Financial Inclusion Research Conference 2013

Bridging the Gap: How can banks reach the unbanked?

The SWIFT Institute

Conference Summary

The SWIFT Institute is dedicated to fostering research and disseminating knowledge and information about the financial services industry.

The Institute funds and publishes independent research and brings together academics and practitioners to inform, debate and learn from each other.

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The SWIFT Institute, in partnership with the Ash Center for Democratic Governance and Innovation and the Mossavar-Rahmani Center for Business and Government, held its first conference at the John F. Kennedy School of Government at Harvard Kennedy School on Thursday, February 28 and Friday, March 1, 2013. The topic was financial inclusion, and several academics presented their research findings to an audience of commercial bankers, central bankers, regulatory experts and other financial industry specialists.

HARVARD Kennedy School
JOHN F. KENNEDY SCHOOL OF GOVERNMENT

HARVARD Kennedy School
ASH CENTER
for Democratic Governance and Innovation

HARVARD Kennedy School
MOSSAVAR-RAHMANI CENTER
for Business and Government 30 YEARS

In a keynote dinner speech on Thursday evening, **Dr Guillermo Ortiz, Chairman of the Board, Grupo Financiero Banorte, and member of the SWIFT Institute's Advisory Council, said financial inclusion was «a fundamental issue in terms of economic growth and a basic concern for poverty alleviation».** A key theme running throughout his speech was that the strategy of importing existing models to provide specific financial services is unlikely to advance the financial inclusion agenda successfully.

Download Dr Guillermo Ortiz speech

Financial inclusion has been widely researched, yet many questions are unanswered, and how to structure the financial system to include the excluded in an appropriate and cost-effective way is unclear. **It is thought that nearly three billion people worldwide do not have access to a bank account or any formal banking services**, and many more of the world's poor who do have a bank account either rarely or never use it. The majority of the unbanked population is located in low-income countries, so while this is predominantly a developing world problem, there are also significant numbers of excluded or unbanked adults in developed regions, including Europe and North America. **For the unbanked it is a challenge to gain access to banks and the services they offer.** For banks it is a challenge to reach the unbanked.

Elisabeth Rhyne, Managing Director of the Center for Financial Inclusion at Accion, has looked in depth at the informal money management models of the poor and found that their financial requirements are complex and often involve many cash transactions of small amounts. There is no bank account hub at the centre of their money management model, but often a 'pocket' system, where money is kept in different places according to its intended use. She doubted that having a bank account would encourage an entire set of money management habits to change, but recognised that the pocket system would not be sufficient for handling higher level of economic activity as someone becomes better off.

Download Elizabeth Rhyne presentation

Financial institutions need to consider informal services as their competition, proposed Professor Guy Stuart of the Harvard Kennedy School, and to think about what value could be offered to a low income customer. Timothy Ogden, of the Financial Access Initiative, continued this thought by asking what is wrong with banking products and services that they are so much worse than the informal models : why would someone prefer to take a remittance in cash than via a bank account ? Ruth Goodwin-Groen, of UN Better than Cash Alliance, stressed the importance of looking at the wider picture other than simply 'poor', and include other variables such as religion and cultural differences, India/Africa, rural/urban, or men/women when assessing the needs of the financially excluded — they vary greatly and a 'one-size-fits-all' approach is clearly very difficult to apply.

Rodger Voorhies, Director of Financial Services for the Poor at the Bill & Melinda Gates Foundation, suggested that the « if only we knew more » approach to understanding the behaviour of the poor may not be all that helpful in helping us address financial inclusion, because poor people are as irrational in their behaviour as anyone else. Picking up on this point, Ros Grady, Conjoint Professor and CEO of the Centre for International Finance and Regulation, emphasized the importance of financial education and helping people to understand what financial products can do to help improve their financial situation.

Link to Rodger Voorhies presentation

Leila Rispens-Noel, of the WIMLER Foundation in Hong Kong, focused on the financial arrangements of the migrant workers of South East Asia and the Middle East who send money home to their families, and she, too, highlighted the importance of financial literacy. The culture of dependency on migrant workers can last a long time, and the families at home receiving the money need to understand why they are saving, and for what. She said there needs to be a more determined effort in this area, as a three-hour training session is not enough to change deeply ingrained financial habits, and more importantly to reach a stage where the cycle of dependency on a migrant worker can be broken.

Link to Leila Rispens-Noel presentation

Although the unbanked population is a large and relatively untapped market, it is not easy for banks to make smooth inroads into this space. As the banking industry becomes more tightly regulated, and 'know your customer' processes are long-term investments and expensive to implement, there is a danger that banks will avoid the risk of getting involved with the unbanked altogether. It is difficult to balance outreach to the unbanked with the need for banks to be safe and sound. The irony of this can be seen in the remittances business, particularly in the Middle East, where the challenge is to keep payments flowing through official channels. Cost is another issue for banks: the poor do not want to pay transaction fees but neither do the banks. Mobile services have emerged strongly in parts of Africa as a low-cost way of managing money and making payments, and these present both opportunities and challenges for banks. Mobile transaction costs are lower than traditional banking transaction costs, but mobile services are able to exist completely outside the established financial sector making it difficult to integrate with other financial services offered by banks. This raises the question; at what point should mobile payments come into the regulatory environment?

Jay Rosengard, Director of the Harvard Kennedy School's Financial Sector Program closed the day by acknowledging the growing consensus of the positive relationship between financial sector development, economic growth, and poverty alleviation.

Link to Jay Rosengard presentation

The challenge facing banks is to identify the point of convergence between their need to make money and consumers who want to be able to use a financial service that's meaningful in the context of their lives.

All papers and presentations discussed at the conference can be downloaded at http://www.swiftinstitute.org/papers/

Speakers

- Dr. Guillermo Ortiz, Chairman Grupo Financiero Banorte-IXE, Member of G30 and Member of the SWIFT Institute Advisory Council
- Yawar Shah, Chief Operating Officer — Customer Intelligence Citibank, Chairman of the SWIFT Board and Member of the SWIFT Institute Advisory Council
- Guy Stuart, Harvard Kennedy School, Ash Center for Democratic Governance & Innovation
- Elisabeth Rhyne, Center for Financial Inclusion at Accion
- Guy Stuart, Harvard Kennedy School, Ash Center for Democratic Governance & Innovation
- Kurt von Mettenheim & Lauro Gonzalez, São Paulo Business School
- Savita Shankar, Asian Institute of Management
- Leila Rispens-Noel, WIMLER Foundation
- Susan Johnson, University of Bath
- Jenny Aker, Fletcher School, Tufts University
- Xavier Giné, World Bank
- Ian Radcliffe, World Savings Banks Institute
- Rodger Voorhies, Bill & Melinda Gates Foundation
- Jay Rosengard, Harvard Kennedy School, Mossavar-Rahmani Center for Business and Government
- Gottfried Leibbrandt, Chief Executive Officer, SWIFT and Member of the SWIFT Institute Advisory Council

Areas impeding advances in financial inclusion

Financial inclusion has been widely researched, yet many questions are unanswered, and how to structure the financial system to include the excluded in an appropriate and cost-effective way is unclear. For the unbanked it is a challenge to gain access to banks and the services they offer. For banks it is a challenge to reach the unbanked.

The conference highlighted the following areas which are currently impeding advances in financial inclusion:

Education

Raising levels of financial literacy is important on several fronts: the poor need a better understanding of how more structured banking/financial services can improve their lives; banks need to ensure their staff can explain complex products to people not familiar with the banking world, and even more fundamentally, banks need to educate themselves on what the poor actually want and will benefit from. Specific points arising from the conference were:

- Financial literacy should be included for the wives of migrant workers. They need to understand the value of saving, and appreciate what they are saving for.
- The poor need to be encouraged to stay committed to their savings goals, and this is likely to require a change in some quite deep-seated habits and thinking. Often when poor people receive a windfall, they become very generous and give it away to family and friends.
- Banks need to communicate simply what the products can do… money management education is required.
- In the case of migrant workers, individuals need to understand how money can improve their lives so the cycle of dependency can break and workers can return to their families.
- Training also applies to bank staff. Often they do not know the range of products and what may best suit someone's needs. Banking services can be very complex. If the bank staff do not understand well enough to explain, it is even harder for the customer to understand if a product/service is right for them.

Banking solutions

The banking sector must understand that the needs of the poor may not be in tune with the products and services that are currently provided.

The market for services to the poor is a big, untapped space but **the poor in one part of the world are likely to have different outlooks and needs than the poor in another part of the world — one size definitely does not fit all.**

- Research suggests that the needs of the poor are not being met, not that they do not have need of financial services.
- Are financial services, such as payments via mobile phones, an end in themselves or simply a means to a larger objective of real financial inclusion as measured by access to financial services to increase income, accumulate assets, and improved living standards? If the latter, **the challenge is to develop bridges that link formal financial services entry points to full engagement with the formal financial sector**.
- Banks like long-term relationships and need to see the segment as a long-term investment.
- In many poor areas the social networks surrounding informal financial systems are very strong. Banks need to offer smaller loans to be useful.
- **KYC (Know your clients): can be an issue in that the poor do not have the adequate levels of identification and paperwork required by banks to open an account.**

- Banks are not really interested in no-frills services for the poor. They need to look at the 'value proposition' point of view. Banks want to make money and consumers wants to improve their lives: where is the point of convergence?
- Should financial inclusion compete with the informal service? Banks need to think of informal services as their competition. What value does a financial institution add to a low income consumer? What is it about traditional banking services that make them less attractive than the informal arrangements?
- Banks are focusing on finance which is very narrow as people move money between different resources/uses. Putting money into livestock, for example, could be better than holding cash because it can multiply quickly… the returns can often be greater in another resource.
- Many accounts have been opened in the name of financial inclusion, but then left dormant. Why are dormant accounts not used? Is it to do with the service offered? Are the accounts the right ones? Has there been a lack of educational follow-up on how to use the account?
- **The cost of transactions is high. The poor do not want to pay these costs which can mount up quickly, especially if they make lots of small, low-value transactions.**
- Remittances are a big business in many parts of the world and a lifeline for many families… banks should make it their social mission to help migrant workers. They don't have a plan and they don't know when they will have saved enough to return home.

- Mobile money lowers transaction costs for banks, but requires lots of trust issues for the client. They have to trust in an SMS instead of a receipt and remember their PIN. These can be difficult concepts for people with low levels of literacy.
- How do can people send their money home to a rural village in the Philippines, a specific one… not just 'the Philippines'?

Communication

Banks need to reassess how they communicate their complicated products. They should focus on what people need to know rather than what the banks want to communicate, and there is often a 'disconnect' between the two.

- Communication can be something very simple… sophisticated marketing campaigns are often not necessary.

Regulation/Risk

As the banking industry becomes more tightly regulated, and 'know your customer' processes are long-term investments and expensive to implement, banks have to balance the risk of getting involved with the unbanked with their obligations to be compliant and safe.

- **Cash management, risk management and asset accumulation are the three main issues facing those on a low income/or unbanked. They have complex financial lives.** They handle real cash often, while most of the transactions of the banked are digital. Their incomes are more volatile and they handle more risk than the banked. They are interested in building assets but face risks there too.
- In the UAE, remittances are beginning to flow through non-official channels. With increasing regulation, the banks may choose not to get involved. This business may move further away from the banks to a less regulated space.
- There is no 'one-size-fits-all' model. Public policy and financial inclusion are very strongly related in many countries.

Cultural

The 'poor' of the world is not an easy, homogenous group that can be treated with one approach. There are many factors such as country, region, country, gender and age that must be taken into account to understand the needs so that banks can tailor their offering. Also, financial arrangements in some parts of the world are closely linked to social structures, and the poor expect advice and social contact as a 'package' with their financial assistance.

- Lots of people have bank accounts but the percentage of active accounts is quite low globally… about 7%. The percentage rises in the developed world. Why do we care about banking the unbanked? Is the number of bank accounts a meaningful measure of banked/unbanked?
- We need to look at what inclusion already does for the included. Currently there is a gap between interventions and aspirations and that comes from not thinking about the already included.
- Financial inclusion should focus on money management (MM). MM should include the 'doing'…the actual transactions, and the 'thinking' that leads to the transactions. The poor have complex financial requirements and make many transactions. Often the MM system could be as informal as a pocket for this and a pocket for that. The MM system of the included is more formal and usually based around a bank account. All transactions (mortgage; pension; credit card; ATM withdrawals, etc.) are linked to a bank account.
- Does getting a bank account move someone from one MM system to another, and what else would lead someone to move from one MM system to another?
- The transactions of the poor would not change all at once (savings, loans, wage advance, cash in hand, shopkeeper credit). What would make the poor interested in the transition?
- Poor people are as irrational as anyone<. It's difficult to get people to behave rationally in an irrational context.
- In the UAE, people want to see the physical cash, not stored value on a card.
- Who are the unbanked? Banks need to help migrant workers because they make a big difference to the economy in some countries
- Often informal services connected with social interactions. People value the social aspects… advice, conversation, relationships.
- Often financial interactions (e.g. loans) with a social context act as an insurance for the future… « If I lend to you now, you might lend to me when I need it. »