DETERMINANTS OF RISK MANAGEMENT MECHANISMS IN MICROFINANCE INSTITUTIONS (MFIS)

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Abstract:

Microfinance institutions (MFIs) are crucial for financial inclusion and supporting economic development in developing countries, but effective risk management is essential for their stability. This study explores the determinants influencing the choice of risk management mechanisms within MFIs, focusing on their impact on organizational and economic performance.

The study employs a qualitative approach using document analysis of recent academic articles, research reports, and case studies from various regions, including Sub-Saharan Africa, South Asia, and Latin America. Nvivo software was used for thematic content analysis, enabling the synthesis of data and identification of recurring themes.
The study's findings indicate that the main determinants of the choice of risk management mechanisms identified are:

- Regulatory Framework: MFIs in stricter regulatory environments adopt more sophisticated mechanisms to comply with requirements.
- Organizational Capabilities: Institutions with limited resources favor simplified or outsourced approaches.
- Perceived Risks: The type of perceived risk, such as credit or operational risk influences the choice of mechanisms.
- Contextual Factors: Economic, political, and social conditions specific to the regions also play a significant role.

Additionally, the identified risk management mechanisms in the study include:
- Internal Monitoring and Audit Systems: Used to identify and monitor credit risks and fraud.
- Portfolio Diversification Policies: Aiming to minimize potential losses related to excessive concentration in certain sectors.
- Technological Tools: Such as risk management software to enhance the monitoring of operations and credits.
- Capacity-Building Mechanisms: Training programs for employees to strengthen compliance with risk management standards.

The results show that MFIs need to tailor their risk management practices according to their characteristics and environment. Larger or regulated MFIs adopt advanced practices, while those with fewer resources use simpler solutions. The study recommends customizing these mechanisms to better meet the needs of MFIs and regulators.

Keywords - MFIs, Risk Management, Regulatory Framework, Organizational Capabilities, Perceived Risks, Nvivo.