

**afi** Alliance for  
Financial Inclusion

## Innovative Policies for Financial Inclusion

### ADB's Microfinance Training of the Trainers Videoconference Session

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Bringing smart policies to life.

## **“Financial Crisis - Opportunities for Financial Inclusion”**

*Generating stronger, more stable economic growth for all  
through greater financial inclusion*

- Financial Inclusion: Historical perspective
- Current State of Financial Inclusion
- Impact of Financial Inclusion
- Overview on Financial Inclusion Policies
- Tradeoffs and Synergies?
- Future Research
- Recommendations

**Until the 1980s:** Loan subsidies and neglect of savings

**End of the 1980s:** Microfinance and institution-building: “financial system” paradigm

**Since 2000:** Expansion of links to the formal financial sector and growing interest of policymakers - the notion of Financial Inclusion

- **Financial Inclusion** aims at drawing the unreached population into the formal financial system so that they can have the opportunity to access a full range of financial services, from savings, payments, and transfers to credit and insurance.

# Current State of Financial Inclusion (1)



An estimated of 2.5 billion adult people – nearly half of the world’s adult population – do not have access to secure, formal financial services such as savings accounts and insurance

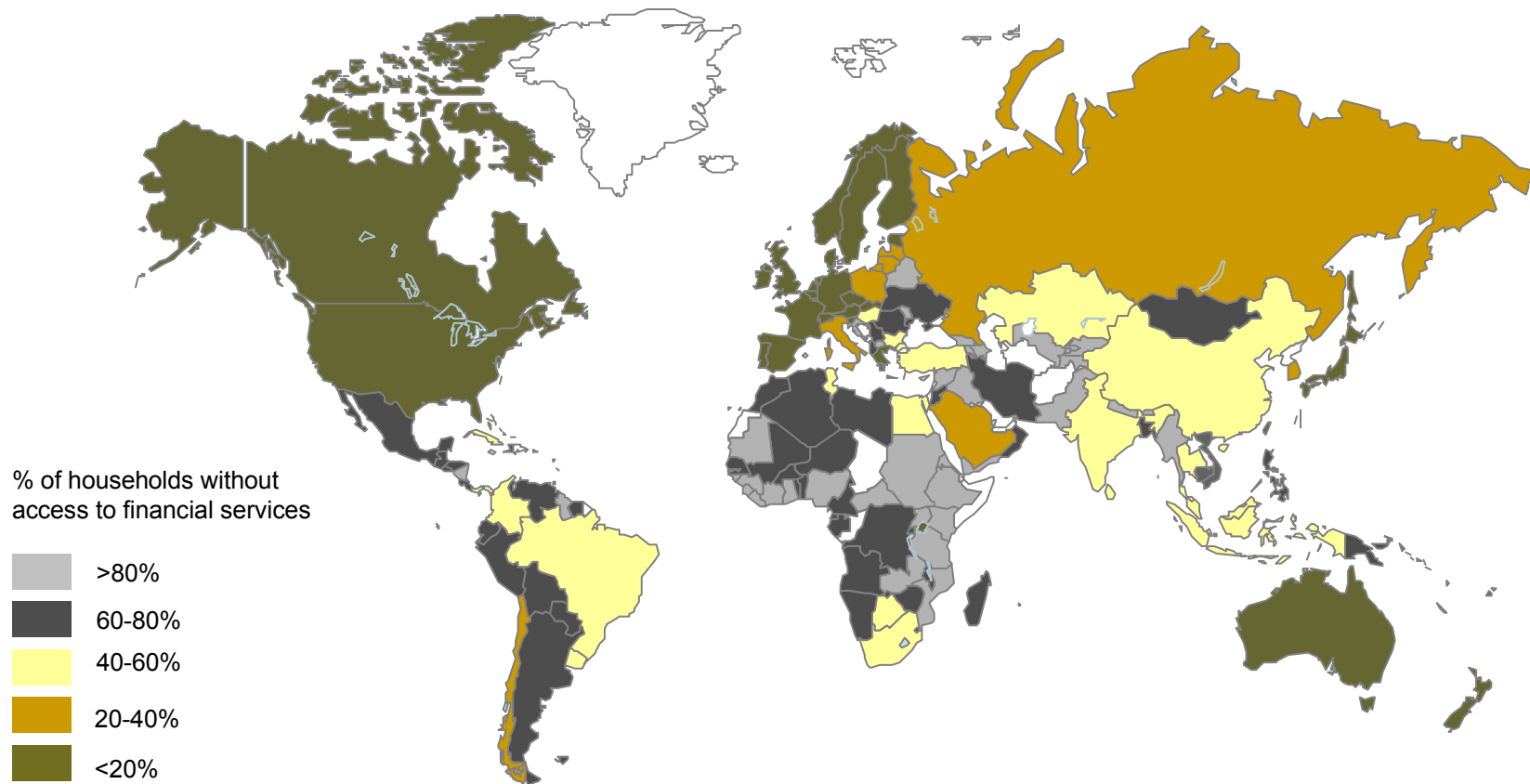
- About 95% of the unbanked are in developing countries

## Example:

- Spain has 96 branches per 100,000 people and 790 branches per 10,000 square kilometers
- Ethiopia has less than 1 branch per 100,000 people
- Botswana has 1 branch per 10,000 square kilometers

# The scale of the opportunity is huge

*About half of the world's population (~2.5 billion adults) is "unbanked"*

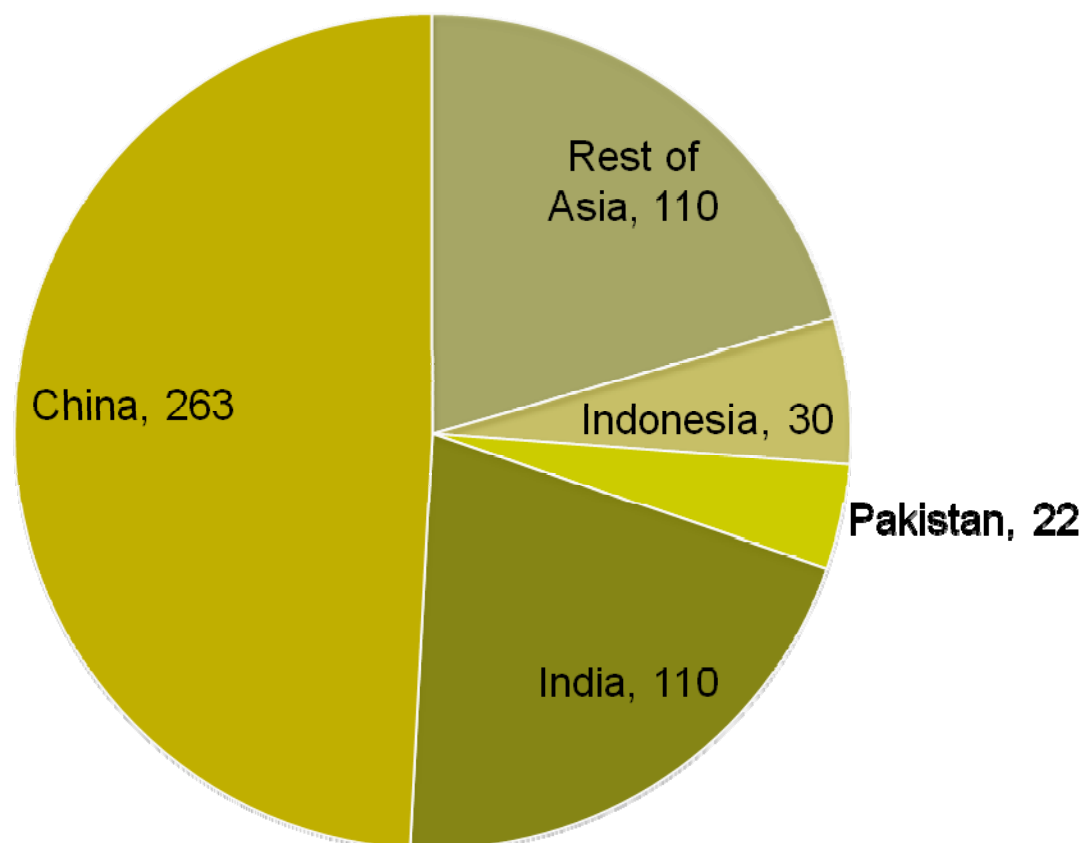


Source: World Bank Composite Measure of Access to Finance 2007, AFI visual modification.

## Current State of Financial Inclusion (2)

### Overview of Financial Exclusion in Asia:

535 million people in Asia remain financially excluded



Source: Boston Consulting Group ; various other sources ,

Compiled by Nimal Fernando in his presentation at the AFI Global Policy Forum 2009

## Current State of Financial Inclusion (3)



### Levels of Financial Inclusion in Asia, per country:

<b>Level of Financial Inclusion</b>	<b>Countries</b>
High (> 50 percent of adult population or households)	Thailand, Malaysia, Sri Lanka, Nepal, Mongolia
Intermediate (30-49%)	India, China, Indonesia, Bangladesh, Vietnam
Low (< 30 %)	Cambodia, Myanmar, Philippines, Papua New Guinea, Pakistan, Laos, Timor-Leste, Solomon Islands, Vanuatu, Samoa, Tuvalu, Kiribati

Table from Nimal Fernando's presentation at the AFI Global Policy Forum 2009

# Majority of Latin America is still financially excluded

Only 35% of households has access to financial services



Source (Map and Figure<sup>1</sup>): World Bank Composite Measure of Access to Finance 2007, AFI visual modification.

# Impact of Financial Inclusion (1)

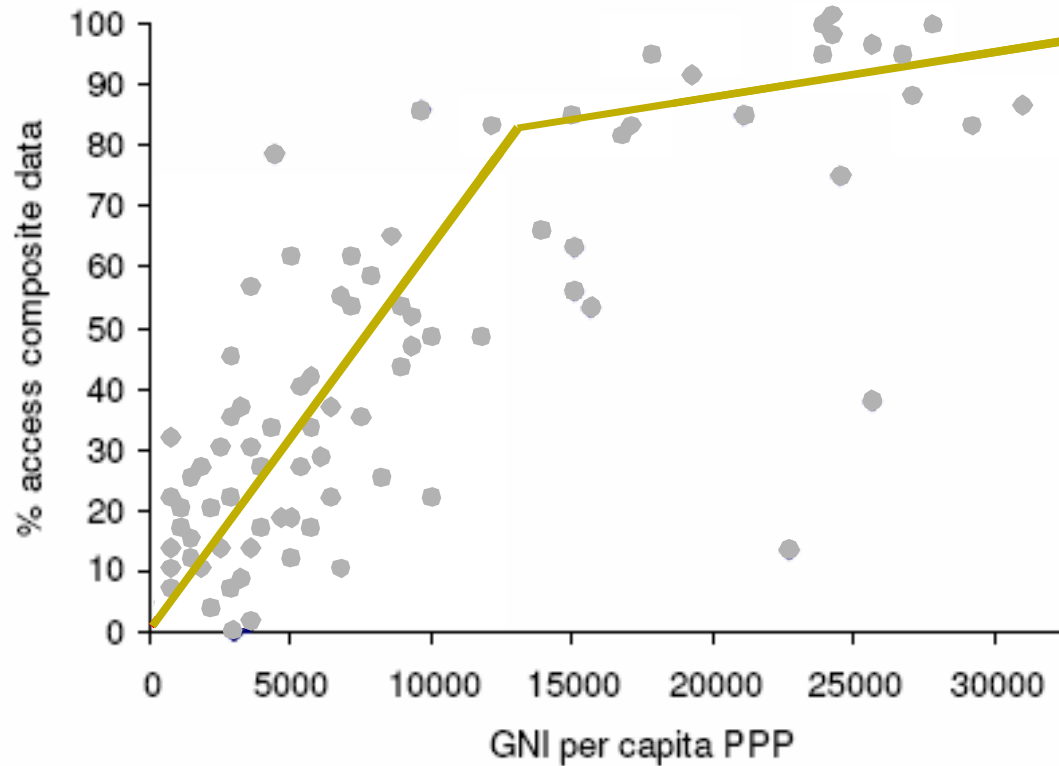
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## Macro-Evidence:

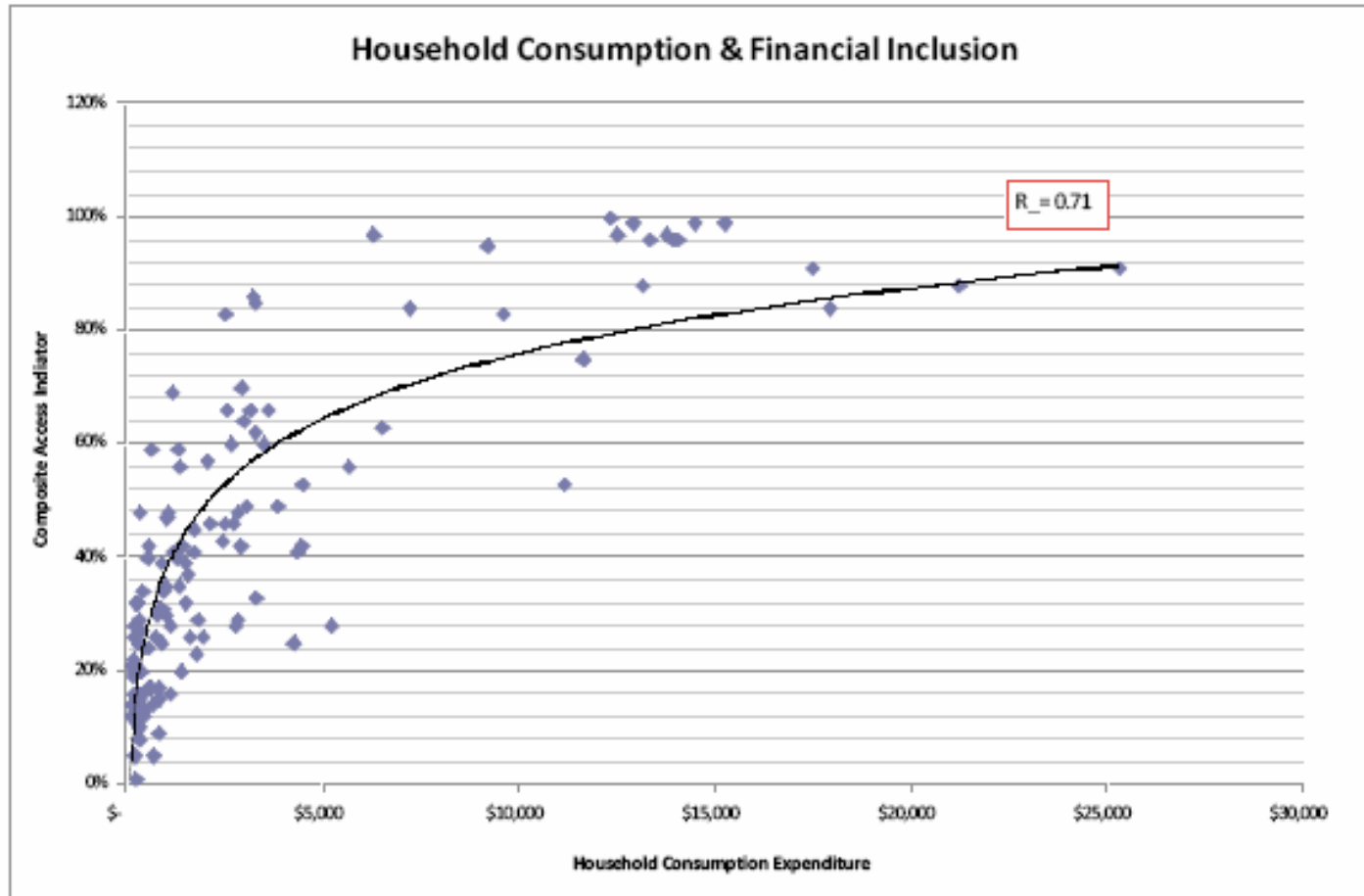
- Substantial evidence that financial development has a causal impact on growth (Levine, 2004)
- There is a link between financial development and reduced income inequality and poverty alleviation (Beck, Demirguc-Kunt, Levine 2007)
- Expansion of access enhances economic growth (Gine, Townsend 2004)

## Correlation of access and GNI per capita



Source:  
World Bank Composite Measure of Access to Finance 2007, AFI visual modification.

# Macro-Evidence



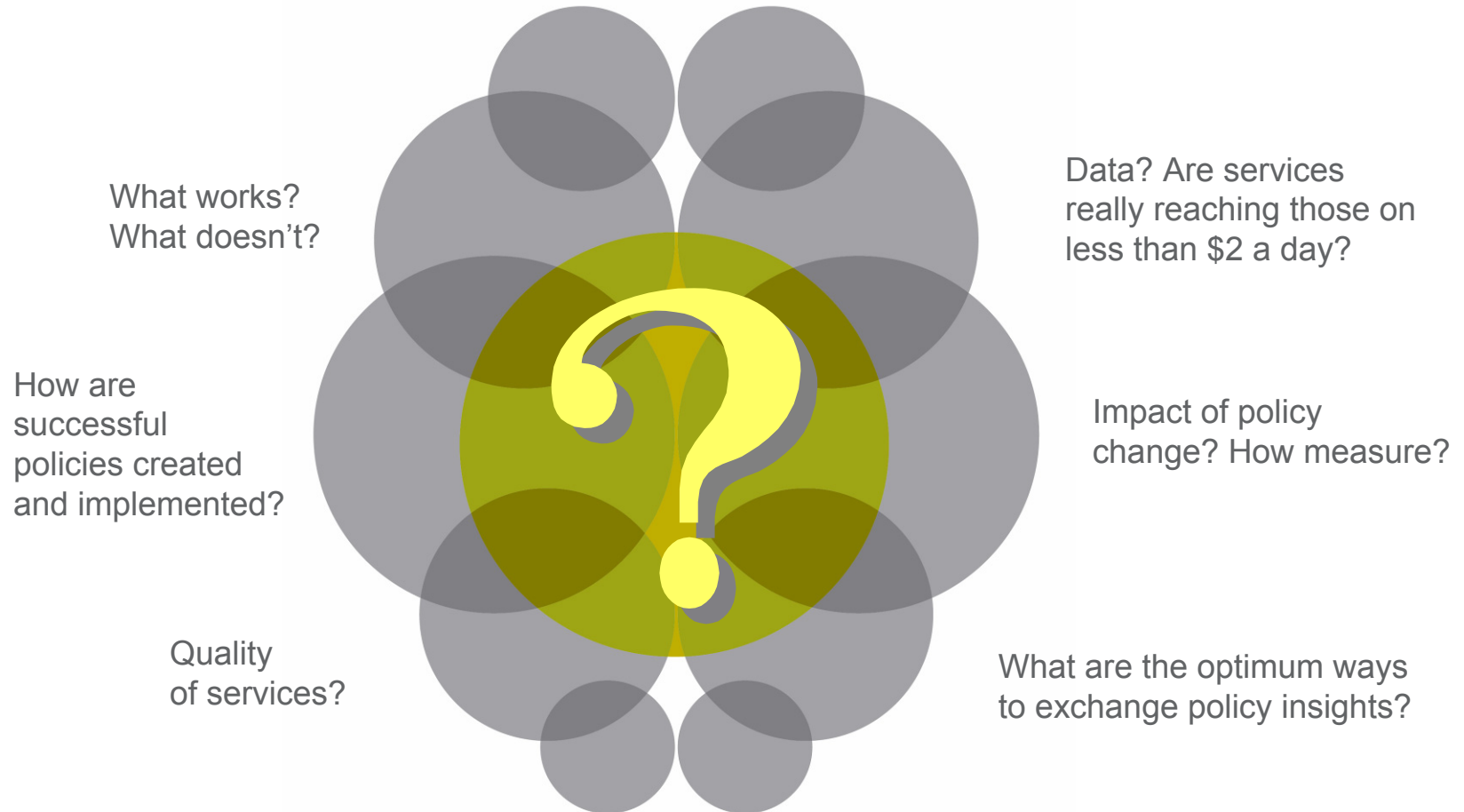
# Impact of Financial Inclusion (2)



## Micro-Evidence:

- Until recently: mostly based on plausibility and anecdotal evidence
- Financial Diaries: volatile cash flows of the poor => frequent usage of a range of financial services
- Randomized control trials: suggest positive effects of microfinance; however, yet too few to draw general conclusions
  - Kenya: access to savings increases female entrepreneurs' investments (Dupas, Robinson 2009)
  - South Africa: access to loans helps stabilize income (Karlan, Zinman 2008)

# Lack of evidence

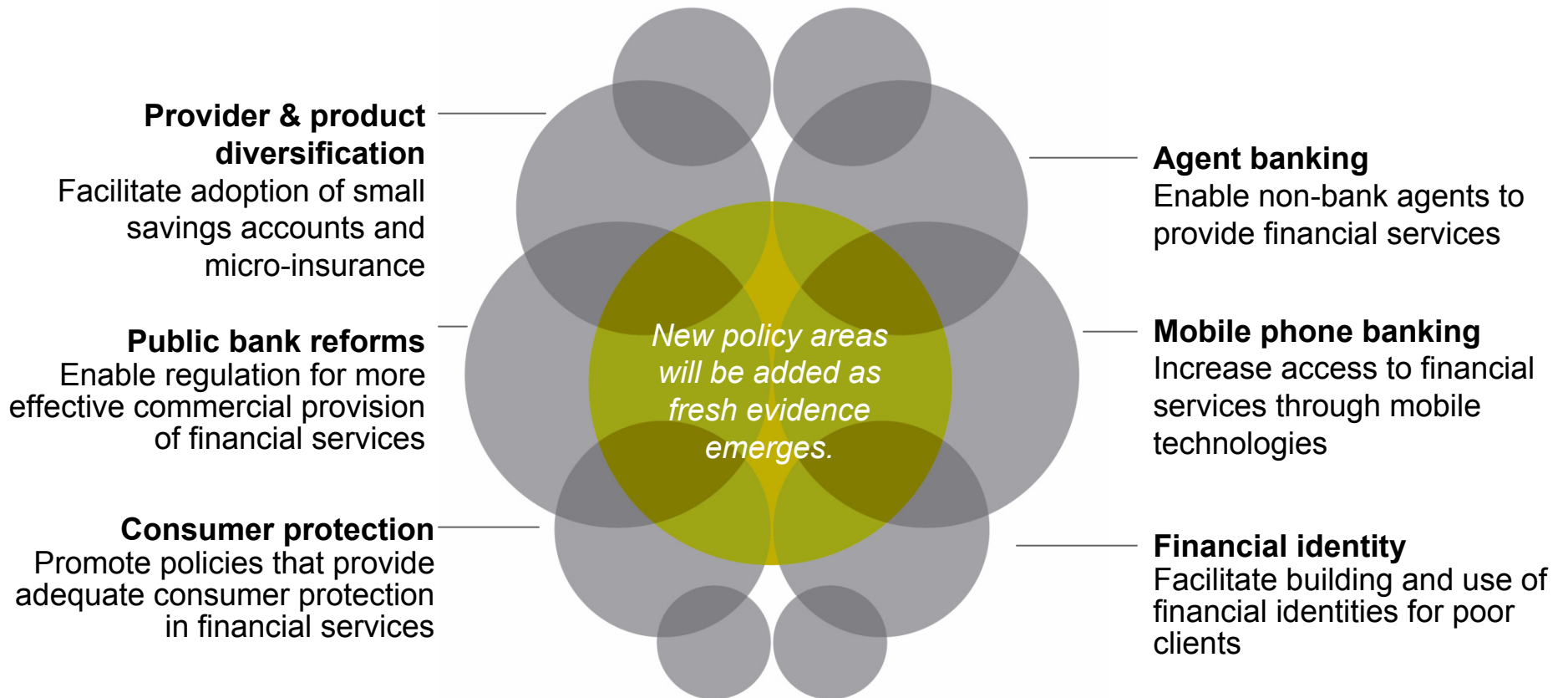


## Key lessons from the global study



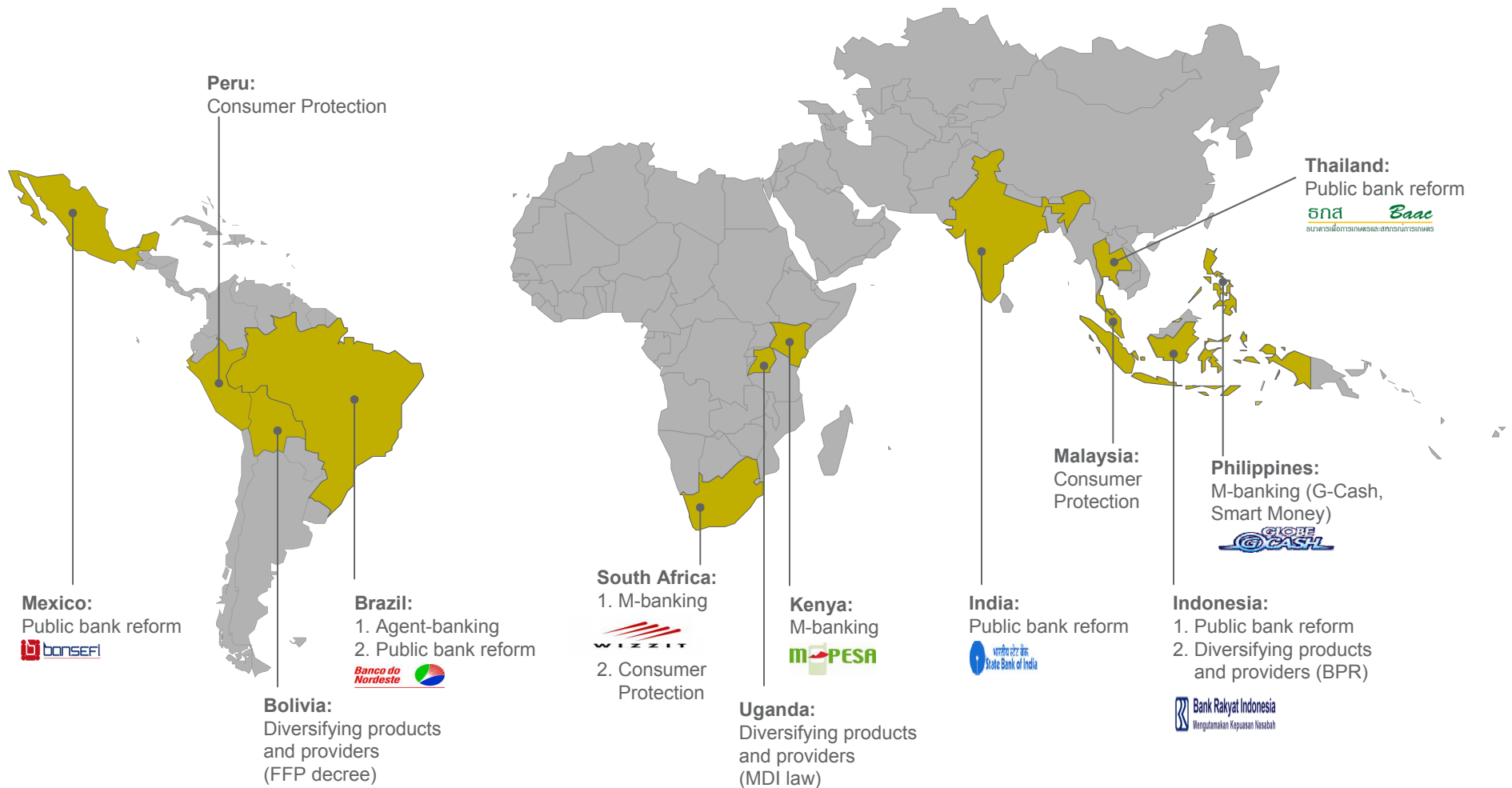
- Regulatory reform efforts in the successful countries benefited from substantial preceding improvements in the financial sector environment.
- Design a specific regulatory framework only if there is a critical mass of sustainable business: avoid “the rush to regulate” - regulation follows market!
- Don’t regulate what you cannot supervise
- The use of ICT can make a substantial contribution to financial inclusion
- Relaxing branching regulations for banks is a powerful and economical alternative to introducing microfinance regulations
- Formulate proportionate and balanced regulatory approach and ensure competition among providers
- Adopt a consultative approach

# Overview of Financial Inclusion Policies



# Where can we find these solutions?

*Developing countries have pioneered many of the most innovative solutions*



# Agent Banking

## In Brazil

- +100,000 retail outlets have been turned into agent banks since 1999
- All 5,600 municipalities now have access to banking services
- +50% of the poorest northern municipalities are served only by agent banks. Used for distribution of welfare payments
- Payments, transfers and deposits are made using real-time POS devices and bank cards
- Savings products have been less successful:
  - ✓ Under 5% of customers claim to make deposits
  - ✓ Less than a third of outlets offer cash-in, cash-out services - most operate as brokers for banks' credit and insurance products.

Brazil's agent network has reached 13 million extra unbanked in less than 10 years.



# Mobile Payments

## The M-PESA success story in Kenya

- Launched in 2007, it had over 7 million active users by 2009 (out of a total population of 40 million)
- Huge potential: only 23% of the population has a bank account, but 80% use a mobile phone
- ATM, bill payments, money transfer
- Preferred method of sending money (used by 47 %)
- Safe, simple, affordable
- USD 1.9 billion moved P2P so far (nearly USD 2 million a day)
- In 2006, 26% of adults in Kenya had access to formal financial services
- In 2009, the figure was 41%

Customers can cash-in cash-out at more than 12,000 agent outlets nationwide – nearly 10 times the number of bank branches in Kenya.



## Diversifying providers (tiered finance)

The poor need a range of financial products beyond credit, such as payments, savings, micro-insurance and remittances

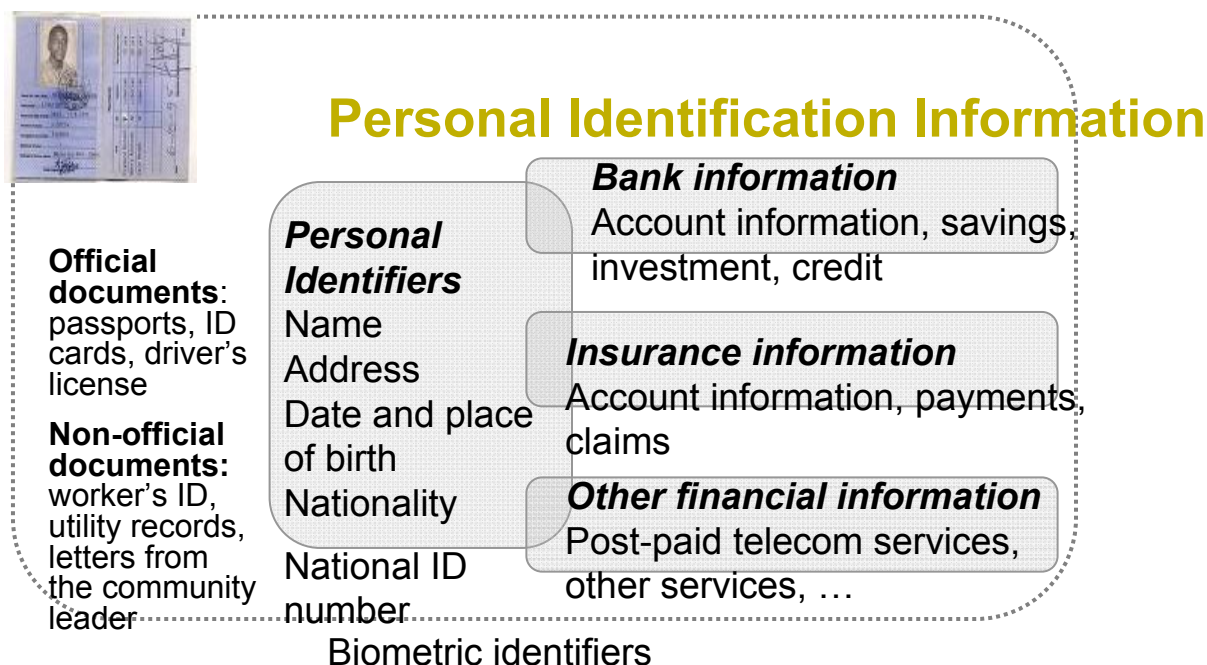


### Tiered Savings Regulation in Uganda

- Microfinance Deposit Taking Institution Act 2003 created a new tier of MDIs supervised by Bank of Uganda & allowed to take deposits
- The number of savers at licensed MDIs rose from below 100,000 in 2002 to around 250,000 in 2006
- Microfinance already on the agenda - the state took the lead to improve financial deepening without directly participating in market transactions

# Getting through the Door

## The Concept of Financial Identity



## Challenges

- Incomplete population registration & lack of national ID systems
- Insufficient data protection – risk of identity theft or misuse of information



**India:** Simplified KYC measures for low-risk customers to open “no-frill” accounts



**Philippines:** Greater variety of IDs accepted



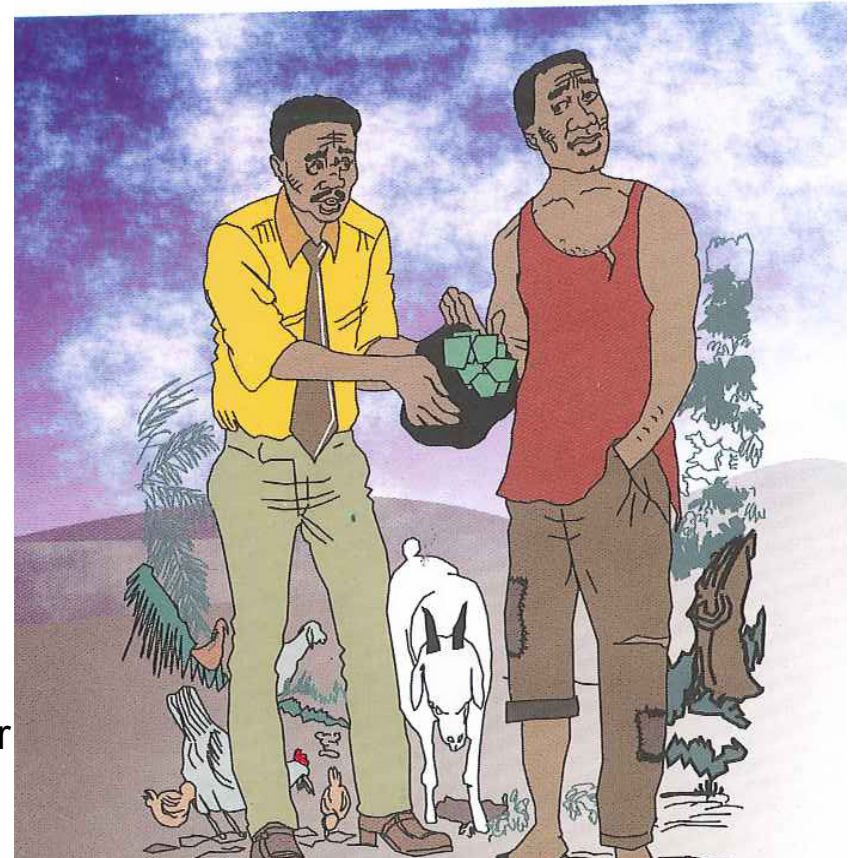
**South Africa:** Simplified address verification using informal networks

# The Weak Link in Financial Inclusion

## Enhancing Consumer Protection

- 4 pillars: Disclosure, Redress, Education, Privacy
- 150 million new users of financial services a year, many with low financial literacy
- Information asymmetry between banks & customers makes customers vulnerable
- Regulators should work with both consumers and industry to supervise market conduct
- “Carrot-and-stick” approach: Self-regulation by banks can help but enforcement is also necessary to ensure transparency
- South Africa has complaint-driven enforcement, with ombudspersons and call centers to manage consumer complaints
- Peru & Malaysia offer credit counseling to the over-indebted and have central credit reference systems that capture outstanding credit card balances

*Do Not Take A Loan If You Do Not Need One.*



- Consumer education can help people protect themselves from unscrupulous lenders

# A Healthier State of Affairs

## State bank reform in Indonesia

- Bank Rakyat Indonesia (BRI) remodeled itself from a loss-making state bank to the world's largest & most profitable microfinance network
- Restructuring began in 1983 as interest rates were liberalized and subsidies withdrawn
- Self-sustainability through savings mobilization & profitable operations
- 16,000 staff trained and provided with performance incentives & technology
- In 2008, net income leapt by 23% to around \$600 million, largely driven by microfinance
- Today, BRI has 21 millions savers, compared to 3.5 million borrowers – an 8 to 1 ratio!
- “SIMPEDES” savings product pays interest and offers customers unlimited withdrawals

Each of BRI's 4,800 'Unit Desa' (village banks) was turned into a profit center, offering rural communities microcredit and savings products.



## Overall, balance between financial stability and financial inclusion can be achieved

- None of the recent policy reforms has failed
- Policy reforms are formally not compliant with FATF guidelines, however, alternative mechanisms to ensure minimum compliance with AML/CFT approaches to client identification and verification have been adopted
- Policy reforms are in line with standard policy principles
- EIU Microscope ranking of microfinance environments: Philippines, Bolivia, Kenya and Uganda rank among the top ten out of 55 countries assessed.

# Tradeoffs between Financial Inclusion and Stability?



## Risk Profile: Many new users, but very limited volume

- New instruments and institutions pose risks, but these are hardly systemic in nature
- Regulation and supervision is well developed for traditional services, but technology-based solutions require attention
- Regulators: concerned with consumer protection & reputational risks
- Past crises have often bypassed the lower end of financial markets
- Access to savings is critical to help the poor cope with crises, and to make small financial institutions independent from other debt sources

# Questions for Future Research



- **Systematic diagnostic efforts** to identify ‘binding constraints’ to financial access will help policymakers set strategic priorities for action.
- **Randomized controlled trials** (RCT) should be incorporated more effectively into regulatory decision-making and be systematically used to obtain insights into the appropriate sequencing of reforms.
- **Updated information** on levels and trends of financial inclusion is a critical step towards evidence-based policy decisions. Data collection must be tailored to objectives and available resources. Policymakers should expand collaboration with researchers to build capacity to collect demand side data.
- **Risk analysis** of the scaling-up of technology-based financial inclusion policies with respect to financial stability is necessary to fill critical knowledge gaps due to rapid recent innovation.

- **Careful analysis of the risks posed by transactions of the poor**
  - Brings informal savings into the system
  - Diversifies funding base
- **Leverage successful innovations among developing countries**
  - Home-grown capital to fund investment
- **Shift from credit to savings – benefits:**
  - Enhanced household capacity to manage crisis impact
  - Diversified funding base to cushion credit crunch
  - Enhanced economic resilience (growth, poverty reduction)
- **Link social protection policies and financial inclusion**
  - **Special issues to consider: consumer protection for poor people**

***Thank you!***

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