Sustainable microfinance:

The balance between financial sustainability and social responsibility

A business model integrating remittances

and cross-border entrepreneurship to microfinance

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Abstract

Microfinance has been recognized as an effective tool to alleviate poverty. How to create a sustainability model of microfinance to fulfill both social responsibility and financial sustainability by integrating remittance flows and cross-border micro enterprise activities to microfinance business is the aim of this study. A mixture of methodology including primary data collection, secondary data collection and case study will be employed when conducting research of microfinance institutions (MFIs) in Sub-Saharan Africa.

Keywords: *poverty alleviation, microfinance, financial sustainability, social responsibility, remittances, cross-border entrepreneurship.*

1. Research background

1.1 Impact of microfinance on poverty reduction

Global poverty has been one of the most burning and unresolved issues in the human history. According to World Bank statistics, there is almost 3 billion of world population living under $2.5 per day and among them, around 1 billion living under $1 per day. Government and international organizations have been cooperating to fight poverty in different parts of the world. In recent years, microfinance has been recognized as an effective tool to alleviate poverty (Rubana, 2008; Daley-Harris, 2002; Lalitha, 2008). Microfinance offers the poor a chance to get access to financial service such as credit and savings. They can apply for small loans and use them to run small businesses such as selling chickens, eggs or other basic agricultural commodity. They also have opportunities to save money in saving accounts. Microfinance programs in Bangladesh, Bolivia and Central America all show positive impacts on the poor as they help the poor, first, to smoothen their daily expenditure then to enhance welfare and stabilize income. (Rubana, 2008; Khander, 2003; Khander & Pitt, 2002; Daley-Harris, 2002; Hiatt & Woodworth, 2006).

Microfinance aims to bring financial service to poor people as to provide small-scaled financial services primarily savings, credit and insurance to people performing small or micro business activities such as farming, fishing, herding or micro enterprises producing, recycling, repairing or selling goods (Lalitha, 2008). Microfinance programs are financially supported by governments and international organizations which means that microfinance programs depend on financial grants from donors and governments to great extent. When those financial resources are over, microfinance institutions would find it difficult to maintain the operation of microfinance programs, thus, the impacts on poverty alleviation would be diminished. As a result of this, microfinance programs face resource constraints and are not self-sufficient (Zeller & Meyer, 2002). This hinders microfinance institutions' ability to expand their service to the very poor or extremely poor communities.

1.2 Financial sustainability and social responsibility

In order to realize the aim of reaching poor people, microfinance institutions should find ways how to survive and not to depend so much on donors and governments, i.e. to be self-sufficient. The institutions should be able to cover cost and make profits on services that they offer to customers (Copestake et al., 2002). Many MFIs in Latin America, to name a few, Prodeem, Banco Solidario, have become financially sustainable by cooperating with banks and business organizations as to cross-sell additional products such as savings, pensions and insurances. Those additional services generate stable income for MFIs to cover cost, make profit and be able to serve more customers. In this sense, MFIs are more business oriented. However, too much focus on making profit may lead to shifts in customer groups, from extremely poor to marginal or above poverty line group. MFIs would seek wealthier client groups in urban areas to have more profit rather than target extremely poor clients in rural area (Zeller & Meyer, 2002). On the other hand, if MFIs focus so much on offering services to the poor or very poor, they may not be able to generate enough income to survive since the size of loans or savings that the very poor apply for or deposit is often small, thus, gives MFIs less profit than what they get from large loans offered to wealthier clients. If MFIs would like to realize it social aim as to outreach poor people, MFIs should offer services for marginal poor people so as to have enough profit to survive and develop and offer tailored products for the extremely poor. In another way, there should be allocation of products and resources between different customer groups so that MFIs could stay financially healthy and still focus on reaching the extremely poor as its social responsibility. Taking the arguments of poverty alleviation in Prahalad (2005) into consideration, social responsibility and financial sustainability of microfinance institutions can go hand in hand together and even create win-win situation for both the poor and the institutions. The author suggests that business should treat the poor as potential customers and create the capability among the poor to consume through increase the level of product availability and affordability. By the same token, MFIs should develop and tailor products to serve different levels of the poor including the very and extremely poor.

1.3 Remittance and cross-border entrepreneurship as a possible solution

Within this context, according to Consultation Group to Assist the Poorest (CGAP), remittance can be considered as an alternative source of income for microfinance institutions if they can attract this flow of money. Remittance can be viewed as the positive outcome of migration, benefit the receiving countries extensively. Recent years have witnessed an extraordinary growth of remittance volumes. Statistics from World Bank indicates that remittances worldwide have increased from US$ 30 billion in 1990s to US$ 318 billion in 2007. Between 2002 to 2007 remittance volumes to developing countries increased by 107%.

Latin America, Caribbean, East Asia and the Pacific, along with South Asia have the largest shares of international remittances, whereas, Sub-Saharan Africa is the least popular destination of remittance inflows with only 5% of total world remittance (IFAD, 2007). However, due to the global financial crisis, the amount of remittances has decreased during the last two years. It was estimated that remittance flows in 2009 to developing countries would decrease by 6.1 percent compared to 2008 (Ratha, Mohapatra & Silwal, 2009).

Remittances have a positive impact on both the micro and macroeconomics of the recipient country. On a macro level, remittances contribute significantly to the gross domestic product and foreign exchange earnings of home regions (Azzez & Begum, 2009; Niimi & Özden, 2006). On a micro level, remittances improve the level of household income and living standard of migrant families (Maibo & Ratha, 2005). Remittances are also a crucial source of finance to secure livelihood for migrants' families in home countries (Samal, 2006).

The volume of remittances sent to developing and under-developed countries has been increasing on a yearly basis; however, this source of financial inflow has not been utilized for productive purposes due to a lack of accessibility of financial services among remittance recipients. It can thus be assumed that this substantially lowers the positive impact of remittance on the economic development of home regions. Governments, donors, and finance institutions of different countries have been trying to channel remittances towards productive uses by:

- Connecting remittance transfers to financial services for recipients to gain access to savings and investments programs
- Encouraging MFIs and credit unions to serve as receiving institutions for remittance inflows in order to reach poorer recipients
- Using remittances to support micro, small and medium sized enterprise development (Johnson & Sedaca, 2004).

Remittance inflow can become a stable financial resource for MFIs if they act as financial terminals which receive remittances from abroad and channels them to various programs focused on savings and investment. MFIs have the capacity to improve financial services, especially in order to benefit the low income groups in recipient countries. This can be achieved by offering quality products at lower costs, increasing loyalty among existing clients who receive remittances from MFIs, generating income from free-base products, strengthening the lending capability of MFI by mobilizing savings from incoming remittances. MFIs are able to serve the poorer population, who do not have access to banks, by establishing themselves closer to rural areas (Orozco & Hamilton, 2005; Orozco & Millis, 2007; Hastings, 2006).

Remittances can also be used as capital to support small and micro enterprises in recipient countries. The demand of credits from micro-enterprises is enormous, might be as much as $500 billion worldwide (Leleux & Constantinou, 2007). There are about 500 million microenterprises seeking for credits and loans; however, it is difficult for them to obtain financial resources because of their limited fixed assets and low business volume (Leleux & Constantinou, 2007). Microfinance institutions from host and home country can connect with each other and make use of remittance inflows to support the local micro-enterprises from both sides to expand their business and cooperate with each other. This could be beneficial for microfinance institutions from the profit generated and for poor population from new employment opportunities.

2. Research question

This study aims to explore how to create a sustainability model of microfinance to fulfill both social responsibility and financial sustainability by integrating remittance flows and cross-border micro enterprise activities to microfinance business.

The research question is:

How to integrate remittance inflows and cross-border micro enterprise activities in microfinance business to support microfinance institutions fulfilling both social responsibility and financial sustainability?

These following issues will be addressed in this research:

The first part presents the relevance to integrate remittances and cross-border micro enterprise activities to microfinance business and conceptualizes theoretical framework of financial sustainability and outreach.

The second part, through the lens of business administration, captures:

- the importance of business components such as partner networks, funding strategy, product development and target customers and how they can bring together sustainability for microfinance business.

- the configurations of those business components to create sustainable business model for microfinance.

The third part, within the scope of entrepreneurship, explores the possibility of improving the level of financial sustainability and social responsibility of microfinance by connecting microfinance institutions, microenterprises, local business development organizations from host and home countries of migrants to support entrepreneurship between diaspora communities and home countries.

3. Methodology

Sub-Saharan Africa will be the main geographical focus of this study. This part of the world accounts for 67% of the world's least developed countries. Only 5% of poor people have access to financial service. The shortage of strong institutions, lack of appropriate economic, political and legal environment hampers the financial services to be delivered to poor people in a sustainable way (United Nation Capital Development Fund, 2005). Considering the topic research, it is probably more fruitful to undertake this research in Sub-Saharan Africa as MFIs in this area is not as developed as in Latin America and East Asia.

A mixture of methodology including primary data and secondary data collection and case study will be employed in this study. Secondary data of MFIs successfully integrating remittance and cross-border activity support in their businesses in Latin American, South Asia will be collected and used as research background to generate hypotheses of business components that can create sustainable business model for MFIs. At the same time, data of MFIs in Sub-Saharan African will also be collected to prepare for conducting case study.

After generating hypotheses, certain typologies of configurations for each business components will be created and tested on some cases of MFIs in Sub-Saharan Africa. Multiple case studies will be applied in this research as to increase the confidence in the robustness of the theory generated from hypotheses (Yin, 1994). During case studies, surveys and in-depth interviews could be employed to obtain primary data from chosen MFIs in the mentioned geographic area.

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