



Lending Practices, Low-Cost Strategy and Performance of Microfinance: Empirical Evidence from Nigeria

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Abstract

Micro-financing is an old lending practice in Nigeria. Before the introduction of modern microfinance institutions, microfinance exists informally across the country. The study investigated the relationships between Lending practices, business strategy and performance of microfinance in Nigeria. The MFIs ownership involved are; the Community Bank MFIs, the Private MFIs, the Government MFIs, the NGO MFIs, and the Foreign MFIs in Nigeria. By using questionnaires, the data were collected from 121 MFIs in Nigeria. By using regression technique, the findings of the study indicate that low-cost strategy moderate the relationship between lending practices and performance of MFIs. The result of the study seems to demonstrate that the performance of MFIs is good lending practices as well as low-cost strategy.

Keywords: Lending Practices, Low-Cost Strategy, MFIs, Performance

1. Introduction

Since the microfinance institutions were introduced in the 1980's, their numbers have continued to increase in developing countries across the world. These institutions have experienced remarkable growth and acceptance. More specifically, in Nigeria, MFIs are increasingly being recognized as an essential component of the financial industry in the country.

Like other business organisations, important strategic decisions for a microfinance institution involve learning as well as understanding its business and the nature of its relationships to the business environment. The business environment within which MFI functions is constantly changing. Changes in the forms of threats and opportunities in the business environment can affect not only the products and services of MFI but also its organizational performance. By detecting the changes through the strategic management approach, MFI can avoid the threats and exploit the opportunities.

The literature reveal that theoretical and empirical contributions in the area of MFIs remained limited, particularly in the Nigerian context. The limited theoretical and empirical contributions in this field of study have resulted not only in little knowledge about MFIs but also the lack of information concerning their lending practices, business strategy and their implications to the performance as financial institutions. Given the limited research as well as information in this field of study, the objective of this paper is to examine the



influence of low-cost strategy on the relationship between lending practices and performance of MFIs in Nigeria.

2. Literature Review

Literature emphasizes not only on the need for organisations to adopt strategic management but also its importance to the success of organisations (Homaid et al., 2017; Leinwand, Mainardi & Kleiner, 2016; Linton & Kask, 2017; Oyewobi et al., 2016; Reeves, Haanaes & Sinha, 2015; Rumelt, 2013; Yuliansyah, Gurd & Mohamed, 2017). Interestingly, despite the relevance and applicability of strategic management to organisations such as MFIs, there are no many studies that investigate these financial institutions from this management perspective. The literature show that there is not only little information but also limited research that focused on examining strategic management in the context of MFIs. Yet in Nigeria, MFIs account for about 80 percent of the total number of financial institutions in the country. Apart from their significant numbers, MFIs also play a crucial role in the social and economic development of Nigeria(CBN, 2013; Djalil, 2015).

Though the literature shows that organisations in different industries and nations tend to emphasize on dissimilar performance measurement, findings of past research indicated that growth and financial profitability to be the most communal measures of organizational performance(Boehe & Barin Cruz, 2013; D'Espallier, & Mersland, 2014). For example, the earlier study by Nash (1993) claimed that profitability is the best indicator to measure whether an organization is performing. According to the writer, profitability can be used as the primary measure of organizational success. Doyle (1994) further considered profitability not only as the most measure of performance but also claimed that western companies primarily used profitability measures to determine the extent to which their companies are performing. However, in the case of MFIs, researchers agree that these companies need to adopt different measures of performance. As social business, microfinance have both financial as well as the social objectives. Given this, the performance of MFIs should be measured by using not only financial but also social performance measures (Thomasa & Kumara, 2016).

Microfinance have different organizational objectives as associated to the commercial banks. Their objectives are not only limited to financial profitability but they also include non-financial objectives such as social outreach as well as the impact of their credit on the lives of the poor that borrowed from them. The need to measure the performance of microfinance by using both financial and social measures has also been supported by CGAP (Consultative Group to Assist the Poor), The SEEP (Small Enterprise Education and Promotion Network) and the impact network organization (Thomasa & Kumara, 2016). Of the research conducted on business strategy, many studies have focused on examining the linkage between business strategy and organizational performance. Organisations achieve their objectives by creating and executing effective business strategies. The earlier study by Giglierano (1987) found that organisations accomplished superior performance by developing and implementing effective business strategy that aligned with their business environment as well as based on their competitive advantage.



Over the decades, various definitions of business strategy have been proposed and documented in the strategic management literature. However in general, business strategy has been considered as the way in which a firm achieves its organizational objectives through maintaining its competitive advantage as well as competitive position in a particular industry (Hashim, 2008; Ibrahim & Primiana, 2015; Kamukama et al., 2011; Nkundabanyanga et al., 2017).

Furthermore, the literature reveals that different types of strategies are developed at different levels in organisations. The types of strategy are classified according to the levels they are developed in organisations. In general, three different types of strategy are developed at three different levels. The three strategies include; corporate strategy, business strategy and functional strategy.

With regard to the three types of strategy, the review of past research suggests that previous studies that examined the relationship between strategy and organizational performance have mainly focused on business strategy (Jooh Lee, 1988). Moreover, findings of previous empirical research on the relationship between business strategy and performance of large firms provided strong evidence that suggest business strategy are associated to the performance of these firms (Ansoff, 1984; Hofer & Schendel, 1978; Lee & Mowday, 1987; Linton & Kask, 2017; Oyewobi et al., 2016; Soltanzadeh et al., 2016; Yuliansyah et al., 2017).

3. Methodology

This study used the Least Squares Structural Modeling (PLS-SEM) to analyse the data collected as well as to test the hypotheses of the study. The first part of the data analysis involved descriptive statistics. This involves determining the percentages, means, modes, standard deviations, minimum and maximum value of the items used in collecting the data for the study. In the second part, the partial least squares (PLS) regression modeling was used for testing the research hypotheses. The PLS analyses used in this study involves the assessment of measurement as well as the structural models. The following section briefly describes the statistical procedures used in this study.

In the PLS regression analysis, assessment of measurement model was required for testing hypotheses. The assessment of measurement model in this study involves examining the individual item reliability, ascertaining internal consistency reliability, ascertaining convergent validity as well as discriminant validity. More specifically, this method was employed for testing the reliability and validity of the items and the focal variables used in this study.

As shown in the results, the loading of all items is greater than 0.70 and the composite reliability value (CRV) of all constructs is greater than 0.70. The Average Variance Extracted (AVE) values of all constructs are also greater than 0.50, ranging from 0.520 to 0.665. The Composite Reliability (CR) values ranged from 0.759 to 0.959 Taken together, these results statistically fulfilled the convergent validity criteria recommended by Hair et



al. (2011). In addition, **Error! Reference source not found.** shows that the Cronbach's Alpha scores of all the items are higher than 0.70. The scores ranged from 0.825 to 0.955. These results also suggest the reliability of the measures used in the study.

4. Results

Descriptive of the Respondents

Managers/ CEOs Personal Characteristics

Table 1: Managers Personal Characteristics

	Frequency	%
Gender:		
Male	90	74.4
Female	31	25.6
Age:		
30-40 years	52	43
41-50 years	52	43
51-60 years	17	14
Ethnic:		
Hausa	25	20.7
Yoruba	44	36.4
Igbo	28	23.1
Others	24	19.8

Source: Authors' Computation

Table 1 illustrates 90 respondents (74.4%) are male and 31 (25.6%) are female. 52 respondents (43%) are of aged between 30-40 years and 41-50 years, and 17 respondents (14%) are between 51-60 years old. 25 respondents (20.7%) are Hausa tribe, 44 respondents (36.4%) are Yoruba tribe, 28 respondents (23.1%) are Igbo tribe while others tribe have 24 respondents (19.8%).

Objectives and Ownership of the MFIs

Table 2 shows 71 MFIs (58.7%) primary objective is social oriented and 50 MFIs (41.3%) are profit oriented. 39 MFIs (32.2%) have one owner, 42 MFIs (34.7 percent) have two owners, one MFI (0.8%) have three owners, 12 MFIs (9.9%) have four owners, 25 MFIs (20.7%) have five owners and two MFIs (1.7 %) have six owners.



Table 2: Objectives and Ownership of the MFIs

	Frequency	Percentage
Year of establishment:	52	43.0
2007	28	23.1
2008	21	17.4
2009	18	14.9
2010		
2011	2	1.70
Primary objective:		
Social Oriented	71	58.7
Profit Oriented	50	41.3
Type of owners:		
Community	51	42.1
Shareholders	30	24.8
Partners	21	17.4
NGO	19	15.7
Number of owners:		
One	39	32.2
Two	42	34.7
Three	1	0.80
Four	12	9.90
Five	25	20.7
Six	2	1.70

Source: Authors' Computation

Lending Practices, Low-cost Strategy and Performance

Table 3 below presents the regression results between the Lending Practices, Low-cost Strategy and the performance of the 121 MFIs that participated in the study. The results indicate that competition moderate the relationship between Lending Practices, Low-cost Strategy and the performance. Specifically, it shows the regression between Lending Practices, Low-cost Strategy and the performance of MFIs. The results show as ($\beta = 0.73$, $t = 9.8$, $p < 0.000$).

Table 3: Regression among Lending Practices, Low-cost Strategy and Performance

Hypothesis	Beta	Standard Error	T-Statistics	P-Value	Decision
H: LP, LCS -> P	0.73	0.301	9.8***	0.000	Supported

Note: ***P<0.01, **P<0.05, *P<0.1

The result of the regression analysis appears to provide some support for the hypothesis that Low-cost strategy moderate the relationship between Lending and the performance. The finding is in line with the previous studies by Cull et al. (2011), Gwasi and Ngambi (2014), Moradi et al., (2017) and Nkundabanyanga et al. (2017). According to these



studies, MFIs faced not only intense competition in the financial market but also the intensity of competition had affected their performance.

5. Conclusions

This study examined the influence of low-cost strategy on relationship between lending practice and performance of MFIs. At general level, the results of the correlation analyses as presented in table 1 indicates the regression between Lending Practices, Low-cost Strategy and the performance of MFIs. The results as ($\beta = 0.73$, $t = 9.8$, $p < 0.000$). The result of this study provides some empirical evidence that suggest low-cost strategy moderate the relationship exists between lending practice and the performance of microfinance.

These findings add support to previous studies that suggests business strategy moderate the relationship between business practices and performance of MFIs (Martina & Javalgib, 2015; Moradi et al., 2017). This study offers implications for owners and managers of MFIs. The study is able to demonstrate that lending practices and low-cost strategy has influence on the performance of MFIs in Nigeria

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