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TOWARD UNIVERSAL ACCESS

Addressing the Global Challenge
of Financial Inclusion



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Toward Universal Access

Addressing the Global Challenge
of Financial Inclusion

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Toward Universal Access: Addressing the Global Challenge of Financial Inclusion*

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Introduction and High-Level Recommendations

This chapter highlights key trends, challenges, and opportunities for advancing financial inclusion and proposes major high-level policy recommendations for consideration by the Group of 20 (G-20) policy makers to benefit a wider range of developing countries, including many non-G-20 countries. As such, the chapter serves a broad audience, ranging from policy makers, development finance institutions, and the private sector to experts seeking a synopsis of the key subtopics relevant for financial inclusion and areas of work for advancing progress. The chapter is organized into four sections. The first recommends broad goals and agenda items to accelerate progress in financial inclusion. The second defines the financial inclusion concept and its importance for economic growth and poverty reduction. The third section provides a snapshot of

* This content of this booklet is derived from chapter 10 of *Postcrisis Growth and Development: A Development Agenda for the G-20*, a product of the staff of the International Bank for Reconstruction and Development/The World Bank. This chapter was prepared by a World Bank Group team coordinated by the Access to Finance Advisory of the International Finance Corporation (IFC). Asli Demirgüç-Kunt (World Bank) and Margaret Miller (CGAP) provided technical inputs to the chapter.

each of the pillars proposed as part of the recommendations, and the fourth section summarizes the way forward.

The chapter also contains an annex that takes a closer look at the microfinance industry as a case in point for reviewing the successes, innovations, and lessons learned, which are critical for the broader discussion on financial inclusion.

The Challenge in Brief

Financial inclusion encompasses the range, quality, and availability of financial services to the underserved and the financially excluded. Some 2.7 billion adults—almost 70 percent of the population in developing countries—have no access to formal financial services (table 1). It is important that efforts to improve financial inclusion focus not only on the financially excluded but also on the *underserved* population and firms in developing countries.

The working poor (living on less than US\$2 a day), who make up over 60 percent of the total labor force in developing countries, represent a key target market segment for expanding financial inclusion (figure 1). In addition, because small and medium enterprises (SMEs) are overall one of the largest employers of the working poor, the SME market is a big opportunity for expanding the financial access frontier.

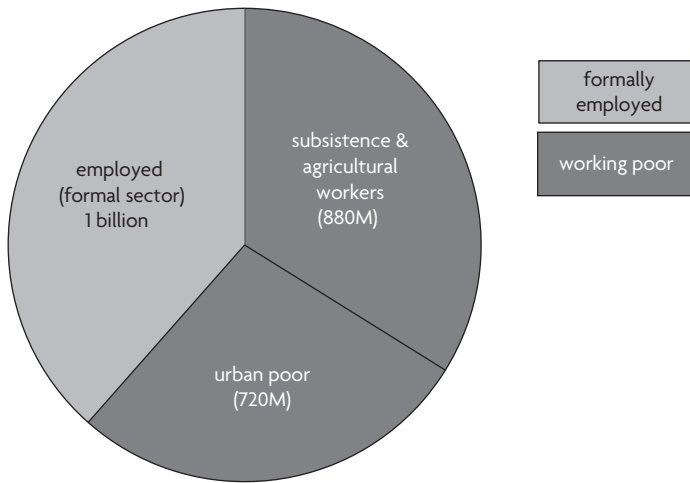
To advance the financial inclusion agenda at the global level, it is important and timely to build on the G-20 commitment, made in Pittsburgh in September 2009, to improve access to financial services for the poor. To advance that goal, the G-20 leaders established the Financial Inclusion Experts Group (FIEG), with two subgroups—one to focus on

Table 1. Current Measurement of the Unbanked

WBG Financial Access ^a	2009 Report	70% or 2.7 billion of the adult population
McKinsey/FAI (Chaia and others)	October 2009 paper	2.5 billion of the adult population
Research: Demirgüç-Kunt, Beck, and Honohan	2007/2008	70% of the population

Source: World Bank Group Team compilation. Note that as of July 2010, the International Monetary Fund launched a new online database on financial access with access indicators per country.

Note: a. Collects and releases data on an annual basis.

Figure 1. Labor Force in Developing Countries

Source: World Bank Group Team Analysis, based on World Development Indicators, and analysis for the Bill and Melinda Gates Foundation.

Note: The total labor force in developing countries numbers 2.6 billion; the total developing countries population is 5.6 billion. Working poor are defined as living on less than US\$2 a day.

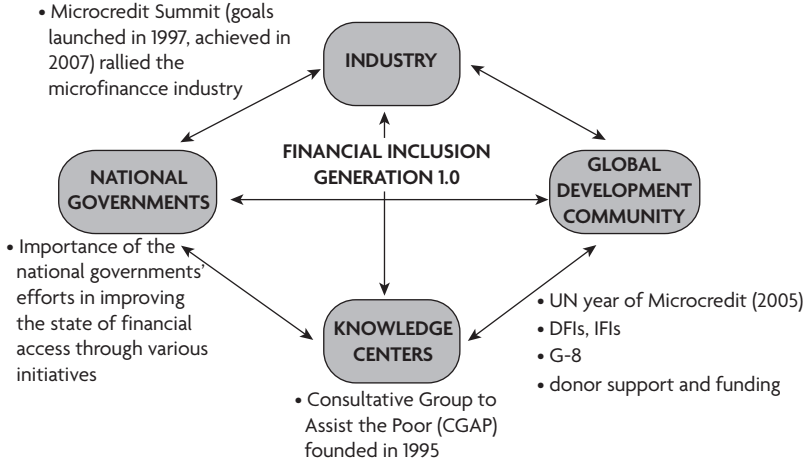
innovative modes of delivering financial services to the poor and the other to focus on improving financial access for SMEs. The work of the subgroups is under way.

Collaborative Model and Implementation Pillars

The successful global efforts in advancing financial inclusion to date indicate a need for collaborative action from multiple stakeholders and channels. The targets and efforts to be charted for the “next generation” of financial inclusion have much to leverage and learn from previous collaborative actions. Figure 2 shows the key stakeholders that were needed to kick-start the movement toward financial inclusion. The key is to align the main incentives and high-level goals among the stakeholders. Past trends indicate that four major types of players are needed: the industry; the global development community; knowledge centers (CGAP), and national governments.¹

Global targets to date and collaborative efforts tied to them involved credit-focused goals. The original goal of the Microcredit Summit when

Figure 2. Collaborative Diamond Model for Financial Inclusion: Generation 1.0 (1990s–2010)



Source: World Bank Group Team Analysis. Diamond model inspired by Michael Porter's "Diamond Model of Competitiveness" used for the diagnosis and recommendations around the competitiveness of nations and industry clusters.

it was launched in 1997 was to reach 100 million of the world's poorest families (with a focus on women) with credit for self-employment and other financial and business services by 2005.

To address the global challenge of financial inclusion, a high-level global target is needed. While striving to fully eliminate the financial inclusion gap is challenging, the time has come to advance and align financial inclusion efforts in order to make a visible and meaningful contribution toward reducing that gap. The global target can be established either through a bottom-up approach (aggregating established or projected country-level targets) or a top-down approach (setting a global high-level target, with the projection that individual country efforts will meaningfully contribute to reaching the target over time), or a combination of the two. For example, if a global target is set to reach 1 billion financially excluded individuals and 50 million SMEs by 2020, this target would be validated with the bottom-up process to ensure that individual countries' projected targets do not fall short of the global goal. One key factor differentiating a global target from earlier targets is that the number to be reached would include those excluded from a range of financial

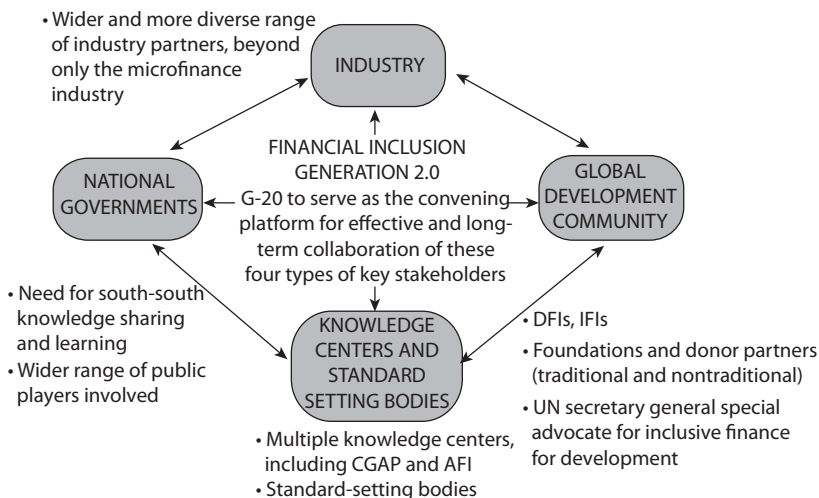
products and services including payments, remittances, savings, and insurance, and not just from credit.

Efforts around this future global target will need to include not only the same four types of stakeholders as the earlier effort but also a broader and more diverse range of players. Figure 3 outlines the preliminary collaborative model needed for the next round of financial inclusion to take off.

Key working pillars need to focus on six themes: the policy environment; financial infrastructure; delivery mechanisms and products; responsible finance/consumer focus; data and measurement; and building upon the work of the FIEG subgroups. Figure 4 outlines the preliminary G-20 agenda items for each of the pillars; a snapshot for each of the pillars is discussed later.²

Expanding the reach of financial access holds significant promise for enhancing the livelihood and well-being of the poor and the growth of small and medium enterprises. Concerted efforts and resource commitments will be needed to effectively implement this agenda and integrate it into the broader assistance work across the international development community. A systematic approach with dedicated resources

Figure 3. Collaborative Diamond Model for Financial Inclusion: Generation 2.0 (2010–2020s)



Source: World Bank Group Team Analysis. Diamond model inspired by Michael Porter's "Diamond Model of Competitiveness."

Figure 4. Reaching the Financial Inclusion Target: Key Pillars

POLICY ENVIRONMENT	<ul style="list-style-type: none">• support national policies for universal access to critical financial services, including G2P• adapt the regulatory environment to support branchless banking• strengthen competition for greater affordability of financial services• support systematic peer-to-peer learning and sharing of financial inclusion policy lessons
FINANCIAL INFRASTRUCTURE	<ul style="list-style-type: none">• develop and promote good business models for retail payments for the underserved• work toward G-8 5x5 goal for remittances• scale up inclusive credit reporting systems, including microfinance credit reporting
DELIVERY MECHANISMS AND PRODUCTS	<ul style="list-style-type: none">• increase the use of mobile banking, agent networks, smart cards• expand insurance for the poor (microinsurance), long-term and short-term savings• strengthen SME finance via innovation, infrastructure, funds• focus on rural, low-access areas• expand financial inclusion for women clients
RESPONSIBLE FINANCE/ CONSUMER FOCUS	<ul style="list-style-type: none">• convene financial services providers to operationalize responsible finance practices• strengthen responsible finance/consumer protection at the country level (via diagnostics, advisory services) and global standards• develop evidence base on financial capability through research, pilots
DATA & MEASUREMENT	<ul style="list-style-type: none">• continue and expand supply side data collections (include SME finance and insurance)• set up global clearing house for institutional level data on access for microfinance and SMEs• improve data on financial usage to inform policy making (demand side)
FIEG SUB-GROUPS	<ul style="list-style-type: none">• SME finance• access through innovation

Source: World Bank Group Team Analysis.

would assist governments in setting an appropriate regulatory and policy framework, help build effective financial infrastructure, and work with financial service providers to enhance product diversification and reach as well as to build financial capability. Developing financial products that meet the needs of the financially excluded in a timely, cost-effective, and responsible manner will require new and innovative approaches.

Financial Inclusion: Defining the Challenge

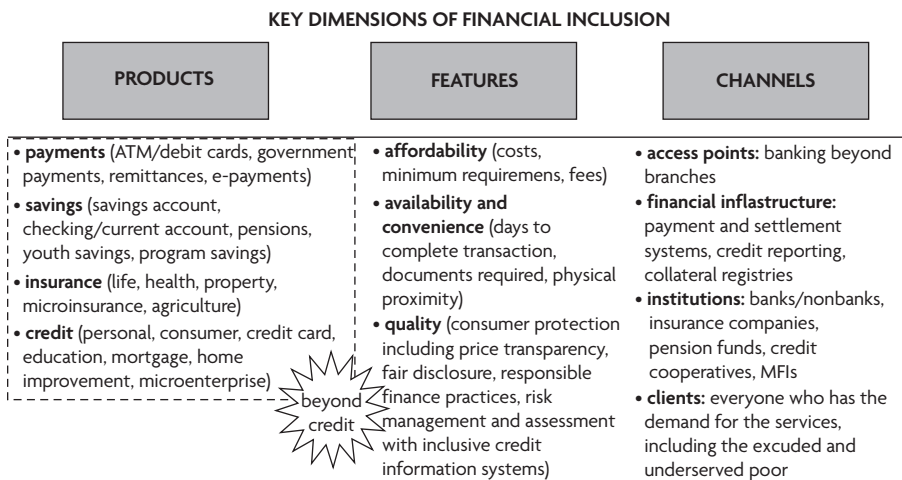
Counting the Unbanked

Financial inclusion encompasses the range, quality, and availability of financial services to the underserved and the financially excluded. While there is a growing consensus on the importance of financial inclusion, the

same consensus does not exist around its definition. Financial inclusion can be defined as a “state in which all people of working age have access to a full suite of quality financial services, provided at affordable prices, in a convenient manner, and with dignity for the clients” (Accion International 2009a). These products and services can be offered cost effectively by a range of financial service providers. Financial inclusion implies that both *unbanked* and *underbanked* households and firms are part of the target market. Figure 5 displays the key dimensions that define financial inclusion, with a particular focus placed on the range of products and delivery channels that go beyond the early microcredit-only approach. It is challenging to strike the right balance between availability, affordability, and sustainability.

Diversified products beyond microcredit, such as remittances, microinsurance, savings accounts, and other financial instruments, are needed to expand financial access. In *Portfolios of the Poor*, Collins and others (2009) show that all 250 of the very poor slum residents they study have some form of debt and savings and all use a minimum of four types of financial instruments (formal and informal) throughout the year. Poor households are continuously shifting between a variety of formal, semiformal, and

Figure 5. Defining Financial Inclusion



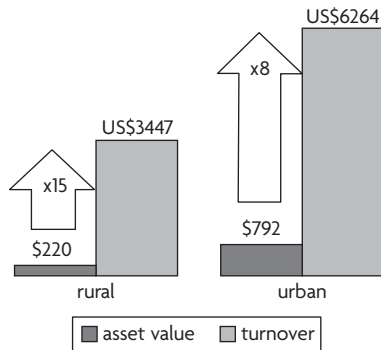
Source: World Bank Group Team Analysis.

informal financial products based on availability, product features, pricing, and other nonprice barriers. The study also demonstrates households’ high turnover in financial instruments over assets and a higher turnover for rural areas (figure 6). The study defines “turnover” as the total sum of money being “pushed” (deposited, lent, or repaid) into instruments plus the money being “pulled” (withdrawn, borrowed, or received) from them.

How many people are financially excluded? Almost 70 percent of the adult population in developing countries, or 2.7 billion people, lack access to basic financial services, such as savings or checking accounts (World Bank Group 2009).³ The regions with the largest share of unbanked populations are Sub-Saharan Africa, where only 12 percent are banked, and South Asia, with 24 percent banked (map 1).

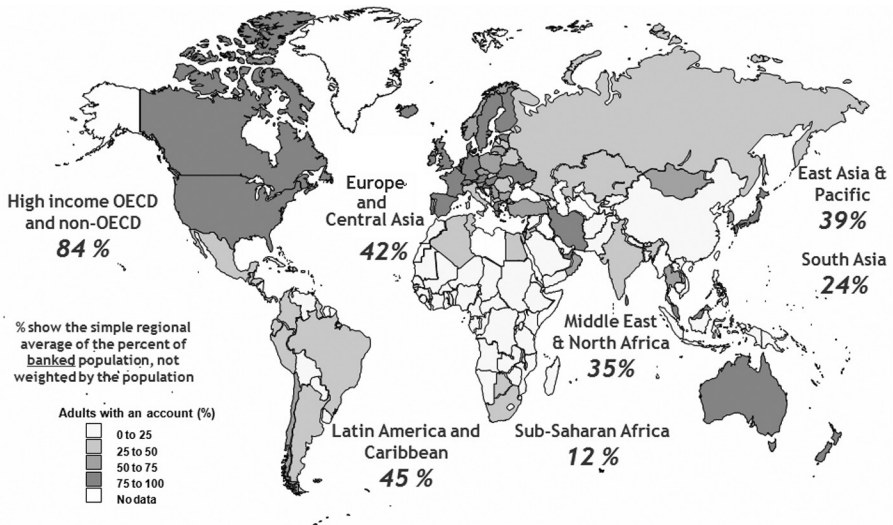
The availability of financial access points varies greatly depending on the level of financial sector development in the country. Developing countries have 3 times fewer branches and automated teller machines (per 100,000 adults) and as many as 12 times fewer point-of sale terminals compared with developed markets (figure 7). For example, regional averages for Africa and South Asia are well below 10 branches per 100,000 adults compared with more than 25 in high-income countries.⁴ When comparing the number of cashless retail payment transactions per capita, the gap is even wider, with developed countries transacting 25 times more a year than developing countries.

Figure 6. High Turnover in Financial Instruments: Rural and Urban



Source: Collins and others 2009.

Note: Year-end asset values and annual cash flow through financial instruments (formal and informal), for the median household in South Africa.

Map 1. Global Map of the Financially Included

Source: For data and methodology, see World Bank Group 2009 and the accompanying methodology paper (Kendall, Mylenko, and Ponce 2010).

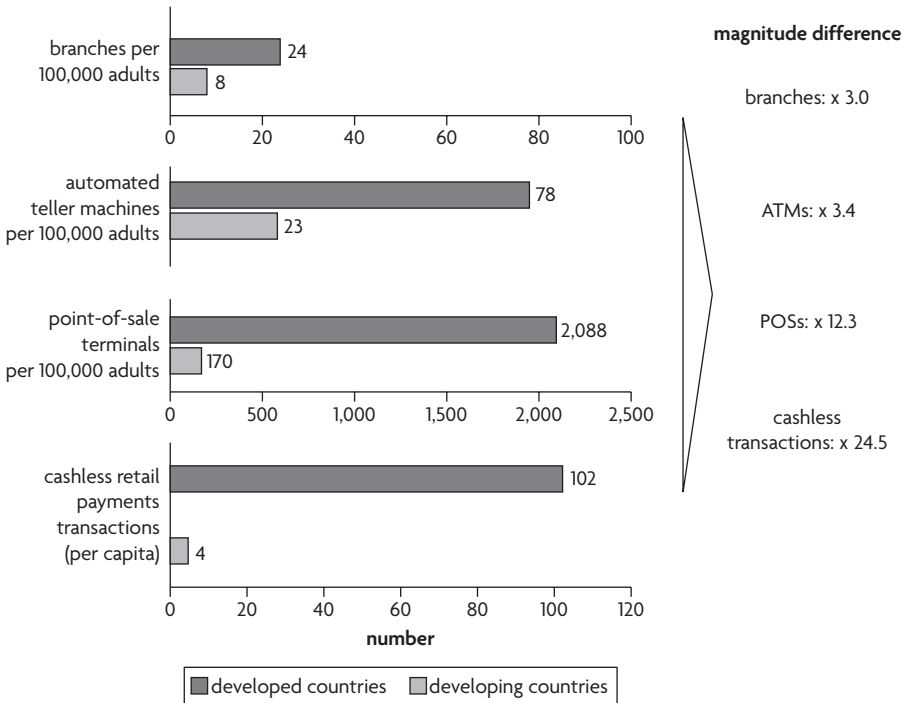
Note: Map shows percentage of adults with a deposit account in regulated financial institutions including banks, cooperatives, specialized state financial institutions, and microfinance institutions. Regional averages show the simple average of country averages of adults banked (not weighted by population), based on the data provided in World Bank Group (2009). Not all countries in each region are included in the average calculation because not all provided survey data.

The drive toward full financial access and full-scale banking applies not only to individuals but also to the underserved SME segment. The need for SMEs to access financial services goes well beyond access to lending. Treasury and cash management, savings, insurance, and transactional products are critical for SMEs to ensure optimal financial management and risk mitigation, and these products also provide private sector financial institutions with increased incentives to focus on the SME segment. The World Bank Enterprise Surveys and Investment Climate Surveys consistently show that SMEs are 30 percent more likely than large firms to rate financing constraints as a major obstacle to growth. The smaller the firm, the higher this percentage is.⁵

Financial Inclusion: Benefits and Constraints

Empirical evidence suggests that improved access to finance is not only pro-growth but also pro-poor, reducing income inequality and poverty

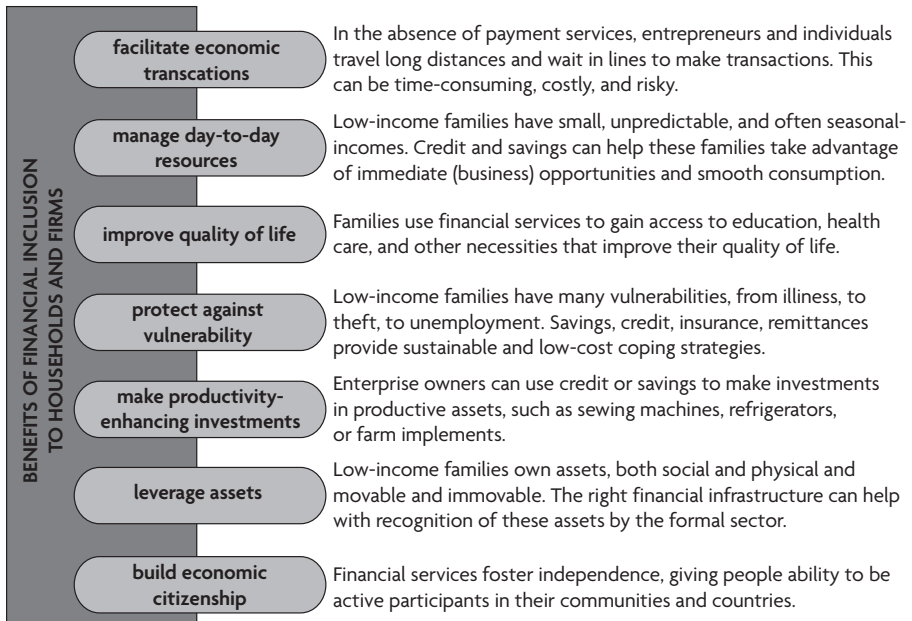
Figure 7. Access and Payment Transactions Gaps



Source: World Bank Group 2009 and World Bank Payment Systems Survey 2008.

(Beck, Demirgüç-Kunt, and Honohan 2008, 2009). Cross-country regressions have shown that economies with better-developed financial systems experience faster drops in income inequality and faster reductions in poverty levels. Financial depth can have direct and indirect effects on small firms and poor households (Beck, Demirgüç-Kunt, and Honohan 2008).⁶ Greater depth is likely to be associated with greater access for both firms and households, making them better able to take advantage of investment opportunities, smooth their consumption, and insure themselves. The numerous benefits of financial inclusion for low-income households and small and microenterprises are summarized in figure 8.⁷

Why are so many people financially excluded when the benefits of financial inclusion are so well recognized? Surveys of financial institu-

Figure 8. Seven Benefits of Financial Inclusion

Source: Adapted from Accion International 2009b.

tions around the world show that the constraints to financial inclusion fall into three categories (Demirgüç-Kunt 2010):

- *Geography or physical access.* While technology—phone and Internet use—has the potential to alleviate this constraint, physical distance still matters.
- *Lack of proper documentation.* Financial institutions require one or more documents for identification purposes, but many people in low-income countries who live in rural areas and work in the informal sector lack such papers.
- *High prices, minimum account requirements, and fees.* Many institutions have minimum account requirements and fees that make even opening a simple account out of reach for many potential users. A study on barriers to financial access and use around the world based on surveys from 193 banks in 58 countries highlights interesting country differentials focused on barriers to financial access. For exam-

ple, the minimum deposit requirement to open a checking account in Cameroon is over US\$700, an amount higher than the GDP per capita of that country, while no minimum amount is required in South Africa or Swaziland (Beck, Demirgüç-Kunt, and Martinez Peria 2008).

Global Mandates

Advancing the financial inclusion agenda can help boost progress toward the achievement of the Millennium Development Goals (MDGs), in particular toward poverty reduction, health, education, and gender equality (Beck, Demirgüç-Kunt, and Levine 2004; Claessens and Feijen 2006; Littlefield, Morduch, and Hashemi 2003) (figure 9).

Financial inclusion as a goal in itself is rapidly emerging as a major focus on global and national platforms. The financial inclusion concept has gained increased attention since the United Nations designated 2005 as the International Year of Microcredit and adopted the goal of building inclusive financial systems. In 2009, Princess Máxima of the Netherlands, was appointed the UN secretary-general's special advocate for inclusive finance for development.

In September 2009 G-20 leaders in Pittsburgh pledged to “commit to improving access to financial services for the poor.” The leaders launched the creation of a Financial Inclusion Experts Group tasked with supporting innovative modes of financial service delivery capable of reaching the poor and scaling up models of small and medium enterprise financing. Two subgroups were formed to lead these two tasks. One, on Access through Innovation, supported by CGAP and the Alliance for Financial Inclusion (AFI) and cochaired by Brazil and Australia, is focusing on

Figure 9. Access to Finance and Millennium Development Goals



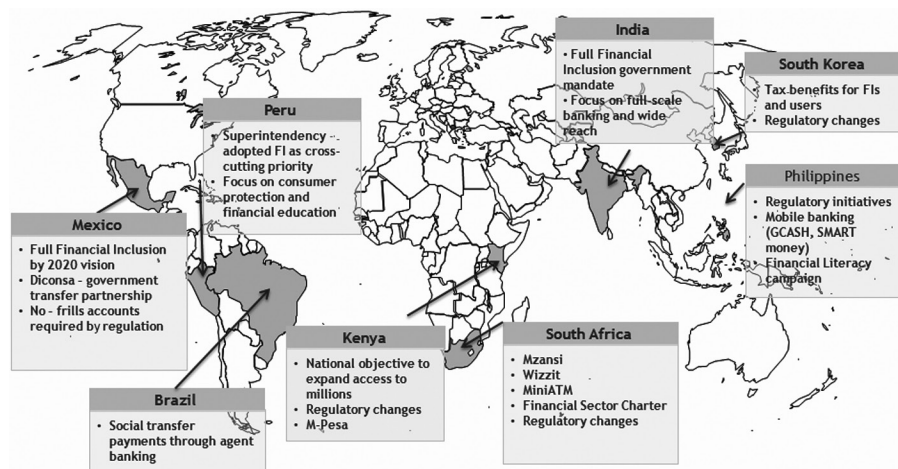
inclusive finance is an important driver for attaining the MDGs, as finance:

- reduces vulnerability to shocks, thus mitigating the risk of falling into poverty
- leads to higher income per capita facilitating achievement of many of the MDGs
- creates reducing inequalities and broadening opportunities, contributing to gender equality

Source: Claessens and Feijen 2006; MDG icons from <http://www.undp.org/mdg/>.

analysis of recent experience and lessons learned with branchless banking and similar innovations in financial service delivery to the poor and on the development of principles for innovative financial inclusion. The nine “Principles for Innovative Financial Inclusion” were announced and endorsed at the G-20 Summit in Toronto in June 2010. The other, on SME finance, is supported by the International Finance Corporation (IFC) and cochaired by Germany and South Africa. Its objective is to identify and promote successful models for public financing to maximize the deployment of private sector resources on a sustainable and scalable basis. The subgroup is working toward this objective by conducting a stocktaking exercise and launching an SME finance challenge. The SME Finance Challenge—“a call to the private sector to put forward its best proposals for how public finance can maximize the deployment of private finance on a sustainable and scalable basis”—was launched at the G-20 Toronto Summit. Final deliverables for both subgroups, including the winners of the SME Finance Challenge, will be announced at the G-20 Seoul Summit.

On the national level, governments are becoming increasingly more proactive, and some are incorporating financial inclusion and the drive to universal access into their national mandate (map 2). For example, India has mandated financial inclusion as a national goal, and the Reserve Bank of India has intensified a number of measures and endorsed quantitative access targets over the last year to further financial inclusion (Subbarao 2009). The government of Mexico is welcoming and supporting ongoing financial inclusion programs and analytical work to advance the goal of full financial inclusion by 2020 (Accion International 2009b). South Africa has mobilized the public and private sectors to design products and interventions that serve as entry-level points for delivering formal financial services to a larger percentage of the unbanked, such as Mzansi accounts with no monthly fee and no minimum balance (Bankable Frontier Associates and Fin-Mark Trust 2009). Moreover, the United Nations committee on building inclusive financial sectors, set up in 2006, urged central banks and governments to add the goal of universal financial inclusion to the two traditional goals of prudential regulation of depositors’ funds and the stability of the financial system (United Nations 2006). There is growing appetite for peer-to-peer learning and for internalizing lessons and

Map 2. Recent Examples of Countries Advancing Full Financial

Source: World Bank Group Team Analysis and AFI.

Note: Map represents selected examples only, not an exhaustive or best practice list of countries with financial inclusion initiatives.

Note that example for the Republic of Korea dates back to the credit card lending boom in 1999–2002 (Kang and Ma 2009).

policy and product solutions from countries championing financial inclusion to those countries that are beginning to address the challenges of financial inclusion.

Financial Inclusion Pillars

Policy Environment

Addressing Market Failures. Financial markets and institutions exist to overcome the effects of information asymmetries and transaction costs that prevent the direct pooling and investment of society's savings.⁸ They mobilize savings and provide payments services that facilitate the exchange of goods and services. In addition, they produce and process information about investors and investment projects to guide the allocation of funds; monitor and govern investments; and help diversify, transform, and manage risk. When they work well, they provide opportunities for all market participants to take advantage of the best investments by channeling funds to their most productive uses, hence boosting growth, improving income distribution, and reducing poverty. When they do not

work well, growth opportunities are missed, inequalities persist, and in extreme cases, there can be costly crises.

Since expanding access remains an important challenge even in developed economies, it is not enough to say that the market will provide. Market failures related to information gaps, the need for coordination on collective action, and concentrations of power mean that governments everywhere have an important role to play in building inclusive financial systems (Beck and de la Torre 2007). However, not all government action is equally effective and some policies can even be counterproductive. Direct government interventions to support access require a careful evaluation, something that is often missing.

Enabling Policy Actions. Even the most efficient financial system, supported by a strong contractual and information infrastructure, faces limitations. Not all would-be borrowers are creditworthy, and there are numerous examples of national welfares that have been damaged by overly relaxed credit policies. Access to formal payment and savings services can approach universality as economies develop, although not everyone will or should qualify for credit. For example the subprime crisis in the United States graphically illustrates the consequences of encouraging low-income households to borrow beyond their ability to repay.

An underlying, albeit often long-term, goal is deep institutional reform that ensures the security of property rights against expropriation by the state. Prioritizing some institutional reforms over others, however, would help focus reform efforts and produce impact in the short to medium term. Recent evidence suggests that in low-income countries it is the information infrastructures that matter most, whereas in high-income countries enforcement of creditor rights is more important. Cross-country variation in financial depth can be explained in low-income countries by the existence of credit information systems but not by the efficiency in contract enforcement; in high-income countries it is just the reverse (Djankov, McLeish, and Shleifer 2007). As noted in the financial infrastructure section of this chapter, credit information systems are key to fostering inclusive financial systems.

But even within the contractual framework, there are certain shortcuts to long-term institution building. In relatively underdeveloped institutional environments, procedures that enable individual lenders to

recover on debt contracts (for example, those related to collateral) are more important in boosting bank lending than those procedures mainly concerned with resolving conflicts between multiple claimants, such as bankruptcy codes (Haselmann, Pistor, and Vig 2006). Given that it is potentially easier to build credit registries and reform procedures related to collateral than to make lasting improvements in the enforcement of creditor rights and bankruptcy codes, these are important findings for prioritizing reform efforts. Introducing expedited mechanisms for loan recovery can be helpful, as shown by the example of India, where a new mechanism bypassing dysfunctional court procedures increased loan recoveries and reduced interest rates for borrowers.

Results can be produced relatively fast by encouraging improvements in specific infrastructures (particularly in information and debt recovery) and the launch of financial market activities that can allow technology to bring down transaction costs. Some examples of these market activities are establishing credit registries or issuing individual identification numbers to establish credit histories; reducing costs of registering or repossessing collateral; and introducing specific legislation to underpin modern financial technology, from leasing and factoring to electronic and mobile finance. These activities can produce results relatively fast, as the success of m-finance in many Sub-Saharan African countries has shown, most recently M-Pesa in Kenya (Porteous 2006 and box 3).

Encouraging openness and competition is also an essential part of broadening access, because they both encourage incumbent institutions to seek out profitable ways of providing services to the previously excluded segments of the population and increase the speed with which access-improving new technologies are adopted. Foreign banks can play an important role in fostering competition and expanding access.

In this process, providing the private sector with the right incentives is key, hence the importance of good prudential regulations. Competition that helps foster access can also result in reckless or improper expansion if not accompanied by a proper regulatory and supervisory framework. As increasingly complex international financial regulations—such as Basel II on minimum standards for capital adequacy (BIS 2010)—are imposed on banks to help minimize the risk of costly bank failures, it is important to ensure that these arrangements do not inad-

vertently penalize small borrowers by failing to make full allowance for the risk-pooling potential of a portfolio of SME loans. Research suggests that banks making small loans have to set aside larger provisions against the higher expected loan losses from small loans and therefore need to charge higher rates of interest to cover these provisions.

A variety of other regulatory measures is needed to support wider access. But some policies that are still widely used do not work. For example interest ceilings often fail to provide adequate consumer protection against abusive lending, because banks replace interest with fees and other charges. Increased formalization of transparency and enforcement of lender responsibility offer a more coherent approach, along with support for the overindebted. However, delivering all of this can be administratively demanding.

The scope for direct government interventions in improving access is more limited than often believed. A large body of evidence suggests that interventions to provide credit through government-owned financial institutions have generally not been successful. One of the reasons is that lending decisions are based on the political cycle rather than on socio-economic fundamentals, as both cross-country evidence and a carefully executed case study for India show.

In nonlending services, the experience of government-owned banks has been more mixed. A handful of governmental financial institutions has moved away from credit and evolved into providers of more complex financial services, entering into public-private partnerships to help overcome coordination failures, first-mover disincentives, and obstacles to risk sharing and distribution (de la Torre, Gozzi, and Schmukler 2006). A good success example is Mexico, where government-owned banks had a useful catalytic function in kick-starting certain financial services (box 1). Ultimately, these successful initiatives could have been undertaken by private capital, but the state played a useful role in jump-starting these services. Direct intervention through taxes and subsidies can be effective in certain circumstances, but experience suggests that this intervention is more likely to have significant unintended consequences in finance compared with other sectors. In addition, how best to use postal financial services and develop these large networks for expanding access to financial services is an important question for policy makers to consider.

Box 1. Mexico: An Example of Development Banks Kick-Starting Financial Services

Three government-owned banks in Mexico were important in getting certain inclusive financial services up and running.

NAFIN (Nacional Financiera). Electronic brokerage of reverse factoring, developed by NAFIN, a government development bank, allows many small suppliers to use their receivables from large creditworthy buyers to obtain working capital financing.

BANSEFI (Banco del Ahorro Nacional y Servicios Financieros). Another example is the electronic platform implemented by BANSEFI, another government-owned institution, to help semiformal and informal financial intermediaries reduce their operating costs by centralizing back-office operations.

FIRA (Fideicomisos Instituidos en relacion con la Agricultura). A government-owned development-finance-institute-turned-investment-bank, FIRA, has brokered quite complicated structured financial products to realign credit risks with the pattern of information between financial intermediaries and the different participants in the supply chains for several industries, including shrimp and other agrifish products.

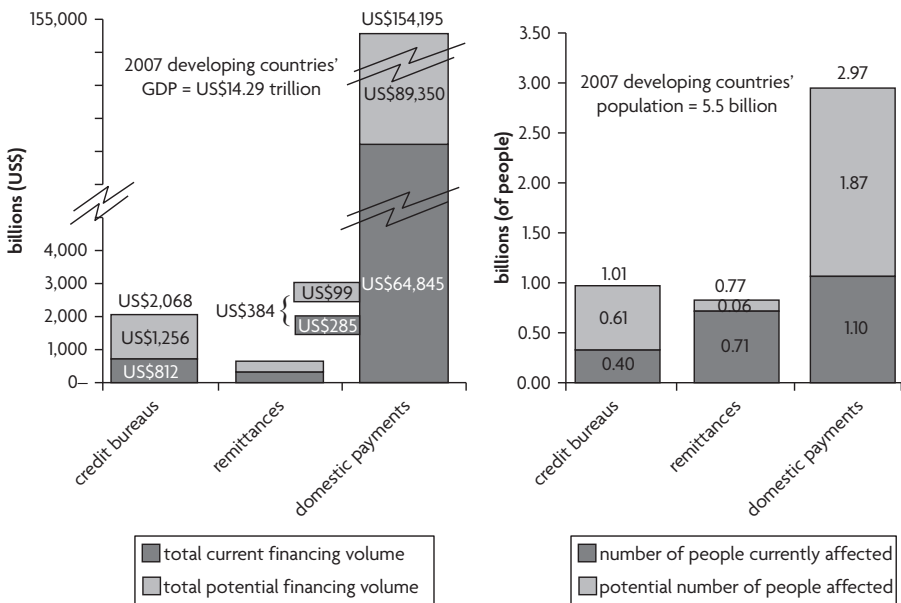
Source: Beck, Demirgüç-Kunt, and Honohan 2008.

With direct and directed lending programs discredited in recent years, partial credit guarantees have become the direct intervention mechanism of choice for SME credit activists. Some seem to be functioning well, breaking even financially thanks to the incentive structure built into the contract between the guarantor and the intermediary banks. For example, the Chilean scheme has the intermediary banks bidding for the percentage rate of guarantee, and the premium charged can be adjusted on the basis of each intermediary's claims record. This approach has resulted not only in higher lending by beneficiaries but in a reduction of loan losses (Cowan, Drexler, and Yañez 2008). Other partial credit guarantees have been poorly structured, however, embodying sizable hidden subsidies and benefiting mainly those who do not need the subsidy. The temptation for an activist government to underprice guarantees (especially for long-term loans when the underpricing will not be detected for years) does present fiscal hazards similar to those that have undermined so many development banks in the past. In the absence of thorough economic evaluations of most schemes, their net effect in cost-benefit terms remains unclear (Honohan 2008).

Financial Infrastructure

Financial infrastructure has the potential to expand access to finance significantly.⁹ Key elements of financial infrastructure such as credit information systems; enforcement of collateral; and functioning payment, remittance, and securities settlement systems are vital to facilitating greater access to finance, improving transparency and governance, and safeguarding financial stability.¹⁰ Recent estimates demonstrate the high impact of financial infrastructure on the current and potential financing volume and reach (figure 10). Current estimates show that 390 million people in developing countries are covered by credit bureaus, over 700 million are affected by remittances, and over 1 billion by payment systems. Future growth, based on expected growth of financial infrastructure where it does not currently exist, and expected increases in the reach of existing financial infrastructure, are likely to increase these figures in some cases by 100 percent or more. For this growth

Figure 10. Current and Potential Impact of Financial Infrastructure



Source: Miller, Mylenko, and Sankaranarayanan 2009.

and impact potential to be realized, concerted collaborative effort is needed from governments, development finance institutions, and financial institutions.

These central elements of financial infrastructure need significant development or improvement in many developing countries, including those with a large number of unserved and underserved. Even in countries that have the basic financial infrastructure, financial service providers such as microfinance institutions (MFIs) and nonbank financial institutions do not participate in key financial infrastructure elements, such as credit information systems. It is key to develop inclusive and efficient financial infrastructure to alleviate the availability and affordability constraints to financial inclusion.

Credit Information Systems. The primary benefit of credit information systems is the establishment of “reputational collateral” through the payment performance of individual and firm borrowers and financial users (Miller 2003). Lenders are able to make more informed decisions about creditworthiness when they have access to a borrower’s payment history, including both positive and negative information. Major benefits of credit reporting include:

- *Greater access by individuals to loans and other financial services at banks.* Individuals who have a credit history can use it to obtain services at financial institutions. Studies show an 89 percent increase in the loan approval rate when positive and negative information is included in the credit report and an 11 percent increase in the loan approval rate when credit reports capture information from retail as well as other lenders (Barron and Staten 2003).
- *Decrease in the cost and processing time for loans.* Credit reports speed up the decision-making process and turnaround time for loans, which reduces the transaction cost of making the loans. These savings can be passed on to the borrower in the form of lower interest rates.
- *Greater access to financing by SMEs.* In studies done that covered 5,000 firms in 51 countries, the percentage of firms reporting constraints to financing is lower for firms operating in environments *with* a credit bureau (27 percent) than it is for firms operating in environments *without* a credit bureau (49 percent) (Love and Mylenko 2003).

Lack of access to credit information systems, for example, exposes MFIs and other financial institutions to the risk of nonperforming loans because they are not able to accurately assess a borrower's repayment capacity, thus increasing the risk of overindebtedness. In mature and dynamic microfinance markets, lack of such information on microfinance lending can have an impact on MFI portfolios. Access to inclusive credit information systems open to banks and MFIs, as well as to data from other providers such as nonbank financial institutions and nontraditional data providers, can help to mitigate these risks of client overindebtedness and deteriorating portfolios. The fundamental value proposition for microfinance credit reporting is to alleviate this credit risk problem (Sankaranarayanan 2010). For regulated financial institutions, public credit registries also play a critical role in prudential regulation, financial sector supervision, and systemic-level risk monitoring.

Collateral Registries and Secured Transactions Systems. Collateral registries and secured transaction systems represent another key building block of financial infrastructure that is underdeveloped in emerging markets.¹¹ While 78 percent of the capital stock of the typical business enterprise in emerging markets consists of movable assets, such as machinery, equipment, or receivables, financial institutions are reluctant to accept movable property as collateral. Banks strongly prefer land and real estate as collateral. This requirement constrains access to credit for individuals and SMEs. To address this constraint, modernizing secured transactions and collateral registries contributes to financial inclusion by:

- *Increasing the level of credit.* In countries where security interests are perfected and there is a predictable priority system for creditors in case of loan default, credit to the private sector as a percentage of GDP averages 60 percent compared with only 30 to 32 percent on average for countries without these creditor protections (Safavian, Fleisig, and Steinbuks 2006).
- *Decreasing the cost of credit.* In industrial countries borrowers with collateral get nine times the level of credit given their cash flow compared with borrowers without collateral. They also benefit from longer repayment periods (11 times longer) and significantly lower interest rates (50 percent lower) (Chaves, de la Pena, and Fleisig 2004).

Payment Systems and Advancing the 5x5 Remittances Goal.

A safe and efficient national retail payment system is a prerequisite for the promotion of financial inclusion. Infrastructure for retail payments systems includes a legal and regulatory framework and involves cooperation between various participants in the financial system to build system rules, instruments procedures, standards, and other aspects to enable the transfer of money between various counterparties safely and efficiently. Retail payment services are often the first point of entry of the underserved and unserved into the financial sector.

One important form of retail payment services is remittance transfers—cross-border person-to-person payments, typically of relatively low value; these transfers represent a lifeline for more than 700 million people in developing countries.¹² The World Bank estimates that remittances totaled US\$420 billion in 2009, of which US\$317 billion went to developing countries, involving some 192 million migrants or 3 percent of the world population. The money received is an important source of family (and national) income in many emerging markets, representing in some cases a very large percentage of the GDP of the receiving countries (World Bank 2010a).

The average cost of sending remittances varies significantly across country corridors, according to the World Bank's Remittance Prices Worldwide data. Figure 11 lists the most and least costly country corridors.

There is a unique opportunity for reducing the cost of remittances, resulting in more money for migrants and their families. Recognizing the importance of migrant remittances for the global development agenda, the G-8 announced the formation in February 2009 of a Global Remittances Working Group to facilitate the flow of remittances worldwide. In July 2009 the working group secured the commitment of the G-8 heads of state to reduce the global average cost of transferring remittances by 5 percentage points in five years – “5x5” (box 2). If that commitment is met, remittance recipients in developing countries would receive up to US\$16 billion dollars more each year than they do now. This added income could then provide remittance recipients with more disposable income resulting in higher rates of consumption, savings, and investment within local economies and higher levels of economic growth (World Bank 2010a).

Figure 11. Remittance Cost across Selected Country Corridors

Most costly country corridors for sending \$200 (cost in US\$)	
Australia to Papua New Guinea	\$43.32
Tanzania to Rwanda	\$40.78
Brazil to Bolivia	\$31.88
United States to Brazil	\$31.37
United Kingdom to Rwanda	\$30.72

Least costly country corridors for sending \$200 (cost in US\$)	
Singapore to Bangladesh	\$4.48
United Arab Emirates to Pakistan	\$4.87
Singapore to Philippines	\$6.12
United Arab Emirates to Sri Lanka	\$6.29
Malaysia to Philippines	\$6.88

Source: World Bank Remittance Prices Worldwide database (1Q2010) (<http://remittanceprices.worldbank.org/>).

Note: The global average total cost is calculated as the average total cost for sending US\$200 with all remittance service providers (RSPs) worldwide; nontransparent RSPs (that is, RSPs that do not disclose the exchange rate applied to the transaction) are excluded as well as corridors from the Russian Federation, since in these cases the exchange rates were not provided and cost would be higher if data were complete. In the lists of most and least costly country corridors, the cost includes the transaction fee and exchange rate margin. Only those corridors with a sufficient degree of transparency (that is, all the relevant information was provided by all RSPs) are featured. Corridor averages are unweighted and do not reflect the market shares of the different firms that compose the average.

Box 2. G-8 Summit (L'Aquila, July 2009) to 5x5 Declaration

"Given the development impact of remittance flows, we will facilitate a more efficient transfer and improved use of remittances and enhance cooperation between national and international organizations, in order to implement the recommendations of the 2007 Berlin G-8 Conference and of the Global Remittances Working Group established in 2009 and coordinated by the World Bank. We will aim to make financial services more accessible to migrants and to those who receive remittances in the developing world. We will work to achieve in particular the *objective of a reduction of the global average costs of transferring remittances from the present 10% to 5% in 5 years* through enhanced information, transparency, competition and cooperation with partners generating a significant net increase in income for migrants and their families in the developing world."

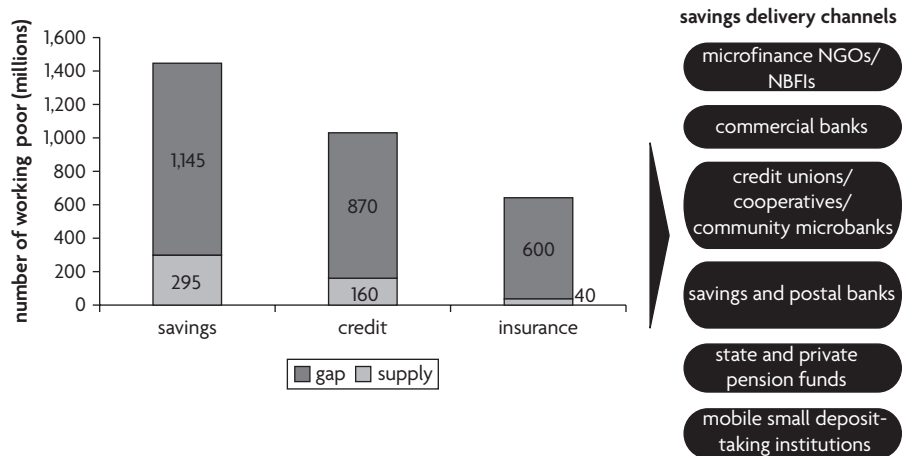
Source: G-8 (2009).

Delivery Mechanisms and Products

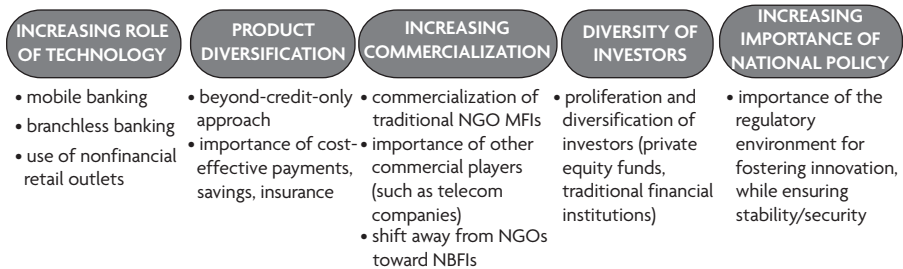
There is a near-universal need for safe and secure savings and payment products as well as a large unmet demand for insurance and credit (figure 12). Financial services for the underserved are costly, time-consuming, and unreliable. The needs of low-income households for financial services are high—one study estimates that households in Bangladesh are transacting about 60 percent of their annual income through financial instruments (a combination of formal and informal) (Rutherford 2005). While the need for appropriate and effective credit products remains important, the focus of interventions is increasingly expanding to include additional product types covering savings, payment systems, and insurance. The following product snapshot highlights these additional three product types.

Delivery mechanisms that leverage technology solutions for wider reach represent one of the key products and delivery innovations for expanding the financial access frontier. The increasing role of technology for the distribution of financial services, greater product diversification beyond the credit-only approach, increasing commercialization, a widening range of players investing in financial inclusion, and the increasing importance of policy environments all help advance progress

Figure 12. Supply vs. Gap for Financial Products



Source: World Bank Group Team Analysis and analysis for the Bill and Melinda Gates Foundation.
Note: *Based on 1.64 billion working poor in developing countries.

Figure 13. Global Trends Shifting the Financial Inclusion Frontier

Source: World Bank Group Team Analysis.

Box 3. Case Study: M-Pesa (Kenya)

Perhaps the most commonly cited case study on the ability of branchless banking to transform the financial realities of a population is the case of M-Pesa, a mobile money service offered by Safaricom in Kenya. The service is very popular: as of April 2010, 9 million Kenyans (40 percent of the population) owned an M-Pesa account. According to a 2009 CGAP brief, 77 percent of survey respondents believe that M-Pesa has raised their household income. Indeed, data show that money is remitted significantly more frequently and at lower cost compared with traditional options. Furthermore, since M-Pesa's launch, the number of Kenyans considered financially included has almost doubled.

Source: CGAP 2009, FSD Kenya, Mas and Radcliffe 2010.

in improving financial inclusion (figure 13). Delivering financial services to the unbanked using mobile banking technology holds significant promise (box 3). An estimated 1 billion people in emerging markets have a mobile phone but no bank account, and it is expected that this number will reach 1.7 billion by 2012. Moreover, studies indicate that this segment represents a strong market opportunity with the potential for the delivery of mobile money services to the unbanked customers to generate annually US\$5 billion in direct revenues and US\$2.5 billion in indirect revenues for mobile operators (CGAP-GSMA 2009). Many product and service innovations that have changed the way that financial services have been provided to low-income consumers are also to be found in the microfinance industry (see annex).

Savings Products. The supply gap for savings products is larger than the supply gap for either credit or insurance products. Estimates indicate that the penetration gap in the supply of savings services is as wide as 70 percent (see figure 12). As a result, initiatives that promote savings products for low-income households have begun gaining traction globally. These initiatives have gained attention in recent years as growing evidence shows that strong asset-building skills are key to poverty reduction. While not everyone can and should borrow money, everyone can save a small amount of money. The delivery channels for savings products are diverse and multiple, ranging from MFIs to commercial banks to savings and postal banks.

Matched savings accounts, also known as individual development accounts, are an example of a savings product designed for low-income populations. Holders of these accounts receive matched savings contributions, usually at the rate of 1-to-1 or 2-to-1, with the provision that the account must be used toward certain approved purposes. These purposes may include funding a small business, purchasing a home, or paying for education. Beneficiaries of matched savings accounts are also sometimes required to participate in financial education training. Pilots in Peru, Taiwan, China, and Uganda have shown promising results. Child savings accounts are another new savings product sometimes combined with matched savings accounts.¹³ Countries such as the Republic of Korea, Singapore, and the United Kingdom are experimenting with or implementing child savings accounts.

Payment Systems and Remittances Products. The potential for linking money transfers to financial inclusion remains underexplored. Microfinance institutions occupy a unique position in servicing those poor clients receiving remittances from abroad or within-country transfers. How microfinance institutions could reduce transaction costs and increase the economic impact of those transfers is an area for innovation in the short and medium term. Using clients' remittances histories to evaluate creditworthiness (World Bank 2010b) or designing client savings' programs for remittances funds are examples to be further piloted.

Governments are beginning to use government-to-person (G2P) payments in ways that promote financial inclusion. Today, it is estimated that the number of low-income people receiving government social protection

transfers (conditional or unconditional cash transfers¹⁴) is roughly the same as the number of microfinance clients—about 170 million worldwide (Pickens, Porteous, and Rotman 2009). While traditional G2P payments aim solely to supplement income and provide basic poverty alleviation, many governments are experimenting with the disbursement of funds electronically, often through mobile or card-based banking accounts. In many cases, payment recipients must have a bank account, which automatically places the beneficiary in the financial system and opens the door to additional formal financial services. However, obstacles still exist with this model: for example, infrequent use of the savings account may nullify much of their benefit and make them less profitable and therefore less attractive to banks. More pilot programs and research on how to link G2P to financial systems is necessary to harness the potential for using transfer payments as a way to achieving financial inclusion.

Microinsurance Products. With only 3 percent of the world's low-income population covered by any form of formal insurance against life-cycle shocks or calamities that may affect a whole family, community, or region, microinsurance represents an emerging product frontier. Most people continue to manage risk through informal mechanisms, such as borrowing from friends and family and self-insuring, by investing in assets that can be sold in hard times. There is increasing interest in offering clients access to microinsurance products in partnership with insurance companies. Innovation is taking place in the area of index-based risk transfer products—financial instruments that make payments based on realizations of an underlying index relative to a prespecified threshold. The underlying index is a transparent and objectively measured random variable. Examples include area average crop yields, area average crop revenues, cumulative rainfall, cumulative temperature, flood levels, sustained wind speeds, and Richter-scale measures (Microinsurance Network 2010). The World Bank has launched the Global Microinsurance Benchmark Database to help provide information on the quality of microinsurance expansion in terms of products, market size, and financial and operational performance.

Low-Cost, No-Frills Accounts. An additional product innovation refers to going “back to the basics” and developing simple, no-frills accounts that have the potential to reach a wide share of the unbanked

segment of the population. Many countries, including Brazil, Malaysia, Mexico, and South Africa, have encouraged or have rolled out such financial products and services to expand the usage of formal financial services. However, financial inclusion products and policies that focus on targeting a single barrier to access, such as fees, will succeed only if that barrier was a binding constraint in the first place. Basic accounts may not prove effective if distance and a lack of financial capability deter their uptake and use. The behavior of the banks is another common theme: policies that banks see as requiring them to behave in a way they view as unprofitable will fail. To achieve financial inclusion, political mandates to banks should be aligned with incentives (World Bank Group 2009).

One example of a successful basic no-frills account that increased use of formal financial services is the Mzansi account in South Africa. Mzansi is an entry-level bank account, based on a magnetic stripe debit card platform, developed by the South African banking industry and launched collaboratively by the four largest commercial banks together with the state-owned Postbank in October 2004. The Mzansi account was set up as a simple account with minimum, low-fee requirements. Since its introduction 6 million South Africans have become account holders (box 4). While not all Mzansi account holders are new to the banking system and

Box 4. Mzansi Accounts (launched in 2004 in South Africa)

Features: No monthly fees

No minimum balance

One free monthly cash deposit

Maximum account balance of US\$1,875 beyond which clients must graduate to regular savings accounts

Results: More than 6 million Mzansi accounts opened (by December 2008), a significant number out of a total of 32 million adult population. Two-thirds of the Mzansi account holders had been unbanked.

At least one in ten South Africans has a Mzansi account

One in six banked people are active Mzansi clients

Banked population increased from 46 percent (2004) to 64 percent (2008)

Source: Bankable Frontier Associates and FinMark Trust 2009, World Bank Group (2009).

not all the newly banked are Mzansi account holders, the percentage of adults banked in South Africa increased from 46 percent in 2004 to 64 percent in 2008. Of the increase, the Mzansi first-time banked contributed close to half: 8.2 percent of the 18 percent increase.

Target Market Segment: Rural. Rural areas require special attention and tailored interventions because they represent low-financial-access areas with the most concentrated poverty levels. Financial access is limited in most rural areas in developing countries because of high transaction costs and risks attributed to low levels of economic activity, poor infrastructure, high levels of production and price risks in dominant rural economic activities such as agriculture, and poor public policies such as interest-rate caps and debt write-offs (Nair and Kloeppinger-Todd 2007). Financial inclusion strategies and interventions need to leverage the existing (even if limited) financial infrastructure in rural areas (such as financial cooperatives) and new technologies and designs (such as agent correspondent networks and branchless banking) to sustainably expand access to finance.

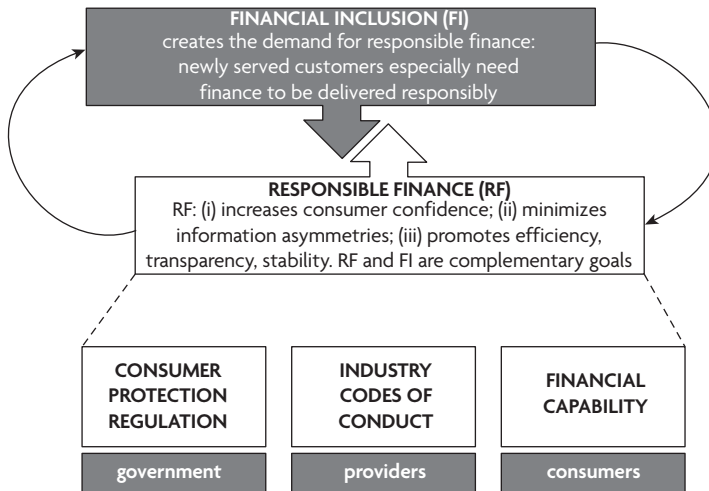
Target Market Segment: Women. Women represent a key target segment for three reasons.¹⁵ First, women traditionally face greater access barriers to formal banking services and thus are also credit-constrained to a greater extent than men. Second, experience has shown that repayment is higher among female borrowers, mostly resulting from more conservative investments and lower moral hazard risk. The lower moral hazard risk might stem from lower mobility and higher risk aversion. Third, women's access to financial services has a high potential to yield positive effects because women seem to focus more on children's health and education than men do. A study of the Grameen Bank in Bangladesh finds that credit has a larger effect on the behavior of poor households when women are borrowers (Pitt and Khandker 1998; Khandker 2003). Focusing on women may empower them in the intrahousehold decision process. The widely recognized empirical study on the link between microfinance and women's empowerment is Ashraf, Karlan, and Yin's (2008) follow-up to their 2006 study of commitment saving devices in the Philippines.

In addition, women are among the poorest clients and make up a sizable and growing share of small businesses globally, currently representing an estimated 25–38 percent of all registered small businesses worldwide. For example, in China women own one-third of small businesses, of which 17 percent have more than 1,000 employees, and in Southeast Asia it is estimated that women make up more than 40 percent of the workforce and are starting businesses at twice the rate of men (GEM 2007). Because the poverty concentration is higher among women than men, many microfinance pioneers (such as BancoSol and Grameen Bank) originally focused on serving women. While not all MFIs focus specifically on women, the Microcredit Summit Campaign counted that as of end 2007, 70 percent of microfinance clients worldwide were women (Daley-Harris 2009). Among those customers classified as the “poorest,” the share was even higher at 83 percent (Armendàriz and Morduch 2010).

Responsible Finance/Customer Focus

Responsible finance is addressed by advancing three areas: financial consumer protection regulation, industry self-regulation, and financial capability. Responsible finance practices are defined as those promoting more transparent, inclusive and equitable provision of financial products and services. Achieving these practices requires action by three key stakeholders (figure 14): the financial services industry (through industry self-regulation including codes of conduct and standards), governments (through consumer protection policies, regulation and institutional arrangements), and consumers (through enhanced consumer awareness, consumer advocacy, and financial capability).

The current postcrisis environment is providing additional impetus to advance responsible finance as an element of financial inclusion. Until the financial crisis, an estimated 150 million new customers globally were buying financial services each year. Global consumer debt was 12–14 percent of GDP in the first half of the 1990s but increased to 18 percent in recent years. Mortgage debt rose still more rapidly—from 46 percent of GDP in 2000 to over 70 percent in 2007 (Rutledge 2010). The crisis demonstrated the danger of overborrowing, whether by individuals misled through predatory lenders or by overly optimistic individual or firm borrowers. For that reason, when discussing the big strides in financial inclusion that many countries

Figure 14. Three Dimensions of Responsible Finance

Source: World Bank Group Team Analysis.

need to make, it is imperative to complement those efforts with key improvements in responsible finance practices.

Many of the lessons from the crisis in global financial markets are well known. Key insights include:

- The role that unscrupulous business practices played in the crisis (predatory lending, misleading product information, and fraud)
- The lack of adequate oversight and consumer protection in an era of deregulation and the actual limits on the effectiveness of market forces for instilling discipline, especially when systemic failures emerge. The lack of transparency and disclosure made it difficult to evaluate and price risk throughout the financial system.
- The limited level of financial capability in the population, even among relatively educated and “sophisticated” financial consumers. When consumers did not understand credit terms, they too often became overindebted.

Other causes of the crisis included compensation schemes, misaligned incentives, explosion of new financial products that were not adequately rated, and macroeconomic policy. Still, the fact that consumers became unwitting participants through their credit and investment decisions contributed to the spread and scale of the crisis.

The mortgage crisis demonstrates the importance of responsible lending together with adequate risk management and funding instruments and consumer protections. The subprime debacle in the United States shows that extending access can be extremely harmful to both borrowers and lenders if not done in a sound and responsible way. Households were lured to borrow against their own interest by securing loans based on the hypothetical and ever-increasing value of housing assets irrespective of borrowers' capacity to repay; the originators of these loans had no incentives to manage credit risks prudently, and the broader housing market was financed through complex and risky financial structures. The crisis led to a lasting mistrust among bond investors (mortgage portfolios no longer being perceived as safe collateral). Efforts to cater to underserved categories must rely on sounder principles such as borrowers' capacity to repay, know-your-customer rules, proper risk management tools, tighter regulations, and robust funding mechanisms. A growing number of economies including middle-income countries are expressing urgent needs in that direction.

The financial crisis has also served as an advance warning to potential microfinance markets that are overheating. Several dynamic microfinance markets (Bosnia and Herzegovina, India, Morocco, Nicaragua, and Pakistan) are showing symptoms of stress, demonstrated by deteriorating portfolio quality, increasing loan delinquencies, and perceived or real overindebtedness of clients. These symptoms are largely the result of inherent vulnerabilities in the market, such as concentrated market competition and multiple borrowing, overstretched MFI systems and controls, and an erosion of MFI credit discipline. To address these rising concerns, local and global initiatives (such as the SMART campaign) are focusing on responsible microfinance.¹⁶

Consumer protection regulations and laws are necessary to level the playing field between consumers and financial services providers, minimizing the market failures that can arise from the frequent imbalance of power, information, and resources between the two parties. The government has a leading role to play in ensuring that appropriate consumer protection regulation is tailored to promote financial access and the financial sector development of the country. Consumer protection regulation is closely associated with prudential regulation. Policy objectives on these two fronts should therefore be aligned. Consumer

protection implies that consumers should be provided with transparency (disclosure of full, simple, and comparable information), choice (fair, noncoercive, and reasonable marketing and selling practices; fair collections), redress (inexpensive and speedy mechanisms to address complaints and resolve disputes), and privacy (control over collection of and access to personal information) (AFI 2010; Rutledge 2010; World Bank Group 2009).

Financial capability is the combination of knowledge, understanding, skills, attitudes, and especially behaviors that people need to make sound personal finance decisions, suited to their social and financial circumstances (CGAP 2010). The need for building financial capability is especially high in nascent low-access markets (box 5). The key objective of financial capability programs is to raise financial awareness and improve financial behaviors of consumers so that they can make the best-informed financial decisions, given their economic and social circumstances. Financial capability programs can be delivered through multiple channels—financial institutions themselves, the education system (for example, through financial education in school curricula), regulatory and supervisory agencies (central banks, banking or financial regulators, consumer protection agencies), the media (newspapers, radio, television, Internet), social marketing (road shows, street theatre, entertainment), nongovernmental organizations (consumer associations, debt counseling centers), and others.

Box 5. Lack of Financial Capability in Practice

Selected Headline Statistics

Pakistan	Only 3 percent of adults understand what is meant by mobile banking and mobile phone banking; 71 percent of adults think they can easily live their life without a bank account.
Mozambique	5 percent of adults have insurance products; half the adult population (50.2 percent) claims never to have heard of insurance or insurance products.
Tanzania	Only 26 percent of people interviewed had heard of interest on savings accounts; none understood how this worked.

Source: FinScope. www.finscope.co.za

To advance responsible finance practices, financial institutions should be driven by two principles: do no harm (protective element), and do good (ensuring and proving that their finance is pro-growth and pro-poor). Providers also stand to benefit from responsible finance practices. The “do no harm” element rests on principles of transparency, disclosure, and improved risk management practices that protect the customer and the financial institution. The “do good” element refers to the proactive approach by the industry or financial institutions to support the positive impact of their financial operations on individuals, communities, and countries in which they operate.

To give substance to the “do good” element, private banks should develop and operationalize indicators and measures that give evidence of and motivate the positive impact of their businesses. Responsible finance initiatives for the microfinance sector have been defined, and some are already in endorsement stage. Examples are the Social Performance Task Force, which aims to engage with microfinance stakeholders to develop, disseminate, and promote standards and good practices for social performance management and reporting, and the SMART Campaign, which promotes client protection principles.¹⁷ The campaign has about 1,000 signatories and is already in the implementation stage.¹⁸ Responsible finance more broadly applied to the mainstream private banking sector is still being shaped at the multilateral and global level.



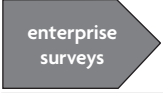


Data and Measurement

Financial inclusion data is critical in supporting evidence-based policy making, helping inform the prioritization of efforts, and tracking progress of the proposed targets. Without standardized, comparable, and regularly updated data at the global and national level, progress tracking and target setting is suboptimal and lacking direction. Thus data and measurement are an indispensable area of work that requires defining measurable financial inclusion dimensions and improving current and future data collection efforts and indicators toward the goal of establishing an international financial inclusion data platform.¹⁹

Financial inclusion data are at an early development stage, where it is critical to ensure that the necessary indicators are covered and that the key data are collected and published annually so that progress can be tracked. Three sources of data can be used to measure and benchmark

financial access and policy as well as barriers to financial access: regulators of financial services (supply side); financial institutions (supply side); and surveys of users—individuals or households and firms (demand side). Figure 15 outlines the major existing data reports covering financial inclusion indicators. Currently, the World Bank Group and the International Monetary Fund (IMF) each do a survey that collects global, comprehensive financial access data on an annual basis. The other reports are focused on a specific dimension of financial access. While the supply-side data from financial institutions or regulators tend to be more cost-effective, they lack the power to reveal information about the client experience and the needs of nonconsumers that demand-side surveys can reveal. Thus, comprehensive, standardized demand-side data at the global level are also needed (AFI 2009).

Figure 15. Measuring Financial Access: Key Existing Reports

name	developer	key facts
 financial access	<ul style="list-style-type: none"> World Bank Group (WBG) published annually 	<ul style="list-style-type: none"> statistics on financial access in 139 countries usage statistics: deposits, loans, branches policies and regulations: bank agents, postal networks, branch and credit regulations, consumer protection SME financing volume statistics added in 2010
 financial access survey (FAS)	<ul style="list-style-type: none"> IMF 	<ul style="list-style-type: none"> cross-country geographic and demographic outreach of financial services outreach: bank branch network, ATMs financial instruments: deposits, loans, debt securities, insurance
 enterprise surveys	<ul style="list-style-type: none"> World Bank (WB) 	<ul style="list-style-type: none"> comprehensive firm-level data in emerging markets, collected in 3–4 year rotation currently gathering data covering 122 countries
 household and consumer surveys	<ul style="list-style-type: none"> World Bank WB and Gates FinMark (FinScope) 	<ul style="list-style-type: none"> household level indicators of access to finance World Bank's household surveys global household survey (forthcoming) FinScope: 14 countries in Africa and Pakistan, focus on consumers' usage and perception on financial services
 financial infrastructure indicators and data	<ul style="list-style-type: none"> World Bank 	<ul style="list-style-type: none"> Doing Business indicators: Getting Credit (covering credit reporting and collateral registers in 183 countries) global payment systems survey (covering 142 countries) global remittance price database (launched in 2008, shows remittance data in 178 corridors)

demand side
 supply side

Source: World Bank Group Team Analysis.

On the supply side, the World Bank Group has published *Financial Access 2009* based on the results of a regulator survey (Kendall, Mylenko, and Ponce 2010). Building on earlier World Bank research (Beck, Demirgüç-Kunt, and Martinez Peria 2007, 2008), this initiative set out to collect core statistics on access to financial services and to review policies supporting broader financial access. *Financial Access 2009* was the first in a projected series of annual reports that publishes statistics on the number and value of deposit accounts and loans and retail locations in 139 countries. The report also collected information on several broad policy topics including provision of financial services through postal networks, the use of bank agents, regulations related to opening accounts, branch regulations, credit regulations, and transparency and consumer protection. The *Financial Access 2010* survey is under way, with the report expected in the fall of 2010. This year's survey asks for information on SME finance in addition to updating the 2009 information.

The IMF has recently launched a new online database of results from its inaugural Financial Access Survey, designed to underpin research on the provision of consumer financial services worldwide. The database measures the reach of financial services by bank branch network, availability of automated teller machines, and by four key financial instruments: deposits, loans, debt securities issued, and insurance.^{20, 21}

Supply-side financial infrastructure indicators provide additional insight into discrete aspects of the enabling environment for financial access. The 2010 *Doing Business* report released in September 2009 covers 183 economies, the largest share of the globe since the report was first published in 2004. Among the 10 indicators covered by the report, "Getting Credit" is the most relevant one for assessing progress on reforms that support the development of credit information sharing systems, collateral registries, and secured transactions.²²

Additional financial infrastructure indicators are covered by the Global Payment Systems Survey and the Global Remittance Price Database. To track progress toward the 5x5 goal, the World Bank launched the Remittance Prices Worldwide database in 2008.²³ These narrowly focused indicators are especially useful as they are able to inform specific reforms needed to create a better enabling environment for financial

access. However, they highlight only a part of the puzzle, and more of these specific indicators that easily link to reforms are needed.

On the demand side, household and specialized surveys fill in the gaps on usage as well as provide rich demographic analysis. Household surveys such as the Living Standards Measurement Survey and specialized surveys such as World Bank Access to Finance surveys, FinScope's FinAccess Surveys, and World Bank Group's Enterprise Surveys are other sources that enrich the analysis. By allowing for sex-disaggregated analysis, recent surveys have also highlighted women's significantly lower access levels in countries such as South Africa, Pakistan, and Tajikistan. In addition to gender-related aspects of financial inclusion, household surveys can also provide rich data on geographical aspects of financial inclusion, such as the rural-urban divide. The forthcoming global household survey spearheaded by the World Bank Group with the support of the Bill & Melinda Gates Foundation will provide a measure of use of different financial services around the world.

The regulators have a role to play in facilitating data collection efforts. Supervisors concerned with financial stability often collect data on financial depth based on the aggregate value of deposits and loans as well as large loans. It is significant, however, that less than 70 percent of the sample countries collect information on the number of bank deposits and a mere 30 percent collect information on regulated nonbank deposit accounts. Data on loans are even more limited (Kendall, Mylenko, and Ponce 2010).

There are multiple avenues to support data collection efforts. For example, the government of India encouraged measurement and reporting to track and advance its mission of increasing lending opportunities to women, which contributed to positive results (box 6). The Bank of Thailand recently made a clear case that it is in the interest of regulators and policy makers to monitor policy progress over time and to express demand for data. The Central Bank of Kenya was highly involved in the design and implementation of its national financial surveys. In turn, this involvement emboldened policy makers to use the data from the FinScope survey conducted to make a key decision about how heavily to regulate the relatively new mobile payment system offered by M-Pesa (AFI 2009). Similarly, encouraging other stakeholders to make an investment in the study may promote wider usage.

Box 6. Government-Led Initiatives in Data Collection in India

Following an Indian government directive and action plan to increase access to bank loans for women, the Reserve Bank of India (RBI) in 2000 asked public sector banks to disaggregate and report annually on the percentage of credit to women within their total lending. The directive urged banks to earmark at least 2 percent of their net bank credit for women and raise it to 5 percent in 5 years time. The aggregate net bank credit to women has since increased to 6.3 percent in 2009 with 25 banks reaching the target. Although the full impact of the policy requires further analysis, tracking the data has increased awareness of women's low access levels.

Source: Reserve Bank of India 2009.

The Way Forward to the G-20 Korea Summit

Advancing progress in financial inclusion will mean reaching out to a significant portion of the 70 percent of adults in developing countries that currently do not have access to financial products and services. The global effort in financial inclusion will be driven by setting global targets, focused not only on credit, which is only part of the needed portfolio of financial services and products but on a range of financial products and instruments including payments, remittances, savings, and insurance.

Global goals will trigger an important focus on data collection and measurement for both individuals and firms. Data and measurement of the SME finance gap needs improvement and standardization in order to track progress. All of the data collection projects described here need to be supported and improved on an ongoing basis.

To expand financial inclusion and build the foundations for sustainable growth, the World Bank Group recommends that the G-20 convenes a global partnership with relevant stakeholders around common set of global financial inclusion targets. The effort should focus not only on credit but on a range of financial products: payments, savings, remittances, and insurance. The targets would step up pressure to close existing data gaps—in particular, the SME finance gap and policy-related indicators—ensuring that the basic elements are in place to measure progress against the target on an annual basis. Key implementation pillars will include policy environment, financial infrastructure, delivery mechanisms and products, responsible finance, data and measurement and, building on progress made by the Financial Inclusion Experts Group. The implementation will

require an integrated and concerted effort leveraging four key drivers: the global development community, the financial services industry, national governments, and centers for knowledge sharing and standard setting bodies. The G-20 is in a unique position to convene those forces for economic development and to complement the effort with the creation of a funding mechanism to provide resources needed for the implementation of the financial inclusion agenda.

Annex The Microfinance Industry

Evolution and Successes in the Industry

Microfinance offers poor people access to basic financial services.²⁴ Now a key component of the global financial inclusion effort, it emerged in the 1970s with the provision of small, collateral-free or low-collateral loans to poor clients in developing countries.²⁵ The core principles in micro-lending have traditionally included group lending and liability, preloan savings requirements, progressive loan amounts, and the guarantee of access to future credit if the current loan is repaid promptly. The industry has matured and diversified significantly over the past several decades, going beyond credit-only to encompass a broad range of financial products and services that also include savings, insurance, and remittance and cash transfer services to poor households and microenterprises.

Recipients of microcredit are typically poor or low-income and lack access to formal financial institutions. Microfinance clients are a diverse group of people that require diverse types of products. With rare exceptions, typical microcredit clients do not come from the poorest 10 percent of the population, because the poorest often do not have the resources or the consistent income to make even minimum payments on a loan. Clients are also typically self-employed or entrepreneurs—often rural—whose businesses involve a diverse array of products and services often sold from their home. Historically, most microfinance clients were women, although this profile is changing as men make up an increasing portion of client portfolios, which are often also aimed at youth, children, and the very poor.²⁶

Microfinance has become increasingly integrated in the formal financial system. Microfinance expanded robustly between 2004 and 2008, when annual asset growth averaged 39 percent. The industry growth trend continued despite the economic turmoil of the past three years. Although considerable challenges have accompanied this growth, essentially it has meant that millions more low-income citizens could become part of the formal financial system (table 2). Growth has been partly fueled by the emergence of new funders. Of the 61 microfinance funders surveyed by CGAP in 2008, 38 were public donors and 23 were investors. The actual commitments provided by both were roughly equal in 2008, reflecting the growing importance of funding from private funds.

Table 2. Microfinance at a Glance, 2008

Gross loan portfolio (US\$)	43.8 billion
Deposits (US\$)	23.8 billion
Number of borrowers	83.2 million
Average loan balance per borrower (US\$)	536.6

Source: MIX data 2008; median indicators based on a sample of 1,870 MFIs. www.mixmarket.org

The business model for financial service delivery is disaggregating as new partnerships among MFIs, banks, and, more recently, telecommunications and credit card companies allow each actor to carry out the role in service delivery most suited to its comparative advantage. Moreover, technology-driven delivery models are spreading rapidly.

Commercial banks, local and international, are recognizing the value proposition of lending to the poor, allowing microfinance to grow far beyond what would likely have been possible through donor funds alone. Initial public offerings (IPOs) by microfinance institutions are a relatively recent development in the industry's path to commercialization. To date, three IPOs have occurred in microfinance: Bank Rakyat Indonesia in 2003, Equity Bank Kenya in 2006, and Banco Compartamos in 2007. The Banco Compartamos' IPO marked the first offering by an institution originally founded purely as a microlender. SKS, one of the leading MFIs in India, just recently launched an IPO.²⁷ Many banks are now providing microfinance either directly (examples are the ACLEDA Bank in Cambodia and Lao People's Democratic Republic, and XacBank and AgBank, both in Mongolia) or indirectly through links with MFIs.

As the microfinance industry has grown, research on its impact and efficacy has also been given more salience.²⁸ While microfinance expands the opportunities of the unbanked, ongoing research is helping distill the welfare impact of microfinance products on low-income populations. Unfortunately, scientific testing of the impact of microcredit is surprisingly difficult. Qualitative research points to the benefits of microcredit, as reflected in the voices and anecdotes of clients (Collins et al. 2009), whereas quantitative research using experimental research presents a more nuanced picture.²⁹ A number of rigorous impact evaluation studies are currently under way exploring how microfinance affects different clients in different regions. There is an increasing recognition

and acceptance that microfinance is an instrument for increasing access to financial services rather than a tool that directly reduces poverty. Microfinance should not be seen as a substitute for investments in basic education, health, and infrastructure (Helms 2006).

Microfinance is high on many government agendas. The heightened interest has both up- and downsides. A more widespread understanding of what it takes to build sustainable access, more enabling legal and regulatory frameworks, and a greater focus on consumer protection and education are welcome. The reintroduction of low interest rate caps and the creation of government-sponsored direct lending institutions in some countries are troubling developments.

The microfinance industry is entering a new phase. While the focus in the first decades of the industry's evolution was on extending loans to the poor (focusing on microenterprise credit) and thus bringing as many low-access consumers as possible into the financial system, the next period will likely focus on sustainable growth along with product innovation to serve the very diverse financial needs of poor people.³⁰ Despite the considerable expansion and success, there are notable challenges to the microfinance industry. Five such challenges stand out: local financial market infrastructure (that is, local debt and equity markets, payments systems, rating agencies, and credit bureaus) and the regulatory and supervisory framework for microfinance remains weak in many countries; inadequate attention has been given to the quality of client services and too few efforts made to better understand changing market conditions and client needs; information is limited on the trade-offs between outreach, product offering, and profitability; product diversity remains limited, especially well-designed deposit products and transaction accounts that could be the gateway product for other services; and government policies and regulation continue to hinder the development of microfinance in many countries.

Financial capability training is beginning to take on a larger role as a key component of microfinance for low-income populations. Financial capability is the combination of knowledge, understanding, skills, attitudes, and especially behaviors which people need in order to make sound personal finance decisions, suited to their economic and social circumstances. The latest financial capability initiatives have borrowed from ideas about behavior change in regards to fields like health. Two pilots are

underway in India: the SKS Foundation's Ultra Poor Program in rural Andhra Pradesh has reached over 400 women who were too poor to qualify for SKS's microfinance services.³¹ The goal of the program is to bring very poor beneficiaries to a point where they can use their existing savings and assets to grow and diversify their capital base and potentially access microfinance. To help these women to learn basic money management skills, SKS delivers practical and interactive financial education modules during weekly group meetings. Another field experiment, in Gujarat, involves 1,000 low-income microfinance clients who receive approximately 10 hours of basic financial literacy education over a six-week period. The sessions are built around videos, which are complemented by discussion groups. A similar initiative is looking at the impact of a financial education program designed for the specific needs of mine-workers in South Africa (Imali, Shastry and Shapiro forthcoming). Although financial capability is still a developing field, the existing body of evidence suggests that it could be a powerful tool towards increasing financial inclusion. Randomized control trials to ascertain the cost-effectiveness of this policy intervention and qualitative studies are under way.

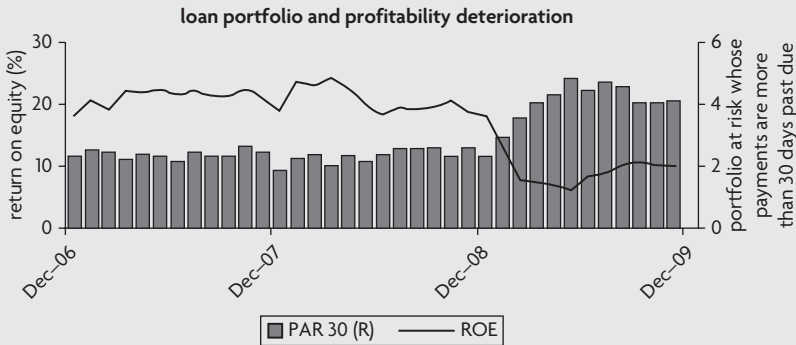
Financial Crisis and Developments in the Microfinance Industry

The microfinance industry's resilience to macroeconomic crisis was tested during the deepest global downturn in recent history. The crisis affected advanced and developing countries differently: while the first contracted by 3½ percent, developing countries appear to have weathered the crisis better, in part because of developing countries' limited integration in international financial markets and the economic resurgence in Asia, led by China and India (IMF 2009). The microfinance industry has had 15 years of continued growth and has been exposed to other crises (political upheavals, recessions, financial sector breakdowns); however, those crises were confined to specific regions and countries. Microfinance providers, unlike a decade ago, are today much more connected to international financial markets.

The financial crisis has also helped to expose other important issues for the sustainability and proper functioning of the microfinance industry, including domestic savings mobilization and responsible financial practices. The crisis has shown the importance of expanding deposit

Box 7. Microfinance amid the Financial Crisis

Providers' Signs of Stress. Microfinance institutions (MFIs) around the world appeared to face increased liquidity constraints in 2009. As expected, Tier II (assets between US\$3–50 million) and III (assets below US\$3 million) small MFIs in Sub-Saharan Africa and South Asia were more vulnerable to liquidity shortages. The portfolio quality of MFIs deteriorated in 2009, especially in Europe and Central Asia, with **PAR30** and loan loss provision increasing. Growth and profitability have slowed among providers but the fundamentals of the sector remain strong (see figure below).



MFI Clients Affected by the Global Crisis. Increased food and fuel prices, a slowdown in remittances, and employment layoffs in industries linked to international trade (such as food processing, textiles) negatively affected MFI clients' economic well-being. The crisis has also revealed that microfinance providers need to adopt better client-centric policies and to measure the impact of their products on the welfare of clients.

Microfinance Donors and Investors. Despite the adverse context, investors in microfinance have continued to support the industry but at a lower rate. Even during the first semester of 2009 microfinance investment vehicle funds under management grew at an annualized rate of 16 percent. Retail-oriented private funds increased in 2009, demonstrating that the microfinance sector remains attractive to private funding. The International Finance Corporation and KfW, the German development bank, responded to the crisis by launching a Microfinance Enhancement Facility designed to support sound microfinance institutions facing funding shortfalls worldwide.

Loan Portfolio and Profitability Deterioration

Sources: Median PAR drawn from sample of 50 Tier 1 MFIs. SYM50 from Symbiotics <http://www.syminvest.com>, CGAP 2009a.

mobilization among microfinance providers as a safety buffer in times of liquidity constraints. The importance of safe savings products for low-income people as a way to create wealth and move out of poverty is also being emphasized by donors and academia across the board. The increased emphasis on saving fits well with increased awareness of the need to promote responsible lending and borrowing among both providers and consumers. Worrying trends of overindebted clients or cli-

ents with multiple loans, abusive MFI practices, and overconcentration of investors in small markets are to be closely monitored.

Innovations for Scaling Up Microfinance

Microfinance is probably the socially responsible industry that has experienced the most development in terms of product and delivery innovation. New products and services are emerging to promote financial inclusion of low-income populations, moving beyond the credit only approach (for example, savings products, microinsurance, and government to person payments). In particular, these products and services have tried to create new avenues to provide financial services to the poor, strengthen the link between financial services and more comprehensive measures of financial inclusion, and empower the poor in their financial lives by providing consumer protections and financial capability.

First, branchless banking represents a key delivery innovation that has broadened access to financial services. Barriers such as distance to branches, cash crime, mistrust of financial institutions, and the perception of being unwelcome in banks have impeded the poor from involvement in the traditional banking system. However, the recent expansion of cellular technology has given banking providers an unparalleled delivery channel for their services. Branchless banking—the delivery of financial services outside of conventional bank branches by using information and communications technologies and nonbank retail agents—has shown promise for bringing financial services to traditionally underserved markets. Given the reach of branchless banking, it has been employed as a delivery channel for products like conditional cash transfers. The convenience and lower costs of branchless banking have also been a boon for those seeking remittance and other payment transfer savings.

Second, initiatives to provide basic access to those at the very bottom of the pyramid have also gained momentum in recent years. These initiatives stem from the observation that traditional microfinance does not reach the poorest members of a population, who often lack basic literacy skills and knowledge of money, which prevents them from using microfinance. In addition, these individuals are often geographically isolated in rural environments, which compounds the challenge. An example of a program aimed at this issue is the CGAP-Ford Foundation Graduation Program, which focuses on providing tools for the poorest to graduate out of extreme poverty.³² The graduation model targets the

“ultra poor”—people who have no assets and are chronically food insecure. The graduation program combines support for immediate needs with longer-term investments in training, financial services, and business development so that within two years program participants are equipped to help themselves “graduate” out of extreme poverty.

Finally, information and communication technologies are also contributing to expanding financial access across the world, facilitating connections between individual donors and poor people (person-to-person approach). Online marketplaces that connect individuals willing to donate or invest funds in intermediaries that channel funds to various undertakings of low-income people are becoming very popular (examples of such marketplaces are Kiva, Babyloan, MYC4, and Vittana). These are practical examples of how the goal of financial inclusion can be supported with communications technology.

Endnotes

1. Note that the ordering of the stakeholders is not indicative of any priority order.
2. A snapshot for the FIEG pillar, which represents the ongoing work that originated from the G-20 Pittsburgh Summit, is not included; the details on work areas will be included in the FIEG G-20 Seoul Summit deliverables.
3. Aligned with this estimate, an additional source that builds on datasets compiled from cross-country data sources on financial access and socioeconomic and demographic characteristics finds that 2.5 billion adults do not *use* formal financial services to save or borrow (Chaia and others 2009).
4. World Bank Group 2009.
5. A comprehensive review of the SME finance gap and its challenges, including an analysis of 163 cases of SME finance interventions compiled through a collective effort involving G-20 member countries, non-member countries, development finance institutions and private sector players, will be presented in the FIEG SME Finance Subgroup’s report to be delivered at the G-20 Seoul Summit in November.
6. Note that financial depth is most often described or measured by the extent of private credit as a percentage of GDP. Financial development is broader, encompassing the development of the entire financial sector.
7. For a further discussion specifically related to the poor’s management of day-to-day resources (benefit 2), see Collins and others (2009), based on financial diaries conducted in Bangladesh, India, and South Africa.
8. The section is taken from Beck, Demirgüç-Kunt, and Honohan (2009).
9. Estimates of financial infrastructure impact have been developed here based on data from several World Bank sources, including the Doing Business project,

- the Global Payment Systems Survey, and the Remittance Prices Worldwide Database, and from the IFC's lending portfolio.
10. Financial infrastructure is therefore part of the "soft" (intangible) infrastructure that consists of "institutions, regulations, social capital, value systems, and other social and economic arrangements." In contrast, "hard" infrastructure consists of highways, port facilities, airports, telecommunication systems, electricity grids and other public utilities. For more detail, see Lin 2009.
 11. For a comprehensive account of the importance of collateral registries and secured transactions and the reform aspects of modernizing these mechanisms, see World Bank 2010c.
 12. Definition of remittance transfers are from World Bank/BIS, "General Principles for International Remittance Services."
 13. Child savings accounts teach asset building from a young age by providing free savings accounts to children at birth, often with the provision that the money cannot be withdrawn until a certain age. For more details on savings products and asset building (not exclusive to child savings), see Zimmerman and Banerjee 2009.
 14. Such programs were first popularized in Latin America and the Caribbean but have spread to Africa, Asia, and Europe. Although CCTs are still a relatively novel concept, evidence from Mexico's *Oportunidades* program suggests that CCTs can increase savings and investment, promote banking, and create more responsible spending habits.
 15. This paragraph relies on Beck, Demirgüç-Kunt, and Honohan 2008 (p. 124, box 3.6), with updates from Armendàriz and Morduch 2010 (ch. 7).
 16. For more information on the microfinance crisis in these markets, see Chen, Rasmussen, and Reille (2010).
 17. For more information on the Social Performance Task Force, see <http://www.sptf.info>.
 18. For a full list of campaign endorsers, see <http://www.smartcampaign.org/about-the-campaign/campaign-endorsers>.
 19. At the Alliance for Financial Inclusion First Annual Global Policy Forum, in Nairobi in 2009, the Bank of Thailand proposed to spearhead the effort of translating pressing policy questions into survey designs and working together with policy makers from many countries to pave the way for an international financial inclusion data platform.
 20. The IMF "Access to Finance" data project is supported by Princess Máxima of the Netherlands, the UN special advocate, with the Netherlands providing funding for the first project year.
 21. Announced in October 2009 (<http://www.imf.org/external/np/sec/pr/2009/pr09351.htm>); the first database was published online in June 2010.
 22. The Getting Credit ranking is composed of two measures: a measure of the legal rights of borrowers and lenders (the legal rights index), and a measure of the scope and quality of credit information systems (the depth of credit information index).

23. The database, available online, covers 178 country corridors worldwide originating from 24 major remittance sending countries to 85 receiving countries, representing around 60 percent of total remittances to emerging economies. The objectives of this database are to implement the General Principle 1 (from the General Principles for International Remittance Services issued by the Committee on Payment and Settlement Systems) on transparency and consumer protection and to provide a global benchmark to assess remittance price trends.
24. This annex was prepared by CGAP in April 2010 as background documentation for this report.
25. The ideas and aspirations behind microfinance are not new. Small, informal savings and credit groups have operated for centuries across the world, from Ghana to Mexico to India and beyond. In Europe, as early as the 15th century, the Catholic Church founded pawn shops as an alternative to usurious moneylenders. See http://www.cgap.org/gm/document-1.9.2715/Book_AccessforAll.pdf for more background.
26. See CGAP work on graduation pilots for more information on borrowing constraints for the very poor. Microcredit is not always the answer. Other kinds of support may work better for people who are so destitute that they are without income or means of repayment.
27. <http://www.microcapital.org/microcapital-story-indian-sks-microfinance-plans-to-raise-13-billion-rupiah-usd-303-million-in-equity-possible-future-ipo> and “SKS Microfinance Files for IPO”, *Wall Street Journal*, March 26, 2010: <http://online.wsj.com/article/SB10001424052748704094104575144924260883344.html>
28. For a discussion on the impact of microfinance, see Rosenberg 2010.
29. Banerjee and others 2009; Karlan and Zinman 2009; and a meta-study of microloan impact evaluations through 2005 can be found in Goldberg 2005.
30. CGAP Focus Note: Growth and Vulnerability in Microfinance. <http://www.cgap.org/p/site/c/template.rc/1.9.42393/>.
31. This pilot program is part of the CGAP-Ford Foundation Graduation Program, a global effort to understand how safety nets, livelihoods, and microfinance can be sequenced to create pathways for the poorest to escape from extreme poverty.
32. CGAP Brief, “Creating Pathways for the Poorest: Early Lessons on Implementing the Graduation Model,” December 2009.

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Comments by Alfred Hannig

Alliance for Financial Inclusion

We at the Alliance for Financial Inclusion (AFI) believe that most of the successful policy solutions to increase access to financial services for the poor have been innovated in developing countries. The recognition of financial inclusion innovations spearheaded by developing-country policy makers from both G-20 and non-G-20 countries is therefore critical. We also welcome the particular emphasis the G-20 is putting on non-G-20 developing countries.

We agree that peer learning, mutual exchange, and replication of successful policy innovations play an increasingly fundamental role in expanding financial inclusion within coordinated efforts of key stakeholders.

For our members, AFI represents a global network or platform for peer learning. We would therefore urge some revision in the section regarding convening of key stakeholders. With regard to the suggested key working pillars, we would emphasize the following three pillars as the most relevant: policy environment, responsible finance/consumer focus, and data and measurement. This assessment is based on the findings of the recent AFI Financial Inclusion Policy Survey and the policy principles to be proposed by the G-20 Access through Innovation subgroup.

Additional Lessons Learned

Additional lessons learned from the AFI Financial Inclusion Policy Survey can also help further inform this debate. Among the findings:

- There is a new openness and demand for technology solutions. Policy makers see the opportunities and want to familiarize themselves with the risk profiles of technology-enabled financial services.
- Public-private dialogue and consultation is critical for fostering access.

Comments on the paper “Toward Universal Access: Addressing the Global Challenge of Financial Inclusion,” by Peer Stein, Bikki Randhawa, and Nina Bilandzic in chapter 10 of this volume.

- Learning from the experience of others is most effective in spreading knowledge on what works. There are two-way learning opportunities, since policy makers often prefer to internalize messages from a messenger facing similar realities, concerns, challenges, and pressures.
- Developing countries increasingly move toward evidence-based policy through data for financial inclusion and prefer to adopt self-set targets.
- Developing-country demand can be roughly grouped into three categories: unlocking the knowledge of champions and experienced countries; providing opportunities for effective peer learning and for replication of successful solutions with modification based on each country's unique condition; and supporting capacity-building efforts of countries that are at the earlier stages of the learning cycle.

Polylateral Development

The emerging mode of collaboration in the financial inclusion sphere reflects the characteristics of a new development approach. We in AFI call this polylateral development. By polylateral development, we mean systematic and sustainable lateral flows of knowledge and resources among and led by developing countries, resulting in socioeconomic growth and development progress—and in our case specifically greater access to finance.

In the field of financial inclusion, we have seen successful examples over the years of peer-learning and South-to-South knowledge exchange in other fields. But polylateral development from AFI's perspective is the comprehensive combination of several modes of delivery, some new and some not so new. The key success factor is that the developing country itself is in the driver's seat, determining which activities it would like to undertake and for what purpose.

AFI is a living example of polylateral development in action. How does AFI bring polylateral development to life?

- AFI has a country-led governance structure and membership base forming a global network focused on financial inclusion.
- Activities and initiatives are not imposed on individual countries or the wider network; instead the countries must request and demand activities and operations.

- AFI recognizes that developing countries have innovated some of the most successful solutions relating to increased financial inclusion but that these experiences are often not widely available.
- AFI has created a sustainable platform and conduit for developing countries to share their experiences and learn from each other so that solutions can be adapted or replicated by their peers through face-to-face meetings and online knowledge exchange—and are supported by grants that the countries themselves request.

Possible Action Steps

Let me conclude with three remarks regarding possible action items that the G-20 could take against the background of this approach:

We welcome the suggested Global Partnership for Financial Inclusion that lays out the way countries can act together in collaboration with the private sector to achieve sustainable and balanced growth through financial inclusion. Inherent in the design should be empowerment for emerging and developing countries.

The G-20 should create a global funding mechanism under the Global Partnership for Financial Inclusion. To create a funding mechanism that can serve the different needs of countries in a most effective way, the G-20 should call for self-set financial inclusion targets among developing countries (G-20 and non-G-20 countries), which can be combined and used as global targets by 2020.

Comments by Yongbeom Kim

Presidential Committee for the G-20 Seoul Summit

Building on discussions that have already taken place regarding access to finance, the purpose of these comments is to focus discussions on why financial inclusion should be a key agenda item for the G-20 this year.

Financial Inclusion Leads to Balanced Economic Growth

Financial inclusion is important because it leads to balanced economic growth. As clearly articulated by the G-20 leaders in Pittsburgh, strong, sustained, and balanced economic growth is essential to ensure continued global economic recovery in the short term and durable global economic prosperity for all in the longer term. In this context, the potential for economic growth is maximized when existing resources are efficiently and optimally allocated. At the same time, to achieve balanced growth, the current underserved population must have an opportunity to access and make use of the available resources in a safe environment. This will enable the poor to contribute to the overall growth.

Financial Inclusion Facilitates Innovation

Financial inclusion also facilitates innovation. Innovation, often led by entrepreneurs and small and medium enterprises (SMEs) especially in the developing economies, is one of the key drivers of enhanced productivity and growth. However, it is also these individuals and SMEs who often lack the credit history or collateral to secure financing for those ideas and innovations. At the same time, various studies have shown that these segments of the population are very much in need of a safe place to save. An inclusive financial system that goes beyond credit and includes access to a broad range of appropriate financial services is one of the key conditions to unlocking the huge potential of currently untapped growth.

Comments on the paper “Toward Universal Access: Addressing the Global Challenge of Financial Inclusion,” by Peer Stein, Bikki Randhawa, and Nina Bilandzic in chapter 10 of this volume.

Financial Inclusion Facilitates Better Use of Existing Assets

There is also a substantial body of literature showing that financial inclusion is a cornerstone for economic development.¹ For example, Hernando de Soto, in *The Mystery of Capital*, points out that the failure to achieve sustained and robust economic growth in many underdeveloped countries stems not so much from lack of resources but more from the lack of a cohesive legal and regulatory framework. This creates difficulties in using existing assets to finance new projects. What is needed to facilitate economic growth in underdeveloped countries is not more capital but the transformation of so-called “dead assets” into “liquid capital” to provide better access to finance.

Financial Inclusion Provides the Counterbalance to Stricter Financial Regulation

Finally, financial inclusion provides the counterbalance required against the tightening of financial regulation that is currently under way. In response to the recent crisis, national regulators and international standard setters have been concentrating their efforts in tightening financial regulations. However, there has also been some fundamental rethinking of the role of the governments in finance provision. This has provided opportunities to advance policy reforms aimed at increasing financial inclusion. It is crucial to maintain the goal of financial inclusion at a time when stricter regulation is being introduced so that the overall financial system can balance the need for greater stability with the need to ensure greater accessibility. It is in this context that financial inclusion is a timely issue for global discussion and coordinated international actions. There are many reasons why financial inclusion is important to the G-20 and the global economy.

How Financial Inclusion Can Be Improved

There is a need to increase the reach of traditional financial services through development of a multilayered financial industry architecture. A more nuanced and specialized market structure is needed that allows large, medium, and small banks and nonbank financial institutions, such as credit unions and building societies, to cater to customers of different income brackets with affordable and tailor-made financial products.²

To make this happen, governments must establish appropriate competition and licensing policies for the financial industry, as well as more effective supervision. They must also determine the right manner in which access to finance should be broadened, taking care not to increase moral hazard and imprudent lending practices.

Korea's Example of Increasing Access to Finance

The Republic of Korea has had valuable experience in broadening access to finance for those in need. Since the 1970s Korea experienced rapid economic development and throughout this period, it has implemented various policy measures to increase SMEs' access to finance. For example, the Korean government established a program in 1976 to extend credit guarantees to SMEs that demonstrate growth potential but lack collateral. As of April 2010 credit guarantees were extended to 220,000 SMEs, for a total value of US\$33 billion.

Korea is also working hard to enhance low-income households' access to finance. The Korea Post has been providing microinsurance services, and a Microcredit Bank was launched last year to support those who have minimal access to finance.

Why Financial Inclusion Should Be on the G-20 Agenda

The financial inclusion issues are best addressed at the G-20 level because the G-20 is the premier forum on international economic cooperation. It is currently exploring various policy options to bring the global economy closer to the objectives of strong, sustainable, and balanced growth. On top of this, Korea is firmly determined to set development as one of the key agenda items for the G-20 Seoul Summit. Financial inclusion perfectly complements our growth-oriented approach on development, which is why Korea is so committed to this issue.

By bringing the issue of inclusive finance to the G-20 table, Korea hopes to foster international cooperation to overcome common difficulties in designing and implementing necessary reforms—at both national and multinational levels—to increase financial inclusion in a responsible and effective manner. The World Bank's proposal to establish a Collaborative Diamond Model for Financial Inclusion 2.0 and to launch a global partnership for financial inclusion is an excellent example of fostering international cooperation. The Bank's efforts should be com-

mended. Similarly, Korea will also seek active participation of non-G-20 countries through networks such as the Alliance for Financial Inclusion and the Consultative Group to Assist the Poor, to maximize the impact of global initiatives on financial inclusions. We hope that the G-20 Seoul Summit will serve as an important stepping stone in realizing these important initiatives.

Korea is committed to ensuring meaningful dialogue and, ultimately, to achieving concrete deliverables to increase financial inclusion at the Seoul Summit.

Notes

1. Rajan and Zingales (2003) explain that capital accessibility is a critical factor to higher production capacity. They explain that the differences in national wealth and how well capitalism settles in a system depend on how much of a stranglehold the establishment, such as large banks, has on capital flow. If access to capital is limited, low-income individuals, who have only hard labor as their production factor, would be left with no means to raise capital to enhance their production capacity. They must put in a hard day's labor just to survive. If they had easier access to capital they could use in their production activities, they would be able to lay the foundation for stable economic growth. This is why the discussion on access to finance is so relevant.
2. See Lin, Sun, and Jiang (2009) for a good survey of this point.

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Chair's Summary by Princess Máxima of the Netherlands

UN Secretary-General's Special Advocate for Inclusive Finance for Development

Financial inclusion was cited as a critically important component of stability, equitable economic growth, and poverty reduction. Financial inclusion means universal access, at a reasonable cost, to a wide range of financial services for everyone needing them, provided by a diversity of sound and sustainable institutions. Two-thirds of the adult population in developing countries (2.7 billion people) lack access to basic formal financial services. A similar gap in access impacts small and medium enterprise (SMEs), which are engines of job creation and growth.

Opening

I commended the G-20 for its leadership on financial inclusion. At the Pittsburgh Summit, the G-20 leaders recognized the huge impact that the gap in access has on households, businesses, and economies around the world. They mandated a Financial Inclusion Experts Group to identify lessons learned about innovative approaches for improving access and to focus on access by SMEs. Innovations in the field are already drastically reducing the costs of delivery and creating products catering to the unbanked. Services like M-Pesa in Kenya, which uses mobile phones to make payments and deposit small savings, demonstrate that financial services that poor individuals and businesses need can be delivered in an affordable and sustainable manner. I stressed the need to talk in a common language that creates a continuum of access to finance across the value chain, from individuals through microenterprises to SMEs, and the need to engage all the stakeholders who can help to improve access.

Comments on the paper "Toward Universal Access: Addressing the Global Challenge of Financial Inclusion," by Peer Stein, Bikki Randhawa, and Nina Bilandzic in chapter 10 of this volume.

Presenter

Peer Stein, gave an overview of financial inclusion. Empirical evidence suggests that improved access is pro-growth and pro-poor. Financial inclusion needs to go beyond credit: there is a near-universal need for safe and secure savings and payment products and international remittance payment systems. While several emerging markets have demonstrated national commitment and urgency to advancing inclusion, more remains to be done, especially at the global level. Inclusion needs to leverage all service providers, as well as recent innovations that deliver services outside bank branches. Financial inclusion must happen in a responsible manner, with appropriate consumer protection regulations, industry practices, and financial literacy efforts. To make progress and build the foundations for sustainable growth, the presenter recommended that the G-20 convene a global partnership with the relevant stakeholders around a common global financial goal. Implementation would focus on policies, financial infrastructure, delivery mechanisms, products, responsible finance, and data. The G-20 is in a unique position to bring together major drivers of finance—the financial services industry, national governments, the global development community, and centers for knowledge sharing—and complement implementation with political and policy leadership and the creation of a funding mechanism to support different needs of countries.

Discussants

Alfred Hannig, agreed on the importance of peer learning and involving non-G-20 countries and other stakeholders. AFI's experience points to an increasing openness and demand for technology solutions and for knowledge sharing, especially from country champions such as Brazil, Kenya, and the Philippines. He emphasized the importance of policies, consumer protection, and data and measurement. Drawing on insights from an AFI survey, Dr. Haning recommended a new “polylateral development” approach. Possible actions include financial inclusion targets self-set by countries and new funding mechanisms that can serve the different needs of countries.

Yongbeom Kim, underscored the importance of financial inclusion in the G-20 context of recovery, financial stability and economic growth, and the way forward to the Seoul Summit. He stressed the role of government and the policy environment and shared insights from the Korean experience on microinsurance. Mr. Kim concluded by welcoming the idea of the global partnership for financial inclusion, and ensured Korea's full commitment in delivering concrete outcomes at the Seoul Summit.

Key Issues Raised in Discussion

- *The role of the G-20.* The G-20 is in a unique position to compel action by convening stakeholders, providing political and policy support for national goals, and providing adequate resources for financial infrastructure, technical assistance, and peer-to-peer learning. The G-20 should focus on issues that need strong international cooperation and leadership, including monitoring overall progress, and not duplicate existing efforts.
- *The role of government.* Governments can advance inclusion through policies, regulations, and the enabling environment, and by supporting innovative business models. Public-private partnerships are key to advancing the financial inclusion agenda.
- *Inclusion goals.* Bottom-up and top-town approaches to target-setting have different advantages to motivate progress. Many global targets have faced difficulties in implementation. To be successful, implementation requires country-specific targets and working groups, coordination and engagement of all stakeholders, conducive policy environments, and funding.
- *Approaches for advancing financial inclusion.* Diversity of approaches and delivery means is essential. Solutions need to be sustainable and provide accessible and affordable financial products that poor clients and SMEs need.
- *Best practices and learning.* There was widespread agreement that developing a successful global mechanism for cross-country learning is important.

Concluding the session by underscoring the importance of G-20 leadership, I noted that financial inclusion requires long-term commitment by all the stakeholders. The policy environment, public-private partnerships, and funds to support infrastructure and peer learning are all important for advancing inclusion. Three issues merit particular attention: savings, rural finance, and insurance. I reminded advocates to engage all the stakeholders who can deliver these and other needed services and improve financial inclusion, including policy makers, financial institutions of all kinds, mobile phone operators, the rural sector, investors, multilateral agencies, and nongovernmental organizations.

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