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- We document that these organizational features are common amongst MFIs
Experiment Overview

- Project Question: Are loan officers strategically withholding endorsements under baseline compensation scheme?
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- **Mitigation** - reduce/mitigate penalty of borrower graduation
  - Financial penalty of graduation phased in over six months

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**Objective** - lower the costs of endorsements to study if incentive structure was generating a meaningful problem
Experiment Design

No random variation in when loan officers receive compensation change.
All loan officers in the organization learn about the change in compensation at the same time in a surprise announcement.

Randomize when we elicit endorsements:
- Control: randomly selected half of loan officers are asked to provide endorsements a few days BEFORE announcement (under status quo scheme).
- Treatment: other half of loan officers are asked to provide endorsements a few days AFTER announcement (under new compensation scheme).

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  - Only endorsements received at Mitigation and Recognition predict repayment and business growth in GL
Quality of Endorsements

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  - For ML, we observe all borrowers for at least one loan cycle
Result 2 - Endorsements Only Valuable After Incentive Change

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- Default rate for borrowers endorsed after compensation change - 17%**
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  - Non-graduated borrowers endorsed in mitigation and recognition do not experience business growth
Compensation changes caused loan officers to furnish an additional 11% endorsements. Loan officers strategically withheld endorsements under baseline compensation scheme. Graduated borrowers endorsed after compensation change exhibited much better repayment and business growth than those endorsed at baseline. Loan officers strategically withheld endorsements of MOST QUALIFIED borrowers at baseline. These are the costliest borrowers for the ML loan officers to lose. Consistent with this, non-graduated borrowers endorsed after mitigation and recognition had better repayment in the ML portfolio.
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Institutional features that give rise to this misalignment of interests:

1. MFI has an internal graduation program
2. The standard microloan and graduation loan are managed by different loan officers
3. The microloan officer is paid based on size and quality of her portfolio
4. There is no bonus given to the microloan officer when her borrowers graduate

MIX market data - survey of 3100 MFIs across the world 2002 - 2017
- Half have a graduation program
- 80% of MFIs pay loan officers a via standard scheme
- No info on points 2. and 4.

Conducted interviews with 40 MFIs in Latin America and South Asia to collect information on points 1-4
- 65% of the MFIs have a graduation program
- Of MFIs with graduation programs, 31%-54% also satisfy points 2-4
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Endorsements furnished after the compensation shift are much more predictive of repayment and business growth in graduation loans.

⇒ Loan officers were withholding endorsements of MOST QUALIFIED borrowers under baseline compensation scheme.

After our study, Fondo Esperanza reorganized management structure to resolve misalignment between loan officers and borrowers.

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