How innovation drives financial inclusion

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At a time when the world's two largest economies are engaged in a destructive quest to limit trade between people, any evidence of the benefits impact of globalisation cannot come soon enough.

Recently, we got just such an illustration in the form of the World Bank's Findex report on global financial inclusion. The report is a detailed survey of the banking, saving and borrowing patterns of households in 140 countries. It covers developed and developing nations, rich and poor, women and men, tracing progress in the expansion of access to financial services.

Ready availability of reliable banking and payments facilities is essential for human flourishing. Contrary to what one might think, it is not for the rich and highly educated that these services are most important. Small-scale farmers, migrant workers and budding entrepreneurs in frontier markets depend critically on cheap and transparent payments and credit systems, as they have few alternative employment options and usually have meagre funds of their own.

Without basic financial services, the way of life of these people would be compromised and their living standards would decline.

It is therefore an auspicious development that the six years between the first (2011) and third (2017) editions of the Findex report have seen significant increases in the percentage of the world's population with mobile money or bank accounts. Sixty-nine per cent of adults worldwide now use one or both of those services, compared to 51 per cent at the start of the decade.

Nowhere has the recent spread of financial services occurred most visibly than in emerging markets. While the share of adults owning accounts in these countries, at 63 per cent, remains far below their high-income counterparts, it stood at just 40 per cent six years ago. This rate of growth is remarkable even when compared to other measures of global development, such as the reduction of extreme poverty and the fight against communicable diseases, on which we have made great strides in recent decades.

One trend more than any other helps to explain the recent progress of financial inclusion, namely the expansion of mobile banking and payments.

The revolutionary effects of M-Pesa in Kenya are already relatively well-known. Since its introduction in 2007, this mobile money payments system has more than halved the cost of fund transfers and cut processing times from hours to a few minutes or seconds. M-Pesa has forced incumbent money transmitting services such as Western Union to slash their fees. It has also

introduced millions of Kenyans to the formal finance sector, facilitating access to bank and savings accounts.

The extent to which other economies in sub-Saharan Africa have rushed to follow in Kenya's footsteps is often not fully recognised, yet the Findex report bears it out. Since 2011, half a dozen countries, including Ghana, Nigeria, Senegal and Tanzania, have more than 40 per cent of adults with a mobile money or bank account.

Financial technology is also having a marked impact on the emancipation of women in societies that have tended to be highly patriarchal.

Aside from considerations of empowerment and autonomy, there are obvious practical reasons to want women to have access to finance. As well as making up half the adult population, they are chiefly in charge of household decisions and the raising of children, so financially active and literate women have a positive impact on the wellbeing of those around them.

And women who own a bank account can save and build businesses independently from their husbands and fathers. In communities that are traditionally averse to enterprise, giving access to financial services to the few – including women – with entrepreneurial ambition can accelerate development.

The spread of innovative banking and payments provision gives cause for celebration. Yet, just as the developing world gallops towards financial inclusion, Western countries are making it harder for their own people to borrow, save and invest.

America provides perhaps the starkest illustration. As of 2015, 7 per cent of U.S. households, nine million of them, did not have a bank account. An additional 19.9 per cent were "underbanked" in that they had to resort to alternative (usually higher-cost) providers for credit and other banking services.

Experts disagree on the drivers behind the scale of America's unbanked problem. A paper published last week by the Kansas City Federal Reserve Bank finds that income, education, employment and race all predict one's likelihood of using basic banking services. Indeed, as Lisa Servon shows in her illuminating book The Unbanking of America, the poor and minorities often prefer to use alternative financial services because they find them more transparent, more accessible and even more respectful than banks are to them. But this convenience has a price, and it's sometimes steep.

The Kansas Fed researchers also find a strong correlation between internet connectivity and access to banking. While this relationship may reflect the general marginalisation of a fraction of the population who are poor, unbanked and unconnected, it points to the increasing importance of technology for securing access to financial services, even in mature markets.

But too often regulation stands in the way of innovation-led financial inclusion. The Federal Deposit Insurance Corporation, a key U.S. bank regulator, has dragged its feet since 2008 on issuing new bank licenses. Similarly, a promised nationwide charter that could lower barriers for

new fintech platforms has been slow to materialise. Innovation in payments in the M-Pesa mould is hampered by disparate money transfer rules across the 50 states.

Poor people's access to banking is also hampered by a growing mire of anti-money laundering laws that threaten to turn ordinary citizens into felons, and by rules aimed at protecting consumers that make serving some of them uneconomical for banks. In the UK, the Financial Conduct Authority's proposed cap on overdraft charges, which had been shelved but is now again under consideration, would almost certainly have this effect. Indeed, similar measures against payday loans have shut out hundreds of thousands of borrowers from that market.

Rich countries should take their lead from emerging markets and let innovation drive financial inclusion. Unless countries remove regulatory barriers to account ownership, they risk the poorest falling ever further behind. The political and social consequences of that would be dire.

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