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Impact of access to financial services, including by highlighting remittances on development: Economic empowerment of women and youth

Note by the UNCTAD secretariat

Executive summary

As the international community is set to define a post-2015 development framework for sustainable development, financial inclusion has become an important item on the international policy agenda. Financial inclusion can contribute to poverty reduction, economic and social development, and financial stability. Physical, economic, regulatory and cultural factors underpin the lack of access to financial services. The poor, women, youth, the rural population and those in the informal economy are particularly affected. The use of new technology and innovative business models that help overcome barriers to such access could contribute to improved inclusion.

As highlighted by major international summits and platforms, such as the United Nations High-level Dialogue on International Migration and Development, remittances could be turned into a promising source of demand for financial services and contribute significantly to financial inclusion. This will require reducing the transaction costs of remittance transfers to ensure facilitated, safer and speedier transfers, including through the development of new financial products.

Governments have an important role to play in implementing well-designed comprehensive policies. These include setting up sound regulatory frameworks and providing incentives for extending the supply and affordability of services, as well as creating an expanded demand for financial services, such as through financial education and consumer empowerment.

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Introduction

1. Financial inclusion has become a key item on the international policy agenda as the international community moves towards a post-2015 development framework and sustainable development goals. Its importance for sustainable development has been increasingly recognized by international forums such as the Group of 20 (G20), where financial inclusion is incorporated into the financial regulatory and supervisory agenda, with specific targets and goals being set. Interest in financial inclusion also emerged from the post-crisis financial regulatory reform efforts wherein financial inclusion is increasingly recognized as an essential component of financial stability and prudential regulation. For those economies that depend heavily on remittances, financial inclusion matters in maximizing the developmental impact of remittances by formalizing the remittance flows, reducing the costs of transfer and channelling remittances into productive activities through the banking system.

I. Trends and issues in financial inclusion

Recent developments in financial services

2. Financial services play a pivotal role in the functioning of markets and the economy and contribute to economic and social development. The importance of financial services for the economy is manifold. As infrastructure services, financial services have meaningful linkages with the economy at large, providing valuable inputs for activities in the primary, industrial and tertiary sectors, and for individuals as well. Through a variety of banking, securities and insurance services, financial services facilitate domestic and international transactions, mobilize and channel domestic savings and broaden the availability of credit for small and medium-sized enterprises (SMEs) and households. Trade is also facilitated not only by a more friendly business environment but also by specific products such as letters of credit and insurance.[1]

3. As an economic services industry in its own right, financial services contribute to output and employment. Commercial banking revenue is estimated to have grown 4.2 per cent in 2013, with a modest average annual growth of 1.3 per cent, to about $3.5 trillion between 2008 and 2013.[2] Several activities within financial services have high value added and require qualified jobs. Financial services typically have grown faster than gross domestic product (GDP) in the pre-crisis period (figure 1). In countries of the Organization for Economic Cooperation and Development (OECD), financial services grew at an average annual rate of 6.3 per cent between 2001 and 2012, faster than the overall services sector and GDP.[3] While attaining impressive heights before the global crisis, the growth rate declined significantly after the crisis.

UNCTAD, 2007, Trade and development implications of financial services, TD/B/COM.1/EM.33/3, 3 August.

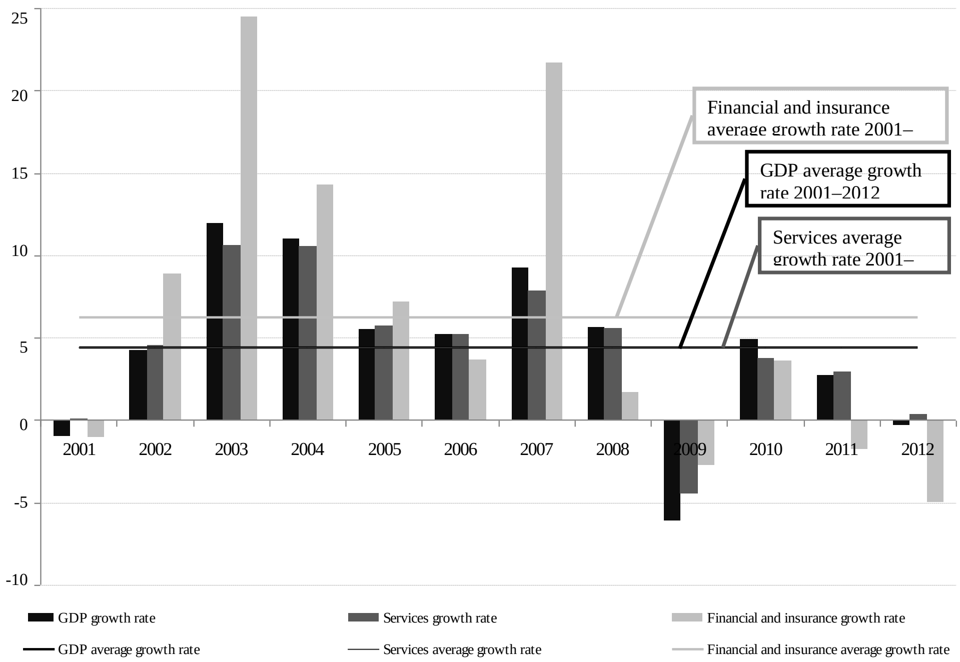
UNCTAD, 2014, Services, development and trade: The regulatory and institutional dimension, TD/B/C.I/MEM.4/5, 3 February.

OECD statistical database.

Figure 1

Annual change in gross domestic product, services, and financial and insurance services in countries of the Organization for Economic Cooperation and Development, 2001–2012

(Percentage)



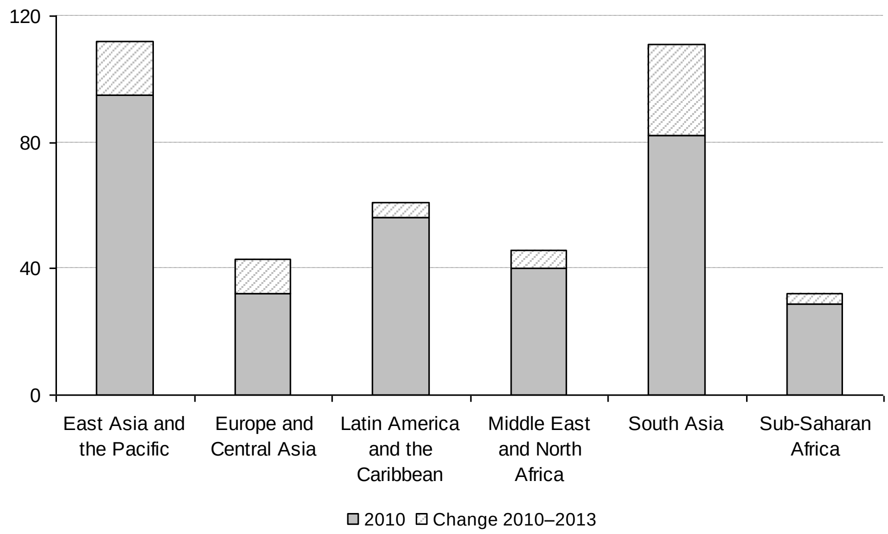
Source: OECD.

4. Increased international financial flows and transactions have become an essential component of the sector, highlighting the importance of the international dimension in the provision of basic financial services. Developing countries are net importers of financial services, with global exports largely dominated by developed countries, although some developing countries have recently expanded their presence. This points to the importance of factoring in the foreign supply of financial services into measures aimed at expanding access to financial services to individuals and firms. Cross-border exports in financial services reached $445 billion in 2013, with an annual growth rate of 10 per cent between 2000 and 2013. Developed countries account for 80 per cent of global exports of financial services, which stood at $357 billion in 2013. The same year, the share of developing countries was 19 per cent, or $85 billion, the highest share since 2000, with exports having expanded at an annual growth rate of 12 per cent, outpacing that of developed countries (10 per cent).

5. Developing Asia, boasting $68 billion worth of exports of financial services in 2013, accounts for nearly 80 per cent of the exports of developing countries. There is heterogeneity among developing economies, with the top 10 developing exporters of financial services accounting for over 87 per cent of the total exports of developing countries. Between 2000 and 2013, financial services in developing countries grew faster than the overall services sector.

6. International remittance flows have been significant and growing, particularly to developing countries, and represent a major source of external finance for them. In 2013, global remittance flows reached $542 billion, of which $404 billion were to developing countries. Remittances are projected to rise to $680 billion by 2016.[4] This reflects the continued increase in the number of migrants. In 2013, there were 232 million international migrants, or 3.2 per cent of the world population, 48 per cent of which were women. This represents a significant increase from 175 million in 2000[5] and could rise to 405 million by 2050. South–South migration (36 per cent) is larger than South–North migration (35 per cent). Between 2010 and 2013, all developing regions witnessed growth in remittance inflows, with the largest change observed in South Asia (figure 2). In the least developed countries (LDCs), remittances accounted for over 4 per cent of GDP, larger than that of foreign direct investment in 2011.[6] Between 2003 and 2012, remittances grew faster than foreign direct investment and official development assistance in these economies, driven by the largest increase in Asian LDCs. The growth of remittance flows appears to be driven by the rapid economic growth in the receiving countries of migrants.

Figure 2
Evolution of remittances inflows into developing countries by region, 2010 and 2013
(Billion dollars)



Source: The World Bank (2014), Migration and Development Brief No. 22.

State of play in financial inclusion

7. Against the backdrop of the growing size and importance of the financial services, and a robust growth in international remittance flows, lack of access to financial services

[4] Ratha, S De, E Dervisevic, C Eigen-Zucchi, S Plaza, H Wyss, S Y, and SR Yousefi, 2014, Migration and remittances: Recent developments and outlook, Migration and Development Brief No. 22, World Bank.

[5] United Nations, Department of Economic and Social Affairs, 2013, Trends in international migrant stock: The 2013 revision – migrants by destination and origin, POP/DB/MIG/Stock/Rev.2013/Origin, December.

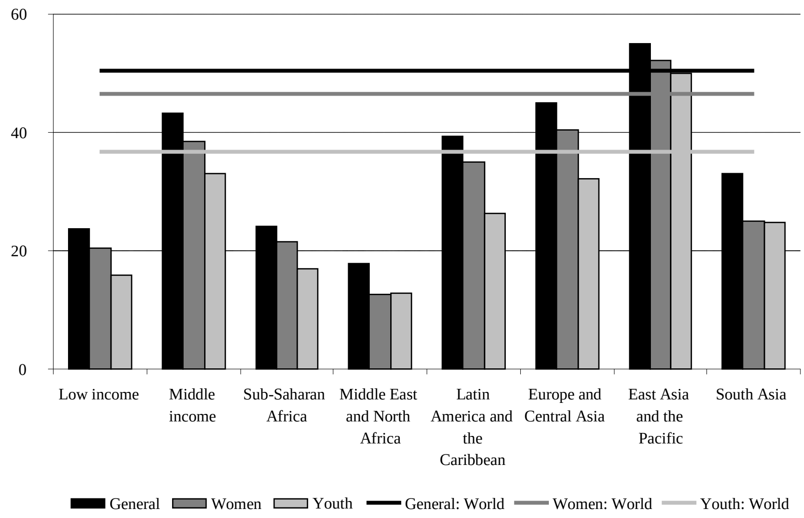
[6] *UNCTADStat* database.

represents a major impediment to income opportunities and the economic welfare of individuals, particularly for the poor, women and youth, as well as for firms, particularly SMEs and microenterprises. Financial inclusion is commonly defined as the proportion of individuals and firms that use financial services. It refers to a state in which all working age adults have effective access (convenient and responsible services delivery at affordable and sustainable cost to customers) to credit, savings, payments and insurance from formal providers.[7]

8. There is evidence that the poor benefit greatly from basic payments, savings, automated payments and insurance services. While research is being carried out on the better measurement of inclusion, density measurement is common. Statistics relating to the number of people having a bank account in a formal financial institution is particularly useful, as all formal financial activity is tied to accounts. There is a large variation in the degree of financial inclusion around the world. In 2011, only 50 per cent of people over 15 years of age held an account with a formal financial institution (figure 3). Over 2.5 billion adults – about half of the world's adult population – do not have a bank account. There are remarkable disparities in the use of financial services between developed and developing countries. The share of adults in developed countries that have an account with a formal financial institution is more than twice that of developing countries.

9. The level of financial inclusion varies widely among developing countries, by income groups and region. The degree of account penetration is associated with income levels, with middle-income countries registering twice as high a penetration ratio as low-income countries. Research suggests that the variation in account penetration rate is positively associated with income equality. East Asia and the Pacific stands out as the only region that registers an account penetration rate exceeding the global average. The Middle East and North Africa, and sub-Saharan Africa lag behind the global average.

Figure 3
Proportion of people with a formal bank account by income and region, 2011
(Percentage)



Source: UNCTAD computation based on the World Bank *Global Findex Database*.
Note: "General" includes people over 15, and "youth" includes people between 15 and 24.

[7] Global Partnership for Financial Inclusion, 2011, Global standard-setting bodies and financial inclusion for the poor: Towards proportionate standards and guidance, White Paper, October.

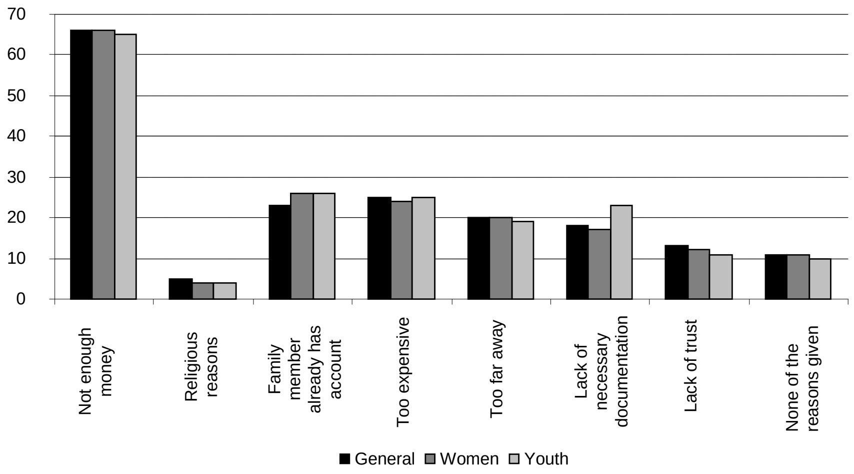
10. Within countries, a wide disparity is observable across gender and age groups, and geography. In all regions and income groups, the proportion of women with formal bank accounts is lower than that of both genders, and in most cases, youths have an even lower ratio. Globally, only 47 per cent of women and 37 per cent of youths hold a formal bank account, and again, East Asia and the Pacific stands out as the region surpassing the global average in both categories. The largest disparity between women and the total population is observed in South Asia. In contrast, in Latin America and the Caribbean, and in Europe and Central Asia, there is a larger difference between youth and all categories. Urban populations with higher population density have easier access to retail access points (bank offices, automatic teller machines (ATMs)) than rural populations.

11. For firms, the lack of access to finance is the biggest obstacle affecting SMEs, microenterprises and new firms in developing countries. Access to affordable finance is associated with innovation, job creation and growth. Three fourths of microenterprises and SMEs in the world are microenterprises, and 80 per cent of microenterprises and SMEs are informal. World Bank surveys find that only 34 per cent of firms in developing economies take out bank loans, compared with 51 per cent in developed economies. New firms, start-ups and services firms are particularly credit constrained, as lenders have little information on their performance or credit worthiness. Firms in the informal sector face major challenges in accessing finance, as many do not have bank accounts to run their business.

Obstacles to financial inclusion

12. Various factors affecting supply and demand of financial services inhibit the access of individuals and firms to financial services. While some of the unbanked people and firms exhibit no demand for accounts, most are excluded because of physical, economic, administrative and psychological barriers such as cost, travel distance, amount of documentation and lack of trust. Over 60 per cent of adults list the lack of disposable money as the reason for having no accounts; many consider that these barriers prevent their access to financial services (figure 4). These barriers tend to have a disproportionate effect on the poor, women, youth, rural populations, informal workers and migrants. Affordability of accounts is a major constraint, as fixed transaction costs with small amounts of transaction may disproportionately represent a heavy burden. Low bank branch penetration in rural areas could significantly increase the costs of access. Documentation requirements for opening an account may exclude workers in rural areas, the informal sector or migrants, owing to the lack of official pay slips, tax payments or proof of residence. Where financial sector is underdeveloped, people may not trust financial institutions, or their financial knowledge and literacy may be limited.

Figure 4
Self-reported barriers to use of formal accounts, 2011
(Percentage)



Source: Demirguc-Kunt et al. (2012), Measuring Financial Inclusion: The World Bank's Global Findex Database.

13. At a more structural level, the degree of financial sector development, market structure and regulatory framework affect financial inclusion. Financial services are characterized by market failures arising from information asymmetry and imperfect competition. When not adequately regulated, information asymmetry could result in an undersupply of credit to a particular population group and moral hazards causing excess supply and indebtedness. Imperfect competition could lead to market concentration, raising costs of finance and market segmentation, with resultant undersupply in rural areas and the poor. Undiversified financial sectors could be vulnerable to external shocks and disrupt stable supply. The existence of such market failures points to the importance of sound regulations, including the need to promote effective financial inclusion, universal access and competition.

14. The prevalence of regulation in the sector implies that government failure may occur with inadequate or excessive regulations acting as barriers to access to finance, preventing optimal provision of services. The Financial Services Authority of the United Kingdom of Great Britain and Northern Ireland identified some policies as having a deterrent effect on low-income population access to financial services, such as money-laundering regulations with stringent requirements on identity and proof of residence, saving and investment regulations creating bias against low-value customers and cash-based social security benefits depriving the need to use formal banking services. While policies are needed to ensure equitable and affordable access, these should be designed to minimize market distortion by striking a balance between efficiency and equity concerns.

II. Options to improve access to financial services

15. The major impediments to financial inclusion, which raise the actual and perceived transaction costs for individuals and firms to access finance, point to possible avenues for addressing such constraints. The use of new technology and innovative business models to improve the supply and outreach of financial services, and improved financial literacy and capacity by users appear among the most prominent avenues. Extension and better affordability of traditional financial services, including greater access to bank branches and

lending, remain important, given the amount of credit still channelled through traditional banking services.

New technology

16. Technology has gradually improved the provision of financial services in the past, such as credit cards, debit cards, prepaid cards and ATMs. Exponential progress in information and communications technologies has opened the way for new financial services and business models exhibiting a significant potential for financial inclusion. Innovative services, such as mobile payments and mobile banking, have significantly reduced physical and economic barriers impeding financial access, particularly for those living in remote and rural areas. Such services have proved to be particularly useful in areas where population density is low and mobile penetration is high.[8] The impact of new technologies has been amplified by the private sector's adoption of business models that complement technology platforms.

17. Mobile money schemes capitalize on the rapid uptake of mobile telephony in developing countries to offer some financial services to rural and marginalized areas. In developing countries, almost 250 mobile money schemes were implemented in July 2014,[9] compared with only 130 in March 2012. In Africa, there were more than 130 of those schemes in 2014, compared with around 60 in 2012. Unlike traditional banking service providers, mobile network operators have invested in extensive networks and started to offer financial services through wireless applications, including the possibility to store money in a mobile phone to make transfers or payments. Under these schemes, cash value is held elsewhere, in a bank or in a postal bank, and a network of agents facilitates the conversion of cash into mobile money, cash-in, and the opposite, cash-out. Mobile money may be linked to a bank account to provide access to other financial services such as savings, credits and insurance. Transfers are the most used services and have the potential to facilitate remittances.

Box 1. Kenya: M-PESA

At the end of March 2012, M-PESA had 15 million active customers who had transferred an estimated K Sh 56 billion every month. With over 37,000 mobile money agents, M-PESA was linked to 25 banks and could be accessed via 700 ATMs. Its distribution services have a sales force of 37,000 across the country.[10] The share of the Kenyan population having access to commercial bank accounts increased from 20 per cent in 2007 to approximately 50 per cent in five years, largely owing to the proliferation of mobile banking. Under this platform, domestic mobile transfers between consumers still predominate, but the reception of international mobile transfers by Western Union from around the world is also available. Notably, M-PESA alone processes more transactions domestically within Kenya than Western Union does globally. Consumers can make or receive mobile payments to and from a broad array of entities encompassing businesses, monthly payments to utility providers and government agencies. Other financial services linking mobile money to bank accounts are also provided. These include transfers between mobile money and bank accounts, micro savings, credit and insurance.

Source: UNCTAD.

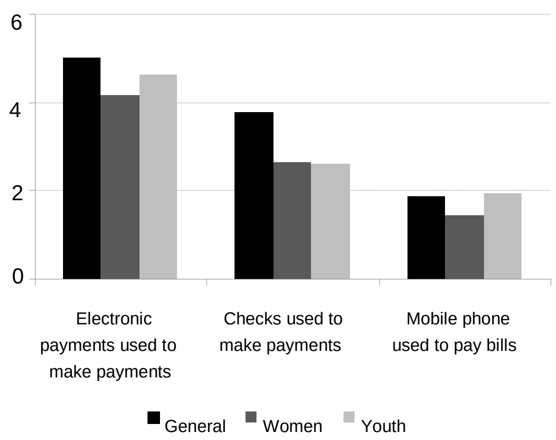
[8] UNCTAD, 2012, *Mobile Money for Business Development in the East African Community: A Comparative Study of Existing Platforms and Regulations* (Geneva, United Nations publication).

[9] GSM Association.

[10] UNCTAD, 2013, Report of the Multi-year Expert Meeting on Trade, Services and Development on its first session, TD/B/C.I/MEM.4/3, 12 March.

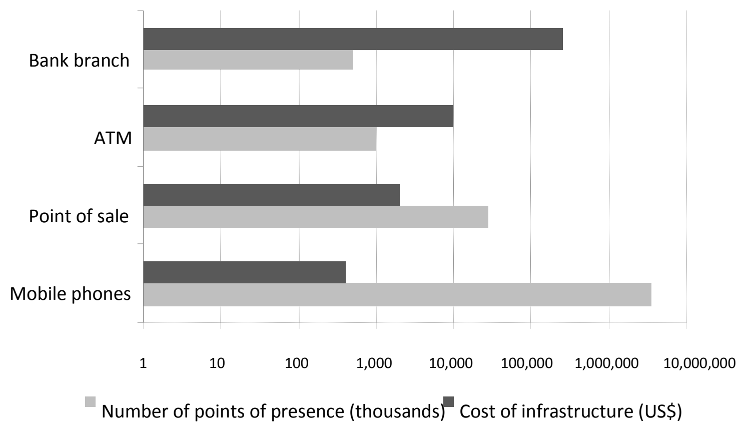
18. Financial operations carried out with mobile phones present important advantages from the viewpoint of financial inclusion. Most significantly, it is more gender neutral and youth friendly. Figure 5 shows that the difference in the proportion of women users and that of all users is smaller with mobile phone payments than other modes of payments. It is also the only mode of payment where the proportion of young users is higher than that of average users. The potential of mobile money relates to the higher coverage of existing infrastructure, and its cost is lower than in other networks. The cost of the necessary infrastructure to make a transaction is lowest for mobile phone than all other modes (bank branches, ATMs, points of sale, and mobile phones have the higher number of points of presence (figure 6).

Figure 5
Developing countries: Methods of payment, 2011
(Percentage)



Source: UNCTAD computation based on the World Bank's Global Findex Database.

Figure 6
Cost of infrastructure in dollars and number of points of presence in thousands by channel of delivery
(Logarithmic scale)



Source: UNCTAD computation based on data from the Consultative Group to Assist the Poor.

19. Mobile money has proved to be particularly useful for extending the coverage to rural areas and servicing farmers, creating opportunities for related new services and business for agricultural development. While the global demand for financial services from smallholders was estimated at $450 billion in 2012, only 2 per cent was being met. This has led mobile money services providers to develop specific mobile financial services for farmers, such as farmer-specific insurance, credit and saving products, and complementary information-based services. It has also led banks to increasingly seek partnerships with mobile money service providers to expand their customer base and take advantage of information related to mobile phone usage patterns and mobile money transactions as alternative solutions for credit scoring systems.

Box 2. Nigeria: Mobile finance and agricultural development

In 2011, only 29.7 per cent of people in Nigeria had an account at a formal financial institution, while there were over 127 million mobile phone subscriptions in 2013. In this context, Cellulant Corporation is currently implementing an electronic wallet scheme developed by the Federal Ministry of Agriculture, under which farm inputs are distributed to farmers. Over one million farmers have already benefited from the scheme. Cellulant is working with Nigeria's Bank of Agriculture, a Government-owned development bank with a mandate to mobilize rural savings and provide low-cost credit to smallholders and commercial farmers, and small and medium-sized rural enterprises. This collaboration is in an advanced stage and envisages broadening the Bank of Agriculture offer with mobile money services that include money transfer, bill payments, mobile banking, microinsurance payments and mobile wallets.

20. Mobile money is not a panacea for financial inclusion, as it still accounts for a much smaller portion of the value of transactions than traditional instruments. In Kenya, the daily value of transactions between banks is almost 700 times larger than for transactions between M-PESA mobile accounts.[11]

Innovative business models and services

21. Innovative business models and services have emerged and expanded addressing traditional barriers to access to financial services, both on a for-profit and non-profit basis, and have created new business opportunities. Product designs that address market failures, meet consumer needs and overcome behavioural obstacles can foster encourage the use of financial services. Innovative insurance products can mitigate weather-related risks in agricultural production and help promote investment and productivity. Improvements in lending to small and micro enterprises can be achieved by leveraging existing networks, for example, correspondent banks. Novel mechanisms have broadened financial inclusion by delivering credit through retail chains and lowering costs by using existing distribution networks.

22. Since the 1970s, microfinance has been growing in many countries with or without special regulations (for example, the Grameen Bank in Bangladesh). Microfinance is provided by microfinance institutions and commercial banks. Many financial institutions – commercial banks, development banks, community banks and regional banks – increasingly target lower-income segments of the population, and unbanked and under-banked segments, which are often ignored or not fully covered by traditional commercial

[11] W Jack and T Suri, 2011, Mobile money: The economics of M-PESA, Working Paper 16721, National Bureau of Economic Research.

banks. These institutions differ widely in business models. Some of these banks rely on the introduction of banking agents, allowing commercial establishments to offer basic financial services on their behalf, focusing on low-cost accounts targeted at the low-income population. They also differ in coverage and profitability. Some banks are for-profit operation, such as commercial banks, while others, such as development financial institutions, are not-for-profit orientated. Yet others depend on subsidies for their operations.

23. Microfinance in particular has greatly helped underserved households, SMEs and self-employed entrepreneurs in developing countries. Much of the criticism on microfinance relates to microcredit. It is often argued that microfinance services serve more for consumption smoothing and risk management than for investment and entrepreneurship among the poor, and benefits often are concentrated on wealthier households. The expansion of micro credits, relaxed credit screening and underwriting standards could cause an oversupply of lending to non-creditworthy clients and also lead to overindebtedness among low-income debtors.

24. State-owned, cooperative, development and community banks, and Islamic finance, have proved to be particularly amenable to extending access to finance to a broader range of untapped population and income groups. Where private banks failed to extend credit to productive sector, many developing countries resorted to State-owned or public banks and development banks to support financial inclusion. The role of State-owned banks, national development banks and community banks in providing indispensable productive investment is significant. Such banks account for 80 per cent of total assets in South Asia. State-owned banks have proven resilience in compensating the credit crunch and promote competition in oligopolistic markets. Increasing the diversity of agencies involved in remittance transfers – postal banks, financial cooperatives and microfinance facilities – could reduce the costs of transfer. With regard to credit products, financial inclusion is sought by Islamic commercial banks, Islamic rural banks and Islamic cooperatives that provide microfinance services.

25. New mobile banking and payment technologies have given rise to technology-based business models that can broaden access to basic financial services through a greater use of correspondent banks (representatives of a bank carrying out transactions on behalf of banks) using existing networks of agents and institutions, such as post offices, supermarkets, grocery shops, convenience stores, gas stations and lottery outlets. They offer only elementary transaction services or a broader range of financial services. There are growing signs that correspondent banking has had a substantial impact on financial inclusion.

Box 3. Brazil: Postal services for financial inclusion and trade

In Brazil, Banco Postal acts as a correspondent for a private bank, Bradesco, and is an important part of the Brazilian Government's strategy of supplying financial services to underprivileged people in remote locations, through a system of correspondent banks. This strategy encompassed a gradual reduction of regulatory requirements on correspondent banking. Beyond the partnership with the post offices, financial institutions reached out for other retail establishments, including lottery agencies, and have even developed riverboat banks to take financial services to distant communities along the Amazon River. The national network of 6,000 post offices offers universal access to postal, express and basic financial services. Banco Postal is present in 4,860 of the 5,561 municipalities. A total of 12.4 million people living in 1,525 municipalities in which a post bank agency was opened did not have a bank agency prior to that time. Moreover, Banco Postal was acting as the sole financial intermediary for 5.98 million people. The postal bank, other correspondent banks and traditional bank agencies are mostly complementary networks, with Banco

Postal focusing on more low-income clients. The poorest municipalities, equivalent to 29 per cent of the entire population, accounted for 50 per cent of all Banco Postal accounts.

Source: UNCTAD.

26. Post offices have long been utilized to provide some financial services, particularly basic banking services as a means to expand financial access. They can contribute more to financial inclusion by offering a full range of financial services. Post offices have the world's largest physical network, with a total of 662,000 offices in 2011, in comparison with 523,000 bank branches and ATMs worldwide. There are twice as many post offices (500,000) as commercial bank branches (275,000) in developing countries. While banks focus on cities with denser populations, post offices operate in remote and even disadvantaged areas. Some 80 per cent of post offices in sub-Saharan Africa are concentrated in small and medium-sized towns and rural areas where 83 per cent of the population lives. According to the Universal Postal Union, an estimated one billion people in over 50 countries are banked through postal systems. Post offices that offer legally independent and regulated financial services can be a practical option in expanding access to financial products for the poor and SMEs.

Box 4. Morocco: Financial inclusion and post offices

In Morocco, the post office plays a key role in providing money transfers and basic financial services to all segments of the population, particularly the rural poor. Poste Maroc has been the major player in the domestic transfer market, and it maintains that status today through its financial services subsidiary Al-Barid Bank. The "Mandatti express" product offers instant cash-to-cash services within the Bank's network of 1,000 post offices offering financial services throughout the country. In terms of international remittances, the Poste Maroc Group is linked with other players in the postal and banking sector through the International Financial System of the Universal Postal Union and Eurogiro. Al-Barid Bank is an agent for both Western Union and Moneygram, which spotted an opportunity in its dense rural network.

In 2010, the postal savings activity was converted into a regulated bank – called Al-Barid Bank (postal bank) – a fully owned subsidiary of Poste Maroc, which received a limited banking licence from the central bank and was charged with promoting financial inclusion. The banking licence is limited by client segment, meaning that Poste Maroc can focus solely on segments C and D of the population (second and third quintiles in terms of income, where A is the wealthiest segment and E is the poorest). Today, it opens 2,000 accounts a day and is considered one of the best examples of a postal bank in the developing world. Official banking levels went from 34 per cent to 47 per cent of the population. Al-Barid Bank is the main reason why banking levels in Morocco increased to 52 per cent in 2012.

Source: Universal Postal Union, 2013, *Global Panorama on Postal Financial Inclusion: Key Issues and Business Models.*

III. Remittances and financial inclusion

27. Remittances have significant potential to contribute to human and social development. It is important to harness this potential through the effective use of financial services in the post-2015 sustainable development agenda, and to achieve universal access by catalysing on remittance flows. One of the targets being considered for sustainable development goals is to reduce to 5 per cent or below the transaction costs of migrants'

remittances by 2030, including regulatory and administrative costs. It is estimated that a 5 per cent reduction on remittances costs could yield $15 billion in savings. These efforts are in line with international discussions on migration and remittances such as under the United Nations Conference on Sustainable Development and the High-Level Dialogue on International Migration and Development. This target is in line with that of reducing the global average costs of remittance transfer from the present 10 per cent to 5 per cent in five years, as agreed in such platforms as the Group of Eight and the G20.

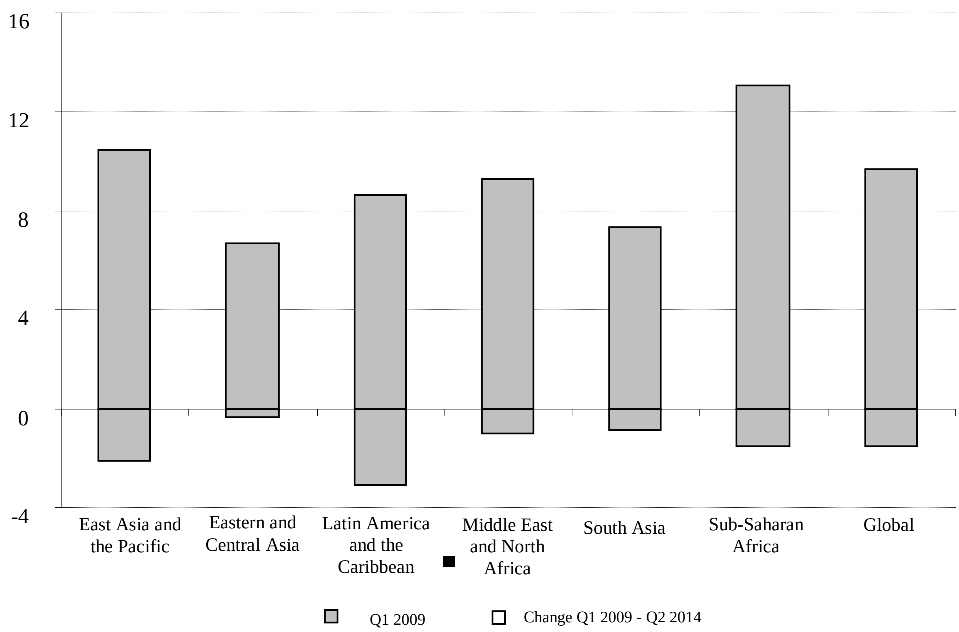
28. There is a strong relationship between remittance flows, financial inclusion and poverty reduction. Research shows that a 10 per cent rise in remittances leads to a 3.1 per cent in poverty reduction.[12] It is therefore important to make transfer systems less costly, more efficient and more transparent. It is generally recognized that remittances are usually regular and predictable flows, which in principle makes remittance recipients relatively more inclined to join the formal financial sector. Lower-income countries tend to have both higher levels of remittances as a share of GDP and less account penetration. If banks or credit unions are used to transfer remittances, remittance senders and recipients have an incentive to open a bank account. Thus, remittances have the potential to boost demand for financial instruments. Many providers of financial services have recognized this potential and have started to offer additional services along with remittance accounts. The positive impact on financial inclusion of bundling remittance accounts with other financial products is therefore significant. There is a need to improve data on remittances.

29. The high costs of remittance transfer have been identified as major impediments to remittance flows. In the second quarter of 2014, the global average cost of sending remittances was at 8.1 per cent, reaching a new all-time low (figure 7). The cost of sending remittances decreased for all regions. Latin America and the Caribbean registered the largest decline of all regions, with an average of 5.6 per cent. Sub-Saharan Africa, with an average cost of 11.6 per cent, remains the region with higher remittance costs. Between 2009 and 2014, the number of remittance transfer corridors with costs below 10 per cent increased from 53–77 per cent. In many LDCs, costs still range from 14–20 per cent. Among G8 countries, the average cost of sending money from Japan, Canada, and France is above the global average, while costs in the Russian Federation, the United States of America, Italy, and the United Kingdom are below the average. Among G20 countries, South Africa remains the most costly country to send remittances from, with an average of 19.56, followed by Japan with an average of 14 per cent. The least expensive sending country, together with the Russian Federation, is Brazil (4.24), followed by the United States (5.78) and the Republic of Korea (5.99). China is the most expensive country in the G20 to send money to, with an average cost of 10.89 per cent, while Mexico and Turkey are the cheapest receiving markets, with averages of 4.51 and 7.28 per cent, respectively.[13]

[12] UNCTAD, 2011, *Impact of Remittances on Poverty in Developing Countries* (New York and Geneva, United Nations publication); UNCTAD, 2012, *The Least Developed Countries Report 2012: Harnessing Remittances and Diaspora Knowledge to Build Productive Capacities* (New York and Geneva, Sales No. E.12.II.D.18, United Nations publication).

[13] World Bank, 2014, Remittance Prices Worldwide, Issue No. 10, available at https://remittanceprices.worldbank.org/sites/default/files/rpw_report_june_2014.pdf.

Figure 7
Developing economies: Trends in remittance costs during the first quarter of 2009 and second quarter of 2014
(Percentage)



Source: The World Bank (2014), Remittance Prices Worldwide, Issue No. 10.

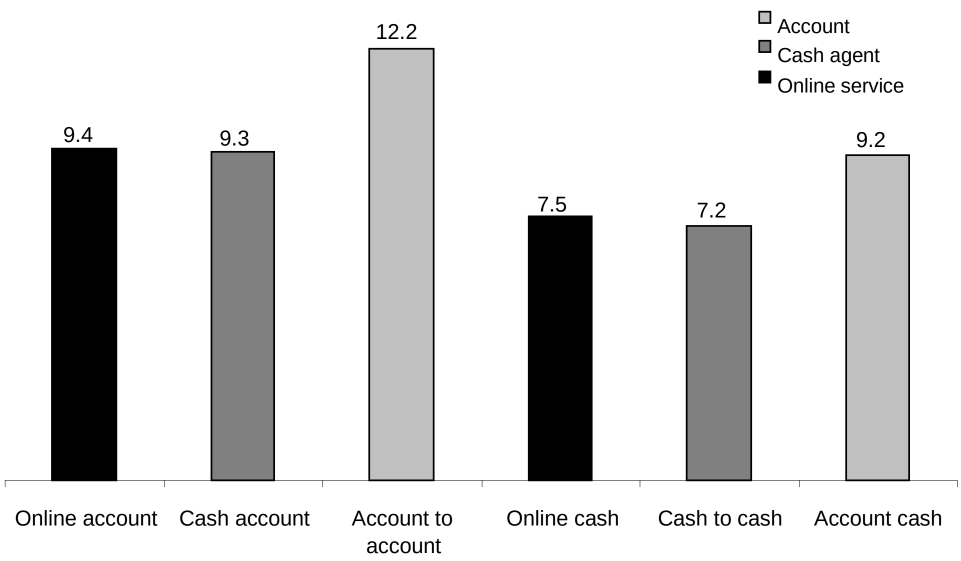
30. South–South remittances are still costly mainly due to capital controls or prohibition of remittance transfers. There is a lack of information and uncertainty on “lifting fees”, mainly for transfer to bank accounts by remittance services providers. Exclusivity contracts between banks or the national post office in source countries and international money transfer agencies serving West African corridors seems to be a factor contributing to a lack of competition and high remittance costs. The establishment of two regional payment systems – Regional Payment and Settlement System of the Common Market for Eastern and Southern Africa and the East African Cross-Border System – is expected to facilitate cross-border payments within these regions. The African Union has decided to create an African institute for remittances to facilitate removal of obstacles.

31. Commercial banks are the most expensive remittance channel, with an average cost of 12.1 per cent, while post offices are the cheapest, with an average cost of 4.7 per cent (figure 8). Money transfer organizations (MTOs), present in 85 per cent of migration corridors, is situated in the middle, with an average cost of 6.6 per cent.[14] Regarding the type of products, cash services remain the most widely available (41 per cent) and one of the most cost-effective ways to send money, with an average cost of 6.6 per cent. An increased number of non-cash services is available, including account-to-account services, as many MTOs have started offering such services. Average transfer costs have suffered little effect, with account-to-account services to any bank remaining at 13 per cent. The cost of transfers within the same bank has slightly declined to 7.78 per cent. Cash-to-account services are more widely available and the cheapest product type at an average cost of 5.5 per cent, and services offered online gained ground. Online services account for 16 per cent of the total sample. The average cost for these services in 2014 was 6.13 per cent.

[14] Ibid.

International money transfers through mobile remittances have not progressed, owing to concerns relating to anti-money laundering and combating the financing of terrorism, lack of cross-interoperability of remittance platforms and exchange controls. Kenya, Uganda and the United Republic of Tanzania, for example, have regulations on mobile remittances. In these countries, the mobile money model is led by mobile network operators. In some of these countries, MTOs have to partner with a bank to provide remittance transfer platforms.

Figure 8
Average price for sending remittance of $200 by service model, 2011
(Percentage of remittance amount)



Source: Dalberg Global Development Advisors.

32. The combined use of banking, postal and telecommunication networks, and inter-operability may generate more efficient channels, with lower costs and more potential to reach low-income recipients in remote locations. Some countries, such as Mexico and El Salvador, pool resources of banking, microfinance and credit unions to expand the whole payment network, thus promoting efficient and broad distribution of remittances.[15] Some banks allow for remittance transfers without the need for the sender or the recipient to open an account. Such a multiplicity of channels is important in promoting competition, incentivising cost-effective channels of remittances and formalizing informal channels. Moreover, improving transparency and information on the costs associated with each channel of remittances, possibly through price databases, will enable senders to choose the most cost-efficient options. This requires data collection, monitoring and evaluation of the available options. Policies need to envisage transversal coverage, which means independence from specific technologies. Regulation should promote interoperability of platforms or even shared infrastructure to reduce operational costs, increase networks and financial access, facilitate competition and achieve economies of scale.

33. It is important to maximize the development impact of remittances by channelling them to investments in productive sector, social services and infrastructure. There is

[15] UNCTAD, 2011, *Impact of Remittances on Poverty in Developing Countries* (New York and Geneva, United Nations publication).

evidence that remittances are mainly spent in household consumption, representing 70 per cent of amounts transferred, followed by home-related spending, health and education.[16] They do not have a robust effect on the demand and use of credit, owing to the lack of credit products. Financial counselling and diaspora funds could usefully address this issue. Diaspora bonds could be used as a tool for development financing, but also strengthened by prospects of attractive return on investment. India, Ethiopia, Kenya, Nepal and the Philippines have already used diaspora bonds, and Nigeria and Trinidad and Tobago are processing their issue. Several countries have Islamic financing products. Another strategy consists of providing tax and credit incentives to induce migrants and diasporas to invest in their home countries, for example in Bangladesh and Brazil. Internationally, there is still progress to be made on leveraging remittances for capital market access at the macro level through the recognition by credit-rating agencies of the importance of remittances, securitization and diversified payment rights.

34. Several countries have integrated remittance products into national policies on financial inclusion. Under the National Financial Inclusion Strategy of India, many public sector banks offer accounts that charge no fees for remittances. The Philippine Development Plan (2011–2016) explicitly notes the need to promote financial inclusion and facilitate remittances domestically and from abroad. The central bank has approved alternative ways of making remittances, and competition is helping to lower transaction costs and reduce the time needed for delivery.

35. Trade and cooperation agreements at regional and multilateral levels, and regulatory cooperative schemes provide a platform through which financial inclusion, the temporary movement of natural persons and remittances can be promoted. Such policies include the promotion of services supply by Mode 4 through commitments set out in the General Agreement on Trade in Services (GATS), which have been scarce and have focused mainly on higher-skilled categories. The current Doha Round negotiations, including discussions on operationalizing LDC services waivers and the recent request by LDCs for preferential market access, may potentially contribute to remove barriers to the movement of people by expanding quotas, providing objective criteria for economic needs tests and recognizing qualifications. Regional integration initiatives may contribute to reducing barriers to financial inclusion, migration and remittances, and may prove to be more amenable to cooperative mechanisms, such as on labour mobility issues, addressing the portability of social benefits.

IV. Policies and regulations for financial inclusion

36. Government can play an important role in financial inclusion by developing sound regulatory and institutional frameworks, supporting the availability of information and taking direct measures, such as subsidies and mandatory requirements, targeting financial inclusion. Evidence points to the role of government in setting standards for disclosure and transparency, regulating aspects of business conduct and overseeing effective recourse mechanisms to protect consumers. Competition is also a key part of consumer protection. To harness the promise of new technologies, regulators need to allow competing financial service providers and consumers to take advantage of technological innovations. The regulatory stance can influence business models and new services.

37. Many countries have formulated financial inclusion strategies that are public documents, developed through a consultative process involving various public sector bodies

[16] UNCTAD, 2013, *Maximizing the Development Impact of Remittances* (New York and Geneva, United Nations publication).

(ministries of finance, central banks), private firms (commercial banks, non-bank financial institutions) and civil society (microfinance organizations). Financial inclusion strategies are often led by central banks. South Africa, Malawi and Zambia have developed a comprehensive financial inclusion policy. In Kenya, the central bank was aided by Financial Sector Deepening Trusts, and surveys and research conducted by Finmark Trust. A typical strategy would highlight a headline target. For example, Nigeria's strategy (2012) aims to reduce financial exclusion from 46–20 per cent by 2020.

38. The nine principles for innovative financial inclusion endorsed by G20 leaders in 2010 aimed at creating an enabling policy and regulatory environment for innovative financial inclusion. Among these principles are implementing policy approaches that promote competition and provide market-based incentives for the delivery of sustainable financial access and the usage of a broad range of affordable services and a diversity of service providers, promoting technological and institutional innovation as a means to expand financial system access and usage, and protecting and empowering consumers to have financial literacy and capability.

39. Governments from 108 developing countries have adopted principles to guide their regulatory institutions in promoting financial inclusion, and regulatory institutions from 46 developing countries have made specific commitments under the Maya Declaration. Specifically, they have made the following commitments:

(a) To draw up a financial inclusion policy that creates an enabling environment for cost-effective access to financial services making full use of appropriate innovative technology and substantially lowering the unit cost of financial services;

(b) To establish a sound and proportional regulatory framework that achieves the complementary goals of financial inclusion, financial stability and financial integrity;

(c) To promote consumer protection and empowerment;

(d) To develop an evidence-based financial inclusion policy based on the collection and analysis of comprehensive data and generation of comparable indicators in the network.

40. Governments have a particularly important role in promoting universal access to basic financial services and financial inclusion through subsidies and a variety of direct measures. Policies to expand account penetration – such as requiring banks to offer basic or low-fee accounts, granting exemptions from onerous documentation requirements, allowing correspondent banking and using electronic payments into bank accounts for government payments – are especially effective. Regulation can impose on financial institutions universal services obligations and other requirements: priority sector lending, mandatory lending to SMEs, loans to poor people at lower interest rates with easy repayment rates and no profit margins, prohibition to refuse basic financial services to poor clients and prohibition of not servicing particular areas.

Box 5. China: Regulatory measures to promote financial inclusion

China developed a national strategy for building an inclusive financial system in 2013. The China Banking Regulatory Commission has provided that the banking sector ensure presence of minimal financial services in all townships and villages by increasing the number of branches and exploring innovative alternatives to physical facilities, including mobile units and ATMs. To address the credit issue in rural areas, the Commission approved the set-up of village and township banks by banks and rural mutual credit cooperatives. It transformed the Postal Savings and Remittance Bureau into the Postal Savings Bank of China with the mandate to develop commercially viable loan products for rural enterprises, migrant workers and farmers. This postal bank is the fifth largest bank in

China with more than 870 million accounts by asset size. On agriculture-related credit, banks are required to maintain a growth rate of no lower than the average level of all loans. To accommodate the credit needs of SMEs, the Government issued guidelines encouraging banks to set up small business units to support SMEs. With a view to promoting competition by increasing the number of banks, the Commission will approve and regulate banks to be set up with qualified private capital.

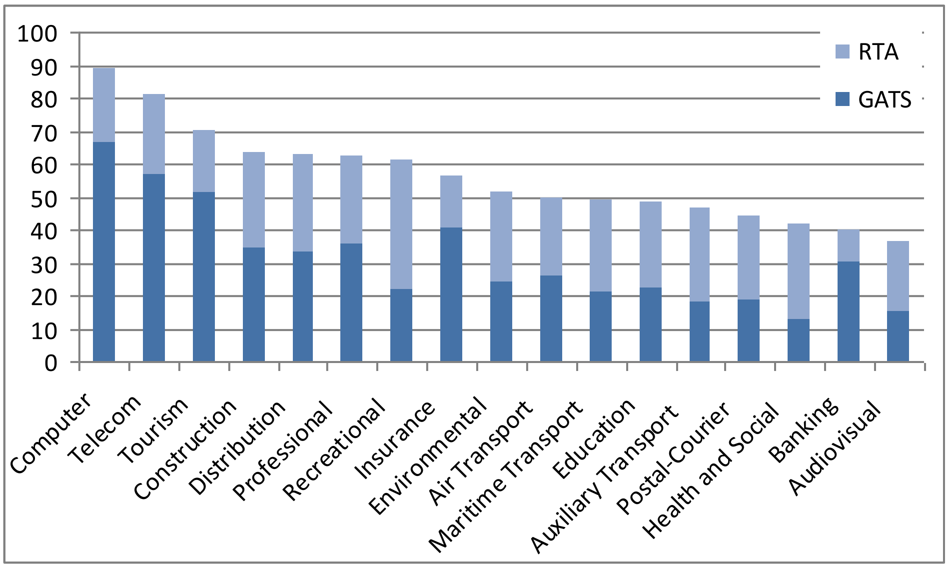
41. On the demand side of financial services, improved financial literacy, capabilities and consumer empowerment could increase demand for financial services. Gaining ability through financial education to manage family budgets, do life planning, select appropriate financial products and make more informed choices concerning the transfer and use of remittances helps consumers to cope with some of the complexity of access to financial services. It is possible to enhance financial capability, knowledge and skills through well-designed, targeted policies. Effective promotion of financial literacy and education requires a multi-stakeholder engagement with governments playing an active leading, coordinating and supporting role. Nigeria has drawn up a framework for financial literacy and seeks to educate the population to improve its understanding of financial products and to develop skills and confidence to become more aware of financial risks and opportunities. The framework covers the institutionalization of financial literacy training in the education system, the dissemination of information outside the school system and the design of outreach programmes.

V. Financial inclusion, trade agreements and regulatory reforms

42. Trade liberalization and regulatory reform are relevant to financial inclusion, as they have an impact on measures that specifically support financial inclusion, such as universal access policies. In particular, the effective regulation of foreign firms has become a particularly salient issue when there is a substantial presence of foreign banks in domestic financial markets. Therefore, trade liberalization efforts need to be carefully coordinated and synchronized with adequate domestic regulations to promote financial inclusion. In the context of multilateral trade liberalization efforts under the Doha Round and the parallel liberalization processes such as the Trade in Services Agreement and regional trade agreements (RTAs), including mega-RTAs, there is a need for a coherent approach to these processes to ensure the right to regulate, including adequate scope for national regulatory measures facilitating financial inclusion. Further, financial regulatory reform processes could have direct and indirect implications for national regulatory measures.

43. The level of commitments under GATS and RTAs varies across sectors (figure 9). Financial services exhibit a relatively high level of GATS commitments but see the least improvements in an RTA context, particularly in banking. Developing countries have proved to be cautious in making commitments in banking through Mode 1. This may reflect the concern of regulators that Mode 1 liberalization may create more risks, as it is easier to exercise regulatory control over banks established within their jurisdiction through commercial presence, particularly by establishing subsidiaries rather than direct branching. Second, Mode 1 commitments require an open capital account, as capital should be permitted to flow freely to the extent that such capital is essential to the provision of the services concerned, such as cross-border deposit taking and lending. For example, India and China have not made commitments for Mode 1 trade in most banking services.

Figure 9
Average level of commitments under the General Agreement on Trade in Services and regional trade agreements for all countries



Source. UNCTAD calculation based on World Trade Organisation dataset.

44. Recent RTAs have increasingly moved towards deeper liberalization and have introduced some innovative provisions that may affect financial inclusion policies. Commitments may be based on applied levels of market access conditions, including through standstill requirements, that is to say, not allowing countries to decrease the conformity of the measure with respective obligations, and the "ratchet clause" that provides for an automatic incorporation of further future liberalization measures. National treatment may be applied on a horizontal basis to all sectors and modes. The third party most-favoured nation clause increasingly incorporated in recent RTAs aims to ensure that a party to an RTA obtains best possible preferential treatment available in other RTA partners. Some of these approaches are being replicated under ongoing plurilateral negotiations aimed at a trade in services agreement.

45. Some horizontal measures increasingly incorporated in RTAs could have implications for national measures in favour of financial inclusion. Recent mega-RTA negotiations have sought to address the potentially anticompetitive effect of Stated-owned enterprises that tend to receive some preferential treatment, including preferential finance. Some regional disciplines have sought to establish "competitive neutrality" between State-owned enterprises and private companies by eliminating such structural advantages. Many countries have stressed the importance of State-owned enterprises in delivering public policy goals, including access to financial services.

Box 6. Association of Southeast Asian Nations: Financial inclusion

Financial inclusion has long been on the agenda of the Association of Southeast Asian Nations (ASEAN). Key concerns relate to increasing access to financial services for underprivileged groups, particularly for lending, insurance, and remittance; developing innovative financial products and instruments for the poor; strengthening consumer protection; and promoting financial literacy. In ASEAN, financial inclusion for SMEs is included in the ASEAN Economic Community 2015 Blueprint, which states that the access of ASEAN SMEs to finance should be facilitated to enhance their competitiveness. Access to finance by disadvantaged individuals is given increasing attention. ASEAN financial services liberalization is based on the principle of respect for national policy objectives and the level of development of individual members and is expected to permit ASEAN members to take measures for financial inclusion.

46. The global financial regulatory landscape is in the process of reshaping by shifting the regulatory focus to macroprudential objectives. The central reform agenda is to strengthen bank capital and liquidity standards under Basel III, which has some bearing on efforts aimed at financial inclusion. A matter of concern was that by assigning higher risk weight on holding minority interests in emerging markets banks and holding short-term assets, new rules might discourage cross-border investment and lending to SMEs and project finance. A central issue that emerged from national reform debate is whether and how to isolate essential banking services in retail and commercial banking from high-risk investment banking. The "Volcker rule adopted in in the United States in December 2013 prohibits deposit-taking banks from engaging in most forms of proprietary trading to curtail the perceived implicit government guarantee on deposits from being applied to proprietary trading. The United Kingdom is introducing a more restrictive ring-fencing of retail banking from investment banking by requiring that all investment banking be conducted by a separate subsidiary with independent governance and its own extra capital.

47. While many developing countries have yet to adopt the Basel II framework and Basel III is not mandatory, there are indirect implications in that it would form best practices for developing countries to follow and comply in the medium term. Bank subsidiaries in developed countries often have significant market shares in developing countries, and the changes in regulatory regime applying to parent banks in developed countries could also affect them.

Conclusion

48. Financial inclusion is central to poverty reduction, and inclusive and sustainable development. Physical, economic, regulatory and cultural factors contribute to a lack of access to financial services, which particularly affects the poor, women, youth, rural populations and those in the informal economy. The use of new technologies such as mobile money, and innovative business models has exhibited a large potential in circumventing and overcoming barriers to access. Governments have an important role to play in setting up sound regulatory frameworks and setting conditions so that incentives can be provided to extend supply and affordability of services, and creating an expanded demand for financial services, such as through financial education and empowerment. Remittances are the major source of external private financial inflows into developing countries and represent a promising source of demand for financial services; therefore, the reduction of transaction costs and facilitated, speedier and safer transfer of remittances, including through new products, could contribute significantly to financial inclusion.