Why do some MFIs transform from an NGO to a Bank?

“To reach significant scale and financial sustainability.”

The transformation of NGO MFIs into regulated institutions was a model that started to appear in the late 1980s. Transformation can take a number of forms:

- Microfinance NGO transformation to a bank – e.g. BancoSol in Bolivia, K-Rep in Kenya, BRAC in Bangladesh, OIBM in Malawi and OI-SASL in Ghana.
- Traditional, regulated financial institutions penetrating the microfinance market, including state-owned institutions – e.g. BRI in Indonesia.
- Creation of commercial MFIs – e.g. IPC and Opportunity partners in Eastern Europe.
- Merger between a commercial bank and an MFI, or merger between two or more MFIs – e.g. CONFIE in Nicaragua, BOM in Mozambique.

Of the 7,000 NGOs providing microfinance around the world, less than 100 have initiated transformation into privately owned, regulated MFIs. However, there is some evidence that most of these have achieved encouraging results.

Access to additional/commercial sources of funds

Some NGOs feel unable to meet the large and growing demand for micro-credit because their sources of funds are limited to donations, income from lending and subsidised loans. As banks, they can access other sources of capital more rapidly and increase leverage.

Wider range of financial services

As NGOs, most MFIs are only allowed to provide clients with credit. As a bank, they can provide a wider range of financial services, including savings. This expands their outreach by attracting a larger pool of clients.

From an industry perspective, transformation is encouraged for a number of reasons. Firstly, the involvement of private investors, with their own capital at risk, is said to enhance the internal control and governance of MFIs. Secondly, transformation can promote higher efficiency and financial performance – which can in turn significantly affect an MFI’s ability to meet its social goals. Finally, since regulation of financial institutions typically involves higher reporting requirements, it can improve financial transparency and accountability.

The concern that transformed MFIs may lead to mission drift has not become a reality in most cases. Instead, most transformed MFIs have been able to further their outreach – their scale and scope of operations – mainly because of greater access to resources. Moreover, most transformed institutions do not have a predominantly private ownership structure.

Note however that not every microfinance NGO needs to transform. There are large, efficiently run NGOs, such as ASA and BRAC in Bangladesh, that do not intend to become regulated financial institutions.

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