Editorial

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One important development in the financial sector of emerging economies is the growth of microfinance institutions and instruments alongside formal commercial banks and non-bank institutions. There is growing research on the type of financial services provided in each of these, seemingly competing, financial institutions and markets. There is also heated debate on policy issues (such as regulation) and some unresolved research questions, such as the impact of the financial services on financial sector growth, savings, investment and general economic growth. In addition, there is increasing interest, by policy makers and practitioners, in management issues and practices, in both microfinance institutions and banks, especially where the two overlap. This special issue of the *International Journal of Financial Services Management* is devoted to these research questions, under the theme 'Microfinance and banking services in emerging economies'. Banks and banking services are the topics of the first four papers, while the microfinance industry is the topic of the next two papers. The special issue closes with a paper that addresses an over-arching topic of the determinants of foreign direct investment, in the context of finance and growth.

The major debate in the banking literature, and one which is particularly relevant to emerging economies, is the question of the contribution of banking sector development to economic growth. The study by King and Levine (1993), and more recently the survey by Levine (2005) and studies by Cole et al. (2008), Deidda and Fattouh (2008), Dell'Ariccia et al. (2008) and Romero-Ávila (2007) , among others, have shown that development of the financial sector, and in particular the banking sector, contributes to economic growth. The conclusions from these studies have important implications for governments and central banks. It is implied that measuring the efficiency of the banking system and understanding the factors that determine banking efficiency, are essential tasks, that should provide inputs for policy makers in their future policy formulation and in evaluating past reforms. In this context, the paper by Djoundourian and Raad reviews the Lebanese banking system, focusing on the reforms during the period 1993–2002. The paper uses a tested model by Battese and Coelli (1995) to evaluate the efficiency of the banking sector in post war Lebanon, and is closely related to a recent paper by Ben Naceur and Ghazouani (2007) on 11 Middle East and North Africa (MENA) region countries, including Lebanon, over the period 1979 to 2003. However, while the paper by Ben Naceur and Ghazouani (2007) finds that financial development has no – or even a negative – effect on economic growth, the present paper on the Lebanese banking sector, by Djoundourian and Raad, finds that bank efficiency improved during the period studied and the policy implemented by the government of encouraging bank consolidation probably contributed to this improvement.

Related to the debate on the contribution of the banking sector to economic growth is the issue of bank concentration and its impact on competition and efficiency, in the sector in particular, and on the local economy in general. The evidence in the literature is rather mixed. Beck et al. (2006) carry out a cross-country assessment of the impact of bank concentration on the fragility of the banking system and on the likelihood of banking crises. Controlling for bank regulation and institutional environment, it is found that bank crises are less likely to occur in more concentrated banking systems. Craig and Hardee (2007) examine the impact of consolidation in the banking industry on SMEs' access to credit and find that access is much less likely in markets dominated by large banks. Corvoisier and Gropp (2002) test the relationship between bank concentration, market power, and the pricing of products by banks; they find mixed results that depend on the product being offered. On the one hand, if banks operating in concentrated markets use their market power to extract rents, then the result would be the higher pricing of bank services. On the other hand, if concentration in the sector is the result of inefficient banks being taken over by efficient banks, then this should lead to increased efficiency and more competitive pricing of banking services. In this special issue, the paper by Malul and Shoham makes important contributions to the above papers, by investigating the determinants of concentration in the banking sector, and especially the impact of concentration on welfare - the latter being measured by interest rate spreads and by the number of branches per 1000 people. Interestingly, cultural variables are found to be important determinants of banking concentration.

The paper follows earlier work in which cultural influences on economic variables and financial decisions have been shown to be important. For example, Brown and Mitchell (2008) show that for the period 1994–2004, share prices on the Shanghai and Shenzhen stock exchanges were more likely to end in eight, than four. This preference was explained by the fact that in China the number eight is considered a lucky number, while four is considered unlucky. Likewise, de Jong (2002) shows that culture is important in determining inflation. In particular, it is found that inflation tends to be lower in countries where there is greater aversion to uncertainty and higher in countries that are characterised by the acceptance of inequality.

If cultural variables matter for bank performance, the question of foreign bank entry into domestic markets should be important. Murinde, Miroux and Lim examine the debate on foreign direct investment in the banking sector of developing countries. The key arguments in favour of and against foreign bank entry are isolated, with some concluding observations on what really matters in this debate.

Nevertheless, it may be argued that the above issues are driven by the degree of access to financial services. Banks are the principle providers of external finance to small and medium enterprises (SMEs), but at the same time SMEs often find it difficult to access this source of external funds, due to scale economies in lending and problems of information asymmetry (Choe, 2007). Indeed, constrained access to external finance by SMEs, which is driven by informational opacity problems, is an important issue for policy makers, and one that has attracted the attention of much academic work (see amongst others Beck and Demirgüç-Kunt, 2006; Berger and Udell 2006; Cull et al., 2006; Heffernan, 2006). In this special issue, the paper by Tagoe, Anuwa-Amarh and Nyarko examines the relationship between the information management practices of SMEs and their access to bank finance in Ghana. The paper is based on the idea that the ability to signal credibility can improve SMEs' access to bank finance, and that signalling can be achieved by good information management.

Arguably, some of the major players in financing SMEs are microfinance institutions (MFIs). The declaration by the United Nation of 2005 as the international year of microcredit, as well as awarding the 2006 Nobel Peace Prize to Professor Muhammad Yunus and Grameen Bank, have both directed public attention to the microfinance industry and to MFIs. This is the topic of two papers in this special issue: the paper by Manos and Yaron and the one by Hussain and Makame.

Manos and Yaron review methods by which the performance of MFIs was, is, and should be measured. The proper measurement of MFIs' performance is important for various reasons. Firstly, although most MFIs enjoy – at least in their early days – substantial flows of subsidies and donations, in the longer run most of them aspire to become financially viable in order to survive, grow and accomplish their socially-oriented goals. For example, in the American context, Pollinger et al. (2007) note that many MFIs reported difficulties in covering expenses without relying on grants and other subsidies, and that 30% of MFIs operating in 1996 were no longer in operation, or no longer extending loans after two years (see also Bhatt et al., 2002). Secondly, measurement of MFIs performance and sustainability is important for understanding the relationships between MFI performance and governance issues such as management compensation, board effectiveness and diversity (Hartarska, 2005). Thirdly, MFI performance measures are used by microfinance rating agencies. To the extent that such ratings help MFIs to raise funds (Hartarska and Nadolnyak, 2008), it is important that these institutions use good measures.

Hussain and Makame also look at the microfinance industry and in particular at the issue of mainstreaming microfinance. The paper presents a case study of the CRDB Bank, one of the big private commercial banks in Tanzania, and its involvement in wholesale lending to Savings and Credit Cooperative Societies (SACCOs). With the rapid growth and development of the microfinance industry, the range of providers of financial services to the poor has expanded. Nowadays, microfinance services are offered by specialised MFIs, as well as by public and cooperative institutions, and by commercial banks (Copestake, 2007). Does this mainstreaming of microfinance services shift the focus from reducing the poverty of recipients to increasing the profits of providers? Morduch (2000) discusses the potential trade-off between financial performance and the achievement of social goals. Hussain and Makame use a case study to show that the involvement of commercial banks in microfinance activities, and in particular the involvement of the CRDB bank in wholesale lending to the microfinance industry, can lead to a win-win situation: On the one hand, it allows commercial banks to profit from microfinance activities. On the other hand, it facilitates access by poor people to financial services from which they were previously excluded, and promotes good practice by operators in the industry.

Over-arching the issues discussed above is the matter of foreign direct investment (FDI) in the context of banks and economic growth. Given the intense competition for FDI inflows among emerging economies, understanding the determinants of these flows may be important if they contribute to economic growth. Tsai and Huang (2007) investigate the impact of FDI inflows to poverty alleviation in Taiwan, and find that inward FDI did not significantly increase the mean income of the poor. However, understanding the determinants of FDI inflows in order to develop strategies to attract FDI to less industrialised economies is imperative, in the light of the more favourable empirical evidence on the contribution of FDI inflows to productivity and economic growth (Borensztein et al., 1998; Calliano and Carpano 2000; Javorcik, 2004; Metwally, 2004). The paper by No, Muhammad, Tamwesigire and Mugisha examines the determinants of FDI inflows to Rwanda, including macroeconomic instability, market size, openness of the economy and foreign exchange. Market size, as measured by GDP, is found to be the most important determinant of FDI inflows, while inflation rates are shown to be insignificant in attracting FDI.

Hence, the special issue offers a good collection of research papers, which altogether offer new insights into microfinance and banking services in emerging economies. The papers also contribute to our knowledge by offering a variety of research methodologies and by drawing on the key problems in different economies. It is hoped that this special issue will not only inform practitioners and policy makers, but will also motivate further research on microfinance and banking services in emerging economies.

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