Move over, microfinance

Financial inclusion is now seen as the way forward in improving the lot of the world’s very poor, writes Sam Mendelson

More than two billion people in the world lack access to formal financial services. This, of course, is largely because they lack the funds to make them attractive customers for financial services firms. Nearly 70 per cent of people in sub-Saharan Africa and about 66 per cent of people in south Asia, for example, live on less than $2 a day, according to World Bank figures.

Given the tiny sums that so many subsist on, it could be argued that there is a chicken and egg problem when it comes to financial access for the poor. It is one of the reasons why microfinance was long seen as the way to help. Microfinance, however, has lost some of its lustre. Now, financial inclusion is seen as the way forward.

The inaugural Financial Inclusion 2020 (FI2020) Global Forum was held in London in October, organised primarily by the Center for Financial Inclusion (CFI), which is part of Accion. (Accion made its first microloan in 1973.) The aim is to achieve full financial inclusion by 2020, with an end to extreme poverty by 2030.

According to the CFI, financial inclusion is “a state in which all people who can use them have access to a suite of quality financial services, provided at affordable prices, in a convenient manner, and with dignity for the clients. Financial services are delivered by a range of providers, most of them private, to a financially capable clientele.”

This is clearly an ambitious project both in terms of aim and timescale. Nor is it just about being “good”. Access to quality credit, savings, insurance and payments services can, it is assumed, not only help the individual better manage their life but also help build a stable financial system and drive economic participation and growth.

Providing services, however, is not enough, as the CFI stresses. It references research by Eldar Shafir, who is the William Stewart Tod professor of psychology and public affairs at Princeton University, and Sendhil Mullainathan, professor of economics at Harvard, that shows how scarcity of resources takes its own psychological toll on the poor, making it harder for them to make long-term decisions.

The very poor tend to focus on dealing with the next crisis (“tunnelling”), on borrowing for the very short term, whatever the cost. They often find that their decision-making powers are undermined by high levels of stress.

One of the aims of financial inclusion is to help ease this psychological burden. Whereas microfinance, which was long considered the panacea for bringing financial services to the poor, offers particular products to a sub-set, financial inclusion wants to enable everybody, whatever their needs and background. Financial inclusion is also intended to be pragmatic with regard to what users are offered and what they do. “No-hassle” emergency loans, for example, could be part of the wider plan.

Clearly, attaining full financial inclusion will not be easy. The Forum highlighted the need to educate potential customers, support private sector innovation and help regulators be flexible with regard to new ideas – while still protecting consumers, many of whom may not know their rights or have the confidence to insist on them.

The problems are partly geographic. According to the CFI, the majority of the financially excluded live in just six countries: Brazil, China, India, Indonesia, Nigeria and Pakistan. Others in the top 10 are Bangladesh, Mexico, the Philippines and Vietnam.

There are also stumbling blocks of gender and culture. Men and women can have very different roles within a family and community; they may have a different focus on what is most important financially, as well as different access to resources.

Still, there are bright spots. Technology is expected to be a great enabler of providing low-cost, secure and diverse financial services to those on a low income. “In an increasingly interconnected world,” said Michael Corbat, CEO of Citi, “rapid advances in technology and communications mean that solutions like mobile banking and electronic payments are unlocking access to financial services”.

There are also promising shifts in demographics and income. “Hundreds of millions of people who, until recently, subsisted on less than $2 a day are moving into an income bracket of between $4 and $10-12,” according to Beth Rhyne, CFI’s managing director.

The target year of 2020 may not be far away – but it could be that financial inclusion is also closer than we think.

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