Djan, Kwame Ohene; Mersland, Roy

Article — Accepted Manuscript (Postprint)

Does Religious Affiliation Influence the Design of Corporate Governance? Evidence from the Global Microfinance Industry

Strategic Change

A later version of this paper has been published as:
Djan, K. O.. & Mersland, R. (2017), "Does religious affiliation influence the design of corporate governance? Evidence from the global microfinance industry". Strategic Change Journal. Vol. 26: 101-116.
DOI: 10.1002/jsc.2113
ORCID (Roy Mersland): 0000-0002-6683-2737

Does religious affiliation influence the design of corporate governance? Evidence from the global microfinance industry

Kwame Ohene Djan, School of Business and Law, University of Agder, Norway

Roy Mersland, School of Business and Law, University of Agder, Norway

ABSTRACT

Does religious affiliation influences the governance choices of firms? Using data from the global microfinance industry we theorize that Christian Microfinance Institutions (MFIs) should have slacker governance compared with secular MFIs. Our overall results indicate that Christian MFIs do not have a slacker governance design. For instance, Christian MFIs tend to have higher audit quality and a significantly higher number of board meetings compared with secular MFIs. The tests indicate, however, that Christian MFIs are relatively less regulated by national banking authorities.

KEY WORDS:

Religion, Corporate Governance, Microfinance Institutions, Christian Organizations

1. INTRODUCTION

Firms organize their governance according to their nature and needs (Fama and Jensen, 1983; Demsetz, 1983). Adams et al. (2010) argue that corporate governance arises endogenously as firms choose governance design, depending on the overall governance situation of the firm. Factors such as profit orientation, legal incorporation, firm size, market situation and task characteristics are known to influence a firm's governance design. What has not been studied in the literature is whether religious affiliation influences the governance choices of firms. This paper aims to fill this void, examining whether Christian organizations and secular organizations operating in the same markets are governed differently.

Hall (2002) notes that, until quite recently, religious bodies and faith-based organizations were free of many pressures for accountability. However, he remarks that the continuous record of misdeeds involving clergy, religious bodies, and faith-based organizations have tarnished the image of high purpose and that in reality, political influence has long protected religious entities from being held answerable. Across the globe, several spectacular scandals involving Christian organizations have emerged. One example is financial improprieties of the leadership of the Orthodox Church in America between 2005 and 2008 (Cooperman, 2006). Another example, from Norway, is a case of embezzlement by the CEO of Betanien, a large Christian Foundation that operates hospitals, kindergartens, nursing homes and a university college. In court, the CEO admitted spending more than US$2 million of the foundation's money on revelry, prostitutes and private consumption (Newspaper VG May 2nd, 2015). Another incident concerns a faith-based mutual fund established by the Baptist Foundation of Arizona in the USA to finance charities managed by the Church. According to Hall (2002), after having sold securities worth more than US$500 million during half a century, the foundation contributed only US$1.3 million to the church. Thus, there is certainly a need to better understand governance in religious organizations.

An industry that has attracted Christian actors is the microfinance industry, where the hope is that the provision of financial services to economically poor families and their income generating activities will foster economic and social development (Armendariz and Morduch, 2010). Opportunity International, a Christian international microfinance network, in the early 1970ties preceded Nobel Prize Laureate Mohammad Yunus in servicing economically poor people with microcredit (Mersland et al., 2013). In the global dataset applied in this study, approximately one-sixth of all Microfinance Institutions (MFIs) have a Christian origin. The microfinance industry offers a unique setting in which to study governance differences between Christian and secular organizations.

This study is inspired by Du (2013), who investigates the impact of religion on agency costs, finding that religion has a significant negative influence on owner-manager agency costs. Our hypothesis is that such religious influence results in different governance systems. Agency theory suggests that governance structures are necessary to mitigate divergences in motivations between owners/stakeholders of firms and their managers (Jensen & Meckling, 1976; Fama & Jensen, 1983). Besley and Ghatak (2005), however, indicate that some organizations are mission-driven and that those working in such organizations are *motivated agents*, i.e., agents who pursue goals because they perceive intrinsic rewards from doing so (Besley & Ghatak, 2005). Thus, if Christian MFIs are more mission-driven than secular MFIs, we should expect them to have slacker governance structures than secular MFIs.

The data used in the analysis contain information from 402 MFIs in 73 countries. Of this number, approximately 17% have a Christian origin. Generally, the results do not support the hypothesis that Christian organizations exhibit slacker governance than secular organizations. There are few significant differences between the governance structures of Christian and secular MFIs. With regard to some governance variables, Christian MFIs actually display stricter governance practices than their secular counterparts: They have significantly higher numbers of board meetings per year, better audit quality and significantly higher numbers of international directors. However, in regard to public regulations, Christian MFIs are relatively less-regulated by national banking authorities.

This paper is structured in six sections. Following this introduction, section two reviews the relevant empirical literature, while section three describes the basic applicable theories and the research hypotheses. The data and research methodology are set out in section four, the results are presented in section five, and section six concludes the study.

2. LITERATURE REVIEW

2.1 CHRISTIAN INVOLVEMENT IN MICROFINANCE

Microfinance is banking in small amounts, targeting low-income families and their income generating activities. The best known form of microfinance is microcredit, which is a small loan, normally between US$ 50 and US$ 5,000, which the borrower repays in frequent installments over a short time, often between 3 and 24 months. Microfinance also involves other banking services, such as payment services, savings and insurance. The continuous rapid growth of microfinance over the last three decades will soon make microfinance the world's largest banking market in terms of number of customers. It is estimated that 500 million people in low-income countries already have some type of micro insurance, and the largest microfinance bank, Equity Bank in Kenya, now holds more than 50% of all savings accounts in the country (Mersland, 2013).

Microfinance is not a recent phenomenon. Adam Smith (1776, p. 39) noted, "Money, says the proverb, makes money. When you have got a little, it is often easy to get more. The great difficulty is to get that little." It is easy for historians to identify initiatives aimed at helping economically poor people to "get that little". For example Hollis and Sweetman (1998) present six pro-poor credit systems in Europe between the 16th and 19th centuries. Others have focused on savings as a way to "get that little" (Teck, 1968). The savings bank system dates to the early 19th century (Horne, 1947).

Among the active agents in securing economically poor people access to credit and savings facilities has been the church and individuals motivated by their Christian faith. For example, the Catholic Church in Italy in the 15th century set up not-for profit pawn brokers called Monte di Pietá as an alternative to high priced money lenders (Menning, 1992). Similarly, Catholic priests have often served as "midwives" when savings and credit cooperatives, a still widespread banking system dating back 150 years, were established (Teck, 1968). Additionally, Protestant churches and church-members have been and continue to be active in bringing financial services to economically poor people. For example, pastors, priests and Christian businesspeople were at the forefront in establishing savings banks during the 19th century, and in England, Anglican reverend Henry Duncan is known as the "father of savings banks" (Horne, 1947).

Today, several Christian actors are involved in microfinance, including the international network of Opportunity International, which operates 43 MFIs in 26 countries, and the Vision Fund of World Vision, which operates 42 MFIs in 42 countries. Other important international Christian microfinance actors include Catholic Relief Services, Mennonite Economic Development Associates (MEDA), the Norwegian Mission Alliance, World Relief, Cordaid, Oikocredit and the Strømme Foundation (Mersland et al., 2013).

2.2 CHRISTIAN ORGANIZATIONS AND THE ISSUE OF CORPORATE GOVERNANCE

Smith and Rayment (2007) explain that spirituality in the workplace concerns individuals and organizations perceiving an occupation as a spiritual path, as an opportunity to grow and contribute to society in a meaningful way. Spirituality, as defined by Smith and Rayment (2007), is a state or experience that can provide individuals with direction or meaning or feelings of understanding, support, inner wholeness or connectedness. Hilary and Hui (2009) argue that firms that operate in different social environments exhibit different behaviors. They further observe that, in reality, firms do not make decisions, people do, and what people do outside work is likely to affect how they make decisions at work.

Hall (2002, p. 2) notes that "As the scope, scale, and range of services provided by faith-based organizations has expanded and their dependence on government funding has increased, the need for resolution of unanswered questions about their accountability has intensified." He observes that, on the one hand, the increase in government subvention has predictably brought with it higher standards of accountability and financial management. On the other hand, to the extent that religious bodies and faith-based organizations continue to rely significantly on private funds, they have become subject to the general problems of accountability that affect corporate management and governance. Indeed, in present times, questions about financial mismanagement, self-dealing, conflicts of interest and public disclosure are as likely to be raised about religious organizations as about secular ones (Hall 2002; Tsafe & Rahman, 2013).

A limited number of studies have explored the impact of religious affiliation on the management and governance of economic organizations in general. Miller and Hoffman (1995) report a negative correlation at the individual level between religiosity and attitude towards risk and danger. Similarly, a study by Osoba (2003) reveals that risk-averse individuals attend church more often than risk-seeking individuals. Hilary and Hui (2009) build on these findings in further studying the effects of religiosity on corporate decision making in America. The findings reveal a significant negative correlation between the level of religiosity in a county and the level of risky investments taken by companies. Combining these views and empirical findings, one might intuitively assert that corporate governance systems and structures would differ between Christian and secular MFIs. Knox, Blankmeyer, and Stutzman (2006), in a study of relative economic efficiency in the nursing industry in Texas, identify significant differences in the economic efficiency of religious-affiliated and private secular facilities. Their findings reveal that, although quality appears to be homogeneous, private secular facilities are significantly more efficient than religious-affiliated homes. This buttresses our earlier intuitive assertion that religiosity may impact corporate governance systems.

2.4 PREVIOUS EMPIRICAL RESEARCH FINDINGS

In what follows, we review the relevant empirical MFI governance literature. We focus on findings related to the governance variables that will later be tested as we seek to identify differences in governance structures between Christian and secular MFIs. Governance is high on the microfinance research agenda because it is considered one of the major risks in the industry (CSFI, 2012). Generally, research has focused on how different governance variables influence the social and financial performances of MFIs. In this paper, the focus is not on how such variables influence MFI performance but on whether Christian MFIs organize their governance differently from secular MFIs. The aim is therefore to learn more about how religion influences governance structures in organizations in general and in MFIs in particular.

MFIs can be organized as shareholder-owned firms (SHF), member-based cooperatives, non-governmental organizations (NGOs) or state-owned companies, with the first three accounting for the bulk of MFIs. Shareholder-owned companies compose 33%, member-based cooperatives compose 13%, and NGOs compose 52% of our dataset. The effects of *ownership type* on MFI performance is a core research area (Mersland, 2009), although researchers have found little effect of ownership differences in MFIs (Mersland and Strøm, 2009).

Another interesting feature of the microfinance industry is that some MFIs are regulated by national banking authorities, while others are not. Hartarska and Nadolynak (2007) report little direct effect of *regulation* on MFI performance, although indirectly, it can have a positive effect because with regulation often comes permission to mobilize savings, which increases access to funding.

The effect of *board size* has been studied in several papers. Most interesting is probably Hartarska and Mersland (2012), who apply a stochastic frontier analysis, allowing them to simultaneously study effects on both financial and social performance. Moreover, they include curvilinear effects and find that MFI performance improves as up to 9 board members are added and decreases after that. Thus, compared with most regular firms, MFIs benefit from larger boards.

Mersland and Strøm (2009) include the effect of having *international directors*, arguing that this could create greater board diversity, as found by Oxelheim and Randøy (2003) in a sample of Scandinavian firms. However, Mersland and Strøm (2009) found that MFI performance improved as a result of having local rather than international directors.

Whether it is beneficial for an MFI to have *female leaders* is examined by Strøm et al. (2014), who find that having a female CEO is positively related to MFI performance. They conclude that the positive effect is not because of improved governance under female leadership but because female leaders obtain positive results in an industry that caters largely to female customers (Strøm et al., 2014).

The *number of board meetings* is often used in studying the control dimension of boards. For the microfinance industry, Beisland et al. (2014) find no association between the number of board meetings and MFI performance.

Strøm et al. (2014) argue that in a young industry such as microfinance, the *expertise of managers* is more influential on MFI performance than the design of corporate governance. Following this argument, Pascal et al. (2015) find that MFIs managed by CEOs with a business education perform better, both financially and socially, than MFIs managed by CEOs without a business education.

Auditing, both in the form of having financial statements reviewed by high quality external auditors and having an internal auditor within the MFI report directly to the board, is an important governance variable, and some researchers have studied the association between audit quality and MFI performance. Hartarska (2009) finds that MFIs with externally audited accounts perform equally well as MFIs without audited accounts, while Mersland and Strøm (2009) find that MFIs with internal auditors exhibit better financial performance than MFIs without internal auditors reporting to the board.

3. THEORIES AND HYPOTHESES

3.1 THEORIES ON DIFFERENCES IN GOVERNANCE BETWEEN CHRISTIAN AND SECULAR ORGANIZATIONS

Adam Smith (1776, p.700), in ‘The Wealth of Nations’, noted the central governance problem, writing: “*The directors of such companies, however, being the managers rather of peoples’ money than of their own, it cannot be well that they should watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch over their own. Like the stewards of a rich man, they are apt to consider attention to small matters as not for their master’s honor, and very easily give themselves a dispensation from having it. Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company*”. The fundamental corporate governance problem, from a theoretical perspective, is thus the so-called ‘agency problem’, which results from the separation between ownership and management (Thomson & Conyon, 2012), also termed the ‘separation of ownership and control’ by Berle and Means (1932). Agency costs include the “*costs of structuring, monitoring and bonding a set of contracts”* among agents with conflicting interests (Jensen & Meckling, 1976 pp. 308-309). Thus, a central question of this paper is whether the conflicting interests of owners and managers result in different governance measures in Christian and secular MFIs.

In his much-debated classic work, Max Weber (1930/1958) argues that Christians (in particular protestant Christians) have a stronger work ethic than non-Christians. Similarly, Ter Haar and Ellis (2006) find that religious beliefs provide people with moral guidance. Christopher (2010 p. 689) argues that agency costs are lower in value-based organizations, stating that “*in organizational contexts where sociological, cultural and ethical values are very influential, the costs of control will be less”.*

Weber's theory of a superior "work ethic" among Christians and Christian leaders may well be false. However, the focus of this paper is on whether Christian organizations structure their governance differently from secular organizations. Thus, if leaders and owners of Christian organizations consider agency costs in their organizations to be relatively low, we should expect a slacker governance structure in Christian MFIs compared with secular MFIs.

Stewardship theory is another governance theory that may support relatively low agency costs in Christian organizations and thereby slacker governance in Christian MFIs. Puyvelde et al. (2012 p.436) argues that "*while agency theory assumes that agents have a low identification with the mission of the organization and may externalize organizational problems to avoid blame, stewardship theory, in contrast, assumes that agents have a high identification with the mission of the organization*". Besley & Ghatak (2005) emphasize that individuals who care about a particular cause can be considered 'motivated agents' and that such individuals are likely to end up as employees in mission-oriented nonprofits such as Christian MFIs.

Another important factor is that, if agents in Christian MFIs practice basic Christian ideology, there may be less need for strict governance of Christian MFIs. For instance, in the book of Colossians 3:23, the Bible says that, *"Whatever you do, work at it with all your heart, as working for the Lord, not for human masters".* Thus, we should expect owners of Christian MFIs to establish less strict governance standards because they expect that their leaders will be more cause-motivated and better stewards than leaders of secular MFIs.

3.3 THE RESEARCH HYPOTHESES

The overall hypothesis in this paper is that Christian organizations have "slacker" governance compared with secular organizations. In the following section, we present specific hypotheses for the eight individual governance variables studied in this paper. For all the variables, we predict slacker governance in Christian MFIs compared with secular MFIs. Insights into the microfinance industry do, however, indicate that for some of the governance variables, there is a chance of finding the opposite. In these cases, we present rival hypotheses.

i. Ownership structure

The theory of ownership cost suggests that shareholder-owned firms compared with mutually owned firms are better at minimizing agency costs stemming from the separation of ownership and management (Hansmann, 1996, Mersland, 2009). Thus, a shareholder structure could be considered a stricter ownership structure compared with a mutual ownership structure. However, mutual ownership, either in the form of NGOs or member-based cooperatives, are relatively better at reaching and serving vulnerable customers (Hansmann, 1996, Mersland, 2009). It is thus expected that mutual firms are more socially oriented than shareholder firms (Ebrahim, 2003). Because serving the poor is a biblical imperative, it is expected that Christian MFIs are at the forefront in targeting vulnerable customers (Mersland et al., 2013, Bussau and Mask, 2003). Thus, we expect the following hypothesis to hold:

$H_{1:}$ *The probability of an NGO or cooperative ownership structure is higher in Christian MFIs than in secular MFIs.*

ii. Bank Regulation

In the microfinance industry, there is increasing debate over whether MFIs should be regulated by local banking authorities. Several unregulated MFIs have recently opted to transform into banks and thereby come under regulatory scrutiny (D'Espallier et al., 2015). Because regulators normally demand that regulated institutions have identifiable owners, they normally only allow shareholder-owned institutions to be regulated (D'Espallier et al., 2015). Thus, if Christian MFIs tend to be NGOs, they will have a lower probability of being regulated. Similarly, from the perspective of stewardship theory, it may be assumed that if the goals of agents in Christian MFIs are to be better aligned with those of their financiers, there will be less need of bank regulation. Therefore, we hypothesize:

H_2: *The probability of being regulated by local banking authorities is lower for Christian MFIs than for secular MFIs.*

iii. International Directors

In the general governance literature, having international directors on the board is considered a sign of stricter governance (Oxelheim and Randøy, 2003). Thus, we expect to find relatively few international directors on the boards of Christian MFIs. However, Mersland et al. (2011) indicate that the microfinance industry is international in scope, with heavy investments by international lending institutions. Mersland et al. (2013) further note that several Christian MFIs were initiated by international Christian organizations and that several international lenders – for instance, Oikocredit and several international support organizations such as Vision Fund – have a Christian origin. It may be expected that such initiators, lenders or support organizations would want a board position to follow their engagement (Fama and Jensen, 1983). To account for this view, we propose a rival hypothesis:

H_{3a}: *Christian MFIs have a higher number of international directors than secular MFIs.*

H_{3a}: *Christian MFIs have a lower number of international directors than secular MFIs.*

iv. CEO Business Education

Pascal et al. (2015) argue that because MFIs work with double bottom lines, i.e., they pursue both financial and social objectives, it is not obvious that they prefer hiring CEOs with a business education. In testing this empirical question, Pascal et al. (2015) find that MFIs managed by CEOs with a business education exhibit better financial and social performance than MFIs managed by CEOs without a business education. Some argue that Christian MFIs, in addition to financial and social objectives, should also pursue spiritual objectives (Bussau & Mask, 2003). In line with this tendency for spiritual focus, Mersland et al. (2013) argue that Christian MFIs can employ managers who have a strong spiritual background by their standards but may not necessarily have the relevant educational background. From this point of view, we present the following hypothesis:

H_4: *The probability of having a CEO who has a university business education is lower in Christian MFIs than in secular MFIs.*

v. Board size

Most studies of the effects of board size on firm performance find that larger boards are less effective, negatively affecting performance (Eisenberg et al., 1998). However, Oster & O'Regan (2005) argue that in nonprofit organizations, board size may need to be larger because of the broader mandates of such organizations compared with those of for-profit firms. Bussau & Mask's (2003) argue that Christian MFIs also have a mandate to focus on spiritual results. Thus, in line with the multitask model proposed by Holmstrøm and Milgrom (1991) – that with more tasks to attend to, the size of the board will increase – we hypothesize the following:

H_{5}: *Christian MFIs have larger boards than secular MFIs.*

vi. Number of board meetings

The number of board meetings is a measure of the intensity of board oversight (Adams and Ferreira, 2009). Thus, we may expect Christian MFIs to hold fewer board meetings than secular MFIs. However, in light of the multitask model of Holmstrøm and Milgrom (1991) and the spiritual tasks of Christian MFIs (Bussau and Mask, 2003), we may expect relatively more board meetings in Christian MFIs. Thus, we propose a rival hypothesis:

H_{6a}: *Christian MFIs have more board meetings per year than secular MFIs*

H_{6b}: *Christian MFIs have fewer board meetings per year than secular MFIs*

vii. Auditing quality

High quality auditing, conducted by an external or an internal auditor, improves stakeholders' confidence in financial reporting and increases access to external funding (Lin and Liu, 2009).

Mersland et al. (2013) find that Christian MFIs have lower funding costs as a result of their wider international network compared with secular MFIs. It could be argued that international stakeholders will demand higher quality audits from MFIs. Nevertheless, viewing auditing as a control function, we expect Christian MFIs to have lower auditing quality than secular MFIs. In line with prior research, we regard the use of a Big 4 external auditor (Deloitte, Ernest & Young, PwC and KPMG) and an internal auditor reporting directly to the board as evidence of high quality auditing and propose the following hypothesis:

$H_{7:}$ *Christian MFIs are less likely to use the services of Big 4 external auditors and to have an internal auditor reporting directly to the board than secular MFIs.*

viii. Female CEO

Management and gender has long been on the research agenda (Kanter, 1977). Strøm et al. (2014) find that MFIs managed by female managers exhibit better performance compared with MFIs managed by male CEO and argue that the better performance arises from female CEOs' ability to better understand the female market segments targeted by MFIs (Armendariz and Morduch, 2010). Mersland et al. (2013) find that Christian MFIs serve relatively fewer female customers compared with secular MFIs. This could be a sign of traditional Christian beliefs and practices, which often discriminate against women. Adams and Ferreira (2009) argue that female directors are "tougher" monitors than men. Thus, if Christian MFIs opt for slacker governance or have a generally more negative attitude towards women, they would not prefer female managers. We therefore propose the following hypothesis:

H_8 *The probability of having a female CEO is lower among Christian MFIs than secular MFIs.*

4. DATA AND METHODOLOGY

This study uses data from 402 MFIs operating in 73 countries worldwide. The data were extracted from detailed risk assessment reports produced by the five leading microfinance rating agencies. Over the last decade, in an effort to assure transparency and attract funding to the industry, it has become common for MFIs to be assessed by specialized rating agencies. The information source from which the data were extracted is publicly available at www.ratingfund2.org or from the rating agencies' websites. The rating reports used to compile the database are from the years 2001 through 2010 and are produced by Planet Rating, Microfinanza Rating, Microrate, M-CRIL and CRISIL. Up to six years of information are available for each MFI. The content of a rating report is not standardized, resulting in randomly missing values for several variables. Nevertheless, for this study, the source of information is essential because the rating reports contain detailed information on the backgrounds of the MFIs and often allow one to identify whether an MFI has a Christian origin or not. Table 1 provides summary statistics for the main variables used in this study. As seen in the table, the value of total assets held by the median MFI is $2.67 million (US). The age of the median MFI is 8 years, illustrating the newness of the industry. Also essential to this study, approximately seventeen percent of the MFIs have a Christian origin[1], and sixty-four percent are organized as NGOs or Cooperatives. Thirty-nine percent of the MFIs have an international initiator. The board size of the median MFI is six members, and the median number of board meetings is four. Twenty-nine percent of CEOs are women, and sixty-four percent of CEOs have a business education. The average number of international board members is only 0.59. Twenty-eight percent of the MFIs

1 Very few MFIs with an Islamic affiliation are rated. The dataset does therefore not include islamic MFIs.

are regulated by national banking authorities. Thirty percent of the MFIs employ the services of one of the Big 4 external auditors, and forty-two percent have an internal auditor reporting directly to the board.

The data have a certain sample selection bias, as only rated MFIs are entered. However, for the rated MFIs, most rating categories are represented in the data. Moreover, this selection has advantages because much of the background “noise” has been eliminated by including only MFIs willing and able to be rated. Thus, the dataset includes MFIs that want to reach out to investors and other stakeholders and are willing to let a third party evaluate their operations and make the information publicly available. Thus, we believe that our database provides a relatively representative sample of the microfinance industry.

< Table 1 here >

Control variables include *MFI specific control variables* such as: *MFI age*, which indicates the number of years since the MFI started microfinance operations; *MFI size*, measured using the dollar value of assets as a proxy; and *Int-init*, a dummy indicating whether the MFI was initiated by an international agent (Mersland et al., 2013). *Country-specific control variables* include the *Human Development Index* (HDI) of the country, where the MFI is situated and the *percentage of the Christian population* in the country. Moreover, *regional dummies* for *Latin America, Asia,* and *Africa* are included, while *Eastern Europe* is left out to serve as a reference point in the regressions.

Two different tests are applied to test for differences in governance strictness between Christian and secular MFIs. We first perform *univariate t-* and *χ^2-tests* to analyze differences in mean and median values, respectively, between the two groups on the different hypothesized governance variables. Second, using the random-effects (RE) model, we regress the different corporate governance variables on the predictor variable (the dummy for Christian affiliation) and the set of control variables. Our selection of the RE model over the fixed-effects model was influenced by the time-invariant nature of several of the covariates. The RE model accounts for all unobserved, institution-specific and time-invariant variables by including a term μ_i that reduces any bias caused by potentially omitted variables. When dependent variables are categorical, we use logistic regression models[2]; if not, we use OLS. The variables analyzed using OLS include board size, board meetings per year and number of international directors. The remainder are analyzed by means of a logistic regression. The operational regression model used in this study is as follows:

Religion and Governance

$$Gov - Variable_{it} = \beta_0 + \beta_1 DmRel - Init_{it} + \beta_2\ Controls_{it} + \mu_i + \varepsilon_{it} \ldots\ldots \quad \ldots\ldots (1)$$

where

$Gov - Variable_{it}$ = Governance Variable (*e.g., board size, number of board meetings, etc.*) for MFI *i* at time *t,* where *i*=1.......n and *t*=1.......T

$DmRel - Init$ = Dummy for Christian initiation of MFI

$Controls$ = Control variables (MFI size, age, international initiator, HDI, regional dummies and percentage of Christian population)

2 As a robustness test, we have also run probit regression models (unreported), which yield similar results to those presented in the paper.

μ_i = Unobserved heterogeneity; MFI specific effect

ε_{it} = Idiosyncratic error as it varies across time *t* and MFI *i*

The correlation matrix (Table 2) for the variables included in the study shows that none of the coefficients suggest multicollinearity, the highest being the correlation between *the percentage of Christian population* and *the regional dummies* for *Asia* and *Latin America* (-0.68 and 0.65, respectively).

< Table 2 here >

5. FINDINGS AND ANALYSIS

Table 3 presents the results of the univariate independent *t*-test and the nonparametric χ^2-test to compare, respectively, the mean and median values of the governance variables for Christian and secular MFIs.

< Table 3 here >

Interestingly, as indicated in Table 3, the *t-test* and χ^2-*test* indicate significant governance differences between Christian and secular MFIs in all variables except nonprofit ownership. For some of the variables, however, significant differences are found only for the t-test or the χ^2-*test* and not for both tests simultaneously. Not all findings support our hypotheses. It is worth noting that a relatively large share of Christian MFIs use a Big4 external auditor and employ an internal auditor reporting directly to the board. Thus, in regard to auditing, Christian MFIs appear to exhibit stricter governance than secular MFIs. Similarly, Christian MFIs have significantly more international board directors than secular MFIs. Based on the univariate findings, we cannot confirm our hypothesis that Christian MFIs have slacker governance compared with secular MFIs. We now turn to the multivariate regression analysis and present the results of the Random Generalized Least Squares (RGLS) and Logistic regressions for the governance variables in Tables 4a, 4b and 4c.

< Tables 4a, 4b and 4c here >

As shown in table 4a, the RGLS regression does not reveal a significant relationship between Christian identity and board size. It shows, however, that Christian MFIs have significantly more board meetings per year and have a larger number of international directors than secular MFIs.

Table 4b mirrors the finding reported in Table 3 that Christian MFIs, to a larger extent, hire Big4 external auditors and have an internal auditor reporting directly to the board. This is an important finding, as we now control for international orientation by including a control variable for initiation of an MFI by an international player. The motivation of Christian MFIs to hire Big4 auditors appears to be related to Christian MFIs receiving relatively more internationally subsidized loans, as reported in Mersland et al. (2013), and that such lenders require high quality auditing, both internal and external. Although the sign of the coefficient is in line with the findings reported in table 3, the results in table 4b do not indicate a significant relationship between Christian MFIs and a tendency to have a CEO with a business education.

In table 4c, we find no significant relationship between Christian affiliation and nonprofit ownership. Nor do we find a significant relationship between Christian affiliation and having a female CEO. However, we do confirm the hypothesis that Christian MFIs are less likely to be regulated by national banking authorities than secular MFIs. Taken together, tables 4a, 4b and 4c do not support our general hypothesis that Christian organizations have slacker governance than secular organizations.

Institutional theory can help us understand the findings. According to DiMaggio and Powell (1983) organizations become isomorphic, or similar, when they operate in similar markets, under similar legal regimes and depend on similar networks and funders. Over more than three decades important international initiatives like for instance CGAP, the microfinance branch of the World Bank, USAID, the foreign aid department of USA and Mixmarket, a web-platform where MFIs can match with funders, have focused on knowledge creation and microfinance expansion. Most MFIs are influenced by these initiatives, particularly those in need of networks and funders like the ones included in our dataset. This leaves little room for Christian MFIs to organize their governance structure much different from that of secular MFIs.

6. CONCLUSIONS

The motivations for the paper are twofold: First, we aim to be the first to test whether religious affiliation influences governance choices of firms. Our second motivation relates to the increasing record of misdeeds involving clergy, religious bodies and faith-based organizations.

Thus, we wish to test whether Christian organizations tend to implement slacker governance in general, which may enable misconduct in such organizations.

To test our empirical question, we use data from the global microfinance industry. Approximately one-sixth of the 402 MFIs included in our dataset have a Christian origin. With Christian and secular MFIs operating in the same markets, we argue that the microfinance industry offers an interesting setting in which to study differences in governance between Christian and secular organizations.

We find little support for the hypothesis of slacker governance in Christian MFIs. In fact, compared with secular MFIs, Christian MFIs have stricter governance mechanisms in several respects. Compared with secular MFIs, Christian MFIs have more board meetings, more international directors, more recognized external auditors and a stronger tendency to employ internal auditors who directly report to the board. Only in one regard do Christian MFIs exhibit slacker governance: they appear to shy away from public regulatory oversight to a larger extent than secular MFIs. Board sizes and CEO profiles are similar across Christian and secular MFIs. We argue that Christian and secular MFIs have become similar in their governance structures because they operate in similar markets and depend on the same networks and funders

What can we learn from this study? First, we believe the study sends a message to those who criticize Christian organizations for being unprofessional and not installing systems to control their managers. Our findings reveal that Christian MFIs are at least as good (or as bad) as secular MFIs in setting up their governance structures. Second, we hope the study motivates an increased focus on governance in Christian organizations. Our view is that Christian organizations should be at the forefront in assuring good managerial stewardship.

We suggest looking deeper into the finding that Christian MFIs are to a lesser extent than secular MFIs regulated by national banking authorities. Historically, the link between the government and the church has been conflictive. Do Christian organizations still fear public scrutiny? A second interesting finding that could motivate further research is that Christian MFIs have a stronger tendency than secular MFIs to have an internal auditor report directly to the board and to hire high quality external auditors. Is this because Christian MFIs, by virtue of certain doctrines of Christianity (e.g., 'the protestant ethic' of Weber, 1958) adhere to this principle and want to prove to their owners and financiers that they are good stewards? Or is it simply because Christian MFIs are more dependent on subsidizing funders (Mersland et al., 2013) who demand high quality audit reports, as noted in this paper? Finally, we suggest that researchers look into whether Christian organizations competing in similar markets with secular organizations actually differ in the services they deliver or whether isomorphic forces make them similar despite religious affiliation.

REFERENCES

Adams, R.B., and Ferreira, D. (2009). Women in the boardroom and their impact on governance and performance. *Journal of Financial Economics, 94(2), 291-309*.

Adams, R.B., Hermalin, B.E. and Weisbach, M.S. (2010). The role of Boards of Directors in Corporate Governance: A Conceptual Framework & Survey. *Journal of Economic Literature, 48(1),* 58-107.

Armendariz, B., and Morduch, J. (2010). *The Economics of Microfinance*. London: MIT Press

Beisland, L.A., Mersland, R. and Randøy, T. (2014). The Association between Microfinance Rating Scores and Corporate Governance: A Global Survey. *International Review of Financial Analysis, 35(5),* 268-280.

Berle, A., and Means, G. (1932). *The Modern Corporation and Private Property*. New York: Macmillan.

Besley, T., and Ghatak, M. (2005). Competition and Incentives with Motivated Agents. *American Economic Review, 95(3),* 616-636.

Bussau, D., & Mask, R. (2003). *Christian Microenterprise Development An introduction*: Oxford: Regnum Books.

Christopher, J. (2010). Corporate Governance- A multi-theoretical approach to recognizing the wider influencing forces impacting on organizations. *Critical Perspectives on Accounting*, 21, 683-695.

Cooperman, A. (2006). Accusations of Misused Money Roil Orthodox Church. *The Washington Post*. Retrieved 04.05.2014 from http://www.washingtonpost.com/wpdyn/content/article/2006/02/25/AR2006022501266.html.

CSFI. (2012). *Microfinance banana skins*: Staying relevant. Center for the study of financial innovations, New York.

D'Espallier, B., Hudon, M. & Mersland, R. (2015). *Transformation of microfinance institutions.* Working Paper, CERMi. ULB, Belgium.

Demsetz, H. (1983). The structure of ownership and the theory of the firm. *Journal of Law and Economics, 26*(2), 375-390.

DiMaggio, P. J., & Powell, W. W. (1983). The iron cage revisited: Institutional isomorphism and collective rationality in organizational fields. *American Sociological Review*, 48, 147–160.

Du, X. (2012). Does Religion Matter to Owner-Manager Agency Costs? Evidence from China. *Journal of Business Ethics.*

Ebrahim, A. (2003). Accounting in practice: Mechanisms for NGOs. *World Development, 31*(5), 813-829.

Eisenberg, T., Sundgren, S., & Wells, M.T. (1998). Larger board size and decreasing firm value in small firms. *Journal of Financial Economics, 48*(1), 35-54.

Fama, E.F., & Jensen, M.C. (1983). Separation of Ownership and Control. *Journal of Law and Economics, 26*(2), 301-325.

Hall, P.D. (2002). *Accountability in Faith-Based Organizations and the Future of Charitable Choice.* Paper presented at the Panel on Understanding Accountability in Faith-based Organizations, Montreal.

Hansmann, H. (1996). *The Ownership of Enterprise*. Cambridge, Massachusetts: The Belknap Press of Havard University Press.

Hartarska, V. (2009). The impact of outside control in microfinance. *Managerial Finance, 35,* 975-989.

Hartarska, V., and Nadolynak, D. (2007). Do regulated microfinance institutions achieve better sustainability and outreach? Cross-country evidence. *Applied Economics, 39,* 1-16.

Hartarska, V., and Mersland, R. (2012). Which Governance Mechanisms Promote Efficiency in Reaching Poor Clients? Evidence from Related Microfinance Institutions. *European Financial Management, 18*(2), 218-239.

Hilary,G., & Hui, K.W. (2009). Does religion matter in corporate decision making in America? Journal of Financial Economics, 93, 455-473.

Hollis, A., & Sweetman, A. (1988). Microcredit: What can we learn from the past? World Development, 26, 1875-1891.

Holmstrøm, B., & Milgrom, P. (1991). Multitask principal-agent analyses: incentive contracts, asset ownership, and job design. *Journal of Law Economics & Organization,* 7, 24-52.

Horne, H.O. (1947). A history of savings banks. Oxford University Press. London.

Jensen, M.C., & Meckling, W.H. (1976). Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure. *Journal of Financial Economics, 3*, 305-360.

Kanter, R.M. (1977). *Men and Women of the Corporation.* New York: Basic Books.

Knox, K.J., Blankmeyer, E.C., & Stutzman, J.R. (2006). Comparative Performance and Quality Among Nonprofit Nursing Facilities in Texas. *Nonprofit and Voluntary Sector Quarterly, 35*(4), 631-667.

Lin, Z.J., & Liu, M. (2009). The impact of corporate governance on auditor choice: Evidence from China. *Journal of International Accounting, Auditing & Taxation, 18,* 44-59.

Menning, C.B. (1992). The Monte's Monte': The Early Supporters of Florence's Monte di. *Sixteenth Century Journal, 23*(4), 661-676.

Mersland, R. (2009). The Cost of Ownership in Microfinance Organizations. *World Development, 37*(2), 469-478.

Mersland, R. (2013). Market Opportunities for Microfinance Institutions. Enterprise Development & Microfinance, 24(4), 282-294.

Mersland, R., D'Espallier, B., & Supphellen, M. (2013). The Effects of Religion on Development Efforts: Evidence from the Global Microfinance Industry and a Research Agenda. World Development 41, 145-156.

Mersland, R., Randøy, T., & Strøm, R. Ø. (2011). The impact of international influence on microbanks' performance: A global survey. *International Business Review, 20*(2), 163-176.

Mersland, R., & Strøm, R. Ø. (2009). Performance and Governance in Microfinance Institutions *Journal of Banking and Finance, 33*, 662-669.

Miller, A. S., & Hoffman, J. P. (1995). Risk and Religion: An Explanation of Gender Differences in Religiosity. *Journal for the Scientific Study of Religion, 34*(1), 63-75.

O'Regan, K., & Oster, S. M. (2005). Does the structure and composition of the board matter? The case of nonprofit organizations. *Journal of Law, Economics and Organization, 21*(1), 205-227.

Osoba, B. J. (2003). *Risk Preferences and the Practice of Religion: Evidence from Panel Data*. Working Paper.

Oxelheim, L., & Randøy, T. (2003). The impact of foreign board membership on firm value. *Journal of Banking & Finance, 27*(12), 2369-2392.

Pascal, D., Mersland, R., & Mori, N. (2015). *CEO characteristics and microfinance performance*. Working Paper. University of Agder. Norway.

Puyvelde, S. V., Caers, R., Du Bois, C., & Jergers, M. (2012). The Governance of Non-profit Organizations: Integrating Agency theory with Stakeholder and Stewardship theories. *Nonprofit and Voluntary Sector Quarterly, 41*(3), 431– 451.

Smith, A. (1776). *An Inquiry into the Nature and of the Wealth of Nations* (Vol. 1). Indianapolis: Liberty Classics.

Smith, J. A., & Rayment, J. J. (2007). The Global SMP Fitness Framework A guide for leaders exploring the relevance of spirituality in the workplace. *Management Decision, 45*(2), 217-234.

Strøm, R. Ø., D'Espallier, B. and Mersland, R. (2014). Female leadership, performance, and governance in microfinance institutions. *Journal of Banking & Finance, 42*(C), 60-75.

Teck, A. (1968). *Mutual savings banks and savings and loans associations: Aspects of growth*. New York. Colombia University Press.

Ter Haar, G., & Ellis, S. (2006). The role of religion in development: Towards a new relationship between the European Union and Africa *The European Journal of Development Research, 18*, 351-367.

Thomsen, S., & Conyon, M. (2012). *Coporate Governance: Mechanisms and Systems*: McGraw-Hill Education.

Tsafe, B. M., & Rahman, R. A. (2013). Effects of Spirituality on Board Performance in Malaysian Microfinance Firms. *Middle-East Journal of Scientific Research, 18*(5), 675-688.

Weber, M. (1958). *The Protestant Ethic and the Spirit of Capitalism* (T. Parsons, Trans.). New York: Free Press.

Table 1 *Summary Statistics of Variables used in the study*

Variable	Obs (*n*)	Mean	Median	Std. Dev.	Min	Max
Dependent Variables						
Dm (Nonprofit)	1618	0.64	1	0.48	0	1
Dm Bank Regulation	1584	0.28	0	0.45	0	1
Board Size	1487	7.00	6	3.32	1	23
International Directors	1193	0.59	0	1.28	0	7
Dm Female CEO	1444	0.29	0	0.46	0	1
Board Meet Year	1049	7.43	4	8.43	1	96
Dm CEO Bus Edu	669	0.64	1	0.47	0	1
Dm External Auditors	945	0.30	0	0.46	0	1
Dm Internal Auditors	1442	0.42	0	0.49	0	1
Independent Variable						
Dm Religious Initiated	1606	0.17	0	0.37	0	1
Control Variables						
MFI Assets (×1000)	1585	6349	2672	13200	19.3	248000
MFI Age	1611	9.29	8	6.76	0	79
Dm Intern. Initiation	1602	0.39	0	0.49	0	1
HDI	1613	0.56	0.59	0.14	0.239	0.791
Percent Christian Popl.	1615	0.64	0.85	0.37	0.002	0.995
Lat. America	1611	0.40	0	0.49	0	1

Asia	1611	0.20	0	0.40	0	1
East Europe	1611	0.12	0	0.34	0	1
Africa	1611	0.28	0	0.45	0	1

Table 2 **Correlation Matrix**

	1	**2**	**3**	**4**	**5**	**6**	**7**	**8**
(1) Nonprofit	1							
(2) BankRegul.	-0.45	1						
(3) Board Size	0.20	-0.18	1					
(4) Int. Directors.	-0.18	0.05	0.06	1				
(5) Female CEO	0.13	-0.14	0.11	0.02	1			
(6) Board Meet Yr	0.20	-0.08	-0.04	-0.21	-0.09	1		
(7) CEO Bus Edu	-0.18	0.12	-0.07	0.07	-0.04	-0.24	1	
(8) Ext. Auditors	-0.08	-0.03	-0.02	0.29	-0.14	-0.11	0.14	1
(9) Int. Auditors	0.02	0.02	-0.04	0.16	-0.23	0.39	0.27	0.34
(10) Ln Assets	0.05	-0.01	0.09	0.24	-0.08	0.18	0.12	0.47
(11) Age	0.28	-0.06	0.02	-0.21	-0.15	0.39	-0.15	-0.05
(12) Int. Initiation	-0.05	-0.14	0.15	0.41	-0.05	-0.29	0.14	0.09
(13) HDI	0.24	-0.42	0.07	-0.16	0.26	0.04	-0.23	-0.07
(14) Lat. America	0.41	-0.21	0.15	-0.36	0.02	0.32	0.03	-0.12
(15) Asia	-0.35	0.30	-0.24	0.19	-0.13	-0.13	0.09	-0.13
(16) East Europe	-0.05	-0.17	0.02	0.21	0.16	-0.17	-0.12	0.28
(17) Africa	-0.16	0.23	-0.02	0.03	-0.05	-0.13	-0.00	-0.00
(18) Christ. Popl	0.43	-0.33	0.19	-0.29	0.10	0.26	-0.13	-0.02

	9	10	11	12	13	14	15	16	17	18
(9) Int. Auditors	1									
(10) Ln Assets	0.39	1								
(11) Age	0.15	0.29	1							
(12) Int. Initiation	0.04	0.10	-0.10	1						
(13) HDI	0.07	-0.01	0.04	0.01	1					
(14) Lat. America	0.04	0.02	0.32	-0.23	0.19	1				
(15) Asia	-0.09	-0.18	-0.16	0.08	-0.16	-0.46	1			
(16) East Europe	0.06	0.15	-0.26	0.24	0.29	-0.53	-0.26	1		
(17) Africa	0.05	0.03	0.01	-0.13	-0.49	-0.30	-0.09	-0.13	1	
(18) Christ. Popl	0.12	0.06	0.27	-0.17	0.28	0.65	-0.68	-0.16	0.01	1

Table 3 *The Results of the Univariate T- and Chi-squared test*

	Mean Values			Median Values		
Governance /Agency Cost Variables	Christian	Secular	*t*-value	Christian	Secular	χ^2-value
DM Nonprofit	0.67	0.64	0.836	1	1	0.14
DM Bank Regul.	0.19	0.30	-3.64***	0	0	2.14
Board Size	6.85	7.01	-0.7	7	6	7.0***
Intern. Directors	1.02	0.51	4.98***	0	0	6.87***
DM Female CEO	0.25	0.31	-1.78*	0	0	4.87**
Board Meet Year	8.1	7.3	-1.19	4	4	3.97**
DM CEO Bus Edu	0.58	0.67	-1.96**	1	1	0.54
DM External Audit	0.43	0.27	4.34***	0	0	1.81
DM Internal Audit	0.57	0.39	5.15***	1	0	0.29*
MFI Size	6.64 mil	4.94 mil	1.87*	2.23 mil	2.75 mil	1.83
Dm Intern. Initiate	0.61	0.35	8.3***	1	0	62.1***

Note: *, ** and *** indicate significance levels of 10%, 5% and 1%, respectively.

Table 4a *Differences in Board size, No. of Board Meetings and No. of International Directors*

Governance Variables	Board Size	No. of Board Meetings	No. of Intern. Directors
Christian MFIs	0.04	2.17*	0.32*
MFI Size (*ln assets*)	0.10**	0.2**	0.05**
MFI Age	-0.03*	-0.11***	-0.003
Dm Intern. Initiator	-0.3	-4.54***	0.98***
HDI	-1.04	4.61**	-0.24
% of Christian Popl.	-0.49	1.13	0.20
Regional Dummies	Yes	Yes	Yes
Model Stats			
N	1428	1008	1150
R^2	0.02	0.05	0.21
Wald X^2	11.08	39.39***	89.25***

Note: *, ** and *** indicate significance levels of 10%, 5% and 1%, respectively.

Table 4b *Differences in Probabilities for the Big Four External Auditors, Internal Auditor, Female CEO and CEO Business Education*

Governance Variables	The Big Four Ext. Auditors	Internal Auditor	CEO Business Education
Christian MFIs	3.05*	3.75***	-3.23
MFI Size (ln assets)	0.76	1.91***	1.25**
MFI Age	-0.19	-0.02	-0.11
Dm Intern Init.	-0.47	0.34	0.15
HDI	-0.84	-2.25	-21.07**
% of Christian Popl.	-4.98*	2.90***	2.68
Regional Dummies	Yes	Yes	Yes
Model Stats			
N	922	1384	648
Pseudo R^2	0.19	0.11	0.09
Wald X^2	12.79	275.71***	33.16***

Note: *, ** and *** indicate significance levels of 10%, 5% and 1%, respectively.

Table 4c *Differences in Probabilities for NGO or Coop ownership form, Bank Regulation and Female CEO*

Governance Variables	Ownership (NGO or Coop.)	Bank Regulation	Female CEO
Christian MFIs	0.34	-1.58*	1.90
MFI Size (ln assets)	-1.57***	1.92***	-0.42
MFI Age	0.19***	0.25***	-0.00
Dm Intern. Init	-0.67	2.26**	0.61
HDI	13.26***	-21.15***	1.85
% of Christian Popl.	-2.38*	-2.69*	5.12
Regional Dummies	Yes	Yes	Yes
Model Stats			
N	1548	1521	1389
Pseudo R^2	0.09	0.11	0.02
Wald X^2	46.62***	269.19***	33.37***

Note: *, ** and *** indicate significance levels of 10%, 5% and 1%, respectively.