

The Impact of Foreign Funding on the Performance of Microfinance Institutions in Pakistan

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DEDICATION

This thesis is dedicated to my grandfather and my husband

For their endless support and encouragement

Abstract

The microfinance sector of Pakistan is flourishing since earlier 2000s and it has grown to an appreciable level. Like many developing economies, foreign funding from developed countries has been the major source of funding for the sector. However, there still remains a portion of un-served market due to the gap between funding sources and demand. The focus of this study is to analyze the impact of foreign funding received by Microfinance institutions (MFIs) of Pakistan on their performance. The performance is measured in terms of the growth of their micro credit and non credit micro services (micro insurance and micro savings). For analysis purpose, two approaches have been adopted. First is institutions based approach, in which 05 years (2008-2012) data of 08 non bank MFIs is considered for their micro credit outreach (number of active borrowers and GLP) and profitability (Net income, ROA, ROE). PPAF disbursements to MFIs in the sample are considered foreign funding and are taken as independent variable for this approach. Second approach is industry based in which 07 years (2006-2012) data on variables of microcredit outreach (number of active borrowers and GLP), micro savings (number of savers and savings value) and micro insurance (number of policy holders and sum insured) is considered. An estimated value of foreign funding is taken as independent variable.

The empirical results of institutions based analysis indicate that the impact of PPAF disbursements (as foreign funding) on outreach components, number of active borrowers and Gross Loan Portfolio (GLP), and profitability component of Net Income (NI) is highly significant. Whereas, the relationship of PPAF disbursements (foreign funding) with profitability components of ROA and ROE, is not highly significant but is also not

insignificant. On the other hand, the empirical results of industry based analysis indicate that the relationship of foreign funding with number of active borrowers and GLP is strongly significant thus referring that foreign funding plays an important role in the growth of micro credit sector in Pakistan. The relation of foreign funding with number of savers and value of savings is also significant. However, there comes out be an insignificant relationship of foreign funding with number of policy holders. Same is the case of the relationship between foreign funding and sum insured. The reason of this insignificance may be that micro insurance service is not that much dependent upon fund base of the industry as micro credit and even micro savings.

In addition, a mathematical relationship between outreach of micro credit (number of active borrowers & GLP), based on the results of the study, is formulated for non bank MFIs with around 20% equity and 80% debt. The underlying assumption is that at least half of the debt consists of foreign funding. It is formulated that number of active borrowers for a non bank MFI is directly proportional to amount of foreign funding received by the MFI, if average loan size is kept constant. If average loan size is not kept constant, then GLP becomes directly proportional to foreign funding. The study concludes that foreign funding plays a pivotal role towards the performance of MFIs in Pakistan, especially in terms of micro credit services.

Key Words: *Foreign funding, micro credit, outreach, microfinance institutions.*

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