

Financial Inclusion

Key to Sustainable Development & Climate Change Adaptation

ISAP 2016



Key messages

- *Financial inclusion, which aims to provide appropriate financial services to disadvantaged and economically marginalised segments of society, contributes to both sustainable development and climate change adaptation.*
- *The creation of enabling regulatory frameworks, guidelines and supportive infrastructure by governments is key to the further development and extension of appropriate financial services for the poor.*
- *Delivering appropriate financial services to poor households requires novel delivery methods and products. In Bangladesh, non-governmental organisations that have developed strong trust relationships with the communities and have an organisational culture of experimentation and learning have proved effective actors for designing and delivering all types of microfinance services.*
- *Customisation and diversification of financial products, as well as the packaging of financial with non-financial services, such as skills training (microfinance-plus), will yield greater benefits for participants in microfinance schemes.*
- *As the impacts of climate change and vulnerability differ from one area to the next, continual location-specific action research is needed in areas vulnerable to the impacts of climate change to develop new packages of financial and non-financial services that support resilience building and adaptation. How financial inclusion can best be integrated into local and national level adaptation strategies also needs to be studied.*

Henry Scheyvens

1. Introduction: What is financial inclusion?

Financial inclusion means that all segments of society have access to and are able to effectively use financial services. Efforts to promote financial inclusion focus on disadvantaged and low-income segments of society, as they mostly account for the estimated two billion working-age adults globally who have no access to formal financial services. In developing countries, many people do not have savings accounts, have never received credit from a bank, and hold no insurance policies. Some people have never walked through the doors of a bank. They typically are unable to access formal financial services due to a combination of factors, including cultural norms that act against them (for example, discrimination towards poor people and women), lack of legal identity, low literacy (particularly financial literacy), inability to meet loan eligibility criteria, and for some people the long distances they would have to travel to reach the local bank branches (UN, 2006).

Microfinance is financial services specifically design for and delivered to low income households and as such is a key part of the global financial inclusion agenda. Microfinance programmes targeting the rural poor

use criteria such as maximum size of landholdings and maximum value of total household assets as thresholds for identifying poor households who are eligible to participate in their programmes. These eligibility criteria are opposite in nature to the loan criteria used in conventional banking, which are usually based around ability to repay and the amount of collateral held by the borrower.

Financial inclusion programmes provide a wide range of *financial products* that are relevant to poor people and small businesses, including credit, savings, insurance, and support for payments. These types of services are also common in conventional banking, but the size of the transactions involved are on average much smaller. A first loan could be less than 500 USD, and average savings held by members could be less than 1,000 USD.



Microfinance scheme members at weekly meeting

Financial inclusion programmes are also distinct from conventional financial services in terms of the providers and delivery systems. The providers include public, private and non-for-profit organisations, such as microfinance institutions (MFIs), credit unions, traditional banks, and mobile phone companies or mobile network operators. The *delivery systems* used by MFIs are often distinctive. A common approach is to organise groups of low income households who meet weekly in their villages with field officers to deposit savings, repay loans, request new loans and receive technical guidance on their investments.

Many MFIs package their financial services with non-financial services to promote particular income generating activities as part of their development programmes. For example, in Bangladesh some MFIs promote homestead-based dairying by providing loans for their members to purchase cows, insurance to cover any unexpected death of the animals, training on growing grasses for feed and on construction of sheds to house the animals, etc., and veterinary services. Many NGO-MFIs also provide education, health, disaster relief and recovery and other services in line with their development missions.



Homestead-based dairy farming supported under NGO microfinance programme, Dhamrai, Bangladesh



2. The SDGs and the Paris Agreement: Financial inclusion as a target and enabler

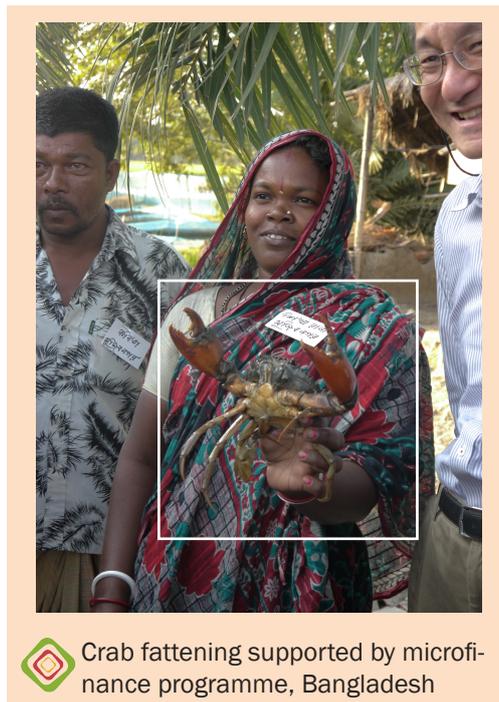
Financial inclusion is important both to the United Nations sustainable development goals (SDGs) and the Paris Agreement on climate change. As explained in Table 1, financial inclusion is explicitly mentioned in targets under SDG1, SDG2, SDG5 and SDG8. While not explicitly identified in their targets, microfinance could also be a key enabler for SDG3 and SDG4, and potentially relevant to SDG7, SDG10, SDG13 and SDG16.

Financial inclusion is not explicitly mentioned in the Paris Agreement, which sets out the agreed global agenda on climate change action, but is highly relevant to its aim to increase the ability to adapt to the adverse impacts

Table 1. Relevance of financial inclusion to the SDGs

Goal	Relevance of financial inclusion
 1 NO POVERTY	SDG 1 “End poverty in all its forms everywhere” explicitly recognises the importance of financial inclusion. Its targets includes all men and women, in particular the poor and the vulnerable, having access to financial services by 2030.
 2 ZERO HUNGER	Financial services are explicitly recognised in the SDG2 target to double agricultural productivity and incomes of small-scale food producers. Around the world, millions of rural households are participating in microfinance programmes that combine financial support, technical training and other services that enable them to invest in livestock rearing, aquaculture, crop cultivation, as well as the processing of agricultural products.
 3 GOOD HEALTH AND WELL-BEING	Financial inclusion is an enabler for SDG3 “Ensure healthy lives and promote well-being for all at all ages.” Many MFIs provide health services at low cost or free of charge to their members, and some offer health insurance and run their own medical centres. Financial inclusion supports Goal 4 “Ensure inclusive and equitable quality education and promote lifelong learning opportunities for all” directly through the educational scholarships provided by some MFIs and indirectly by helping households save for future education expenses.
 4 QUALITY EDUCATION	
 5 GENDER EQUALITY	Financial inclusion is particularly significant to SDG5 “Achieve gender equality and empower all women and girls” and its target to give women access to financial services. About 85% of the poorest clients of microfinance programmes are women (ILO, 2008). Access to financial services can raise the status of women in their households and give them greater control over their financial resources. This also benefits other SDGs, as an observation across many countries is that the financial resources controlled by women are more likely to be spent on household necessities and education than those controlled by men.
 8 DECENT WORK AND ECONOMIC GROWTH	Access to financial services to support the growth of micro-, small- and medium-sized enterprises appears in one of the targets for SDG8 on inclusive economic growth. In some countries there is a trend within the microfinance sector towards providing larger loans for small and medium-scale enterprises as borrowers “graduate” from poverty.
OTHER GOALS	Financial inclusion is relevant to other SDGs. For example, some companies allow off-grid households to pay for portable solar lights in instalments using a PAYGO model, which supports SDG7 on access to affordable, reliable, sustainable and modern energy. Access to financial services can also conceivably contribute to SDG10 on reducing inequalities, and in doing so reduce conflict and promote peace (SDG16), and SDG13 on climate change action.

of climate change and foster climate resilience; an aim shared by SDG13 on climate change action. Microfinance is common in climate-sensitive sectors such as agriculture and is delivered at the levels at which most adaptation actions will take place, i.e. individuals, households and communities (Agrawala & Carraro, 2010). It can increase the options available to these decisions and can also potentially build resilience by enabling households to diversify their income sources, accumulate assets, have access to appropriate financing when disaster strikes and to insure their health, lives, property and incomes. Microfinance could also be packaged with information, methods and technologies that enable households to adapt to altered conditions because of climate change, e.g. households in areas affected by salinisation due to sea level rise could be provided loans to cultivate salt-tolerant crop varieties and invest in aquaculture.



 Crab fattening supported by microfinance programme, Bangladesh

impacted coping and recovery in response to three catastrophic cyclones – Sidr, Aila, and Mahasen – that struck south-western Bangladesh in 2007, 2009 and 2013, respectively. The data for this study were collected through a sample survey conducted in February and March 2014 by InM. A total of 3,687 households in three districts – Khulna, Patuakhali and Satkhira – were surveyed. Some of the surveyed households had access to microfinance (emergency loans, microcredit and microsavings) through PKSF’s Programmed Initiatives for Monga Eradication (PRIME) programme. The study found that access to microfinance through PRIME assisted households with their recovery. Twice as many PRIME households as non-PRIME households were able to use current income and savings for coping. Conversely, more non-PRIME households placed themselves at risk by resorting to informal loans. The study also

found that impacts on poverty reduction and resilience building were greatest when households had access to savings, credit and insurance services, rather than just to credit, and when microfinance was provided as part of a support package that included non-financial interventions (Khan, Khalily, & Scheyvens, 2015b).

3. Generating new knowledge

There is a rich and continuously growing literature on microfinance; however, only a few studies have explicitly examined the links between microfinance and adaptation. The Institute for Global Environmental Strategies (IGES) and the Institute of Microfinance (InM) launched a collaborative research programme in 2012 to explore these links. Two of the studies investigated the impact of access to microfinance provided by local MFIs that are supported by the Palli Karma-Sahayak Foundation (PKSF), the largest microfinance wholesaler in Bangladesh, on the strategies used by poor households to cope with climate-related shocks and stresses. One study used survey data of 480,918 poor households in Greater Rangpur in north-western Bangladesh to investigate whether access to microfinance prior to a period of hardship known as *monga* had any impact on the coping strategies employed by the households. *Monga* is a period in the agricultural season when there is a near famine situation due to low demand for labour. The study found that without access to finance, households were more likely to resort to coping strategies that put their long-term welfare at risk. These included selling labour in advance, selling assets and borrowing at high rates of interest from informal lenders (Khan, Khalily, & Scheyvens, 2015a).

A second study examined how access to microfinance

4. From knowledge to action

Financial inclusion programmes and the legal frameworks under which they operate are being strengthened to reflect the knowledge generated by research, lessons accumulated through practice, and the emergence of new technologies. Key focus areas to advance financial inclusion include:

- **Regulation and infrastructure:** Governments have critical roles to play in financial inclusion, including constructing enabling regulatory environments, developing guidelines and providing risk management infrastructure, such as enhanced weather and data information.
- **Digital services:** Making use of digital services such as cellular networks could significantly increase the accessibility and use of financial services by increasing the ease of transactions, enabling greater customization of products, reducing transaction costs and increasing access to information relevant to business development.
- **Product development:** The needs and opportunities of poor households may sometimes be

assumed rather than fully understood by the organizations that set out to assist them. Investing in generating a better understanding of client needs and diversification of products to reflect these needs is an important issue for the global financial inclusion agenda. Product diversification can mean providing both flexible and commitment savings options, not only small loans but also larger loans for small and medium-scale enterprises as borrowers “graduate” from poverty, and loans with variable terms to reflect actual investment opportunities, e.g. seasonal loans for crop agriculture, etc.

- **Insurance services:** As poor households are often unable to escape from poverty because of “shocks”, e.g. the main breadwinner of the household suddenly falls ill or the household’s property is all lost because of a natural calamity, etc., there are high expectations that risk insurance services can contribute to both poverty reduction and adaptation. Supportive regulatory frameworks, reinsurance and alternative providers as well as novel delivery mechanisms and products, such as index insurance, are needed, as poor households are highly exposed and sensitive to shocks yet have low ability to pay insurance premiums. It is also important that insurance services incentivize other risk migration strategies, e.g. premiums can be reduced for farmers who employ methods to reduce risks to crops and livestock.
- **Adaptation strategies and action research:** Adaptation is a continual process, which means that individuals, households and communities need ongoing access to supportive services. These services include access to climate and weather information, information on methods for adjusting their livelihood activities to reflect changing climate conditions and climate risks, and access to the financial services necessary for them to take action. The role of financial services in adaptation thus needs to be contextualized within strategic frameworks at national and local government levels that recognize and coordinate all the various measures and instruments that support adaptation, including financial services. As the impacts of climate change and vulnerability differ from one area to the next, continual location-specific action research is needed to develop new packages of financial and non-financial services that support resilience building and adaptation.

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