Corporate Governance and Microfinance Institutions

WHAT WE DO

IFC works with microfinance institutions (MFIs) in countries where we operate, helping them strengthen their systems, structures, and relationships so they can set and meet objectives, manage risks and opportunities, and monitor performance. MFIs provide a range of financial services to micro and small enterprises, as well as to retail customers. Our guidance is tailored to ensure that governance structures are aligned with each MFI's specific activities and risk profiles.

MFI GOVERNANCE CHALLENGES

Certain aspects of governance represent common challenges for MFIs. Among these challenges:

- Managing the potential tension between commercial profitability and the social aims of the organization: Sometimes known as *mission drift*, this can occur when commercial considerations outweigh social impact aims.
- Determining ownership and shareholding structures and transforming into regulated financial institutions: There is often a lack of clarity, given that many MFIs evolve out of charities and non-governmental organizations.

Ensuring that governance practices keep pace with rate of growth: This includes professionalizing boards, finding and compensating qualified candidates, providing board training, and setting up the appropriate governance structures for the organization to manage the increased risks that come with growth.

THE BUSINESS CASE

As microfinance institutions have grown and professionalized over recent decades, their need for improved governance practices has increased. The growing challenges and risks facing MFIs—including changing market conditions, competition, and new technology—as well as the opportunities that come with such changes, spell a greater need for appropriate structures and systems to oversee and manage risk. A proactive, constructive board of directors, coupled with robust internal structures, is central to sound risk management and governance. Well-structured governance systems can help manage the tension generated by the MFI's double-bottom line of social impact and profitability. These systems are essential to addressing the complications that arise from non-standard shareholding structures.

BACKGROUND

Corporate governance is defined as the structures and processes by which companies are directed and controlled. Good corporate governance helps companies operate more efficiently, improve access to capital, mitigate risk, and safeguard against mismanagement. It makes companies more accountable and transparent to investors and gives them the tools to respond to stakeholder concerns. Corporate governance also contributes to development. Increased access to capital encourages new investments, boosts economic growth, and provides employment opportunities.

IFC CORPORATE GOVERNANCE GROUP

The Group brings together staff from investment and advisory operations into a single, global team. This unified team advises on all aspects of corporate governance and offers targeted client services in areas such as increasing board effectiveness, improving the control environment, and family business governance. The Group also supports corporate governance improvements and reforms in emerging markets and developing countries, while leveraging and integrating knowledge tools, expertise, and networks regionally and globally.

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IFC'S APPROACH

IFC has worked with numerous MFIs across six continents. Our engagements have ranged from training, reviews, and assessments to implementation support for comprehensive corporate governance improvement plans. This advisory support often complements our investment business activities in the MFI sector. Our efforts include support for MFIs that are in the process of transformation. With these organizations, we provide guidance on creating the appropriate governance structures. We also work with their boards to set a strategy that strikes the balance between profitability and social impact. Our advisory support is tailored to the needs of the MFI and the unique circumstances of the market, which vary significantly from country to country and region to region.

REGIONAL/COUNTRY EXAMPLE

KazMicroFinance lends to micro and small enterprises, including women entrepreneurs and customers in rural areas of Kazakhstan. When IFC conducted a corporate governance assessment in 2009, KMF's governance practices were not aligned with the successful growth the company was experiencing. It had no board of directors, no strategic guidance or management oversight, and weak internal controls and risk management.

Working with IFC, the company established a professional board with an independent audit committee, as well as a clearly defined risk management function and a separate independent audit department. These improvements have enabled KMF to grow sustainably with better risk management, including credit, operational and financial risk and strong client protection practices. Now the leading MFI in Kazakhstan, KMF has been successful in attracting significant debt and equity investment, as a result of these governance improvements.

RELATED RESOURCES:

Paper: Corporate Governance in Microfinance Institutions

Lessons Learned: Applying Corporate Governance to the DNA of a Transforming Microfinance Institution: Mission, Culture, and Risks Learned

Website: The Consultative Group to Assist the Poor (CGAP)

Website: Microfinance Gateway

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