ong'ayo, 2002; Randhawa & Gallardo, 2003). Our interviews revealed that international board members tend to push for the achievement of social goals. Those we questioned stressed that they are motivated to share their experience with the CEOs of MFIs in order to reduce poverty and assist in reaching poor people. Based on the above discussion, we derived the following hypothesis:

H2: A higher proportion of ***international*** *board members is positively associated with the outreach performance of MFIs.*

3.3 Female Board Members

The corporate governance literature identified several arguments in favour of the recruitment of female board members, such as the increased diversity and independence of opinions on the board, their positive influence on strategic decision making and the leadership style of the organization, and an improved organizational image with stakeholder groups (Adams & Ferreira, 2009; Burgess & Tharenou, 2002; Daily, Certo, & Dalton, 1999). Empirical evidence indicates that increasing the number of female board members has a positive relationship with the monitoring efforts of the board as a whole, which may contribute to improving value creation and organizational performance (Adams & Ferreira, 2009; Erhardt, Werbel, & Shrader, 2003).

With respect to the boards of MFIs, females may have a particularly important role to play as in many cases most of the customers are women (Mersland & Strøm, 2009). This also holds for the MFIs in the three East African countries in our dataset. Female board members may be strongly motivated to serve the needs of these female clients. Moreover, they may be better informed about the financial services needed by the poor, which may help to improve outreach performance (Strøm et al, 2010). This too was corroborated by our interviews. Female board members claimed to have better insights into what women need and said that they were motivated by a desire to contribute to meeting the needs of the poor. Based on the above discussion we derived the following hypothesis:

*H3: A higher proportion of **female** board members is positively associated with the outreach performance of MFIs.*

3.4 Founding Board Members

Corporate governance research is inconclusive with respect to the relationship between founding board members and organizational performance. Some papers have shown that founders serving on boards may have a lot of power over strategic decision making and board composition due to their history with the organization (Nelson, 2003; Wasserman, 2003). Another section of the literature suggests that founding board members identify more strongly with the mission of the organization than non-founding members (Block & Rosenberg, 2002). Finally, it has been argued that founders may have developed unique social capital through their relationship with the suppliers of input and capital, as well as with their customers (Ben-Ner & Van Hoomissen, 1994).

These characteristics of founding members may help the organization to achieve better growth and performance (Baum & Bird, 2010; Meyskens, Robb-Post, Stamp, Carsrud, & Reynolds, 2010; Willard, Krueger, & Feeser, 1992). Founding members may possess firm-specific attributes that can help the organization to break through start-up barriers. These attributes may comprise managerial, technical, motivational and/or political skills and can be difficult for non-founders to replicate. Thus, founding board members may have a positive impact on performance, especially during the early stages of organizational growth, by providing knowledge and commitment tailored to the organization's aims.

It has also been pointed out, however, that founding board members may adversely affect performance. Founders may identify themselves too much with the organization and have a tendency to treat it as their "baby" (Wasserman, 2003). Consequently, they may try to control and dominate decision making for too long, pushing their ideas and views at the cost of others, which may compromise organizational performance (Schein, 1983). A related argument states that founding board members continue to sit on boards, claiming to be motivated by the organization's mission, but in reality they are more concerned with retaining control than enhancing performance (Nelson, 2003). Another possible negative effect is that the presence of founder board members may crowd out other board members with links to valuable resources. Finally, while, as mentioned above, the presence of founder board members may be particularly beneficial during the early stages of organizational growth, in later stages they may become a barrier to growth. As indicated in the entrepreneurship literature, founders are particularly good at designing new products and services, but their ability to lead and create good governance structures may diminish over time (Wasserman, 2003; Willard et al, 1992).

This discussion of the role of founding members also applies to MFIs. The person who started the MFI – often with the aim of reducing poverty – still serves on the board in many cases (Alonso, Palenzuela, & Merino, 2009). Such board members may be particularly motivated to hold on to the mission of poverty reduction. Our interviews with founding board members corroborated several of the above observations. Many of these board members indicated that they started the MFI to help poor people to gain access to financial services. They showed themselves to be passionate about working for the MFI and serving the poor. At the same time, several of them claimed that they had held on to their board position because they believed they were the right person to ensure the MFI attained its mission.

In the light of the above review of the corporate governance literature on the relationship between founding board members and organizational performance, the question still remains over whether the commitment of a founding board member to the institution and its mission creates a positive relationship with social performance and whether or not this positive relationship is dependent on where the MFI is in its life-cycle. Therefore, we derived the following hypotheses followed by table 1 which summarises all the stated hypotheses:

*H4a: A higher proportion of **founding** board members is **positively** associated with the outreach performance of MFIs.*

*H4b: A higher proportion of **founding** board members is **negatively** associated with the outreach performance of MFIs.*

*H4c: A higher proportion of **founding** board members is **positively** associated with outreach performance, but the positive association diminishes over the MFI's life-cycle.*

Table 1: Summary of the Hypotheses

Board Composition	Outreach Performance		
	Breadth	**Depth**	
	Customers	Female customers	Average loan
Independence	+	+	-
International	+	+	-
Female	+	+	-
Founders	+/-	+/-	+/-

4.0 DATA AND METHODOLOGY

4.1 Sample and Data Collection

We collected data on the boards of MFIs in sub-Saharan Africa, focusing on the three East African countries of Kenya, Tanzania and Uganda. We chose to collect our data in this region for a number of reasons. First, sub-Saharan Africa is considered to be the poorest continent in the world, and is recognized as one of the largest markets for microfinance (CGAP, 2010). Within the continent, East Africa has the most developed microfinance industry (CGAP, 2010). The three countries show significant similarities in their legal and regulatory regimes (La Porta, Lopez, Shleifer, & Vishny, 1997), but at the same time are heterogeneous in terms of the development of their national microfinance industry. The importance of MFIs for the development of the region and the combination of cross-country institutional similarities and industry variations makes the East African region an interesting context for microfinance research.

Microfinance in these countries only really took off in the 1990s (Hospes et al, 2002; Randhawa & Gallardo, 2003), although microfinance activities were initially developed in the 1980s. For example, the Uganda Finance Trust was established in 1984, while Kenya's Women's Finance Trust was established in 1982. However, it was in the mid-1990s that the governments of the three countries began to recognize the importance of providing financial services to the poor and introduced several rules and regulations to support the industry (Randhawa & Gallardo, 2003). Despite these efforts, a study by FinScope (2009) showed that only a small percentage of the poor had access to financial services and there was still a huge unmet need.

Table 2 provides an overview of access to financial services in Kenya, Tanzania and Uganda. It shows that the proportion of people with no access to either formal or informal finance ranges from 30 percent (Uganda) to 56 percent (Tanzania). Moreover, it shows that only between 17 percent (Tanzania) and 33 percent (Uganda) of people have accesses to formal modes of finance through banks or non-governmental organizations (NGOs) and SACCOs (savings and cooperative societies). According to the data from the MIX market dataset (www.mixmarket.org), at the end of 2009 the number of active borrowers from MFIs in Kenya, Tanzania and Uganda was 3.3 million, less than 3 percent of the total population of the three countries. These figures show that there is still much room for enhancing the outreach of MFIs to the poor in the three countries. This makes a study of the determinants of improved outreach particularly relevant. As indicated earlier in this essay, governance may be one such important determinant, of which board composition, studied here, is one element.

Table 2: Financial Institutions and Access to Financial Services in East Africa

Financial access and number of MFIs	**Uganda**	**Kenya**	**Tanzania**
Full access to financial services (banks)	21%	18.5%	12.4%
Partial access to financial services (SACCOs, NBFIs - non-bank financial institutions, NGOs)	12%	8.1%	4.3%
Informal access to finance (groups, individuals, money lenders)	34%	35.0%	27.3%
Excluded (no access)	30%	38.4%	56%
Number of SACCOs (approximate)	3,000	4,000	3,000
Number of NGOs (approximate)	250	300	200

Sources: FinScope (2009); Johnson and Zarazua (2011)

Data on corporate governance indicators are generally difficult to obtain. This is no different for non-profit organizations such as MFIs. We collected our data from various sources. The most important source was a survey conducted by one of the authors in the three countries between January and August 2010.We contacted umbrella microfinance associations in each of the three countries to provide us with a list of the names of MFIs, their CEOs, and their contact addresses. The researcher visited all the MFIs on the list (excluding cooperatives) and asked them if they would take part in the research by filling in a survey. The survey included questions about their governance, board members' demographics, clients, activities and operations. Moreover, the researcher asked the respondents to provide audited financial statements (and/or annual reports) from 2004 to 2009. Finally, the researcher asked them to provide names and contact details of any other MFIs they knew of. We then visited these

MFIs as well and asked for the same information using the same survey instrument. This methodology is referred to as *snowball sampling* (Goodman, 1961; Heckathorn, 1997).[*] Altogether, we finally identified and contacted 103 MFIs, of which 49 (almost 50 percent) completed the survey.

We also collected data by visiting the MFIs' websites. Several of these provided information on governance, clients, activities and operations, as well as published audited financial reports. We were also able to verify some of the data we had obtained through the survey using information from the MFIs' websites.

Together, these sources provided us with information about governance indicators and financial information for the period 2004-2009 for 63 MFIs. Our sample represents between a quarter and a third of all MFIs (excluding cooperatives[†]) in the three countries. We recognize that our method of collecting information may have introduced bias, in particular by leaving out smaller MFIs that provide little or no information with respect to governance and financial statements. This sample-selection bias is a well-known problem in research on microfinance. For example, several studies have made use of data from the MIX market or rating reports. These studies suffer from a similar selection-bias problem, because the data they use are mostly from larger, more developed MFIs.

4.2 Variables

Dependent Variables

As already explained, our analysis focused on the relationship between board composition and the outreach performance of MFIs. According to the microfinance literature, MFI outreach can be measured in terms of both breadth and depth. In line with the standard in microfinance research, we measured breadth as the ***number of customers*****,** specifically the logarithm of the total number of customers served by the MFI (Mersland & Strøm, 2008). The greater number of customers served, the greater is the breadth of the outreach. Depth was

[*] Snowball sampling is a sampling technique where existing respondents recruit new respondents from their vicinity to create a sample that is large enough for research. This technique is mainly used in sociological research to create a sample of respondents from a population that is difficult to approach, such as drug users, alcoholics, and so forth. In our case, this technique was very helpful for solving the problem of finding MFIs not listed by the relevant microfinance umbrella organization.

[†] Cooperatives have a different governance structure (i.e. the customers are also the owners of the organization). They are usually much smaller and, in most cases, do not have audited financial statements.

measured as the ***proportion of female customers***, that is the ratio of female customers to total customers. As an alternative measure of depth, we looked at the (logarithm of the) ***average loan size per customer***. Again, both measures are in line with what is used in the literature. A higher proportion of female customers indicate a higher depth of outreach, while a lower average loan size indicates a higher depth of outreach, since most poor customers receive small loans (Schreiner, 2002).

Independent Variables

We used the following four measures of board composition. First, we measured board ***independence*** as the proportion of outsiders on the board, where outside directors are defined as those who are not current or past employees and who do not have significant business or family ties with the MFI's management (Adams & Mehran, 2005). We acknowledge that the proportion of outsiders does not equate to true board independence. However, similar to Combs et al (2007), we argue that an outsider-dominated board will be more independent that an insider-dominated board because outsiders do not have an employment relationship with the MFI. Our measure of the independence of the board members is in line with other previous studies (e.g. Wagner III, Stimpert, & Fubara, 1998). Second, we used the proportion of board members who originate from a country other than the country where the MFI is located to measure the extent to which the board is ***international*** (Mersland et al, 2011). Third, board ***gender diversity*** was measured as the proportion of board members who are female (Adams & Ferreira, 2009). Finally, ***board membership by founders*** was measured as the proportion of board members who are among the original founders of the MFI.[*] We also had a ***founder-age*** interaction variable which represents the life cycle effects as shown in hypothesis 4c.

Control Variables

We included a number of control variables that, according to previous empirical literature, may be correlated with the outreach performance of MFIs (Mersland et al, 2011; Strøm et al, 2010). First, we used ***board size***, which is measured as the logarithm of the number of people sitting on the board. Larger boards may provide a wider range of skills and experience, which

[*] It should be noted that, as a robustness check, we explored the possibility of a concave relationship (quadratic terms) for all independent variables. However, we did not find any significant evidence in favour of such a prediction.

may contribute positively to higher outreach. On the other hand, larger boards may experience more difficulties making decisions due to problems with communication and/or different viewpoints, leading to lower outreach. We also included ***MFI age***, which was measured as the number of years since the organization started its operations. Older MFIs may have developed more experience in reaching the poor, suggesting a positive correlation between outreach and the age of an MFI.

Next, we controlled for the MFI's financial performance using ***operating self-sustainability***, measured as the ratio of revenue from operations to all expenses, and ***return on assets,*** measured as the ratio of net operating income to average annual assets. Several studies have argued that, because focusing on outreach can be costly, financial performance and outreach are negatively correlated, that is, there is a trade-off between financial and social performance (Cull, Demirguc-Kunt, & Morduch, 2007; Hermes & Lensink, 2011). Others, however, have claimed that financial and social performance are complementary, suggesting a positive correlation between the two (Gonzalez & Rosenberg, 2006). We included a dummy variable indicating the ***MFI type***, which took the value one if the MFI is operating on a for-profit basis, and zero otherwise. Controlling for MFI type is important since for-profit MFIs are generally assumed to have a weaker outreach than non-profit ones (NGOs). Finally, we included ***country*** and ***time*** variables to capture variations in the economic development of the three countries and in social outcomes over time.

A common challenge in corporate governance research is the issue of possible reverse causality. The methodological concern here was the possibility of an omitted unobservable variable that would affect both our independent and dependent variables (Larcker & Rusticus, 2010). The literature further shows that many of the variables of interest in corporate governance investigations are not truly exogenous, that is they are determined completely outside the model systems but are endogenous (Carter et al, 2010; Hermalin & Weisbach, 2003).However, we believe that controlling for financial performance variables, as we did in this study, helps to reduce endogeneity problems.

4.3 Regression Methodology

Given that we had three different measures of outreach performance, we decided to use the system regression method, which allowed us to jointly estimate the equations for the different measures. We argue that a joint estimation is theoretically more correct since the social performance of an MFI is multidimensional (i.e. it may include various measures of the depth and breadth of outreach). By using the system regression method we were able to capture the joint effect of the various outreach measures, taking into account the potential interdependency between them. We used panel data estimation, using data for six years, and applied the seemingly unrelated regression (SUR) methodology (Greene, 2008). We also performed a Breusch-Pagan test to check the extent to which the residuals in the SUR regression were independent.

5.0 DESCRIPTIVE STATISTICS

Table 3 gives the summary statistics for the variables used in this study. In terms of the dependent variables, first, we found that the average number of customers served by each MFI in the region is almost 36,000, of whom 63 percent are women. This indicates that the MFIs in the region concentrate on serving female customers. Second, the average loan size per customer is 348 US dollars. Both the high ratio of female borrowers and the relatively low average loan size reflect the fact that the MFIs in our sample are focused on serving the poor.

With respect to our board composition variables, Table 2 reveals that 36 percent of all board members are independent. Moreover, we calculated to what extent the boards can be categorized as highly independent. We defined a board as being highly independent if more than 50 percent of its members are classed as independent. In our sample, this is the case of 27 percent of the boards. These figures suggest that the MFIs are generally dominated by insiders.

International board members make up 21 percent of all board members. Additionally, 20 percent of the boards can be defined as highly international, i.e. comprising more than 50 percent of international members. These figures indicate that the international board members in our dataset are concentrated in a minority of the boards in the sample. Moreover, when comparing these figures to those from other studies, it seems that East African MFI boards are relatively less international than the boards of MFIs in other regions. Mersland et al (2011), using a worldwide sample of MFIs, found that on average 55 percent of board members can be classed as international.

The boards in our sample do not show a high degree of gender diversity as only 24 percent of all members are female. Moreover, only 13 percent of all boards have a high proportion (more than half) of female board members. Given the high proportion of female borrowers, these numbers could be considered rather low.

Finally, founding board members represent 33 percent of our sample, as 19 percent of all boards can be classed as founder dominated, that is, more than half of their board members are among the original founders of the MFI.

The average number of board members on the boards in our sample is seven. The average age of the MFIs is nine years, which can be considered young. In terms of MFI types, for-profit MFIs represent 38 percent of the sample, indicating that most MFIs in this region are working on a not-for-profit basis. In terms of financial performance, the MFIs in this region are able to cover their costs, as operating self-sustainability is on average above 100%. However, they are not profitable since the average return on assets is negative (-1%). Finally, 34 percent of the MFIs are located in Kenya, 30 percent in Uganda, and the remaining 26 percent in Tanzania.

Table 4 presents the correlation between the variables used in the empirical analysis. The correlation coefficients between the explanatory variables are somewhat high, but are below the critical level of 0.8 (Kennedy, 2008). Moreover, the variance inflation factor (VIF) analyses run among all the independent variables (i.e. board composition and control variables), produced values ranging from 1.1 to 2.3, indicating low levels of multicollinearity. Also, in the econometric analysis, we ran regressions with a few variables at a time (Strøm et al, 2010. In addition, since panel data estimation provides more data points, the multicollinearity problem here was reduced even further (Wooldridge, 2006).

Table 3: Summary Statistics

Variable	Observations (firm-years)	Mean	Std. Dev.	Min.	Max.
Dependent Variables					
Number of customers	220	35742.3	74917.93	10	715969
Ln number of customers	220	9.474	1.562	3.135	13.481
Female customers – proportion	184	0.633	0.221	0.101	1.000
Average loan	207	348.319	353.949	9.000	2158
Ln average loan	207	5.426	0.982	2.197	7.676
Composition Variables					
Independent board – ratio	331	0.364	0.253	0.000	1.000
Independent board – high	331	0.276	0.448	0.000	1.000
International board – ratio	331	0.216	0.298	0.000	1.000
International board – high	331	0.202	0.409	0.000	1.000
Gender diversity – ratio	326	0.246	0.226	0.000	1.000
Gender diversity – high	326	0.134	0.341	0.000	1.000
Founder board members – ratio	331	0.335	0.235	0.000	1.000
Founder board members-high	343	0.198	0.399	0.000	1.000
Interactive term: Founder - MFI age	311	2.476	2.234	0.000	11.000
Control Variables					
Number of board members	331	7.184	2.237	2.000	14
Board size (ln)	331	1.916	0.354	0.693	2.639
MFI age	311	9.697	6.960	0.000	31.000
Operating self-sustainability	256	104.355	42.412	6.421	521.871
Return on assets	228	-0.016	0.130	-0.851	0.599
MFI type	328	0.387	0.488	0.000	1.000
Kenya	343	0.344	0.476	0.000	1.000
Uganda	343	0.300	0.459	0.000	1.000

Table 4: Correlation Analysis

Variables	1	2	3	4	5	6	7	8	9	10	11	12	13
1. Ln number of customers	1.000												
2. Female customers – proportion	0.145	1.000											
3. Ln average loan	0.268**	-0.321**	1.000										
4. Independent board	-0.115	0.020	-0.174**	1.000									
5. International board	0.205*	0.139	0.168*	-0.412**	1.000								
6. Gender diversity	0.098	0.290**	0.124	0.334**	-0.292**	1.000							
7. Founder board members	-0.333**	0.084	-0.203**	-0.485**	-0.034	-0.056	1.000						
8. Board size	0.368**	-0.171	0.477**	0.397**	0.067	0.163*	-0.549**	1.000					
9. MFI age	0.549**	-0.025	0.367**	0.325**	-0.101	0.369**	-0.444**	0.487**	1.000				
10. MFI type	0.249**	-0.281**	0.331**	0.094	0.068	-0.027	-0.342**	0.354**	0.454**	1.000			
11. Operating self- sustainability	0.095	-0.168**	0.177*	-0.052	-0.200**	0.017	-0.088	-0.044	0.155*	0.110	1.000		
12. Return on assets	0.093	-0.110	0.088	-0.025	-0.233***	-0.009	-0.048	-0.065	0.137*	-0.156*	0.757*	1.000	
13. Kenya	0.133*	-0.096	0.001	0.127	-0.186**	0.071	-0.016	0.031	0.199**	-0.082	0.028	0-073	1.000
14. Uganda	-0.156*	-0.157*	0.159*	-0.006	0.083	-0.043	0.046	-0.025	-0.010	0.102	-0.029	-0.474	0.471

* p < .05; ** p < .01

In Table 5, Panel A, we present the results of a simple t-test analysis comparing the outreach performance of MFIs with high versus low board independence (where high independence is where more than half of the board members are independent). The results show that MFIs with highly independent boards serve significantly larger numbers of female borrowers and have significantly smaller average loans than MFIs whose boards are less independent. Both of these results suggest that more independent boards perform better in terms of outreach.

Panel B shows the results of the t-test comparing the outreach performance of MFIs with a high versus a low proportion of international board members, where high is again defined as more than half of the members being international. These results indicate that MFIs with a high proportion of international board members lend significantly more to women, suggesting better outreach performance. This finding is in line with Mersland et al (2011).

The results in Panel C of the table reveal that MFIs with a high proportion (more than half) of female board members also perform significantly better in terms of lending to women. This result corroborates previous findings by Mersland and Strøm (2009). Moreover, we also find that MFIs whose boards are dominated by women also have more clients.

When we analyze the difference in outreach performance of MFIs with a high versus a low proportion of founding board members (again the cut-off point is 50 percent), we find no significant differences between the two groups with respect to our three measures of outreach performance. This suggests that dominance of the board by founding members is not correlated with better outreach performance.

Summarizing the results of the simple t-test analysis, we find some evidence to support three of the four hypotheses (i.e. those relating to board independence, having an international board and board gender diversity) regarding the relationship between MFI board composition and outreach performance.

Table 5: Performance Differences between Board Members

	Panel A: Independent board - proportion			Panel B: International board - proportion		
	High	**Low**	**Diff**	**High**	**Low**	**Diff**
Outreach Performance						
Number of Customers	28894	37915	9021	31685	36814	5129
Female Customers	0.692	0.620	**0.07****	0.703	0.614	**0.088****
Average Loan	246.614	375.772	**129.15****	296.152	363.222	67.070

	Panel C: Board gender diversity – proportion			Panel D: Founding board members - proportion		
	High	**Low**	**Diff**	**High**	**Low**	**Diff**
Outreach performance						
Number of Customers	43706	34628	**9078****	17009	38362	21353
Female Customers	0.822	0.601	**0.221***	0.679	0.624	0.054
Average Loan	357.888	346.882	11.006	296.963	356.021	59.058

* $p < .05$; ** $p < .01$

6.0 MULTIVARIATE ANALYSIS

As explained above, we performed SUR estimations to capture the joint effect on the various outreach measures, taking into account their potential interdependence[*]. The results of the estimations for our three outreach variables are presented in Table 6. We performed the Breusch-Pagan test, which is a test of the extent to which the residuals in the SUR regression are independent. The chi-squared test was highly significant, implying that we had to reject the hypothesis that the residuals of the variables are independent. This result confirms that it is statistically more correct to jointly run multiple social performance indicators.

The results in Table 6 reveal the following. First, we find a positive and a statistically significant association between the proportion of independent board members and our three measures of outreach performance. In particular, the outcome supports the notion that independent board members help MFIs to serve a larger number of customers (i.e. greater breadth of outreach) and encourage them to focus more on lending smaller amounts to their clients (i.e. greater depth of outreach). Thus, in support of our hypothesis 1, the results indicate that there is a positive relationship between board independence and the breadth and depth of an MFI's outreach performance. This suggests that independent board members are more likely to have the incentive and ability to help MFIs achieve their social mission of reducing desperate poverty.

Second, Table 6 shows that the proportion of international board members is positively and significantly associated with two of the three measures of outreach performance. More specifically, the table reveals that a higher proportion of international board members is correlated with a larger number of customers and with a higher proportion of female customers. This supports hypothesis 2, that there is a positive relationship between the degree to which the board of the MFI is international and the breadth and depth of outreach performance. It suggests that MFIs with international board members benefit from their superior monitoring ability and their better access to valuable resources, leading to better outreach performance. These results are in line with those of recent studies highlighting the positive impact of international initiators, donors, debt and networks on the outreach performance of MFIs (Mersland et al, 2011).

[*] Although our analysis is aimed at investigating the link between the board composition of MFIs and outreach, we also ran a number of robustness checks, including looking at the effects on the financial performance of the MFIs. These results are available on request.

Table 6: SUR Model – Joint Estimation of Measures of Outreach Performance

Variable	Ln number of customers	Proportion of female customers	Ln average loan
Independent board	1.468*	0.156*	-2.101***
International board	0.889**	0.332***	-0.210
Gender-diverse board	-0.544	0.381***	0.914**
Founder board members	-0.057	-0.082	-0.374
Control variables			
Board size	0.142	-0.224***	1.604***
MFI age	0.131***	0.002	-0.008
MFI type	0.123	-0.131**	-0.332**
Operating self-sustainability	-0.497	-0.017	0.409**
Return on assets	2.019**	0.085	-0.326
Kenya	0.308	-0.109**	0.487***
Uganda	-0.635**	-0.170***	0.695***
Year dummies	Yes	Yes	Yes
Obs.	148	148	148
R^2	0.468	0.447	0.685
Chi^2	130.04	119.84	321.27
Pr	0.000	0.000	0.000

* p < .05; ** p < .01; *** p < .001

Third, our research provides evidence to support our hypothesis that board gender diversity is associated positively and significantly with outreach performance. The table shows a positive relationship between board gender diversity and the proportion of female customers, and a negative relationship between gender diversity and the size of loans, in both cases lending support to the notion that a higher proportion of female board members increases the depth of outreach.[*] Thus, we extend the results of Strøm et al (2010), which indicated a positive influence of female board members on MFIs' financial and outreach performance. As mentioned earlier, this result may be explained by the fact that female board members have unique competencies and knowledge with respect to the specific needs of female customers (Mersland & Strøm, 2009).

Finally, we find no support for hypothesis 4a or 4b, that is, our results do not reveal any association between the proportion of founding board members and outreach performance. One possible explanation for this outcome may be that the presence of a founder on a board is beneficial only during the MFI's early stages of growth. Having more founding board members initially may lead to better monitoring and provide access to valuable resources but their ability to improve governance structures may diminish over time. We captured this possibility in hypothesis 4c. This hypothesis states that a higher share of founding board members is positively associated with social performance but that positive association diminishes over the MFI's life-cycle. Stated differently, this hypothesis states that the marginal positive effect of founding members on social performance diminishes as the MFI gets older. We analyzed this by interacting the founding board member variable with the MFI age variable. We expected the founding member variable to have a positive coefficient, but the interactive term to have a negative one. The results are presented in Table 7. They reveal some support for hypothesis 4c, at least in the case of the number of customers (i.e. breadth of outreach). Thus, while founding board members may initially lead to better monitoring and provide access to valuable resources and thus to better social performance, their ability to facilitate these board roles diminishes over time, which is in line with the findings from the entrepreneurship literature. Comparing the results in the two tables reveals that including the interactive term does not change the outcomes for the other board variables.

[*] We also tested for the existence of a non-linear relationship between board gender diversity and outreach performance. However, we found no statistical evidence of the existence of such a relationship.

Table 7: SUR Model – Outreach Performance including Founder-Age Interactive Term

Variable	**Ln number of customers**	**Proportion of female customers**	**Ln average loan**
Independent board	2.037**	0.119	-2.155***
International board	1.340**	0.349***	-0.186
Gender-diverse board	-0.061	0.413***	0.961***
Founder members	2.794**	0.105	-0.100
Founder - MFI age	-0.335***	-0.022*	-0.032
Control variables			
Board size	0.469	-0.203***	1.635***
MFI age	0.223***	0.008*	0.001
MFI type	0.358	0.146***	-0.310
Operating self-sustainability	-0.424	-0.012	0.416**
Return on assets	1.886*	0.076	-0.339
Kenya	0.119	-0.122***	0.469***
Uganda	-0.701*	-0.174***	0.689***
Year dummies	Yes	Yes	Yes
Obs.	148	148	148
R^2	0.533	0.459	0.686
Chi^2	167.32	125.73	323.50
Pr	0.000	0.000	0.000

* $p < .05$; ** $p < .01$; *** $p < .001$

Our empirical results in Tables 6 and 7 also show that some of the control variables are significantly associated with the outreach performance of MFIs. In line with past research, our findings suggest that large boards are negatively associated with MFI performance (Mersland et al, 2011; Yermack, 1996). Specifically, we found that large boards are negatively associated with a focus on female customers and positively associated with average loan size. We also found that older MFIs have a greater breadth and depth of outreach as MFI age is positively and significantly associated with the number of customers and the percentage of female customers served. The relationship between legal status and outreach is not very strong; the only evidence we found was that non-profit MFIs seem to have a higher proportion of female borrowers. The idea that for-profit MFIs would be less concerned about the social mission appears intuitive. The fact that we did not find strong evidence of this suggests that the social mission is important throughout the industry, regardless of the legal status of the MFI. Operating self-sustainability and return on assets are only significantly related to one each of the three outreach measures, namely average loan size and number of customers, respectively. Overall, these results do not provide strong evidence for either complementarity or substitution between social and financial performance. Finally, the country dummies were mostly statistically significant in the three regression models, indicating that country differences affect outreach performance.

7.0 CONCLUSION AND IMPLICATIONS

During recent years, microfinance practitioners have stressed that the governance of MFIs should receive more attention because inadequate governance presents one of the most serious risks to the industry. This study explored the relationship between MFIs' board composition – as a governance mechanism – and outreach (i.e. social) performance. Combining the agency and resource-based theory with information from interviews with MFI board members, we suggested that four characteristics of boards may be instrumental in helping MFIs to achieve better social performance, namely, the independence of board members, their nationality, their gender and whether or not they were among the original founders of the institution.

Our multivariate analysis showed the following positive relationships between these characteristics and outreach performance: a higher proportion of independent board members to number of customers and average loan size; international board members to number of customers and proportion of female customers; female board members to female customers and average loan size; and founder board members to number of customers. Furthermore, we found that the relationship between outreach performance and the proportion of founding board members is moderated by the age of the MFI, with the positive impact diminishing over time.

These results suggest that board members with specific attributes may help MFIs to attain social objectives. For example, independent board members may have a greater incentive ability, international board members may have superior monitoring ability and better access to valuable resources, and female board members may have unique competencies and knowledge with respect to the specific needs of female customers. Our main conclusion is therefore that for MFIs aiming to improve their outreach performance boards and board composition do matter.

Our study makes a contribution in several dimensions. Theoretically, we fill the gap left by previous studies by exclusively considering the link between board composition and social performance. This is a valuable addition to the existing research on MFIs. Having an understanding of board composition and its role in the achievement of the social objective has implications for best practices in the MFI industry. More specifically, studying the influences of founders in the context of MFIs is an important aspect due to the youth and entrepreneurial nature of the industry. In addition, the East African context – one of the poorest regions in the world, with one of the largest markets for microfinance – of this study highlights the potential role of MFIs in furthering development and alleviating poverty. No other study has covered this region.

The main policy message of this study is that MFIs should be more careful when selecting board members. Enhancing board diversity – typically by adding more independent, international and/or female members – should be considered as a way of improving the board's expertise in monitoring management and keeping it on the right track (i.e. focusing on social performance). Making the board more diverse might also give a greater understanding of poor customers' needs and provide strong linkages with the providers of resources that are important to the MFI's mission. Our research indicates that founder board members can also be of benefit, but that such board membership tends to become less advantageous as the MFI gets older.

This study has several limitations. First, it only considered MFIs in three countries in East Africa. We suggest that a similar analysis should be carried out using data from a larger set of MFIs from a greater number of countries to test whether the relationship between board composition and outreach performance holds in different institutional and country-specific contexts. Second, we would suggest analyzing further the role played by founding members in influencing outreach performance. It may be that personal characteristics such as background, commitment and leadership moderate the relationship between the presence of founders on a board and the MFI's outreach performance. This, however, would require more detailed data on board members than we gathered for this study.

Third, we used rough proxies for outreach performance. Although these measures have been used widely in the microfinance literature, future research may benefit from developing measures that better measure the poverty of microfinance customers. Finally, future studies could focus on analyzing what is really happening in the boardrooms of MFIs, by focusing more on board processes such as mutual trust between board members, the existence of conflict and the type of conflict management practices used. Such avenues of research will help to deepen our knowledge of how the board – as an important governance mechanism – is linked to the attainment of MFIs' social mission.

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ESSAY 3

THE INFLUENCE OF STAKEHOLDERS ON STRATEGIC DECISION MAKING OF MFIs

The Influence of Stakeholders on Strategic Decision-Making of MFIs

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ABSTRACT

Microfinance institutions (MFIs) provide financial services to low-income people. These organizations have been increasing – both in number and average size – worldwide. This increase calls for these organizations to reconsider their role – particularly in relation to the participation of stakeholders on boards. Based on the literature, this paper identifies five types of microfinance stakeholders who may sit on boards: customers, employees, creditors, owners and donors. The paper explains the different roles played by these MFI stakeholders and discusses how they may contribute to the process of making strategic decisions. The general literature on boards, strategic decision making and stakeholder theory are used to show how the presence of these stakeholders on boards can be both advantageous and disadvantageous to MFIs, specifically with regard to strategic decision-making processes. Propositions are put forward, the implications are discussed and areas for future research on stakeholders and strategic decisions in MFIs are suggested.

1.0 INTRODUCTION

Microfinance institutions (MFIs) provide financial services to poor customers who in most cases have no access to formal financial institutions (Assefa, Hermes, & Meesters, 2012). These organizations evolved as a result of the efforts of committed individuals and development agencies to reduce poverty by promoting self-employment and entrepreneurship. MFIs are currently estimated to serve more than 200 million customers worldwide (Maes & Reed, 2012). Over the last decade, they have increased in size and number, and in some regions, they have become very competitive (Assefa et al, 2012; Galema, Lensink, & Mersland, 2012). As a result, MFIs are being encouraged to include stakeholders on their boards of directors (boards) to help build their competitive advantage and ensure their survival (McIntosh, Alain, & Elisabeth, 2005; Mori & Mersland, in press).

Labie and Mersland (2011) additionally contended that future studies should adopt the stakeholder approach when studying the boards and governance of MFIs. They suggest that paying attention to the primary stakeholders of MFIs may give an accurate understanding of what the most influential governance mechanisms might be. Responding to research calls from Hartarska and Mersland (2012) and Mersland (2011), this paper discusses from a theoretical perspective the involvement of MFI stakeholders on boards and in MFIs' strategic decision making. The specific research question is: how do stakeholders on boards influence the process by which MFIs make strategic decisions?

The paper focuses on strategic decision making because it is one of the roles of the MFI board (Dorado & Molz, 2005; Mori & Randøy, 2011). Strategic decision making involves two perspectives: content and process (Dimitratos, Petrou, Plakoyiannaki, & Johnson, 2011). The content perspective deals with decision outcomes such as growth strategies, while the process perspective deals with the process by which strategic decisions are made. More specifically, the process perspective, which is the focus of this paper, concentrates on how decision makers influence an organization's strategic position through the strategic decision-making processes (SDMPs) they use (Elbanna, 2006).

This paper looks particularly at stakeholders' influence on two characteristics of SDMPs: information gathering/usefulness and political behaviour (Ketchen, Thomas, & McDaniel, 1996). Different stakeholders have access to different information so when they sit on MFI boards they enable the gathering of relevant information that is useful for decision making. However, stakeholders may also have conflicting interests (Spitzeck, Hansen, & Grayson, 2011) meaning that, as board-members want their own interests to be considered, they may bring conflict and political behaviour into SDMPs.

Stakeholders on MFI boards can also influence SDMPs through the different expertise, experience, backgrounds and perspectives they bring (Hillman, Keim & Luce, 2001). Mitchell, Agle and Wood (1997 pg 876) asserted that including stakeholders on boards is a "formal mechanism that acknowledges the importance of their relationship with and interests in the organization". That is, by including stakeholders on boards and in SDMPs, organizations are signaling their commitment to their stakeholders in a visible way. Spitzeck and Hansen (2010) further showed that stakeholders' involvement in SDMPs enables organizations to make innovative strategic decisions. This means that, since different stakeholders possess different information and have different interests, their inclusion on boards may influence SDMPs and the quality of the resulting strategic decisions.

Past microfinance research has examined the representation of stakeholders on the boards of MFIs and their contribution to MFIs' performance (Hartarska, 2005; Hartarska & Mersland, 2012; Mori & Mersland, in press). These studies concluded that stakeholder representation on boards matters and affects MFIs' performance. This paper moves a step further and contributes to the literature by showing from a theoretical perspective how stakeholder involvement contributes to the characteristics of SDMPs. It applies the stakeholder theory and the strategic decision-making literature to map out the involvement of local and international stakeholders serving on MFI boards.

The paper argues that the presence of stakeholders on MFI boards causes SDMPs to be characterized simultaneously by information gathering/usefulness and political behaviour. Stakeholders are a source of useful information, which benefits MFIs by leading to better strategic decisions. However, they also bring costs in terms of conflict, debate and disagreements, resulting in poorer decisions. Furthermore, their involvement in SDMPs may enable MFIs to face the trade-off inherent in their dual objective (financial self-sufficiency and poverty reduction). Stakeholders, like owners, may be motivated to focus only on financial sustainability, while donors may focus only on poverty reduction. The discussion throughout the paper argues that successful MFIs need to make high-quality strategic decisions. In order to reach these decisions, the process should unfold smoothly so that the decision makers can act in a timely manner, considering the useful information gathered and managing the political behaviour engaged in by the various stakeholder groups.

The paper is organized as follows. Section 2 presents a literature review of stakeholder theory and boards and discusses the stakeholders in MFIs. Section 3 gives an overview of SDMPs. Section 4 discusses stakeholders' involvement in SDMPs, and develops some related propositions. Section 5 presents and discusses the model. Section 6 presents conclusions, implications, limitations and suggestions for future research.

2.0 STAKEHOLDER THEORY AND BOARDS

Stakeholder theory is based on the premise that organizations should be responsible to a range of groups in society rather than just their owners (Freeman, 1984). In this way, Freeman argued, the organization is envisioned as the centre of a network of stakeholders, a complex system through which services, information, influence and other resources are exchanged. Stakeholders have been defined in various ways, ranging from the narrow to the broad (Mitchell et al, 1997). A broad definition was introduced by Freeman (1984), who referred to a stakeholder as any group or individual who can affect or is affected by the achievement of the organization's objectives. Mitchell et al (1997) further classified stakeholders according to power, legitimacy and urgency. They stated that, in order for organizations to identify and work with their stakeholders, they should first categorize them in terms of these three dimensions. They also asserted that stakeholders possessing at least two of the three dimensions are those to whom organizations are likely to pay the most attention.

This paper adapts Clarkson's (1994 pg. 5) definition, which states that the primary stakeholders are those who "bear some form of risk as a result of having invested some form of capital, human or financial, something of value, in an organization. Examples of these stakeholders, Clarkson stated, are owners, investors, employees, customers, suppliers, communities and governments. Mitchell et al (1997) called these stakeholders "dominant", stating that they possess legitimacy and power. Spitzeck and Hansen (2010) further argue that, in situations where stakeholders are both powerful and legitimate, their influence over the organization is assured

Proponents of the stakeholder theory have further suggested that including stakeholder representatives on boards is a way of formally demonstrating the strength of their ties with the organization (Mitchell et al, 1997; Hillman et al, 2001). Stakeholders on boards may also cause organizations to incorporate stakeholder interests, may assist in providing a variety of resources and may improve SDMPs (Spitzeck et al, 2011). On the other hand, stakeholders on boards may lead to a conflict of interests (Gijselinckx, 2009). This may impose on boards the political task of negotiating and resolving the conflicting interests of different stakeholders in order to set policies and make good strategic decisions. This implies that organizations need to clearly identify their primary stakeholders in order to minimize conflicts of interest and benefit from the presence of those stakeholders on their boards.

2.1 Stakeholders in MFIs

Labie and Mersland (2011) suggested that, in order to know how MFIs are really managed, it is necessary to consider their many different stakeholders as this will give a clear idea of where true power lies. Various stakeholders play an important role in microfinance due to the industry's diversity. First, a variety of financial institutions are involved in microfinance activities, including commercial banks, credit unions, non-bank financial institutions (NBFIs), and non-profit organizations (Galema et al, 2012). Different types of institutions have different stakeholders. For example, non-governmental organizations (NGOs) may have donors (Galema et al, 2012; Mersland, 2011), credit unions may have customers and commercial banks creditors.

Second, MFIs commonly have two often conflicting objectives: financial self-sufficiency and poverty reduction (Hermes, Lensink, & Meesters, 2011). Their mission – to reach the poor while simultaneously remaining financially sustainable – implies that there will be different stakeholders with varying interests in MFIs' performance. Lastly, the industry has received a lot of international attention, partly due to the United Nations naming 2005 as the "Year of Microcredit" and as a result of the Nobel Peace Prize being awarded to the Grameen Bank and Mohammad Yunus in 2006 (Labie & Mersland, 2011). Today, thousands of international NGOs, politicians and celebrities are getting involved in microfinance and this means that the number of stakeholders, including international donors, creditors and owners, is increasing. These factors all imply that stakeholders play a dominant role in the life of MFIs (Mitchell et al, 1997).

Hartarska and Mersland (2012) discuss groups of MFI stakeholders who may be on boards, including customers, employees, donors and creditors. I borrow these groups and add a further group: owners. Also, due to the international nature of the industry, I categorize stakeholders as either local or international. Local stakeholders are defined as those who are located within the country where the MFI operates and international stakeholders as those located elsewhere. I use this categorization to show how the contextual background of stakeholders can vary. Table 1 defines the groups of stakeholders and lists their interests in MFIs.

Having stakeholders on boards might be a source of goodwill towards the MFI, but one can also imagine it leading to them extracting resources. As Table 1 shows, stakeholders represent a range of interests that could lead MFIs making good or bad strategic decisions. Strategic decisions are important for MFIs as they chart the direction the organization will take (Freeman, 1984; Labie & Mersland, 2011). Thus, any groups with the ability to affect that direction should be involved in SDMPs.

Table 1: Stakeholders on MFI boards

Category	*Group*	*Primary interests in the MFI*
Local	Customers	High-quality products and services Affordable prices of products and services Sustainability of products and services
	Employees	Financial sustainability Good working conditions
	Creditors	Repayment capacity Outreach to poor customers
	Owners	Outreach to poor customers Financial sustainability Generating dividends
International	Donors	Outreach to poor customers Providing technical assistance
	Owners	Outreach to poor customers Financial sustainability Generating dividends
	Creditors	Repayment capacity Outreach to poor customers

3.0 STRATEGIC DECISION-MAKING PROCESSES (SDMPs)

SDMPs refer to a set of activities through which strategic problems are identified, interpreted, tackled and solved (Elbanna & Child, 2007b). The process has also been described as a sequence of behaviours through which decision makers scan the environment to gather data about important events and trends (Dimitratos et al, 2011). They then convert this data into information using interpretation systems, which they use to make strategic decisions (Ketchen et al, 1996). SDMPs can be complex as they involve many conflicting interests. Thus, they can take a long time, possibly facing interruptions, delays and disruptions (Ji, 2010). They can be shaped by environmental and decision-specific factors and by factors relating to the decision makers themselves (Elbanna & Younies, 2008; Hart, 1992).

The literature shows that SDMPs are multi-dimensional in nature, with most studies focusing on selected characteristics (Dimitratos et al, 2011; Elbanna, 2006). Similar to Ketchen et al (1996), this study conceptualizes SDMPs in terms of information gathering/usage (information), and political behaviour. Information refers to the data that decision makers collect and process in making strategic decisions. It has been associated with the ability to make comprehensive decisions and to be rational about all aspects of strategic decisions (Dean & Sharfamn, 1996; Elbanna & Child, 2007a). Information also enables decision makers to be exhaustive or inclusive when making and integrating strategic decisions (Frederickson, 1984). Decision makers enter into the process with known objectives, which determine the value of the possible consequences of an action. The actors gather appropriate information, and develop a set of alternative actions. They then select the optimal alternative (Elbanna & Younies, 2008). Collecting and processing information is therefore essential to making rational and high-quality decisions.

Political behaviour refers to the lobbying, disagreements, conflict and bargaining that surround SDMPs (Eisenhardt, 1999; Ketchen et al, 1996). This characteristic assumes that decisions emerge from a process in which decision makers have different goals, and thus form agreements so as to achieve their goals, leading to a situation where the preferences of the most powerful prevail (Dean & Sharfamn, 1993; Eisenhardt & Bourgeois, 1988). The key assumption here is that organizations and boards are coalitions of people with competing interests. These people may share some goals but they may also have conflicting interests (Elbanna, 2006).

Past research suggests that a high level of the political behaviour of the board is associated with poor performance (Eisenhardt, 1989; Eisenhardt & Bourgeois, 1988) because politics distracts decision makers from dealing with strategic issues. However, other studies contend that conflicts and disagreement as a result of political behaviour may bring about a consensus (Roberto, 2004). Collier, Fishwick, and Floyd, (2004) for example, argued that political behaviour is not always bad. When everyone shares a common vision, political behaviour may be the only means for creating strategic change. However, when power and politics become the dominant basis for strategic decision making, the outcomes are likely to be adverse (Collier et al, 2004).

These two characteristics have been widely discussed in the corporate literature, and have been examined in relation to constructs such as strategic decisions and organizational performance (see the review by Elbanna, 2006). In addition, studies have focused on identifying the effects on SDMPs of individual factors (such as CEOs; Elbanna, 2007), group factors (such as top management team; Eisenhardt, 1989) and organizational factors (such as management policy; Dimitratos et al, 2011; Elbanna, 2006). These studies have shown that various contextual factors contribute to strategic decisions. The present study contributes to the topic by looking at stakeholders' influence on SDMPs, something that has been missing in previous studies.

4.0 BOARD AND STAKEHOLDER INVOLVEMENT IN SDMPs

Involvement in strategic decision making is one of the most important governance and strategy-related roles of the board (Minichilli, Zattoni, & Zona, 2009; Pugliese et al, 2009). Board involvement here refers to the overall level of participation by board members in making strategic decisions that affect the long-term performance of an organization (Judge & Zeithaml, 1992). The board's involvement in SDMPs enables it to challenge the CEO, improve its execution of strategy, reach high-quality strategic decisions, develop a competitive advantage and improve organizational performance (Collier et al, 2004; Pugliese et al, 2009).

For MFIs, the main strategic decisions typically revolve around determining the growth strategy in terms of new product development, a change in geographical outreach, the choice of top managers, lending policies and interest rates (Lapenu & Pierret, 2005). Labie and Mersland (2011) further suggested that MFIs' governance should not only be based on the ability to ensure financial sustainability and regulatory fitness, but also on a clear strategic vision and a high level of transparency. It is also emphasized that strategic vision and transparency can be well articulated when these organizations include stakeholders on their boards and involve them in making strategic decisions (also see Lapenu & Pierret, 2005).

Furthermore, in the wake of the global financial crisis, increasing competition and international recognition of the microfinance industry, strategic decisions are even more important for ensuring MFIs' survival, strengthening the case for the involvement of stakeholders (Galema et al, 2012; Lapenu & Pierret, 2005).

Several microfinance studies have looked at the relationship between the presence of stakeholders on boards and MFI performance. These studies have important implications for stakeholders' involvement in SDMPs. For example, a study by Hartaska (2005) found that boards including employee stakeholders had a lower level of performance, while those including a high proportion of international donors had higher level of social performance. She also found that boards with a high proportion of local, mainly customer, stakeholders had better financial performance. Similarly, Hartarska and Mersland (2012) studied which governance measures promote efficiency in reaching poor customers. Their results showed that MFIs with a large proportion of employees or donors on their boards were less efficient, while those with both local and international creditors on their boards were more efficient

In summary, these studies have shown that microfinance stakeholders sit on boards and their presence on them influences MFIs' performance. Even though these studies looked at stakeholders on boards as a governance measure, we know from the literature that boards make strategic decisions and therefore, if stakeholders are on boards, they must be involved in strategic decision making as well. Since these studies have shown that stakeholders can have both a negative and positive effect on MFI performance, this study analyzes how their involvement in SDMPs determines the board's ability to make strategic decisions. The next section explains the importance of each type of stakeholder, the reasons why they sit on MFI boards and their influence on the two characteristics of SDMPs being studied – information gathering/usefulness and political behaviour. The propositions developed are based on the assumption that stakeholders are represented on boards and, as a result, are involved in making strategic decisions.

4.1 Customers

Microfinance customers are poor people, most of whom are excluded from the formal banking sector. They can be divided into two types: depositors and borrowers. MFIs serve their customers in a variety of ways in consideration of their low-wealth status. For example, depositing and lending processes are different from those of corporate banks (Abbink, Irlenbusch, & Renner, 2006). As a result, it is important for MFIs to involve customer representatives in making strategic decisions so that they meet customers' needs.

Recent studies have shown that many MFIs are now embarking on a market-oriented view instead of the product view taken in the past (Galema et al, 2012). This is a result of competition, customer knowledge, and the organizations' experience with various products and services (Assefa et al, 2012; Bédécarrats, Baur, & Lapenu, 2011). Taking a marketing approach means that customers' needs are put first, making their involvement in SDMPs more important as it provides the board with information about what is best for customers in terms of types and ways of delivery. This information is key to helping MFIs compete with others by making the right strategic decisions.

When customers invest their time and energy in serving on MFI boards and helping with decision making, they will want their personal interests to be considered. Mori and Mersland (in press) showed that customer representation on boards is positively associated with an MFI's financial performance and negatively with its social performance. They argued that the presence of customers on boards leads MFIs to serve better-off customers (by improving their financials) and to neglect the desperately poor, going against the mission of MFIs.

Meanwhile, borrowers and depositors are likely to have conflicting interests concerning strategic decisions, such as the choice of interest rates (Lapenu & Pierret, 2005). For example, depositors will prefer high interest rates while borrowers will want to see low interest rates. The above arguments imply that customer involvement in SDMPs gives them the ability to exercise their influence and bring in conflicting interests (Collier et al, 2004). Based on this, I propose the following:

Proposition 1a: The involvement of customers in making strategic decisions is associated with the board's ability to gather and use information.

Proposition 1b: The involvement of customers in making strategic decisions is associated with a high level of political behaviour on boards.

4.2 Employees

For the MFI to have good outreach and financial sustainability, it must have committed employees. The employees of MFIs are generally local, and include middle managers, credit officers, cashiers and others. They tend to be highly involved in the MFI, often having contact with customers, both in offices and at customers' sites (Labie, Meon, Mersland, & Szafaraz, 2011). As a result, employees can offer relevant information to boards concerning how to improve their products, service and delivery, possibly offering a better competitive strategy (Lapenu & Pierret, 2005). It has also been argued that employees have direct access to detailed information concerning organizational activities (Clapham & Cooper, 2005). Their involvement in SDMPs will give them the opportunity to participate in the long-term growth of the MFI, giving them a sense of ownership that, in turn, will improve the MFI's performance and its strategic decisions (Kuye & Sulaimon, 2011).

On the other hand, employee involvement may produce biased information that may discriminate against certain customer groups: Labie et al (2011) show that some MFI employees are reluctant to interact with certain minorities, such as the disabled. Involving these employees in SDMPs could result in conflict and debate, slowing the pace of decision making (Roberto, 2004).

Employees may also give biased information to boards because they fear repercussions from their bosses (CEOs), or because it may hamper their relationship with the CEO (Wagner, Stimpert, & Fubara, 1998). Moreover, employees will also have their own self-interests they will want the board to consider (Hartarska & Mersland, 2012; Labie et al, 2011). Their involvement in SDMPs could thus lead to debate and disagreements, particularly over issues such as salaries and working conditions.

Hartarska and Mersland (2012) found that boards with a high proportion of employees on them are inefficient. This finding contradicted that of Cerise (2002 as noted in Lapenu & Pierret, 2005), who showed that MFIs with employees on their boards and involved in SDMPs perform better than those without. These arguments suggest that employee involvement has both advantages and disadvantages – bringing in valuable information with less political issues but also possibly biased information and more disagreement – which may produce a curvilinear relationship with the characteristics of SDMPs. Based on the above, I propose the following:

Proposition 2a: The involvement of employees in strategic decision making has a curvilinear relationship with the board's ability to gather and use information.

Proposition 2b: The involvement of employees in strategic decision making has a curvilinear relationship with the level of political behaviour on the board.

4.3 Creditors

The relationship between creditors (local and international) and organizations is linked with increasing the latter's access to funding (Dittmann, Maug, & Schneider, 2010; Hilscher & Sisli Ciamarra, 2011). Creditors' involvement in organizational strategic decision making has two implications for the loans made to organizations and the exercise of proxy voting rights (Agarwal & Elston, 2001), and provides a strong channel of information moving in both directions. One benefit is that, if creditors have access to private information about an organization, the latter may benefit from better access to finance.

Creditors' involvement in SDMPs may also cause a potential conflict of interests regarding financing decisions (Hilscher & Sisli Ciamarra, 2011; Kroszner, 2001). Creditors might encourage the management to undertake higher risk projects. Dittmann et al (2010) have shown that creditors who participate in strategic decision making favour their own interests.

There is currently a high level of involvement by local and international creditors in the microfinance industry (Mori & Mersland, in press). These creditors are a combination of socially oriented and solely business-focused creditors. Socially oriented creditors have a social mission in mind and want to see the MFI achieve the social side of its previously mentioned dual objective. Some of these creditors may not charge any interest in return for lending to the MFI but they will want to get involved in most of the MFI's activities, including making strategic decisions. Business-oriented creditors, on the other hand, act like commercial banks; here, the relationship is purely based on business and the MFI's repayment capacity. Such creditors will want the MFI to be financially sustainable so that they will recoup their money. These two types of creditors thus have diverging interests and the presence of both on a board is likely to lead to debate and disagreement about what the MFI should do.

A study by Olomi, Mori, and Khalid (2012) showed that some MFIs may have a relationship with more than four separate creditors, each of which may sit on the board and influence strategic decisions. They also showed that creditor influence is one of the causes of MFI failure, especially when creditors are highly involved in the MFI's activities. In contrast, Hartarska and Mersland (2012) found that boards including creditor representation lead to MFIs that are more efficient at reaching poor customers, which implies that creditors may have an important role to play on boards and in SDMPs.

From these arguments, it seems that creditors can be both beneficial and a curse to SDMPs, beneficial in terms of providing information and access to finance and a curse because they may use their power and influence to convince MFIs to make decisions in their own interests rather than the MFI's (Dittmann et al, 2010), causing the process to be characterized by (overly) political behaviour.

Proposition 3a: The involvement of creditors in strategic decision making is related to the board's ability to gather and use financial information.

Proposition 3b: The involvement of creditors in strategic decision making is related to a high level of political behaviour on boards.

4.4 Owners

Similar to those of corporate organizations, MFI boards are mostly populated by owner representatives who are residual claimants. The microfinance industry has a variety of local and international owners. Some are international companies, agencies or NGOs, such as the Consultative Group to Assist the Poor (CGAP) which, through its "Council of Microfinance Equity Funds", provides equity in return for shares or influence (Council of Microfinance Equity Funds, 2005; Urgeghe & Mersland, 2011). Other owners include local members of society who provide subscriptions in return for MFI shares. These owners can further be divided into the classic and mixed type (Labie, 2001; Mersland, 2009). Classic owners are profit motivated and their involvement in SDMPs will thus lead to decisions that are profit oriented. Mixed owners (or socially responsible owners) consider both profit and the social impact. Both types sit on boards to control, advise and bring information that will enable the MFI to attain its objectives.

Having a mixture of classic and mixed owners on boards might be a further source of political behaviour in SDMPs. As argued by Elbanna (2006), decision-making board members use political tactics to exert influence on the decision-making process to ensure that their self-interests are embedded in the outcome. An example of a debate that is typical at present among the owners of MFIs is that regarding group versus individual lending. The literature has shown that individual lending is associated with serving less poor customers while group lending is associated with serving the very poor (Cull, Demirguc-Kunt, & Morduch, 2011). Making this type of decision could involve a large amount of conflict among owners given their different interests. Therefore, owner involvement in SDMPs could bring in not only good advice, funding and information, but also increased political behaviour:

Proposition 4a: The involvement of owners in the strategic decision-making process is related to the board's ability to gather and use a variety of information.

Proposition 4b: The involvement of owners in making strategic decisions is related to a high level of political behaviour on the board.

4.5 Donors

International donors and technical assistance providers (TAPs) are supporters and funders who speed up the evolution and success of MFIs. They specialize in giving funds, measuring progress, and spreading good practice (Schreiner, 2000). Their role in SDMPs is important because they contribute to the MFI's ability to achieve its dual objective (Mersland, 2011). Donor involvement is also a way for them to control the use of the funding they provide and to influence their relationship with MFIs (Mori & Mersland, in press). They also bring international expertise, information about funding opportunities and different cultural aspects that can be fruitful for MFIs (Mersland, Randøy, and Strøm 2011).Mersland, et al (2011) further showed that MFIs with international donors have better social performance. However, Hartarska and Mersland (2012) found that boards with a higher proportion of donors are less efficient.

Most international donors have a social mindset regarding MFIs, that is, their support is offered to further the achievement of social objectives. As a result, their involvement in SDMPs may result in less conflict as they will have a similar mission to the MFI's management. Thus, this paper argues that donor involvement in SDMPs is associated with the board's ability to gather relevant information regarding funding, to provide advice based on the international exposure of the donors, and to do so with fewer conflicts:

Proposition 5a: The involvement of donors in the strategic decision-making process is related to the board's ability to gather and use information.

Proposition 5b: The involvement of donors in the strategic decision-making process is related to a low level of political behaviour on boards.

Table 2 summarizes the above discussion, showing how the various stakeholders influence the two aspects of SDMPs, information gathering/usefulness and political behaviour.

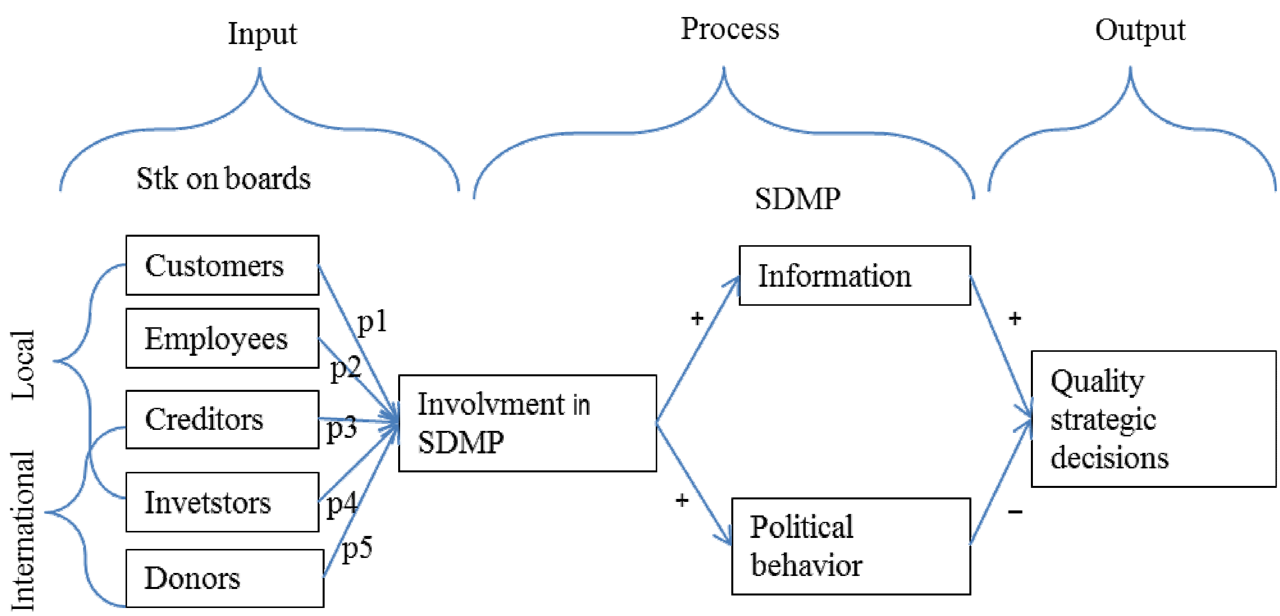
Table 2: Stakeholders and their influence on SDMP characteristics

Stakeholder	***Information gathering/usefulness***	***Political behavior***
Customers	-Information about customers' (depositors and borrowers) needs. -Information that assists with product design strategies and customer-related strategies.	-Self-interested; not focused on the MFI's mission. -Self-interested; focused on their own future relationship with the MFI. -Depositors argue for high interest rates, borrowers for low interest rates.
Employees	-Specific information on customers, needs and products/services that suit the market. -Internal-specific knowledge and information reducing reliance on the CEO.	-Discrimination against minority customers. -May protect the CEO due to concern over their jobs. -May push for higher salaries and better working conditions. -Financial sustainability.
Creditors	-Advise on financial matters. -Bring information and resources regarding sources of finance.	-Socially-oriented creditors focus on the social mission while business-oriented creditors focus on financial sustainability.- -Focus on projects that benefit them.
Owners	Information necessary for the monitoring of their funds. Advising management on MFI objectives.	Socially responsible owners focus on the social mission while classic owners focus on financial sustainability.
Donors	-Information about funding opportunities. -Provide assistance such as training and mentoring. -Information based on international exposure.	-Focus on the social mission.

5.0 THE MODEL

As the previous section showed, different stakeholders on boards influence information gathering/usefulness and political behaviour that characterize SDMPs in different ways. Elbanna and Younies (2008) showed that decision makers can be rational in terms of gathering and utilizing information while simultaneously behaving politically with regard to conflicts of interest and disagreements. Figure 1 represents the model derived from the previous section, which is divided into three parts: (i) inputs (local and international stakeholders on boards), (ii) the process (SDMP characteristics) and (iii) outputs (strategic decisions).

Figure 1: Stakeholders and Their Involvement in Strategic Decisions



5.1 Inputs

Grönroos and Ojasalo (2004) referred to inputs as various stakeholders and their involvement in the processes that result in outputs. They further asserted that the interactions that are created by these inputs influence the efficiency of the decision-making process and its outcomes. Here, the five MFI stakeholder groups who sit on boards are the inputs to the process of making strategic decisions. Their actions and ideas are incorporated into the MFIs' SDMPs.

5.2 Process

The information that is gathered and acted upon is the basis for rationality as regards SDMPs (Elbanna, 2006). Rationality occurs when the decision makers (stakeholders in this case) gather useful information and act upon it to make strategic decisions (Chaserant, 2003). The propositions above argued that stakeholders are a source of a variety of useful information to be gathered and interpreted so as to make decisions. In addition, when stakeholders are involved as decision makers, they are in a position to enter into the decision-making process with known objectives. These objectives are likely to be used to determine the possible consequences of an output and to develop a set of alternative outputs from which the best will be selected (Eisenhardt, 1989).

The above figure and the propositions also suggest that stakeholders on boards are a source of political behaviour due to conflicting interests. Political behaviour occurs because stakeholders, as decision makers, have different amounts of power and different self-interests. Boards containing various types of stakeholders are likely to experience a high level of political behaviour since each member represents different interests and people. However, the literature indicates that these conflicts are minimized when efforts are made to ensure that the members have the same vision, approach and goals. Following Eisenhardt and Zbaracki (1992), political behaviour will arise in SDMPs as long as there are many individuals involved with different interests. If this behaviour is not managed, it may result in poor decisions being made.

5.3 Outputs

The outputs of SDMPs are decisions, which in the context of microfinance, could concern product development, growth strategies such as reaching out to new markets, financing strategies and the setting of interest rates (Lapenu & Pierret, 2005). Stakeholder involvement in SDMPs may result in a shared vision among all the board members involved, which can be important in ensuring MFI survival.

This model has various limitations. First, it is important to consider that a board can at any point be dominated by just one or a few of these stakeholder groups. For example, if it is dominated by customers, the SDMPs will be angled towards their interests, and most of the information gathered will be what customers can access. The strategic decisions may be geared towards serving the better-off customers, and financial sustainability (Mori & Mersland, in press). Meanwhile, if the board is dominated by employees, decisions may lean towards higher salaries, which may lead to the charging of higher lending rates (Labie et al, 2011). Funders such as creditors, donors or owners also have different and conflicting interests. Donors may encourage a social mission, owners financial sustainability. As a result, it is important that MFIs consider the conflicting interests of their stakeholders and assess the damage that could occur if the process is dominated by any one of these groups.

Secondly, the model does not consider the timing in which strategic decisions are made and when is the most appropriate time to involve stakeholders. Eisenhardt (1989) argued that strategic decision making is different at different times. She provided evidence that, when organizations are faced with high competition and uncertainty about the future, they tend to gather more information from various sources and use it quickly to make strategic decisions. This implies that MFIs should take the timing of decisions into account when they involve stakeholders. It may be that when they are facing uncertainty, such as during the current financial crisis, certain groups of stakeholders need to be involved.

This model helps to show that the involvement of diverse stakeholders on boards and in making strategic decisions is crucial for MFIs. Their role can ensure that strategic decisions are made that are in line with the mission of the MFI and that consider all stakeholders' varying interests. The above model serves as a theory-based framework that will be useful for developing a more comprehensive understanding of the microfinance stakeholders who sit on MFI boards and their role in strategic decision making.

6.0 CONCLUSIONS AND IMPLICATIONS

The purpose of this paper was to identify stakeholder representation on the boards of MFIs, and discuss their role and involvement in the strategic decision-making processes. The literature review revealed that stakeholders can provide MFIs with both benefits, in terms of information gathering/usefulness, and costs, in terms of political behaviour. Overall, their inclusion on boards can increase MFIs' ability to survive in the industry. Several studies have indicated that competition is a major driver of the performance of MFIs and should be encouraged in order to lower interest rates resulting in better outreach to the poor (Assefa et al, 2012; McIntosh et al, 2005). To be able to compete in the industry, MFIs need to operate strategically and one way of achieving this is to build closer relationships with stakeholders by appointing them to boards and involving them in strategic decision making. The discussions in this paper serve as a good basis for further research in this direction. The implications are discussed below.

6.1 Theoretical Implications

This paper contributes on a theoretical basis to stakeholder theory and the strategic decision-making literature. In terms of stakeholder theory, it responds to a call by (Laplume, Karan, and Litz, (2008), who suggested that the stakeholder theory should be used to study contexts other than large corporations in the developed world. This paper applies the theory to the context of the microfinance industry, which is unique in various ways. First, it is a young and entrepreneurial industry that focuses on providing finance to the poor (Hermes et al, 2011). Second, it has received a large amount of international attention since 2005, which the United Nations named the "Year of Microcredit" (Labie & Mersland, 2011). Third, there are a variety of organizational forms that offer microfinance services, such as NGOs, banks and cooperatives (Galema et al, 2012). As a result, the industry incorporates various stakeholders. This paper incorporated the unique characteristics of the microfinance industry into the arguments of the stakeholder theory in order to identify these stakeholders, and discussed the benefits and costs of their involvement on boards and in SDMPs.

Most of the strategic decision-making literature looks at the content of strategic decisions, with less attention having been paid to the process side (Ji, 2010). However, Elbanna (2006) contended that the two perspectives are complementary rather than alternatives and that content research can significantly influence the direction of process research and vice versa. This paper contributes to process research by looking at two characteristics of SDMPs: information gathering/usefulness and political behaviour. The paper specifically argued that microfinance stakeholders provide unique information and it discussed the benefits of this information for making decisions. The paper further indicated how the conflicting interests of stakeholders can be a source of political behaviour in relation to SDMPs and how this can harm strategic decision making. To the author's knowledge, this study is among the first to provide a theoretical framework of how stakeholder involvement affects SDMPs in MFIs. Past studies have focused mainly on top management (Eisenhardt, 1989; Elbanna, 2007) and employees (Kuye & Sulaimon, 2011) in large for-profit organizations

6.2 Practical Implications

In view of the current global financial crisis, it is important that MFIs start to consider the interests of various stakeholders in their activities, as it could be crucial for their survival. Holmes and Moir (2007) noted that stakeholders are a source of innovation and competitive advantage. Therefore, MFIs need first to identify their primary stakeholders, then work with them so as to benefit from their expertise.

One of the roles of MFI boards is to make strategic decisions that enable them to compete and succeed (Mori & Randøy, 2011). Appointing stakeholders to these boards involves them in making strategic decisions, a process that is important to the organization's ability to perform and survive (Ji, 2010). This paper has argued that the relationship with stakeholders will open the door for better strategic outcomes, such as new products that match demand, or new ways of providing services, because of the relevant information these stakeholders will provide. Since stakeholders have intrinsic value, this paper claims that their involvement will aid MFIs' long-term survival by enabling them to make unique strategic decisions.

Despite the advantages, MFIs should also be aware that there are costs and risks associated with having stakeholders on their boards. They may be involved in rent-seeking behaviour by trying to meet their own objectives instead of the MFI's and thus complicate SDMPs. Through political behaviour, they may also contribute to the conflict between the dual objective of MFIs. For example, owner or employee board members may want MFIs to serve wealthier customers so that they will receive higher returns or salaries/bonuses.

6.3 Limitations and Further Research

This paper has a few limitations. First, it discussed the influence of individual stakeholder groups on board decisions. It did not consider the interactions between different stakeholders. Future research should explore such effects on SDMPs. Second, the paper lacked empirical evidence regarding the extent to which stakeholders do in fact influence SDMPs. It did, however, develop propositions that could be used as a basis for future empirical studies. The research question of such studies could be: To what extent does each of these stakeholders influence the strategic decision making of an MFI and does stakeholder involvement affect the outcome of MFIs' strategic decisions?

Another area for future studies to explore is stakeholder governance in various contexts. MFIs operate in different countries with different institutions. This has implications for the capacities and skills of the stakeholders and their resulting influence on MFI boards. Furthermore, stakeholders do not influence MFI governance by serving on boards only (Labie & Mersland, 2011). It would be interesting to consider the influence of non-board stakeholders on the decision making and performance of MFIs. This would contribute further to our knowledge of the necessity of stakeholder involvement in MFIs, especially in the light of fierce competition, the financial crisis and the withdrawal of donor support.

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ESSAY 4

THE BOARDS OF MFIS: HOW DO STAKEHOLDERS MATTER?

The Boards of MFIs: How Do Stakeholders Matter?

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ABSTRACT

Microfinance institutions (MFIs) provide financial services to poor people. Governance of these organizations is important so that they can operate efficiently and sustainably. This study analyzes the influence of stakeholders (donors, employees, customers, and creditors) on board structure (board size and CEO duality) and on organizational performance. We used a global data set of 379 microfinance institutions from 73 countries, collected from rating organizations. Supported by the stakeholder theory, agency theory and resource dependence theory, we found that stakeholders are important and have various influences on MFIs. We found that donors are associated with small boards, non-duality and better performance. Employees are associated with large boards, while customers are associated with duality and good financial performance. Creditors opt for duality and better social performance. Implications and areas for future research are discussed.

1.0 INTRODUCTION

Microfinance institutions (MFIs) provide financial services to poor families and microenterprises. Access to microfinance has the potential to help poor people smooth consumption, mitigate risks, build assets and improve their income. The building of a self-sustaining microfinance industry is high on the policy agenda (Cull et al 2009). However, most MFIs struggle to keep afloat financially without subsidies. Various policy papers indicate the importance of governance to the performance of MFIs (Labie and Mersland 2011; Lapenu and Pierret 2005), and industry actors rate "governance" among the most important risk factors in the industry (CSFI 2011). However, relatively little is known about the empirical relationship between governance structures and MFI performance. This study responds to the need for more knowledge on how stakeholders influence board structure and the performance of MFIs. In particular, this study responds to Labie and Mersland (2011), who argue for a more stakeholder-based approach to determining "who" and "what" really count in the governance and performance of MFIs.

MFIs are private organizations incorporated as non-governmental organizations (NGOs), member-based cooperatives or banks[*](Mersland 2009). This means that the stakeholders who are represented on boards may vary depending on the type of MFI. In addition, Labie and Mersland (2011) suggest that good governance is not only based on the ability to ensure the sustainability of the organization, but also on strategic vision and transparency. The authors further suggest that this is possible when organizations adopt a stakeholder approach that includes the key actors in an organization. Thus, in this study we aim to answer three questions: (1) What is the representation of stakeholders across different types of MFIs? (2) To what extent do stakeholders affect an MFI's board structure? (3) What influence do stakeholders have on an MFI's performance?

Similar to other board members, stakeholders on boards are responsible for monitoring and advising managers (Hillman et al 2001). With MFIs' dual objective of serving the poor and becoming sustainable, it is suggested that boards play an important role. We used the agency and resource dependence theories (Jensen and Meckling 1976; Pfeffer and Salancik 1978) to discuss the role of board members. We also used the stakeholder theory (Freeman 1984) to identify and discuss four types of stakeholder: donors, employees, customers and creditors.

[*] The term bank includes both commercial banks and non-bank financial institutions.

Microfinance policy papers provide several recommendations on how boards of MFIs should be structured, in particular in terms of size and stakeholder representation (Rock et al 1998). However, there is little knowledge of which stakeholders are represented, and how and where they are represented. Also, few empirical studies have examined the relationship between stakeholders in and the performance of MFIs (Hartarska 2005; Hartarska and Mersland, 2012).The findings of those few are inconclusive, and this justifies the need for more studies on stakeholder analysis. For example, (Hartaska, 2005) found that donors positively influence social performance, while (Hartaska & Mersland, 2009) found that they are not beneficial. Furthermore, these studies only examined the relationship between stakeholders and performance. We argue that stakeholders may also influence board structure (CEO duality and board size). We therefore generally hypothesized that stakeholders on boards affect board structure and the performance of MFIs.

We used data from public sources, containing 379 MFIs from 73 countries, collected between 2001 and 2008. We used a mixture of techniques to carry out the analysis. For MFI characteristics and board structure variables, we used ordinary least square regressions and probit regression. To tackle endogeneity concerns, we used a two-stage least square regression with instrumental variables to analyze the association between stakeholders and performance.

The results show that stakeholders have various influences on both governance and MFI performance. We found that donors and employees are better represented in NGOs, creditors in banks and customers in cooperatives. We further found that stakeholders are associated with larger internationally-initiated MFIs. In terms of board structure, we found that donors are associated with small boards and non-duality. Thus, the monitoring aspect seems to be important for donors. When donors interact with creditors, they also opt for small boards. Furthermore, we obtained evidence that donors and creditors positively affect MFIs' social and financial performance. Employees, as resource providers, are associated with large boards, but are not beneficial for MFI performance. We also show that customers are associated with duality, lower MFI costs and better financial performance. Similar evidence is seen when customers interact with employees.

The paper proceeds as follows. Section 2 presents the theory, literature and hypotheses. Section 3 presents an overview of the dataset, variables and models. Section 4 presents stakeholder demographics, which is followed by a discussion of the board structure results in section 5. Section 6 discusses the results relating to stakeholder influence on performance and section 7 concludes the paper.

2.0 THEORY AND LITERATURE

2.1 Boards and Performance

Several studies on corporate governance focus on the relationship between boards and organizational performance (Pugliesse and Wenstøp 2007; Johnson et al 1996). Much of the focus has been placed on how board composition, size and CEO/Chair duality affect board members' roles and, ultimately, organizational performance (Elsayed, 2011; Larmou and Vafeas 2010). An underlying assumption of this research is that boards matter; they have the power to affect an organization's decisions, strategies and performance (Judge and Zeithaml 1992).

The role of boards in executing governance responsibilities has been divided into two conceptual categories: monitoring and resource provision (Hillman and Dalziel 2003). The monitoring role charges board members with responsibility for representing the interests of various stakeholders. Board members are expected to monitor the actions of managers, as agents, and ensure that they act accordingly (Jensen and Meckling 1976). Board members' resource provision role involves advising the organization and linking it with key constituencies in its external environment (Pfeffer and Salancik 1978). Because the external environment of an organization is beyond its direct control, it experiences uncertainty. The presence of board members, who represent critical contingencies, is presumed to provide the organization with access to valuable resources (Hillman et al 2009). Members with backgrounds or positions representing important external resources may help the organization to reduce the transaction costs associated with external interdependencies and enhance organizational performance.

Board structure and composition are considered important factors influencing the performance of boards (Lehn et al 2009). Similar to Mersland and Strøm (2009), we examined board structure in terms of board size and CEO duality. According to the agency theory, large boards are inefficient. They are not good monitors because of the problems that can arise from large groups, such as social loafing, free riding and higher coordination costs. Jensen, (2010) for example argues that "When boards get beyond seven or eight people, they are less likely to function effectively and are easier for the CEO to control". Largeness can inhibit a board's ability to initiate strategic actions. Judge and Zeithaml (1992) report that larger boards are less likely to become involved in strategic decision making. Yermack (1996) demonstrated that small boards are associated with better performance. He concludes that any benefits that may be associated with large boards will be overwhelmed by poor decision-making processes. In contrast, the resource dependence theory suggests that organizations with large boards perform better (Hillman et al 2001; Pfeffer and Salancik 1978). From this point of view, board size is a measure of an organization's ability to form environmental links so as to secure critical resources. With access to different areas of expertise, CEOs get better advice from large boards. A larger board may offer an exceptional level of high-quality advice to a CEO, leading to better performance.

CEO duality occurs when one person is both the CEO and the board chair of the organization (Rechner and Dalton 1991; McNulty et al 2011). The organizational literature supports the idea of duality in terms of power and unity of command (McNulty et al 2011). To effectively manage, it is necessary for a decision maker to have clear authority over his/her subordinates (Finkelstein and D'aven 1994). CEO duality helps to avoid confusion among employees as to who is the boss, which facilitates effective decision making. Non-duality creates multiple authority relations that promote role conflict among managers and employees. Agency theorists posit that duality can entrench a CEO, leading to failed internal control systems, and a board's inability to monitor effectively (Mallette and Fowler 1992). Also, CEO duality represents a conflict of interests, in which a CEO who is responsible for the strategic management of an organization is also in a position to evaluate the effectiveness of that strategy (Finkelstein and D'aven 1994). These arguments suggest that some board members will not advocate CEO duality because doing so increases the potential for less effective monitoring, which may endanger organizational performance.

A few studies in the microfinance literature have examined the relationship between board structure and MFI performance. Hartarska (2005) investigated the relationship between governance and the performance of MFIs in Eastern Europe. Among other governance mechanisms, she examined the impact of board size on the MFIs' performance. Her results indicate that MFIs with smaller boards perform better. Mersland and Strøm (2009) examined the effect of MFI board size and CEO duality on MFI performance. Contrary to Hartarska (2005), they did not find any evidence that performance improves with smaller boards. Nor do they find any evidence of the positive effect of CEO duality on performance. The authors conclude that it is hard to say whether MFIs are better governed when the CEO is also the board chair.

2.2 Board Composition and the presence of Stakeholders on Boards

When included on boards, it is suggested that stakeholders have a monitoring role and provide resources to CEOs and organizations (Hillman et al 2009; Luoma and Goodstein 1999). Despite the fact that organizations mainly put stakeholders on boards as a way of showing how important they are, the organizations also benefit (Charreaux and Desbrieres 2001). Stakeholders enable organizations to access various resources, including providing links with other stakeholders. The stakeholder theory posits that including stakeholder representatives on boards is a "formal mechanism that acknowledges the importance of their relationship with and interests in the organization" (Mitchell et al 1997). That is, by including stakeholders on boards, organizations are signaling their commitment to stakeholders in a visible way (Freeman 1984). Since different stakeholders have different interests, their inclusion on boards may affect board structure and organizational performance differently.

Several studies have examined the influence of stakeholders on boards. Luoma and Goodstein (1999) studied the relationship between organizational influences and the addition of stakeholders to boards in the US. Their results show that regulated and larger organizations have more stakeholders on their boards than unregulated and smaller organizations. Their study provides important insights into the process by which board plurality is increased through the addition of stakeholders. Hartarska (2005) investigated the effects of the inclusion on MFI boards of three types of stakeholder - donors, employees and customers - on the social and financial performance of MFIs. Her findings show that boards with employees result in a lower level of performance, boards with donors have better social performance, and those with customer representation have better financial performance. Hartarska and Mersland (2012) studied which governance measures promote efficiency in reaching the poor. Their results show that MFIs with employees on their boards are less efficient. They also provide evidence that the presence of donors on boards is inefficient, while that of creditors is beneficial.

Together, these studies provide evidence that stakeholders are important for boards and the performance of MFIs. However, none of these studies examined the relationship between stakeholders and board structure (size and duality). Since a few studies found that stakeholders affect organizational performance, we argue that this influence may be enacted through the effect of stakeholders on board structure. We now develop hypotheses to examine the relationship between stakeholders (donors, employees, customers and creditors), on the one hand, and board structure and MFI performance, on the other.

3.0 HYPOTHESES DEVELOPMENT

3.1 Donors

Donors are important actors through whom MFIs meet their dual objective. Schreiner (2002) argues that donors are like genetic engineers, speeding up the evolution of MFIs. The literature further shows that donors are good at providing funds, measuring progress and spreading good practice through technical assistance (CGAP, 2004). As funders, donors need to monitor managers in order to ensure their funds are spent appropriately (Alonso et al 2009). This means they would opt for a board structure that provides room for monitoring, that is, a small board and non-duality. In terms of performance, we infer that donors are more interested in social performance, since reaching the poor is part of their mission. Hartarska (2005) found that the presence of donors on boards improves social performance. Other arguments posit that donors fund and assist MFIs, which are likely to be financially sustainable (Rosenberg 2009). Furthermore, donors' objectives are to increase outreach to the poor. Thus, we expect to find that donors are associated with small and non-duality boards and we expect donors to positively influence MFIs' financial and social performance.

3.2 Employees

The corporate literature argues that employees are good at providing inside information to the board (Osterloh and Frey 2005). In MFIs, employees, particularly credit officers, are the cornerstone of their operations (Mori 2010; Battilana and Dorado 2010). Employees on boards may bring relevant information because they are better informed about the issues and problems concerning the MFI, sometimes better than the CEOs. However, because of employees' past experience and different interests, they may bring biased information, which could mislead the board when making decisions. In addition, the corporate literature suggests that employees on boards may not be good monitors of CEOs because they fear their bosses (Wagner et al 1998). Employees on boards could also influence whether the CEO is also the chair, since working for one boss would simplify their lives (Finkelstein and D'aven 1994). Hartarska and Mersland (2012) show evidence of a negative association between MFI boards with employees and performance. From these findings, it seems that employees are a good source of information for boards but monitor CEOs less closely than other stakeholders. Thus, we expect employees to be associated with large duality boards. In terms of their information and monitoring roles, we do not hypothesize about their effect on performance.

3.3 Customers

Customers of MFIs are generally poor people with little education. Thus, one may claim that their representation on boards may not be influential since they cannot contribute effectively to technical discussions. However, microfinance customers know what they want and possess enough knowledge to make certain decisions (Pischke 2002). Furthermore, MFIs are increasingly operating as market- (customer-) driven and not only product-driven organizations (Woller 2002). With increased competition, customer dropout and multi-borrowing, customer orientation is becoming increasingly important for MFIs. Woller (2002), for example, suggests that the key to achieving outreach and sustainability is the extent to which MFIs adopt a market-oriented culture. Mersland and Strøm (2009) argue that customers help by providing better information thereby improving performance. Hartarska (2005) also found that customers on boards improve financial performance. According to the resource dependence theory, a board should be large in order to benefit from its members' resources, and so we expect customers to be associated with large boards. To our knowledge, no literature argues in favour of an association between customers and duality and, therefore, we cannot stipulate their influence in this regard. We do however expect customer representation on boards to positively contribute to performance, in terms of the number of customers and sustainability.

3.4 Creditors

MFIs are increasingly shifting from donor to debt funding, and creditors represent an important stakeholder in the industry. In some cases, creditors become board members. The corporate literature shows that creditors on boards have two implications for organizations, through loans and accessibility of information (Agarwal and Elston 2001). As providers of loans, creditors monitor the allocation of loans to the organization. Their representation on boards also provides a strong channel of information to both parties. For example, the organization may benefit by knowing where and how to access finance (Byrd and Mizruchi 2003). However, creditors on boards may cause a potential conflict of interest in relation to the financing decisions of the organization (Kroszner 2001). For example, the creditor may influence the management to avoid taking on certain projects because they could affect the organization's ability to repay the creditor. Hartarska and Mersland (2012) found that creditors are beneficial for MFI performance. The authors argue that, through monitoring, creditors can positively affect performance. Thus we expect MFIs with creditors on their boards to have small boards and non-duality and, based on the agency theory, better performance.

3.5 Employees & Customers

The marketing literature groups customers into two dimensions: internal and external (Lukas and Maignan 1996). It suggests that internal customers are employees of organizations, while external ones are those buying products/services from organizations (Bowen 1996). We borrow this notion to look at the interaction effects of having both employees and external customers on boards. Both possess valuable information for the MFI and the board. The nature of MFI activities requires employees to work closely with external customers (Batillana and Dorado 2010). We predict that, when both are represented on boards, the boards will be larger and more resourceful, which will lead to better MFI performance.

3.6 Donors & Creditors

Donors and creditors share the characteristic of being providers of funds for MFIs. The difference is that donors give funding in the form of grants, while creditors give loans. Despite this difference, they both wish to see the MFI monitored and the funds used wisely. Creditors need to recover their loans while donors wish to see their grants used properly (CGAP 2009). Interaction between donors and creditors seems to be important because of this shared characteristic. They both want the MFI to perform well. Therefore, we predict that boards with both creditors and donors represented will be small, have non-duality and good performance. Table 1 summarizes all of the hypotheses.

Table1: Stakeholders and hypotheses

Stakeholders	A. Board structure		B. Performance	
	Board size	CEO Duality	Social	Financial
1. Any stakeholder	+/-	+ / -	+	+
2. Donors	-	-	+	+
3. Employees	+	+	+/-	+/-
4. Customers	+	?	+	+
5. Creditors	-	-	+	+
6. Employees & Customers	+	?	+	+
7. Donors & Creditors	-	-	+	+

4.0 DATA AND METHODS

4.1 Data

The data were obtained from secondary public sources. The dataset was compiled from rating reports available at www.ratingfund2.org. These rating reports have been collected by major microfinance rating agencies (MicroRate, Microfinanza, Planet Rating, Crisil and M-Cril) and contain information from 2001 to 2008. Each of the rating agencies is approved to rate and assess MFIs according to the Rating Fund of the Consultative Group to Assist the Poor (CGAP), which is a branch of the World Bank. Information included in the dataset comprises governance and board variables, financial statements and risk management of MFIs. The dataset contains 379 MFIs from 73 countries worldwide. Since board-related issues are reported qualitatively, we also read the reports and identified whether any stakeholders were sitting on the respective boards. When no information was available we reported a blank.

The dataset is structured such that annual observations of performance variables are available for a maximum of five consecutive years. However, governance and organizational variables are reported only once. Following Mersland and Strøm (2009), we assumed that all variables are constant over the whole period since these are variables which do not change frequently. Because of geographical and governance differences between countries, we separately collected information on legal regimes, based on LaPorta et al (1997;2008) and obtained from the World fact book at www.nationmaster.com. The MFIs in the dataset are a mixture of NGOs, cooperatives and banks. Table 2 provides the distribution of MFIs by type and geographical location (country).

Since our data were not self-reported, we found it reasonable to assume that the sample selection bias was minimal and that the sample consisted of several random samples of the governance and performance of MFIs. However, we recognize that not all MFIs are represented in this dataset. Large numbers of small financial cooperatives and NGOs, for example, are not included. However, we think this dataset helps provide a global picture of what is happening generally in terms of stakeholder representation and its influence on governance and the performance of MFIs.

Table2: MFI by country and type

Name of the Country	Type of MFI			Total
	NGOs	Cooperatives	Banks	
Albania	0	0	3	3
Argentina	0	0	1	1
Armenia	2	0	1	3
Benin	4	2	2	8
Bolivia	13	0	2	15
Bosnia	11	0	0	11
Brazil	11	1	1	13
Bulgaria	0	1	1	2
Burkina Faso	0	3	1	4
Cambodia	1	0	11	12
Chile	0	1	1	2
Colombia	6	0	0	6
Dominican Republic	3	0	1	4
Ecuador	8	8	0	16
Egypt	5	0	0	5
El Salvado	2	0	2	4
Ethiopia	0	0	10	10
Georgia	6	0	0	6
Guatemala	5	0	0	5
Haiti	2	0	0	2
Honduras	5	2	1	8
India	23	4	4	31
Indonesia	1	0	1	2
Jordan	0	0	3	3
Kazakhstan	0	0	4	4
Kenya	3	0	6	9
Kyrgyzstan	1	1	1	3
Madagascar	0	1	1	2
Mali	2	1	0	3
Mexico	9	1	6	16
Moldova	0	0	2	2
Morocco	6	0	0	6
Nicaragua	9	1	2	12
Pakistan	1	0	0	1
Paraguay	0	0	1	1
Peru	14	3	12	29
Philippines	6	1	0	7
Roumania	0	0	1	1
Russia	4	10	1	15
Senegal	0	9	1	10
South Africa	1	0	2	3
Sri Lanka	1	0	0	1
Tanzania	3	0	1	4
Togo	1	2	0	3
Trinidad & Tobago	0	0	1	1
Tunisia	1	0	0	1
Uganda	4	0	6	10
Montenegro	1	0	1	2
Cameroun	0	1	4	5
Guinee	0	0	1	1
East Timor	0	0	1	1
Bangladesh	1	1	0	2
Nepal	2	0	3	5
Vietnam	1	0	0	1
Azerbaijan	0	0	6	6
Mongolia	0	0	2	2

Nigeria	2	0	1	3
Mozambique	0	0	1	1
Tajikistan	5	0	2	7
Croatia	1	0	0	1
Chad	0	1	0	1
Rwanda	0	1	3	4
Zambia	0	0	1	1
China	1	0	0	1
Serbia	1	0	0	1
Ghana	3	0	0	3
Malawi	0	0	1	1
Gambia	1	0	0	1
Kosovo	1	0	3	4
Congo Braz.	1	0	0	1
Burundi	0	1	0	1
Niger	0	1	1	2
DRC-Kinshasa	0	1	0	1
Total 73	**195**	**59**	**125**	**379**

4.2 Model and Variables

We used two models to estimate board structure and performance, respectively. Model 1 looks at board structure and has two dependent variables: ***board size***, measured as the logarithm of the number of board members and ***CEO duality***, which is a binary variable (=1 if the CEO is also the board chair or 0 otherwise). Because of the dual objective of MFIs, we also developed a performance model (Model 2) whose dependent variables are social and financial performance. Several performance variables are proposed in the microfinance literature (Rosenberg 2009) but, in accordance with our hypotheses, we concentrated on those variables we considered to be of most interest to stakeholders. The financial performance variables used are ***portfolio yield***, measured as the inflation-adjusted ratio of interest and revenue to the MFI's loan portfolio, and ***financial self-sustainability***, measured as the ratio of subsidy-adjusted financial revenue to total expenses. The social performance variables are the ***number of customers,*** measured as the logarithm of the total number of customers served by the MFI, and looks at the breadth of outreach of the MFI. And ***average loan***, measured as the logarithm of the average loan each borrower receives, and is concerned with the depth of the outreach, a measurement of customers' poverty level (Schreiner 2002).

The presence of stakeholders on boards was measured as a series of binary variables, denoting whether there is a ***donor*** (yes=1), ***customer*** (yes=1); ***employee*** (yes=1) or ***creditor*** (yes=1) on the board. We also had a binary variable for whether there is ***any-stakeholder*** on the board (yes=1) and, to deal with interactions between stakeholders, we had binary variables denoting whether the board has both an ***employee & customer*** (yes=1) and both ***donor &***

creditor (yes=1). To control for variations among and within MFIs, countries and regions, we included a number of control variables (Mersland et al 2011). MFI control variables are s***ize***, measured in terms of the logarithm of assets possessed by the MFI, ***age***, measured as the number of years in operation, ***regulation*** by central bank authorities (yes=1), ***legal status,*** denoting whether the MFI is an independent legal organization (yes=1) or just a branch of another organization (=0), ***ownership type*** (binary variables denoting whether or not the organization is an NGO, bank or cooperative, respectively) and whether the MFI was ***internationally initiated*** (yes=1).

Among the country and region-specific variables included is ***competition.*** This variable was constructed from the MFI's information provided to the rating agencies, and from the agencies' independent judgment of the MFI's competitive situation relative to other MFIs in the country. The higher the score on a scale of one to seven, the stronger the competition. Also included are ***regional*** binaries for countries in Latin America, Asia, Africa south of the Sahara, Eastern Europe and the Middle East. As far as we know, we are also the first to include LaPorta et al's (1997; 2008) ***legal regimes*** variable (company laws), which denote countries that follow French law, English law, Socialist and German law in the list of countries' governance variables. The models are given by the following equations:

Model 1: *Board structure=* f*(stakeholders + MFI control variables + country control variables+ regional dummies + legal regimes + time dummies)*

Model 2: *Performance=* f*(stakeholders + MFI control variables + country control variables +regional dummies + legal regimes + time dummies)*

4.3 Summary Statistics

Table 3 shows the summary statistics of the variables used in the analysis. In terms of board structure, the average board size of an MFI is seven members and CEO duality exists in 17% of the MFIs. The inflation-adjusted portfolio yield is 33%. Financial sustainability is a widely-used proxy for long-term organizational sustainability, and the average value of 95% shows that, on average, these MFIs are not financially sustainable after adjusting for subsidies and other MFI-specific factors obtained from the rating agency.

On average, the MFIs have 14,978 customers, with a minimum of 24 and a maximum of 513,000. This shows that some of the MFIs have greater outreach than others and this may be attributed to their experience in the market. The average loan size of USD 751 reflects the "micro" aspect of microfinance. 30% of the MFIs have a stakeholder of some kind on their board. 9% have donors, 8% have employees, 18% have customers, and creditors are the least represented, appearing on only 5% of the MFIs' boards. Few of the boards have both customers and employees (7%) and few have both donors and creditors (5%).

The MFIs vary in size, with average assets of USD 6 million (Ln 14.58), while the average time in operation is 10.51 years. These size and age statistics show that most of the MFIs are small and young, which is the reason for the low stakeholder representation, as stakeholders tend to increase with the growth of the industry (Luoma and Goodstein 1999). Most of the MFIs (91%) have been established with their own legal status and 27% are regulated, indicating that regulation and transformation is becoming popular in the microfinance industry (Arun 2005).

NGOs make up 51% of the whole dataset, banks form 32% and 17% of the MFIs are cooperatives. International influence is strong in the industry, with 38% of the MFIs having been started by international organizations. Average competition pressure is 4.3 which is above the 3.5 middle point of a sevenpoint scale. French legal regimes are leading by 59%, followed by English regimes 25%, socialism 13% and German regimes 3%. 29% of the MFIs are in Latin America, 25% in Asia, 24% in Africa south of the Sahara, 18% in Eastern Europe and 4% in the Middle East

Table 3: Summary Statistics

Variables	Obs.	Mean	Std. dev.	Min	Max
Board Structure					
Board size	2673	7.23	3.58	2.00	23.00
Ln Board size	2672	1.87	0.46	0.67	3.14
CEO Duality	2654	0.17	0.59	0.00	1.00
Performance					
Inflation-adjusted Portfolio Yield	1020	0.33	0.21	-1.46	1.22
Financial Sustainability	701	0.95	0.30	0.10	2.21
Customers	990	14978	34517	24.00	513000
Ln Customers	990	8.61	1.43	3.17	13.15
Average Loan	1166	751	1322	1.00	24589
Ln Average Loan	1166	5.90	1.22	0.04	10.11
Independent variables					
Any-stakeholder	2428	0.30	0.46	0.00	1.00
Donors	2335	0.09	0.27	0.00	1.00
Employees	2349	0.08	0.26	0.00	1.00
Customers	2296	0.18	0.38	0.00	1.00
Creditors	2328	0.05	0.16	0.00	1.00
Employees & customer	2032	0.07	0.38	0.00	1.00
Donors & Creditor	2032	0.05	0.27	0.00	1.00
MB Controls					
Size - Ln assets	1228	14.58	1.78	0.43	19.33
Age	2957	10.51	8.14	1.00	85.00
Legal status	2918	0.91	0.28	0.00	1.00
Regulation	2921	0.27	0.44	0.00	1.00
NGO	2032	0.51	0.50	0.00	1.00
Bank	2032	0.32	0.47	0.00	1.00
Cooperatives	2032	0.17	0.21	0.00	1.00
Internationally-initiated	2948	0.38	0.49	0.00	1.00
Country and Regional controls					
Competition	2756	4.29	1.56	1.00	7.00
French countries	2032	0.59	0.49	0.00	1.00
English countries	2032	0.25	0.43	0.00	1.00
Socialist countries	2032	0.13	0.32	0.00	1.00
Germany countries	2032	0.03	0.17	0.00	1.00
Region Latin America	2032	0.29	0.45	0.00	1.00
Asia	2032	0.25	0.44	0.00	1.00
Region Africa South	2032	0.24	0.43	0.00	1.00
Region EECA	2032	0.18	0.39	0.00	1.00
Region MENA	2032	0.04	0.19	0.00	1.00

5.0 STAKEHOLDERS' DEMOGRAPHICS

5.1 Where are stakeholders represented?

Table 4 shows that 22.9% of the stakeholders sitting on the boards of MFIs are donors, of whom 13.3% sit on NGO boards. This is to be expected since most donors support NGOs with not-for-profit objectives and are interested in being on boards in order to monitor the use of their funds (Alonso et al 2009). Interestingly, no donors sit on cooperative boards. This is at odds with the fact that the United Nations General Assembly declared the year 2012 as "The International Year of Cooperatives". Why then are cooperatives not popular among microfinance donors?

21.3% of the stakeholders sitting on boards are employees and more of these sit on NGO boards than on other types of MFI. Since employees provide inside information, NGOs can benefit from this. It is argued that the cost of having employees on boards is that they are not good monitors since it is difficult to monitor one's boss (Osterloh and Frey 2005). Having both donors and employees on the boards of NGOs may be beneficial because donors monitor and employees provide information. We found that customers are most present on the boards of cooperatives and also the most well represented of all the stakeholder types. This is not surprising given that cooperatives are customer-owned MFIs. However, we also found that customers are represented on the boards of NGOs and banks, which indicates their importance. Creditors are the least represented on MFI boards and generally they sit on banks' boards. Taken together, we argue that stakeholder representation is a result of MFI type.

Table 4: Stakeholders in different types of MFIs

	% NGO	% Coop	% Bank	Total %
Donors	13.30	0.00	9.60	22.90
Employees	9.20	4.40	7.70	21.30
Customers	6.70	36.50	3.20	46.40
Creditors	2.90	0 .00	6.50	9.40
Total	**32.10**	**40.90**	**27.00**	**100.00**

5.2 Are MFIs with stakeholders different?

Does stakeholder representation influence board structure and MFI performance? Table 5 provides t-test results for boards having at least one stakeholder and those without any.

Table 5: Differences between boards with and without stakeholders

	Mean-With Stk.	Mean-Without Stk.	t-test diff
Board Structure			
Board size	8.70	6.90	1.80*
Duality	0.15	0.16	0.01
MB Performance			
Adjusted portfolio yield.	0.26	0.35	0.09*
Financial self-sustainability	1.00	0.90	0.10*
Number of customers	15738.00	13929.00	1808 .00
Average Loan	1003.00	752.00	251*

* denote significance at 0.01 levels.

Boards with stakeholders are larger than boards without them. This confirms the previous literature, which argues that board size grows with the number of stakeholders (Hillman et al 2001). Portfolio yield is used as a proxy for MFIs' interest income in relation to their loan portfolio and it shows that MFIs with stakeholders on their boards charge less than their counterparts. This could indicate that stakeholders push for low interest rates, but since this is only a univariate it may also be the result of these MFIs being of a larger size. We also found evidence of significant differences as regards financial sustainability, in that MFIs with stakeholders on their boards are more likely to be sustainable. In fact, MFIs with stakeholders on their boards have higher average loan sizes, which is better for sustainability but worse for social performance. This result indicates that there is a trade-off between servicing the poor and ensuring good financial results (Hermes et al 2011). In unreported results, we ran a t-test for each type of stakeholder and obtained similar results to those shown in Table 5. These preliminary analyses illustrate that stakeholders make a difference to MFIs, both in terms of board structure and performance.

We now look at the relationship between six MFI characteristics (size, age, regulation, legal status, MFI type and internationally-initiated) and stakeholder representation. The reasons for examining these characteristics are as follows. The corporate literature suggests that, as organizations become older and larger, the need for stakeholder inclusion increases, since this improves their access to resources (Luoma and Goodstein 1999). Furthermore, the microfinance industry experiences a great deal of international influence (Mersland et al 2011), which may be because of the inclusion of stakeholders on boards. Lastly, there has been a move for MFIs globally to transform and become regulated by central banking authorities (Hartarska and Nadolnyak 2007) and this has an impact on who sits on boards. We tested these relationships using the probit regression method in which the dependent variables are the stakeholder binaries defined earlier. The results are shown in Table 6.

Table 6: Stakeholders and MFI characteristics

Variable	Any-stakeholder	Donor	Employee	Customer	Creditor
Size	0.05**	0.022	0.06	0.12**	0.11
Age	-0.01	-0.06*	0.01	-0.01	-0.04
Regulation	-0.20	0.12	-0.09	-0.45**	-0.73*
Legal status	0.53**	-0.08	-0.01	0.05	0.03
NGO	-2.11	5.36	-0.16	-3.09	4.67
Bank	-2.13	5.16	-0.11	-3.15	5.39
Int. Initiative	0.43*	0.87*	0.29*	0.30**	0.24
Pseudo R^2	0.27	0.16	0.12	0.47	0.14

Probit regressions-regional and time dummies are included. *, **denote statistical significance at 0.01 and 0.05.

Large MFIs are more likely to include stakeholders on their boards than smaller ones. These stakeholders seem to be mainly customers, since only customers are significantly associated with large MFIs. We also found that younger MFIs have donors on their boards. This justifies Schreiner's (2002) notion that donors are like genetic engineers controlling the evolution of MFIs. They sit on boards when MFIs are young, and later leave them to operate independently. Contrary to Luoma and Goodstein (1999), we found evidence that regulations do not attract stakeholders on to boards, which is probably because regulators often do not allow members without technical banking knowledge to be included on MFI boards.

MFIs with their own legal status have more stakeholders on their boards. It is remarkable that the characteristic of being internationally-initiated is both statistically and economically significantly related to most types of stakeholders. Mersland et al (2011) show a positive relationship between international initiatives and MFIs' social performance. We therefore argue that internationally-initiated MFIs have better performance, caused by, among other things, having stakeholders on their boards.

6.0 STAKEHOLDERS AND BOARD STRUCTURE

Do stakeholders influence MFI board structure? Organizations need board structures that allow their boards to be efficient in fulfilling their roles (Linck et al 2008). Here we ran regressions between board structure variables, as dependent variables, and stakeholders on boards, as independent variables. We did so by including each stakeholder variable in the regression, and running pooled OLS regressions for board size and probit regressions for CEO duality. Table 7 gives the results, with panel A showing those relating to board size and panel B those to CEO duality.

Generally, the results show that stakeholders matter when it comes to which structure the board adopts. Panel A shows that donors are associated with small boards, which supports the argument that they require a high level of monitoring. As hypothesized, the presence of employees on boards is significantly associated with larger boards. Since large boards are a source of resources, and employees possess unique information, we argue that participation in their board is beneficial. We also show evidence that funders, both donors & creditors, are associated with small boards. This implies that funders prefer small boards because it allows them to carry out better CEO monitoring (Yermack 1996).

Table 7: Stakeholders and board structure

	Panel A: Ln Board Size						
Independent variable							
Any stakeholder	0.043						
Donor		- 0.109***					
Employee			0.192*				
Customer				-0.044			
Creditor					0.051		
Employee & Customer						0.052	
Donor & Creditor							-0.088**
Control Variables							
Size	0.018*	0.018*	0.017*	0.019*	0.019*	0.028*	0.029*
Age	-0.001	0.001	0.000	0.000	-0.001	-0.001	-0.001
Legal status	-0.203*	-0.235*	-0.192*	-0.241*	-0.237*	-0.214*	-0.209*
Regulation	0.044	0.053	0.043	0.061	0.062	0.092	0.088
Int. Initiative	0.091*	0.139*	0.095*	0.122	0.116*	0.097*	0.106*
NGO	0.018	-0.036	0.001	-0.056	-0.018	0.068	0.041
Bank	-0.217*	-0.260*	-0.247*	-0.285*	-0.262*	-0.177*	-0.206*
Competition	-0.065*	-0.062*	-0.072*	-0.064*	-0.069*	-0.060*	-0.062*
Obs.	854	788	827	812	817	1012	1012
R^2	0.271	0.299	0.283	0.278	0.277	0.242	0.244
	Panel B: CEO duality						
Independent variable							
Any stakeholder	0.299***						
Donor		-0.836*					
Employee			-0.316				
Customer				0.472***			
Creditor					1.419*		
Employee & Customer						1.011*	
Donor & Creditor							-0.026
Control Variables							
Size	0.207*	0.231*	0.206*	0.194*	0.217*	0.206*	0.205*
Age	-0.049*	-0.567*	-0.037*	-0.051*	-0.052*	-0.035*	-0.037*
Legal status	0.223	0.233	-0.060	0.215	0.179	-0.166	-0.059
Regulation	-0.488*	-0.431**	-0.482*	-0.457**	-0.351**	-0.470*	-0.481*
Int. Initiative	-0.537*	-0.447*	-0.652*	-0.459*	-0.544*	-0.744*	-0.648*
NGO	-0.164	-0.165	-0.381	0.112	-0.244	0.412***	-0.377
Bank	0.005	-0.174	-0.208	0.245	-0.260	0.638**	-0.205
Competition	-0.005	-0.035	-0.042	0.007	0.001	-0.041	-0.043
Obs.	793	765	945	753	761	945	945
Pseudo R^2	0.139	0.147	0.121	0.131	0.153	0.154	0.121

OLS regressions - Legal regimes, Regional and Time dummies are included. *, **, and *** denote statistical significance at 0.01, 0.05and 0.1 levels.

Panel B shows that, generally, stakeholders are positively associated with CEO duality. This has two implications. First, it is possible that the CEO invites stakeholders on to the board so that they will remain loyal to him or her and select him or her to chair the board as well. Or, it is possible that stakeholders opt for duality because they want to avoid dealing with multiple sources of authority and responsibilities (Finkelstein and D'aven 1994). We found that donors are significantly associated with non-duality. This relates to the agency argument that the CEO is the donors' agent and so they want to monitor him or her.

Surprisingly, customers and creditors are both associated positively with duality. Customers, we argue, want their interests to be heard, planned for and implemented by one person so as to avoid multiple responsibilities. However, we expected creditors, as funders, to opt for non-duality. This positive association could be the result of creditors wanting to hold just one person responsible for their loans. However, this finding might also be a result of the few observations we have of creditors sitting on boards. Regarding interactions among stakeholders, we found a positive association between duality and the presence of both employees and customers on a board. As internal and external customers, respectively, the results suggest that they opt for duality in order to have one central authority and ease of operation under one boss (Rechner and Dalton 1991).

The MFI control variables show significant results in both panels. Larger MFIs have larger boards as evidenced previously (Adams and Ferreira 2009) and are associated with duality. MFIs with independent legal status prefer small boards. This is not surprising since, when MFIs are subsidiaries of other organizations, they belong to larger, multi-purpose NGOs or large banks, and this leads to large boards. We also saw that MFIs with international initiators have large boards and non-duality. This was expected given that international actors are probably more familiar with governance codes, which recommend non-duality. Regulated MFIs are associated with non-duality, which is often a legal and regulatory requirement for such institutions. For more checks, we ran a board structure model with board gender diversity but the results were not interesting because of the few observations we have of this variable. We therefore choose not to report them.

Taken together, we found that stakeholders matter for the type of board structure put in place by MFIs. This influence may cause MFIs to have different levels of performance. This is examined in the next section.

7.0 STAKEHOLDERS AND PERFORMANCE

Does the presence of stakeholders on boards affect MFI performance? Before we ran this model, we needed to check for endogeneity. It is possible that, instead of stakeholders influencing performance, it is performance that leads stakeholders to sit on boards. Another endogeneity concern was that we might have omitted some unobservable variable that affects both stakeholders and performance variables (Adams and Ferreira 2009). For example, some MFIs may be more progressive than others, and thus have more stakeholders and better performance than others. This effect could lead to spurious correlations among variables, and so we had to control for it (Adams and Ferreira 2009; Mersland and Støm 2011). We addressed these problems by means of instrumental variables (Wooldridge 2006).

In Section 4 we gave evidence that the number of stakeholders sitting on boards is greater in internationally-initiated MFIs. Also, MFIs are normally established either as part of a multi-purpose NGO or with their own legal status in a given country. This has implications for who sits on the board. If the MFI has its own legal status, it has more power to choose which stakeholders can sit on its board than when it is a branch of another organization. Finally, MFIs come in various types: NGOs, cooperatives and banks. As previously evidenced, MFI type has implications for stakeholder representation. Thus, we used internationally-initiated, legal status and MFI type as instruments. We conducted a Durbin-Wu Hausman test (Hausman 1978) and observed that there were endogeneity problems (unreported results). We then ran a two-stage linear regression (2SLS), including three instruments and other control variables, for each stakeholder variable individually. Table 8 reports the results of financial performance.

Table 8: Stakeholders and financial performance

	Panel A:	**Inflation-adjusted Portfolio Yield**					
Independent variable							
Any stakeholder	-0.155*						
Donor		0.453*					
Employee			2.003				
Customer				-0.125*			
Creditor					0.875		
Employee & Customer						-0.157*	
Donor & Creditor							0.492*
Control variables							
Size - Ln (Assets)	-0.005	-0.009	-0.023	-0.008	-0.010	-0.000	-0.003
Age	-0.004*	-0.005*	-0.009**	-0.005*	-0.051*	0.005*	-0.005*
Regulation	-0.041*	-0.043**	-0.019	-0.049**	-0.021	-0.048*	-0.037**
Competition	-0.008*	-0.003	-0.018	-0.007	-0.003	-0.004	-0.007
Instruments			Internationally-initiated; Legal status; MFI type				
Obs.	790	760	766	745	759	862	862
$\mathbf{R^2}$	0.109	0.129	0.111	0.119	0.108	0.141	0.104
			Panel B: Financial Sustainability				
Independent variable							
Any stakeholder	0.093**						
Donor		0.273**					
Employee			-0.288				
Customer				0.134***			
Creditor					-1.258		
Employee & Customer						0.039	
Donor & Creditor							0.120**
Control variables							
Size - Ln (Assets)	0.022**	0.030*	0.034*	0.035*	0.037*	0.037*	0.045*
Age	-0.002	-0.000	-0.002	-0.001	-0.004**	-0.004**	-0.004***
Regulation	0.044	0.037	0.062***	0.019	0.035	0.062**	0.069
Competition	0.027*	0.030*	0.029*	0.036*	0.024***	0.027*	0.016
Instruments			Internationally-initiated; Legal status; MFI type				
Obs.	560	542	544	530	541	636	636
$\mathbf{R^2}$	0.138	0.162	0.139	0.137	0.088	0.129	0.108

SLS regression - Legal regimes, Regional and Time dummies are included in all regressions.

*, **, and *** denote statistical significance at the 0.01, 0.05, and 0.1levels.

Panel A shows the results for the adjusted portfolio yield. Generally, stakeholders on a board are associated with low interest returns. We show evidence that the presence of any stakeholder, customers, and both employees and customers are all negatively associated with portfolio yield. This means that customers fight for lower interest rates. However, we show evidence that donors and creditors push for higher yields. This means that funders want to see MFIs get higher returns so that, in the first case, donors can eventually withdraw their support, and in the second, so that creditors can be repaid.

Panel B shows that stakeholders on boards are associated with greater financial sustainability. This means that when stakeholders sit on boards, they monitor and give the resources that are necessary for MFIs to be sustainable. We found positive significance results in the case of the presence of any stakeholder, donors, customers and of both donors and creditors.

These results give support to several hypotheses. The presence of any type of stakeholder on a board is partially supported, since positively they provide financial sustainability but a negative portfolio yield. Contrary to Hartarska and Mersland (2012), we found that MFIs had better financial performance when donors were on their boards. Following Rosenberg (2009), we argue that donors like to fund, assist and advise MFIs that show a credible track record in terms of financial performance. This enables donors to withdraw their support at a later stage, as suggested by Schreiner (2002).

Similar to the findings of Hartarska (2005), our results provide support for the presence of an association between customers on boards and financial performance. Though customers bring negative yields, they are positively associated with financial sustainability. A similar result is found when both employees and customers are on the board. This means that customers push for lower interest rates but not to such a level that prevents the MFI from being sustainable. From pushing for low interest levels, it means that customers on boards also induce lower costs for MFIs. The results also support the notion that, in MFIs, employees and customers work closely together (Mori, 2010; Battilana and Dorado 2010). Furthermore, we found support for the influence of funders - donors and creditors - on boards. They are both associated with better financial performance.

These results indicate that stakeholders push down MFI costs, and to further check this we ran additional regressions (not reported) to see how stakeholders influence costs. We found that stakeholder presence has negative associations with operational costs, specifically in the case of any type of stakeholder, customers and both employees and customers. Thus the presence of stakeholders on boards leads to lower MFI costs.

Table 9 shows the results on social performance. Panel A shows the results on the relationship between the presence of stakeholders and the number of customers (the breadth of outreach). Here, we found that donors are associated with a higher number of customers and therefore better social performance. The relationship is also significant when both donors and creditors are on the same board. As funders, it could be that this type of stakeholder monitors and advises in a way that leads to more customers. Alternatively, by having greater inside information, these funders may provide additional funding, allowing the MFI to serve more customers. Interestingly, but not surprisingly, we found that boards that include customers (who represent existing customers) are associated with fewer customers. This means that customers serving on boards monopolize the service and so fewer people are served.

Panel B provides the results relating to average loan size. A smaller loan means better social performance as poor customers normally take out small loans (Hermes et al 2011). We found a positive association between the presence of any type of stakeholder and average loan size. However, the presence of donors, creditors and both donors and creditors on the same board are all associated with smaller loans, while customers and both employees and customers on the same board are associated with larger loans. Again, we found support for the positive effect of donors on social performance. Most donors have a social mission of serving the poor and so, when they are on a board, they try to monitor and advise the organization in such a way that meets their objectives.

Creditors are shown to be socially beneficial and associated with smaller loans. This is surprising, as it may appear that creditors would prefer the organizations to provide larger and more profitable loans. However, since most microfinance creditors also have a social mission, they are likely to push for greater outreach to the poor (Rhyne 2005). We also showed that customer representation is associated with larger loans. The results are similar when both employees and customers are represented on the same board. It appears that the presence of customers on boards leads to worse social performance by encouraging MFIs to concentrate on giving larger loans to fewer, less poor customers.

Table 9: Stakeholders and Social performance

	Panel A:	Ln Customers					
Independent variable							
Any stakeholder	0.246						
Donor		3.646*					
Employee			0.252				
Customer				-0.299***			
Creditor					0.948		
Employee & Customer						-0.078	
Donor & Creditor							2.983*
Control variables							
Size - Ln (Assets)	0.459*	0.434*	0.559*	0.463*	0.454*	0.505*	0.491*
Age	0.015*	0.034*	0.014	-0.023*	0.023*	0.013**	0.021*
Regulation	-0.226**	-0.282**	0.089	0.225**	-0.231**	-0.085	-0.109
Competition	0.041	0.080**	0.005	0.017	0.045	0.003	0.037
Instruments	Internationally-initiated; Legal status; MFI type						
Obs.	741	724	716	706	720	691	692
Wald X^2	38.46*	21.59*	46.56*	38.83*	38.37*	47.11*	29.24*
Pseudo R^2	0.488	0.108	0.534	0.505	0.492	0.496	0.178
	Panel B:	**Ln Average loan**					
Independent variable							
Any stakeholder	0.984*						
Donor		-4.558*					
Employee			-6.827				
Customer				1.115*			
Creditor					-3.864**		
Employee & Customer						1.172*	
Donor & Creditor							-4.677*
Control variables							
Size - Ln (Assets)	0.161*	0.189*	0.208*	0.159*	0.177*	0.166*	0.198*
Age	-0.001	-0.009	-0.012	-0.005	-0.002	-0.003	-0.003
Regulation	0.419*	0.357*	0.357**	0.433*	0.350*	0.388*	0.285*
Competition	0.086*	0.004	0.105**	0.106*	0.036	0.109*	0.028
Instruments	Internationally-initiated; Legal status; MFI type						
Obs.	852	819	827	805	818	744	744
R^2	0.354	0.276	0.182	0.456	0.139	0.377	0.277

SLS regression-Legal regime, Regional and Time dummies are included in all regressions. *, **, and *** denote statistical significance at 0.01, 0.05, and 0.1.

For the control variables, Tables 8 and 9 show that large MFIs are associated with poorer social and better financial performance. Since large MFIs can source more funding, they are able to reach more customers, offer larger loans, make greater profits and become more financially sustainable. We also observed that regulated MFIs offer larger loans and serve fewer customers than unregulated ones. This is consistent with the literature that suggests that, as MFIs transform, they begin to work more with fewer and less poor customers in order to adhere to regulatory requirements (Hartarska and Nadolnyak 2007).

In summary, these results show that stakeholders are beneficial for MFIs and for those stakeholders represented on the boards (Labie and Mersland 2011). Donors bring better social and financial performance. The results of having customers on boards are that costs are lower and sustainability is more likely but social performance is poorer. We did not find evidence that the presence of employees on boards affects performance, but when both employees and customers are on the same board they push for low costs and interest rates and advocate larger loans. This is good for employees, since low interest rates brings in more customers and larger loans, which are more profitable for the MFI and provide a better income for employees. When creditors sit alone on boards, they are not all that beneficial to MFIs. However, when they serve on the same board as donors, they are beneficial, which leads to better financial and social performance. It appears that, as funders, they can work better together than when each operates individually.

8.0 CONCLUSIONS AND IMPLICATIONS

This paper responds to the call for research to gain a deeper understanding of stakeholders in MFIs (Labie and Mersland 2011). Using a global dataset, we have shown the relationship between stakeholders and MFI characteristics (size, age, regulation, legal status, MFI type and international initiation), board structure (size and CEO duality) and performance (financial and social). We used a mixture of techniques in the analysis. For MFI characteristics and board structure variables, we used OLS regressions and probit regressions. To tackle endogeneity concerns, we used a 2SLS regression with instrumental variables to analyze the relationship between stakeholders and performance.

We found that stakeholders are represented differently in different MFI types. Donors and employees are more on the boards of NGOs, creditors on those of banks and customers on those of cooperatives. We further found that stakeholders are associated with larger and internationally-initiated MFIs. Stakeholders show their interest by having an influence in different ways on board structure and performance. Donors are strict in monitoring (Yermack 1996) and we found that they are associated with small boards, non-duality and better performance. Similar findings were obtained when boards contain both donors and creditors. Employees, as resource providers, were found to be associated with large boards. Customers are associated with duality, better financial performance but poorer social performance. Similar evidence is seen when customers interact with employees on boards.

It is interesting that donors and creditors are associated with better performance in all cases. This implies that funders are beneficial to MFIs, as advocated by policy papers (CGAP 2009; Rhyne, 2005). The practical implication of this is that donors and creditors should take a more active role in their partnership with MFIs. Our finding that few donors, and particularly creditors, sit on MFI boards should motivate a reorientation among microfinance funders. They should sit on MFI boards more often. Donors and creditors should not just provide funds, but they should also monitor and provide other resources. Particularly because the number of MFI creditors is rapidly increasing in the industry (www.mixmarket.org), there is a need for more research on their role in and influence on MFIs.

Despite the fact that customers cause the social performance of MFIs to be poorer, they are beneficial in terms of pushing for low costs, while at the same time enabling MFIs to be sustainable. Most MFIs have high operational costs, which means that customers can be beneficial to campaigns to reduce costs. However, the finding that the presence of customers on boards leads to poorer social performance should be the subject of new research. To what extent are existing MFI customers hindering further outreach by microfinance services?

A limitation of our study is that only four types of stakeholder are included. Future research could examine more types, specifically those not sitting on boards. How, for example, do rating agencies and local communities (Mersland, 2011) influence MFIs? Finally, the findings that cooperative MFIs do not have donors on their boards and that customers sitting on the boards of cooperative MFIs have a negative influence on their social performance merit further study, especially since 2012 is the UN's Year of Cooperatives.

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APPENDICES

Appendix One: Checklist of Questions on Board and MFI demography

Section 1: Board Demography

1. How many members are sitting on the board? ……………..members
2. Please indicate the following for the board members

Board member	**Founder Y/N**	**Gender (M/F)**	**Education Secondary bachelor, masters**	**Age-Year born**	**Experience in this and other boards Y/N…which**	**Nationality**	**Voting right Y/N**	**Committee member Y/N**
Donor representative								
Investors (shareholders)								
Founders								
Employees								
MFI Top managers								
Customer representative								
Government official								
Banker (creditors)								
Academicians								
Others (please specify)								

3. Who is the chairperson of the board? ________________________ (Male/Female)
4. Is the Chairperson also the Director/CEO of your MFI? Yes /No
5. Is the Chairperson also the founder of your MFI? Yes /No
6. Does the board have any committees? Yes / No
7. If yes, what are they? ____
8. When are board members elected (the number shows after how many years)(please tick)

One	Two	Three	four	five	More than 5 (indicate)

9. On average, how often does the board meet in a year? …………………………..
10. The average length of board meeting is ____________hours
11. How many board members are usually present at the meeting? ___________members
12. Does the board have any rules and procedures? No ( ) Yes ( ) if yes which ones _______________________________________

Section 2: Background of the Organization

1. Name of the MFI ______________________
2. When was the organization established (year) ______________
3. Location of MFI's head office (City/town) ___________
4. What is the legal status of the organization (please circle)
   a) NGO b) Commercial bank c) Community bank d) Cooperative
   a) Private Company f) Company ltd. by guarantee
   g) Other (specify) ____________
5. If you have owners, please list them in the following table

Owners	%

6. How many employees does the organization have ? (as of December 2009) ________________
7. Is the MFI regulated by the banking authorities ? Yes_____ No______ if no, does it plan to transform and become regulated? Yes____ no______
8. What is the organization's main market or customers ?(please circle)
   a) Women only
   b) More women, less men
   c) More men, less women
   d) Equal women and men
9. On average, what percentage of each gender (male /female) does the MFI have as customers?___________
10. How many branches (sales points) does the MFI have? ___________
11. Where does the MFI mainly serve? (please circle)
    a) Rural only
    b) More rural, less urban
    c) More urban, less rural
    d) Equal rural and urban
12. What is the dominant credit methodology? (please circle)
    a) Group lending only
    b) Individual lending only
    c) More group lending, less individual lending
    d) More individual lending, less group lending
    e) Other (specify)
13. Is the MFI a member of any international network /organization?

    Please list the international networks

    ____

Section 3: Respondent profile

1. Name of the respondent ___________ Gender: M/F
2. Position of the respondent __________

3. Do you have any remarks with respect to the board or to this survey that could be relevant for both sides? Please state them:

Request for useful Documents

i. Audited financial statements

ii. Different company reports/documents if available

iii. Board members profile (CVs)

iv. Company brochures, fliers etc.

Thank you for your cooperation

Appendix Two: Interview Guide

BOARD CHARACTERISTICS IN MICROFINANCE INSTITUTIONS (MFIs): EAST AFRICAN CONTEXT

Interview with Board Members

The aim of this interview is to seek your views and collect data on the characteristics and processes of MFI boards in East Africa. I would therefore like to ask you to spend approximately 30 minutes to discuss with me various issues regarding the MFI board which you sit on. I would like to assure you that the information you give me will remain strictly confidential and will be used for academic purposes only.

Background information:

i. Name of the respondent (board member): _______;gender: _____________
ii. Of which MFI are you a member?: ___________
iii. How many years have you been a board member in this MFI? ____________
iv. Do you sit on other MFI boards? ___________ if yes, which MFIs __________
v. Were you appointed because your capacity or because of your institutional affiliation?

Roles and Responsibilities:

i. Could you explain your role as a board member of this MFI?
ii. Why did you accept this position?
iii. Do you sit on any board committees? If yes, which committee?
iv. What do you do in that committee?
v. How often does the board meet per year?
vi. How often does the committee meet per year?
vii. How long (hours) do meetings (board and committee) take on average?

Information and decision processes:

i. What type of information do you receive prior to board meetings? Who avails you the information?
ii. Do you contact other board members before meetings? If yes, why; if no, why not?
iii. What subjects do you normally discuss in board meetings?
iv. During meetings, do you discuss matters regarding the mission of the MFI?
    a. Matters relating to social and financial sustainability (targeting the poorest vs. getting profits)
    b. Is it possible that some members have a strong interest in serving the poor and women, while others have a strong interest in getting high profits?
        i. How do you handle these differences or disagreements?
v. Since you are a regulated MFI (or planning to transform), as a board member, do you think regulation is good for your MFI? Why yes, why? If no, why not?
    a. In board meetings, do you discuss matters relating to the benefits and costs of regulation to your MFI?
vi. How are stakeholders (such as employees, donors, government) involved in the decisions you make as a board?

vii. How are stakeholders' interests captured in board decision making?

Trust, Cooperation and Reputation:

i. In your opinion, would you say that, generally speaking, you are willing to accept decisions made by top managers of the MFI? Why yes or why not?
ii. According to you how important is social interaction with other board members?
iii. What is your opinion with respect to the knowledge and experience of the members of the top management team?
iv. Does the top management team contact you (in person, by phone or through email) outside board meetings, and if so, what do you discuss?
v. How does the MFI benefit from your participation in the board?
vi. Do you have any other comments or questions?

Thank you for your cooperation

Appendix Three: Interviews

1. Interview Approach

In order to get an understanding of the characteristics of MFI board members, the researcher conducted semi-structured interviews with 30 board members from 20 MFIs in the three countries. A set of interview questions (appendix 2) was developed. The interviews focused on how the respondents came to be board members, what motivates them to stay as board members, their background, how their background informs or influences their contribution to the MFIs, what they perceive their roles are, whether they have written terms of reference (TORs), whether they are guided by some form of board manual or policy and whether they feel that they have an influence on key decisions and the performance of the organization. We also inquired into how decisions are made regarding outreach to the poor and financial objectives, which kind of board members are most influential in such decisions and how differences between members are resolved.

Interview data was analyzed using inductive techniques in which the transcribed responses were coded, based on theory, interview responses and type of questions. The exercise continued during and after data collection and focused on identifying patterns, differences, similarities and apparent links in the data. We further clustered information that addressed primary questions such as what, why, who, how and when. This clustering allowed us to identify emergent themes and similar characteristics of some members without introducing premature analytical bias.

2. Respondents' Demographics

a. Age

Years	**Respondents**
18-35	4
35-55	12
Over 55	14
Total	30

b. Education

Degree	Respondents
Below Bachelor	6
Bachelor	16
Masters and above	8
Total	**30**

c. Expertise

Expertise	Board members
Microfinance/Banking/Economics	14
Entrepreneurship/Development	4
HRM/Marketing	2
Investment/Resource mobilization	1
Law and Legal	2
Other	7
Total	**30**

d. Gender

	Respondents
Male	19
Female	11
Total	**30**

e. Founders

	Respondents
Founders	11
Non founders	19
Total	**30**

3. Examples of responses

	Interview responses
Independent members	As a leader in my community, people listen to me when I talk to them. Being on this board enables me to advise the CEO on which strategies they can use to get close to poor people and work well with them. I know my people, and I can talk to them about how microfinance services can benefit them. In this way, I feel through my network, I am able to contribute to the outreach of this MFI even though I am not an insider. (Interview, June, 2010)
International	I have worked in several local and international organizations for more than forty years. After my retirement, I thought I had something unique to share with others but I could not figure out what that was. Then I was approached to work with an international NGO and advise MFIs. It then clicked in my mind: "this is what I want to do for the rest of my life—advising MFIs in helping poor people get financial services". From then up to now, I have volunteered to sit on the boards of MFIs which have this social mission and I advise them on how to fulfil this mission sustainably. (Interview, April, 2010)
Female and founder	I am the founder CEO of this MFI and a woman. With my background, I know what other women need. Being on a board with other skilled women makes me feel that we are able to contribute what our female customers want. Our MFI is 100% for female customers so the board members ought to be female. That is why we are among the most developed MFIs in this country. (Interview, April, 2010)
Founder	Poor people have the same needs as others. Their challenge is getting access to what they need. We founded this MFI in order to serve them. We provide them with various services such as loans, training and insurance. We plan to continue expanding our services to them as long as they tell us they need these services. (Interview, June, 2010)

I g*ive thanks to the God of heaven, for his steadfast love endures forever*

Psalms 136:26